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FOREWORD

By Helen A. Christakos[†] *& Sonal N. Mehta*[‡]

The *Annual Review of Law & Technology* ("*Annual Review*") aims to provide practitioners, judges, policymakers, scholars and students with summaries and analyses of recent developments in technology law, including the fields of intellectual property, antitrust, cyberlaw, constitutional law, telecommunications, business law, entertainment law and international law. Now in its fifth year, this year's *Annual Review* includes detailed analyses of twenty-six important developments during the period of August 31, 2000 to August 31, 2001, as well as shorter summaries of forty recent developments in technology law.

Once again, the Internet and digital technology have taken center stage in the evolution of copyright, trademark, antitrust, business and international law. In this year's *Annual Review*, an entire section has been devoted to developments in cyberlaw, in addition to digital technology and Internet-focused developments in several other fields. Additionally, the *Annual Review* addresses evolving areas of patent law, particularly the written description requirement, and trade secret law, especially the issues arising out of employment relationships. This volume also includes a section on Entertainment law, with two pieces focusing on the evolving body of law surrounding the right of publicity.

I. INTELLECTUAL PROPERTY LAW

A. Copyright

All four of this year's copyright Notes, like last year's Notes, focus on cases that arose from the use of Internet and digital media. These cases also reflect courts' continuing efforts to further delineate the line between

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We would like to thank Professor Peter Menell for his exceptional efforts and vision in bringing the *Annual Review* to fruition, and for his continued support and guidance in this and other ventures. We would also like to thank this year's student authors and advisors, as well as the editorial staff of the *Berkeley Technology Law Journal*, for their tireless work.

protecting the rights of creators of digital information, and prohibiting undue constraint upon public access to and use of that information.

In *New York Times Co. v. Tasini*,[3] the United States Supreme Court upheld the Second Circuit's decision that § 201(c) prohibits publishers of magazines from placing the freelance authors' works into their electronic databases. The Court held that because Congress amended the Copyright Act in 1976 to reduce publishers' bargaining power over authors, it therefore intended to limit the circumstances in which publishers could reproduce freelance authors' works. In considering the user's perspective, the Court held that the section 201(c) revision privilege cannot be extended to databases because the articles were not available on the databases as part of the original collection of works. Because of the high cost of acquiring permission from freelance authors, it is likely that fewer such pieces will be available to the public.

The district court in *Random House v. Rosetta Books*[4] denied Random House's request for an injunction, holding that a contract to publish a book in virtual form, absent a specific provision to publish the book in electronic form, does not automatically grant a publisher the right to publish these same virtual works as eBooks. New York contract law specifies that contract language must be interpreted in accordance with the parties' intentions as revealed by the contract language. Therefore, when contract language is ambiguous, the interpretation of the contract is a matter of fact for the court to determine. This decision was not a clear victory for either side. Random House filed an appeal on September 13, 2001, so we can expect to revisit this issue in next year's *Annual Review*.

Also important was the clarification of the rights Congress granted to the United States Copyright Office in the context of Internet broadcasting regulation. The district court in *Bonneville International v. Peters*[5] held that the United States Copyright Office has the right to establish the rates and terms for a section 114 license because Congress gave the United States Copyright Office interpretive authority over this section of the Copyright Act. The court further held that Congress intended to permit only local transmission over-the-air radio broadcasts, and not AM/FM Internet streaming, under section 114.

This year's *Annual Review* also includes the *A&M Records, Inc. v. Napster, Inc.*[6] decision in which the Ninth Circuit upheld the injunction

3. 121 S.Ct. 2381 (2001).
4. 150 F. Supp. 2d 613 (S.D.N.Y. 2001).
5. Bonneville Int'l v. Peters, 153 F. Supp. 2d 763 (E.D.P.A. 2001).
6. 239 F.3d 1004 (9th Cir. 2001).

against Napster, agreeing with the district court that A & M Records would likely prevail on contributory and vicarious copyright infringement claims. It did, however, remand the case with instructions to reduce the scope of the preliminary injunction by requiring A&M Records to notify Napster of infringing activity on Napster's system. This decision limits the accessibility of music to the public. At the time of publication, no appeal had been filed.

B. Patent

The most significant development in patent law this year, and perhaps in the last several years, is the Federal Circuit's *en banc* decision in *Festo Corp. v. Shoketsu Kinzoku Kogyo Kabushiki Co.*[7] In *Festo*, the court held that an amendment to a claim limitation for any reason related to patentability acts as a permanent bar to the application of the doctrine of equivalents. The United States Supreme Court granted *certiorari* on June 18, 2001. The Court heard oral arguments on January 8, 2002. At the time of publication, the Court had not yet issued its decision.

There have been many additional developments in patent law. Courts have ruled on issues ranging from appellate jurisdiction over patent-related cases to application of the on-sale bar. Both of this year's Notes on patent law focus on the evolving rules surrounding the written description requirement.

In *Purdue Pharma L.P. v. Faulding Inc.*,[8] the Federal Circuit invalidated the claims of a pharmaceutical patent for lack of adequate written description. The court found that the written description failed to convey to one of ordinary skill in the art that that the inventor was in possession of the invention at the time of the original filing because the original specification failed to describe a later-amended claim limitation as being the "important defining quality" of the invention. Thus, for the first time, the Federal Circuit invalidated patent claims for failure to satisfy the written description requirement where the amended limitation narrowed, rather than broadened, the scope of the challenged claims.

In 2001, the United States Patent and Trademark Office ("USPTO") issued Written Description Guidelines intended to assist USPTO personnel in the determination of whether an adequate written description has been provided in a patent application. Though the Guidelines state that a rejection of a patent application is based upon the substantive law itself and not

7. 234 F.3d 558 (Fed. Cir. 2000) (en banc).
8. 230 F.3d 1320 (Fed. Cir. 2000).

the Guidelines, it is important to analyze inconsistencies between the Guidelines and case law.

C. Trademark

The Internet continues to dominate the development of trademark law. This year's *Annual Review* also analyzes the first wave of cases decided under the Anticybersquatting Consumer Protection Act ("ACPA"), identifying issues that consistently arise in courts' application of the ACPA. While most courts strictly limit their application of the ACPA to cybersquatting cases, some courts are applying the ACPA beyond its intended scope.

Similarly, new patterns have begun to emerge since the Internet Corporation for Assigned Names and Numbers ("ICANN") implemented the Uniform Domain-Name Dispute-Resolution Policy ("UDRP").[9] Although the UDRP has resolved several thousand domain name disputes since its inception, the system has come under fire by critics for being biased in favor of complainant trademark owners (who win in over eighty percent of the cases) because complainants are permitted to select the service provider.

There were also important developments this year in area of trade dress law. The Court in *TrafFix Devices, Inc. v. Marketing Displays, Inc.*[10] further refined the rule for functionality, holding that a product feature is functional when it is either essential to the use or purpose, or affects the cost or quality, of the product. Further, there is a presumption of functionality when the product feature was the subject of an expired utility patent, and the patent owner bears the burden of showing the product feature is arbitrary, incidental or ornamental.

D. Trade Secret

This year's trade secret Notes illustrate a geographical split in courts' struggle to find the proper balance between protecting confidential, proprietary information and encouraging employee mobility. In *Globespan, Inc. v. O'Neill*[11] the Central District of California, following federal district court precedent, held that the doctrine of inevitable disclosure violates section 16600 of the California Business and Professions Code which strongly protects worker mobility as a mater of public policy. In *Bernier v.*

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9. ICANN, Uniform Domain Name Dispute Resolution Policy, *at* http://www.icann.org/udrp-policy.html (Oct. 24, 1999).

10. 121 S.Ct. 1255 (2001).

11. No. CV 01-04350 LGB, 2001 WL 801609 (C.D. Cal. Jul. 12, 2001).

Merrill Air Engineers,[12] a Maine appellate court held that information which does not qualify for trade secret protection can be protected by a nondisclosure agreement.

II. ANTITRUST

This year saw several important developments in antitrust law, most notably, the D.C. Circuit's decision in *United States v. Microsoft*.[13] The circuit court upheld the district court's finding of Microsoft's liability under Section 2 of the Sherman Act, while overturning both the breakup remedy and tying liability, remanding both for reconsideration. Microsoft's real victories may have come later, first when the Department of Justice announced that it would drop the tying charge and no longer pursue the breakup of the company, and second in the settlement agreement. In addition to the federal antitrust litigation, Microsoft faces many individual consumer suits under the Clayton Act. In *In re Microsoft Antitrust Litigation*, U.S. District Court for the District of Maryland dismissed thirty-eight private antitrust lawsuits filed against Microsoft.

In addition to monopolization actions against Microsoft, the *Annual Review* includes a Note on collusive settlements under the Hatch-Waxman Act. The Act rewarded research-based drug development with extra patent protection and also modified parts of the regulatory approval process for generic drugs. Although the Act has largely met the goal of stimulating new drug development and increasing the availability of generics, provisions of the Act may have also unwittingly created perverse incentives for anticompetitive activity. Several recent agreements between brand-name and generic companies have attracted significant antitrust attention.

III. CYBERLAW

The rise of the Internet has had significant impact on several different areas of the law. The importance of developments in this area has led to the inclusion of a separate cyberlaw section of the *Annual Review*.

Jurisdiction over the Internet is a continually developing area of law. Courts are stuggling to find a way to apply traditional jurisdictional rules to the Internet. In *Pavlovich v. Superior Court of Santa Clara County*,[14] the California Court of Appeal held that the defendant's actions outside of

12. 770 A.2d 97 (Me. 2001).
13. 253 F. 3d 34 (D.C. Cir. 2001).
14. 109 Cal. Rptr. 2d 909, 911 (Ct. App. 2001), *hearing granted*, No. S100809 (Cal. Dec. 12, 2001).

California, which caused harm within the state, were sufficient for the exercise of jurisdiction by California courts. In *Yahoo!Inc. v. LICRA*,[15] the district court held that it had personal jurisdiction over the French defendants, using the Ninth Circuit's three-part test for determining whether a court may exercise specific jurisdiction. The court also ordered the plaintiff to comply with the orders of the French court.

Regulating conduct over the Internet has also become an increasingly important area of the law. This year's *Annual Review* includes Notes that analyze three different areas of regulation over the Internet, including state Internet regulation, Internet Service Provider immunity under the Communications Decency Act, and the trespass to chattels on the Internet. The first Note focuses on the constitutionality of state Internet regulation in light of the dormant Commerce Clause. The second Note analyzes section 230 of the Communications Decency Act, which provides for Internet Service Provider immunity for obscene materials posted on the Internet. Finally, one Note discusses the innovative use of the common law trespass to chattels cause of action in Internet cases.

IV. CONSTITUTIONAL LAW

In *Barnicki v. Vopper*,[16] the Supreme Court held that anti-wiretapping statutes violate the First Amendment by prohibiting disclosures of intercepted information, especially when that information is of significant public concern. *Bartnicki* is one of several recent cases questioning the constitutionality of prohibitions against publishing illegally acquired information. *Bartnicki* clearly demonstrates the tension that occurs when lawmakers, attempting to deal with new technology, create laws that conflict with constitutional provisions. *Bartnicki* is just one case in what will likely be a long line of cases that address the impact of technology on constitutional law.

V. BUSINESS LAW

The Internet has also had significant impact on commercial law. One of this year's Notes focuses on the evolution of case law surrounding the enforceability of online license agreements. Notably, the presentation of online licenses varies, as does the amount of notice they provide consumers. Some vendors automatically splash their license on the screen and require consumers to click an "I agree" icon; others merely create a link to

15. 169 F. Supp. 2d 1181 (N.D. Cal. Nov. 7, 2001).
16. 53 U.S. 514 (2001).

their license and do not require acceptance. Courts have begun to utilize two broadly defined categories—clickwrap and browsewrap—in order to help characterize the various methods of presentation. Courts have considered these methods of online presentation, holding some licenses binding on consumers and others not.

With the growing importance and prevalence of the Internet, there is increased awareness of potential threats to privacy. In response to privacy concerns, Congress passed the Gramm-Leach-Bliley Act,[17] also known as the Financial Services Modernization Act of 1999, which included provisions for protection of consumers' financial data. One of this year's Notes analyzes these privacy protections in detail and considers whether the Act's provisions for protection of private financial information are sufficient safeguards against threats to privacy.

VI. ENTERTAINMENT LAW

This year's case Notes reflect the courts efforts to balance the right of publicity with the First Amendment. The Ninth Circuit, in *Hoffman v. Capital Cities/ABC, Inc.*,[18] overturned the district court and found that the defendant's publication of a photograph of Dustin Hoffman's head on another person's body was protected by the First Amendment. Because the commercial aspects of the photograph were entwined with the expressive elements and could not be separated, the photograph was protected as a whole.

In *Comedy III Productions v. Saderup*,[19] the California Supreme Court imported the "fair use" element from copyright law to resolve the conflict between Comedy III Productions' right of publicity in all items bearing an image of The Three Stooges, and Saderup's First Amendment right of expression in the his lithographs and shirts bearing the image of The Three Stooges. In applying the fair use factor, the court determined that Saderup's work had no significant transformative element because it did not satirically comment upon society and held that Saderup's works were not protected as a fair use.

17. Pub. L. 106-102, 113 Stat. 1338 (codified as amended in scattered sections of 12 U.S.C. and 15 U.S.C.) (2001).

18. 255 F.3d 1180 (2001).

19. 25 Cal. 4th 387 (2001).

VII. FOREIGN & INTERNATIONAL LAW

This year's *Annual Review* analyzes the first wave of cases to be decided under the European Community Database Directive ("E.C. Directive"), which creates a *sui generis* right to protect databases from unauthorized uses and protects data base structures. Courts in member states are forming different tests for determining what constitutes a substantive investment in the making of a creative database, and are defining the scope of protection afforded under the E.C. Directive differently. Further, the E.C. Directive's reciprocity agreement requires the United States to adopt similar legislation for United States databases to receive equal protection under the E.C. Directive in member states, however, such legislation is not likely to survive strict scrutiny under the United States Constitution.

This year's *Annual Review* also evaluates the United States' response to the World Trade Organization panel report which found that Section 110(5) of the United States Copyright Act violates Article 13 of the Trade-Related Aspects of Intellectual Property Rights ("TRIPS") and Articles 11 and 11*bis* of the Berne Convention for the Protection for the Protection of Literary and Artistic Works ("Berne Convention") in light of China's recent admission to the World Trade Organization. By agreeing to change its law without exception, the United States gave up a critical opportunity to find a mutually satisfactory solution with other offending nations.

The rapid pace of developments at the intersection of technology and law will likely continue in coming years. The *Berkeley Technology Law Journal* and the Berkeley Center for Law & Technology remain committed to providing this reliable, up-to-date resource for lawyers, judges, policymakers, and the academic community interested in following this fast-moving field of law now and in years to come.

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INTELLECTUAL PROPERTY

NEW YORK TIMES CO. V. TASINI

By Amir A. Naini

During the 1980s and 1990s, the advance and widespread availability of information technology enabled many novel forms of communication and commerce.[1] As a result, a new market developed for the electronic distribution of articles previously published only in paper issues of magazines and newspapers.[2] Publishers rushed to take advantage of this market, partnering with database providers to generate vast, comprehensive electronic article databases.[3] The databases became indispensable research resources for a wide range of scholarly disciplines.[4] Soon, freelance authors who had authored many of the articles sought a share of the proceeds from the new revenue source.[5] However, publishers argued that they were merely distributing their magazines and newspapers in a new medium, and therefore owed the authors nothing.[6]

The Supreme Court's decision in *New York Times Co. v. Tasini*[7] determines the rights of collective works publishers and freelance authors in electronic databases. This Note contends that there remains room within the Court's strict interpretation of the Copyright Act for some limited types of electronic distribution of collective works without prior permission from authors. It also describes the proper analytical framework based on the Court's decision and offers examples of compliant databases. In addition, even if the electronic distribution of collective works is not fea-

1. *See generally* NICHOLAS NEGROPONTE, BEING DIGITAL (1995) (recounting the history of media technologies).

2. *See, e.g., About LexisNexis: Premium, Branded Information Products and Portals, at* http://www.lexisnexis.com/about/default.shtml (last visited Feb. 10, 2002) (describing the launch of the Nexis service in 1979 to provide news and business information).

3. *See, e.g., id.* (LexisNexis "provid[es] access to thousands of worldwide newspapers, magazines, trade journals, [and] industry newsletters. . . .").

4. *See* Brief of Amici Curiae Ken Burns et al. at 5, N.Y. Times Co. v. Tasini, 121 S. Ct. 2381 (2001) (No. 00-201), *available at* http://www.nwu.org/tvt/sc-burns.pdf (last visited Feb. 10, 2002) ("For historians, researchers, scholars and students in countless disciplines, the comprehensive, searchable, full-text journal, periodical and newspaper database has become an irreplaceable and priceless resource.").

5. *See* Deirdre Carmody, *Writers Fight for Electronic Rights*, N.Y. TIMES, Nov. 7, 1994, at B20.

6. *See id.*

7. 121 S. Ct. 2381 (2001).

sible, this Note argues that the consequences for historical database completeness and usefulness are not dire, and may be mitigated by retaining full-text search capabilities for the affected articles.

I. BACKGROUND

American copyright law seeks to promote the creation of original works by granting authors certain exclusive rights.[8] While these exclusive rights may lead to financial gains for authors, the fundamental purpose of copyright law is not protecting these gains, but rather promoting broad public availability of creative works.[9] Reflecting the balance between its means and purpose, copyright law fosters availability by rewarding creative efforts with strong rights which enable authors to control their works only for limited times.[10]

Another sort of balancing occurs in the case of collective works, such as magazines and newspapers. In these works, there are a number of competing copyright interests which must be distinguished and reconciled. Collective works are assemblies of numerous individual works.[11] These individual works are each subject to copyright.[12] The unique selection and arrangement of the underlying works makes the collective work itself copyrightable, but the copyright in the collective work extends only to the material and creative elements contributed by the publisher, and is separate and distinct from any copyrights in the underlying works.[13]

The employment relationship between a publisher and an author determines the default distribution of copyright interests between them. If an employee of a collective works publisher produces an individual work, the publisher is considered the author of the individual work for copyright

8. U.S. CONST. art. I, § 8, cl. 8 (granting Congress the power "[t]o promote the Progress of . . . useful Arts, by securing for limited Times to Authors . . . the exclusive Right to their . . . Writings . . . ."); 17 U.S.C. § 106 (1994) (granting copyright owners exclusive rights to copying, preparation of derivative works, distribution, and public performance or display).

9. *See, e.g.*, Twentieth Century Music Corp. v. Aiken, 422 U.S. 151, 156 (1975) ("Creative work is to be encouraged and rewarded, but private motivation must ultimately serve the cause of promoting broad public availability of literature, music, and the other arts.").

10. *See, e.g.*, *id.*

11. 17 U.S.C. § 101 (1994) (defining "collective work" and the related term "compilation").

12. *Id.* § 102(a).

13. *Id.* § 103(a)-(b).

purposes.[14] In contrast, if the publisher contracts with a freelance author for the production of a work, the freelance author retains the copyright in the individual work.[15] The parties may modify the default distribution of rights by contract, but only if they adhere to strict statutory requirements for a signed transfer of the copyright or a written agreement that the work is for hire.[16]

Section 201(c) of the Copyright Act codifies the various rights in collective works:

> Copyright in each separate contribution to a collective work is distinct from copyright in the collective work as a whole, and vests initially in the author of the contribution. In the absence of an express transfer of the copyright or of any rights under it, the owner of copyright in the collective work is presumed to have acquired only the privilege of reproducing and distributing the contribution as part of that particular collective work, any revision of that collective work, and any later collective work of the same series.[17]

Thus, section 201(c) stresses the rights of authors, while also providing an exclusive list of three limited privileges under which publishers may reproduce and distribute individual works as parts of the collective work and other closely related collective works.

II. CASE SUMMARY

A. Factual Background

Jonathan Tasini and five other authors published articles in The New York Times, Newsday, and Sports Illustrated between 1990 and 1993.[18] The authors worked as freelancers, or independent contractors, per oral agreements with the publishers of these periodicals.[19] In no instance did

14. *Id.* § 101 (defining "work made for hire"); *id.* § 201(b) (providing that employer is considered author of the work in the case of a work for hire).

15. *Id.* § 201(a) ("Copyright in a work . . . vests initially in the author or authors of the work.").

16. *Id.* § 204(a) ("A transfer of copyright ownership, other than by operation of law, is not valid unless . . . [it] is in writing and signed by the author. . . ."); *id.* § 101 ("A 'work made for hire' is . . . a work specially ordered or commissioned for use as a contribution to a collective work . . . if the parties expressly agree in a written instrument signed by them that the work shall be considered a work made for hire.").

17. *Id.* § 201(c).

18. N.Y. Times Co. v. Tasini, 121 S. Ct. 2381, 2385 (2001).

19. *Id.*

any of the contracts include terms regarding placement of articles in electronic databases.[20]

At the time of publication, the publishers had licensing agreements with LEXIS/NEXIS, a database owner and provider.[21] Pursuant to these agreements, the publishers regularly provided LEXIS/NEXIS with all of the published articles in a computerized text-only format[22] for inclusion in LEXIS/NEXIS databases.[23] The articles contained codes or tags to ease computerized indexing; these tags included the print publication's name, publication date, section, initial page number, headline or title, and author name.[24] Database users could search the text of the article or any of these tags, and retrieve articles which matched the search terms.[25] No other information that accompanied the articles in the original collective work, such as pictures, advertisements, headline size, or page placement, was transmitted to LEXIS/NEXIS.[26] Consequently, such information was unavailable to the user upon article retrieval from the database.[27]

The New York Times also had licensing agreements with University Microfilms International for the inclusion of Times articles in two CD-ROM products, the New York Times OnDisc ("NYTO") and General Periodicals OnDisc ("GPO").[28] The NYTO contained the full texts of Times articles.[29] LEXIS/NEXIS provided the computer text files to University Microfilms, so the NYTO and LEXIS/NEXIS articles were identically formatted.[30] GPO differed from the other database products by providing image facsimiles of the pages where articles originally appeared, rather than computer text only.[31] Users could search and retrieve articles from both the NYTO and GPO in a similar manner to LEXIS/NEXIS.[32]

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20. *Id.*
21. *Id.*
22. The format used was American Standard Code for Information Interchange ("ASCII"), which assigns a unique numerical code for each alphanumeric character and other common characters such as punctuation. *See id.* at 2397 n.7 (Stevens, J., dissenting).
23. *Id.* at 2385.
24. *Id.*
25. *Id.*
26. *Id.*
27. *Id.*
28. *Id.* at 2385-86.
29. *Id.* at 2386.
30. *Id.*
31. *Id.*
32. *Id.*

B. District Court and Second Circuit Decisions

The authors sued the publishers and database providers, alleging copyright infringement when their articles were placed in the electronic databases.[33] The publishers and database providers responded by arguing that the revision privilege for collective works under the Copyright Act permitted reproduction of the articles in electronic databases.[34] Both sides moved for summary judgment.[35]

The District Court for the Southern District of New York granted summary judgment for the publishers and database providers.[36] The court first determined that a privilege conferred by section 201(c) was transferable from the publishers to the database providers.[37] Then, the court determined that the articles in the databases qualified as "revisions" under section 201(c) because they preserved significant aspects of the original collective work.[38]

The authors appealed, and the Court of Appeals for the Second Circuit reversed and remanded with instructions to enter summary judgment for the authors.[39] The Second Circuit noted that section 201(c) does not permit the publisher to sell individual articles even if all other articles from a particular collective work are also offered for sale.[40] The court reasoned that section 201(c) does not allow the publisher to circumvent this restriction by selling individual articles using an electronic database which happens to also contain the other articles from the original collective work.[41] Hence, the databases could not be considered revisions of the original periodicals.[42] Since the court concluded that the databases were not revisions of the original collective works, it declined to decide the question of whether a section 201(c) revision privilege was transferable.[43] The publishers and database owners appealed, and the United States Supreme Court granted certiorari.[44]

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33. Tasini v. N.Y. Times Co., 972 F. Supp. 804, 806 (S.D.N.Y. 1997).
34. *See id.*; *see also* 17 U.S.C. § 201(c) (1994).
35. *Tasini*, 972 F. Supp. at 806.
36. *Id.*
37. *Id.* at 816.
38. *Id.* at 821.
39. Tasini v. N.Y. Times Co., 206 F.3d 161, 166 (2d Cir. 2000).
40. *Id.* at 168.
41. *Id.*
42. *Id.* at 167-70.
43. *Id.* at 165 & n.2.
44. 531 U.S. 978 (2000).

C. The Supreme Court Decision

1. The Majority

In a seven-to-two decision, the Supreme Court agreed with the Second Circuit that the section 201(c) revision privilege did not cover the databases and affirmed summary judgment for the authors.[45] Writing for the majority, Justice Ginsburg began the analysis by noting that the Copyright Act was amended in 1976 specifically to reduce the superior bargaining power of publishers over authors.[46] Prior to the 1976 amendment, a freelance author's copyright in an article published in a collective work was recognized only when printed with a copyright notice in the author's name.[47] Publishers could exert their power by omitting such notices, thereby jeopardizing the author's copyright in the article.[48] The 1976 amendment recast copyright as a bundle of discrete rights rather than an indivisible right, and made it possible for authors to assign some rights, such as the right to publish in a collective work, without relinquishing their remaining rights.[49]

The Court then read section 201(c) in light of the importance of freelance authors' rights, and emphasized that the three privileges are circumscribed by the limiting word "only."[50] Quoting the legislative history of the Copyright Act amendment, the Court noted that the drafters of section 201(c) envisioned limited scenarios in which publishers could reproduce or distribute freelance authors' articles as parts of other collective works.[51] In particular, the drafters anticipated the inclusion of articles from outdated encyclopedias in new, revised editions, or the republication of specific articles from old magazine issues in subsequent issues.[52] According to the Court, the drafters did not intend section 201(c) to grant more expansive distribution and reproduction rights to publishers.[53] Thus, in the absence of a transfer of the copyright in the individual article from the freelance author to the publisher, section 201(c) acts as a default rule and, "if there is demand for a freelance article standing alone or in a new col-

45. N.Y. Times Co. v. Tasini, 121 S. Ct. 2381, 2387 (2001).
46. *Id.* at 2388.
47. *Id.*
48. *Id.*
49. *Id.* at 2388-89.
50. *Id.* at 2389.
51. *Id.*
52. *Id.*
53. *Id.*

lection, the Copyright Act allows the freelancer to benefit from that demand."[54]

Turning to the facts of the case, the Court noted that the publishers relied solely on the section 201(c) privilege to reproduce or distribute revisions of collective works.[55] In evaluating the publisher's revision defense, the Court explained that the proper perspective was that of the database user.[56] Thus, the proper question was whether the electronic works as perceived by the user fell within the revision privilege.[57]

The Court then analyzed the databases from the user's perspective.[58] The section 201(c) revision privilege could not cover the databases, because they presented articles without the context of the original collective works.[59] In the text-based LEXIS/NEXIS and NYTO databases, the missing contextual features included the graphics, formatting and other articles from the original publication.[60] The GPO database also failed to qualify as a revision, even though the user was presented with the entire pages on which an article originally appeared, because the user could not flip to other pages of the same periodical issue without conducting a new search for articles which happened to appear on those other pages.[61] The tags identifying each article's origins merely indicated that the article was previously part of a particular collective work, not that the database distributed the original collective work.[62] Since none of the databases qualified as a revision, the Court declined to decide whether a section 201(c) privilege was transferable.[63]

2. *The Dissent*

In his dissenting opinion, Justice Stevens began the analysis in a similar fashion to the majority, but quoted different sections of the legislative history to emphasize that Congress' goal in enacting section 201(c) was "to keep publishers from 'revising the contribution itself or including it in a new anthology or an *entirely different magazine or other collective*

54. *Id.*
55. *Id.* at 2390.
56. *Id.*
57. *Id.*
58. *Id.*
59. *Id.* at 2390-91.
60. *Id.* at 2391.
61. *Id.* at 2391-92.
62. *Id.* at 2391.
63. *Id.* at 2387 & n.5.

work.'"[64] Thus, Stevens argued, Congress envisioned section 201(c) as providing freelance authors with rights over any changes to the contributed article or attempts to publish the article as part of a new and different selection of articles, but not over repackaging the collective work in a new medium.[65]

Stevens separated the analysis of whether the databases were revisions into two questions: (1) whether the databases were revisions within the meaning of section 201(c); and (2) whether the aggregation of the electronic versions of the collective works altered the revision analysis.[66] In answering the first question, Stevens took an "incremental approach" and examined the process by which the publishers transmitted articles to database providers.[67] Because the articles from single issues of the periodicals were transmitted in a batch of files consisting of articles from only that issue, Stevens concluded that the electronic articles were proper section 201(c) revisions of the original printed works.[68] Stevens stressed that the principle of media neutrality—whereby the transfer of copyrighted material between different media does not alter the character of that material for copyright purposes—weighed in favor of the publishers and database providers, because the electronic medium itself necessitated many of the differences which the majority felt distinguished the databases from proper revisions.[69]

In answering the second question, Stevens pointed out that aggregating revisions of collective works in large electronic databases cannot be distinguished from aggregating periodicals in a library or bookstore, an activity which does not constitute copyright infringement.[70] Stevens also noted that microfilm reproductions may contain multiple issues of a periodical, or issues from different periodicals.[71] Therefore, aggregation of works in large databases did not alter Stevens' analysis.[72] Finally, Stevens argued that the majority's focus on the database user's experience was misplaced, and that media-specific necessities drove the details of database design

64. *Id.* at 2395-96 (emphasis in original) (quoting H.R. REP. NO. 94-1476, at 122-23 (1976), *reprinted in* 1976 U.S.C.C.A.N. 5738).

65. *Id.*

66. *Id.* at 2394.

67. *Id.* at 2397.

68. *Id.*

69. *Id.* at 2397-98.

70. *Id.* at 2400.

71. *Id.*

72. *Id.*

and function which the majority mistakenly characterized as distribution of articles standing alone.[73]

III. DISCUSSION

The following analyzes *Tasini*'s analytical framework, and explores how the decision may affect developments in the electronic publishing industry.[74] Part III.A.1 evaluates the majority's statutory interpretation and focus on the user's perspective, and concludes that the Court correctly applied the relevant portions of the Copyright Act. Part III.A.2 discusses the potential legal effect of electronic databases' software components. The *Tasini* Court did not directly address this issue, but its focus on the user's perspective suggests that hidden software components will not factor into the analysis of electronic database cases. Part III.A.3 then examines how the focus on the user's perspective informs the prediction of what constitutes a proper electronic revision. It argues that while the Court's decision provides unclear guidance regarding some database navigational features, it also sets forth strict requirements that will limit publishers to facsimile reproductions of collective works. Finally, Part III.B discusses the aftermath of the litigation, and describes how search capabilities may be retained as a partial solution to the problem of database incompleteness.

A. The Contours of Liability in Electronic Database Copyright Cases

1. User's Perspective and Context

By approaching its section 201(c) analysis from the viewpoint of the database user, the Court chose the correct perspective based on the statutory law. As the Court noted, section 102 of the Copyright Act grants copyright protection only for works "fixed in any medium 'from which

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73. *Id.*

74. Some issues relevant to a full predictive analysis are beyond the scope of this Note. First, whether a section 201(c) privilege is transferable remains undecided. *See id.* at 2387 & n.5. For an argument that a section 201(c) is not transferable, see Josh J. May, Note, Tasini v. New York Times Co., 16 BERKELEY TECH. L.J. 13, 24-26 (2000). Second, the Register of Copyrights argued, in a letter sent to a Congressman that was subsequently published in the Congressional Record, that electronic databases display articles within the meaning of section 106(5) of the Copyright Act. *See Experts Weigh* Tasini *Ruling's Impact On Freelancers and Electronic Publishing*, PAT., TRADEMARK & COPYRIGHT J., October 19, 2001, at 557. Since section 201(c) does not contain a privilege for displaying copyrighted works, the Register argued that the database infringed the freelance authors' copyrights. *Id.* The Court acknowledged the Register's argument, but did not need to reach this issue in its opinion. *Tasini*, 121 S. Ct. at 2390 n.8.

they can be perceived, reproduced, or otherwise communicated.'"[75] Copyright does not protect potential expressions; it only protects the perceptible, fixed expressions themselves.[76] The statutory definition of "fixed" is quite broad, allowing fixation in any form so long as it is stable, and making provision for later developed technologies.[77] However, it would go beyond the bounds of the fixation requirement to construe potential or hypothetical outputs of the databases in *Tasini* as being fixed and perceptible.[78] Rather, the databases merely serve as the hidden storehouses of articles while the fixed, perceptible expressions are the articles as actually presented to database users.

Standing at the center of the factual analysis and driving the ultimate result, the Court's focus on the user's perspective is perhaps the most informative aspect of its opinion. With this focus, the Court discounted the intermediate step of database production in which the print publisher sends a batch of text files of an issue's articles to the database provider.[79] The dissent argued that the text files constitute a proper electronic revision.[80] Yet, a user never views this batch of files corresponding to a single periodical issue, but rather interacts with the database through search interfaces.[81] The search may range from a simple one for author name, title, or publication date, to a potentially complex Boolean search of many terms.[82] Regardless of the details of the search, the user is presented with a result-

75. *Tasini*, 121 S. Ct. at 2390 (quoting 17 U.S.C. § 102(a) (1994)). The Court also cited the definitions of "copies" and "fixed" from section 101, both of which repeat the quoted language of section 102 regarding perception of the work. *Id.* (citing 17 U.S.C. § 101 (1994)).

76. 17 U.S.C. § 102(a)-(b) (1994).

77. *Id.* § 101. The legislative history of the Copyright Act confirms that Congress intended a broad definition for "fixed," partly to overrule White-Smith Music Publ'g Co. v. Apollo Co., 209 U.S. 1 (1908), in which the Court held perforated paper rolls uncopyrightable as musical compositions because humans could not perceive them as music. H.R. REP. NO. 94-1476, at 52 (1976), *reprinted in* 1976 U.S.C.C.A.N. 5665.

78. *See* Alice Haemmerli, *Commentary:* Tasini v. New York Times Co., 22 COLUM.-VLA J.L. & ARTS 129, 142-43 (1998) (arguing that it is improper in a section 201(c) analysis to consider database structure or potential output, because copyright law has historically focused on perceptible presentations of works).

79. *Tasini*, 121 S. Ct. at 2391 n.9.

80. *Id.* at 2397 (Stevens, J., dissenting).

81. *Id.* at 2391.

82. A Boolean search relates search terms to one another with logical operators. *See* GERALD KOWALSKI, INFORMATION RETRIEVAL SYSTEMS: THEORY AND IMPLEMENTATION 27-28 (1997). For example, a search using two terms connected with a Boolean AND operator will return only articles containing both of the search terms. Other Boolean operators include OR and NOT. A user may combine many Boolean operators and search terms to achieve highly refined searches. *Id.*

ing list of articles which typically span many issues or publications.[83] The list of articles does not itself constitute infringement, since it simply consists of information identifying matching articles and not the texts of the articles themselves.[84] However, the list of articles enables the next step in the user experience—retrieval of individual articles—which does constitute infringement.[85]

The Court's strict requirements for the necessary level of context properly protect freelance authors' rights in their individual articles. The context requirement serves as a sound dividing line between proper and improper electronic revisions by differentiating the presentation of entire collective works from the presentation of parts of them. Under the Court's reasoning, the text-only databases present an easy case of improper revision, because they lack even minimal context such as surrounding graphics. The Court also correctly held that the image-based GPO database was an improper revision, even though entire pages are presented in original format, because the original collective work consists of more than just the particular pages where an individual article appears. As the dissent pointed out, how much context is enough remains an open question.[86] However, under the Court's reasoning, if an image-based database were to allow the user to go directly to adjoining pages, and to view the entire collective work without conducting a new search, it should be found a proper section 201(c)-privileged work.

2. *Software Components*

All database products require at least a minimal software component to allow user interaction and viewing of the database contents.[87] Since software is itself subject to copyright protection, the addition of new software components to collective works in electronic databases raises a critical question: do these new components automatically sweep all electronic collective works databases into the infringing category? Most criticisms of the *Tasini* district court opinion have focused on that court's interpretation of section 201(c).[88] At least one commentator, however, has raised the

83. *Tasini*, 121 S. Ct. at 2391.

84. *See* discussion *infra* Part III.B.

85. *Tasini*, 121 S. Ct. at 2386.

86. *Id.* at 2397 (Stevens, J., dissenting); *see* discussion *infra* Part III.A.3.

87. *See* Rod Dixon, *Profits in Cyberspace: Should Newspaper and Magazine Publishers Pay Freelance Writers for Digital Content?*, 4 MICH. TELECOMM. TECH. L. REV. 127, 143 (1998), *available at* http://www.mttlr.org/volfour/dixon.pdf.

88. *See, e.g.*, Wendy J. Gordon, *Fine-Tuning* Tasini*: Privileges of Electronic Distribution and Reproduction*, 66 BROOKLYN L. REV. 473, 484-85 (2000) (arguing that the Second Circuit correctly reversed the district court based on a narrower interpretation of

software component issue by arguing that the court wrongly ruled in favor of the publishers because it failed to take account of these additional database components in its copyright analysis.[89]

Additionally, several months prior to the Supreme Court's decision in *Tasini*, the Eleventh Circuit issued an opinion in *Greenberg v. National Geographic Society*,[90] in which it considered the legal effect of a database's software component. In that case, the National Geographic Society produced and sold a CD-ROM set of every printed issue of its magazine from 1888 to 1996.[91] The magazine issues contained numerous photographs from freelance photographers.[92] The CD-ROM product included digital replica images of the magazine issues and a computer program that served as a retrieval system for the images.[93] In dismissing an analogy between the CD-ROM-based database product and microfilm, the court pointedly noted that the combination of a collective work and a new copyrightable element such as software would "present an additional dimension in copyright analysis."[94] The Eleventh Circuit declined to decide the issue however, because the presence of other non-software components in the case was enough to render the database a new collective work which infringed the freelancers' copyrights.[95]

Mention of the software component issue is notably absent from the majority and dissenting opinions in *Tasini*. It is unclear whether the Supreme Court may have considered the argument, since the parties did not raise it.[96] However, the Court noted the two other relevant issues which it

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section 201(c)); John D. Shuff and Geoffrey T. Holtz, *Copyright Tensions in a Digital Age*, 34 AKRON L. REV. 555, 560-62 (2001) (same); Yuri Hur, Note, Tasini v. New York Times: *Ownership of Electronic Copyrights Rightfully Returned to Authors*, 21 LOY. L.A. ENT. L.J. 65, 89-90 (2000) (same); Josh J. May, *supra* note 74, at 21-24 (same).

89. Dixon, *supra* note 87, at 142-45.

90. 244 F.3d 1267 (11th Cir. 2001).

91. *Id.* at 1269.

92. *Id.*

93. *Id.*

94. *Id.* at 1273 n.12.

95. *Id.*

96. Nevertheless, the Court may have encountered the software component argument through both commentary and citation to *Greenberg*. *See supra* text accompanying note 89; Brief for Petitioners at 46, N.Y. Times. Co. v. Tasini, 121 S. Ct. 2381 (2001) (No. 00-201) (citing Greenberg v. Nat'l Geog. Soc'y, 1999 U.S. Dist. LEXIS 13874 (S.D. Fla. 1999), *rev'd*, Greenberg v. Nat'l Geog. Soc'y, 244 F.3d 1267 (11th Cir 2001), *cert. denied*, 122 S. Ct. 347 (2001)), *available at* http://www.nwu.org/tvt/sc-nyt.pdf (last visited Feb. 10, 2002).

did not decide,[97] suggesting that the failure to mention the software component issue means it is comparatively less important to a section 201(c) analysis.

In combination with the Court's focus on the user's perspective, the absence of any mention of the software components suggests that this "additional dimension" may not factor into the analysis of electronic collective works cases. This flows from the focus on the user's perspective, because the critical question in that analytical framework is not whether there are hidden copyrightable additions to the collective work, but whether normal use of the database involves the presentation of individual works. Nevertheless, the Court's silence means that this critical issue remains unresolved.

3. *Predicted Infringing and Noninfringing Databases*

Strict adherence to *Tasini*'s exacting standards will be required for any future attempts to design compliant databases. The publishers argued that the concept of media neutrality excused the differences between the original collective works and the database products.[98] Underlying this argument, as the dissent discussed at length, is the sense that limitations of computer storage and information processing capacities necessitate database features such as the delivery of individual articles rather than full collective works.[99] The Court rejected this argument, suggesting that database design was driven more by market demand for individual articles than any limitations of computer technology.[100] Clearly, after *Tasini*, courts will not be sympathetic to arguments based on technical limitations.

The Court's analysis makes it difficult to imagine any text-only product which would escape infringement, because the computer text format makes no provision for nontextual features such as page formatting or im-

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97. The other issues are transferability of a section 201(c) privilege and whether electronic databases infringe by displaying articles within the meaning of section 106. *See supra* note 74.

98. N.Y. Times Co. v. Tasini, 121 S. Ct. 2381, 2392 (2001); *see* case summary *supra* Part II.C.2.

99. *Tasini*, 121 S. Ct. at 2398 n.9 (Stevens, J., dissenting) (noting that, in the case of GPO, "the demands that memory-intensive graphics files can place on underpowered computers make it appropriate for electronic publishers to divide the larger collective work into manageably sized subfiles.").

100. *Id.* at 2392 n.11 ("We lack the dissent's confidence that the current form of the Databases is entirely attributable to the nature of the electronic media, rather than the nature of the economic market served by the Databases.").

ages.[101] The text format is technically attractive because of its minimal use of computer resources and the ease with which text documents can be electronically manipulated. For example, computer search functions invariably use the text format to scan for matching words in documents.[102] However, the same features which make computer text technically attractive also leave no simple way to encode all of the contextual features of the original work that the Court deems essential to a noninfringing database.[103] Even the dissent's example of a text file of an entire issue's articles would infringe because it would lack the original arrangement of the articles and accompanying pictures.[104] Consequently, publishers should avoid text-only solutions despite their technical advantages.

Noninfringing product designs will most likely be image-based solutions, similar to the GPO database, which present facsimiles of the original publication. As the Court noted, the GPO product allows the user to view the entire pages on which the selected articles appear; what is lacking is the ability to easily view adjoining pages and other pages of the collective work.[105] A noninfringing product must provide the user with the navigational flexibility to move to any of the collective work's pages, and must present the entire original collective work.

Of course, readers of print publications are not limited to paging through the publications sequentially, so electronic databases will most likely be allowed to provide users with the ability to jump to specific pages. A more difficult question is whether navigational aids which help, but do not force, the user to follow an article through nonconsecutive pages would satisfy the Court's context requirements. Publishers could

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101. The standard text encoding scheme, ASCII, simply assigns the numbers zero to 127 to alphanumeric and punctuation characters. *See supra* note 22.

102. *See* KOWALSKI, *supra* note 82, at 2 ("[T]ext . . . has been the only data type that [has] lent itself to full functional processing.").

103. Page formatting and images must be encoded, if at all, by extending the code with mark-up commands. The Hypertext Markup Language ("HTML") is one widely used standard on the Internet, and is recognized by Internet browser programs such as Netscape Communicator or Microsoft Internet Explorer. *See HyperText Markup Language Home Page, at* http://www.w3.org/MarkUp (last visited Feb. 10, 2002). Mark-up commands exist in text format in the document file, but the browser programs interpret them and alter the display of the document accordingly. While HTML provides for a variety of formatting features, its designers did not envision using it to produce electronic facsimiles of print publications. Consequently, the appearance of an HTML-encoded document will vary, sometimes drastically, with the particular browser software and user-controlled settings. HTML is therefore unlikely to enable compliance with all of *Tasini*'s requirements.

104. *Tasini*, 121 S. Ct. at 2399 (Stevens, J., dissenting).

105. *Id.* at 2391-92.

provide such a navigational capability by allowing unrestricted browsing through the collective work page by page, but also providing an option to skip directly to the next page containing the continuation of a particular article's text. This skipping feature might be supplied via a button bar, placed to the side of the document window, which both lists and links to all the pages containing portions of the current article. The button bar seems to satisfy the Court's requirements, because the user may still browse through the entire collective work at will. However, the Court could plausibly view the feature as restricting the user experience to a single article. Regardless of the uncertain legality of the multi-function button bar, database designers must at least be careful not to add navigational features which completely restrict the user experience to single articles.

The majority's dismissal of the dissent's media neutrality argument is wise not only because there is "no grounding in § 201(c) for a 'medium-driven' necessity defense,"[106] but also because the state of computer technology is highly dynamic. Storage and processing capacities are expanding at breathtaking speed.[107] What was impractical a short time ago becomes practical as prices drop and technology improves.[108] In addition, creative software solutions sometimes achieve unexpected breakthroughs.[109] In the GPO database, images of the original works were stored as raw image files of each printed page.[110] In this format, the product required vast storage space for each issue.[111] In the years after the design of GPO, market demand for electronic publications has fostered the creation of new electronic formats which use computer storage much more efficiently, while still presenting users with print publication-like facsimi-

106. *Id.* at 2392 n.11.

107. *See* Peter Leyden, *Moore's Law Repealed, Sort Of*, WIRED, May 1997, at 166 (reporting that Intel co-founder Gordon Moore, whose 1965 prediction that processing power would double every eighteen months has held true so far, foresees surmountable challenges and continued advances in the years ahead), *available at* http://www.wired.com/wired/archive//5.05/ff_moore.2_pr.html (last visited Feb. 10, 2002); *The Art of the Quantum Leap*, ECONOMIST, Dec. 8, 2001, at 19 (recounting the technical breakthroughs that led to rapid increases in computer hard disk storage capacities).

108. *See* Ira Sager et al., *The Mother of All Price Wars*, BUSINESS WEEK, July 30, 2001, at 32 (reporting deep price cuts in the personal computer industry).

109. *See infra* notes 112-113 and accompanying text.

110. *Tasini*, 121 S. Ct. at 2386.

111. *Id.* at 2398 n.9 (Stevens, J., dissenting) ("The GPO version of the April 7, 1996, New York Times Magazine, for example, would demand in the neighborhood of 200 megabytes of memory if stored as a single file . . . .").

les.[112] Modern electronic document formats conserve computer resources relative to raw image files through mathematical representation of fonts and graphics, as well as compression of images.[113] These formats may be the ideal compromise between design efficiency and *Tasini*'s stringent requirements.

B. Partial Solution to the Database Incompleteness Problem

In the wake of the Second Circuit's *Tasini* decision in favor of the freelance authors, scholars warned of potentially drastic consequences for the completeness and integrity of electronic archives.[114] The scholars predicted that publishers would remove infringing works from databases rather than embark on the difficult task of finding freelance authors and negotiating for electronic rights.[115] In the scholar's view, the resulting loss would devastate the research community which had come to depend on electronic archives.[116] However, commentators reminded the legal community that collective rights organizations had formed to address the problem of administrative efficiency in other industries such as music, and could address the problems in this case.[117] Such organizations lower the high transaction costs associated with situations involving many different copyright owners by negotiating standard contracting terms and providing a centralized mechanism for licensing and enforcement.[118] Indeed, the Court pointed to the possibility of this type of arrangement in dismissing the "dire predictions" of the publishers, supportive amici curiae, and the dissent.[119]

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112. One example is Adobe Corporation's Portable Document Format ("PDF"), a universal file format which can be viewed using Adobe's free Acrobat Reader software. *See Adobe PDF*, *at* http://www.adobe.com/products/acrobat/adobepdf.html (last visited Feb. 10, 2002). Another example is the public domain compressed image file format JPEG established by the Joint Photographic Experts Group. *See Welcome to JPEG*, *at* http://www.jpeg.org/public/jpeghomepage.htm (last visited Feb. 10, 2002).

113. *See* L. Leurs, *The PDF Format: Compression*, *at* http://users.belgacom.net/prepresspanic/pdf/info/compression.htm (last visited Feb. 10, 2002).

114. *See* Brief of Amici Curiae Ken Burns et al. at 5-14, N.Y. Times Co. v. Tasini, 121 S. Ct. 2381 (2001) (No. 00-201), *available at* http://www.nwu.org/tvt/sc-burns.pdf (last visited Feb. 10, 2002)

115. *See id.*

116. *See id.*

117. *See* May, *supra* note 74, at 26-29; Robert Meitus, Note, *Interpreting the Copyright Act's Section 201(c) Revision Privilege with Respect to Electronic Media*, 52 FED. COMM. L.J. 749, 773-76 (2000).

118. *See generally* Robert P. Merges, *Contracting into Liability Rules: Intellectual Property Rights and Collective Rights Organizations*, 84 CAL. L. REV. 1293 (1996).

119. *Tasini*, 121 S. Ct. at 2393.

Unfortunately, the conduct of the parties after the Supreme Court decision does not bode well for a quick resolution of the issue. Immediately following the ruling, the New York Times removed 115,000 articles from its on-line database, and published advertisements offering to restore the articles if authors waived all past and future claims.[120] The authors responded by running their own advertisements, demonstrating in front of the Times' headquarters, and filing another suit alleging that the Times was forcing authors to sign waivers by threatening to withhold future freelance assignments.[121] Although the Times has required express transfer of electronic rights in freelance contracts since 1995,[122] it may be concerned that the establishment of a collective rights organization would make it difficult to refuse additional compensation for these rights in new contracts. Hence, the dispute over remedies has many dimensions which may lead to a protracted new phase of litigation.

Even in the absence of a resolution which makes the articles at issue available in archival databases, the gap in the record need not be nearly as large or as complete as argued by the scholars and publishers. First, only freelance articles published from 1978 to the early 1990s are affected.[123] Even these freelance articles may be provided if packaged in an electronic version of the entire original collective work that is noninfringing.[124]

Moreover, even if publishers are concerned about attempting to design noninfringing database products given the uncertainty in the Court's opin-

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120. Tamara Loomis, *Aftermath of* Tasini*: Damages at Issue After U.S. Supreme Court Ruling*, N.Y.L.J., July 12, 2001, at 5.

121. *Id.*

122. *Tasini*, 121 S. Ct. at 2402 (Stevens, J., dissenting). Note that authors or their survivors have the inalienable power to terminate transfers of electronic rights between thirty-five and forty years from the execution of the freelance contracts. 17 U.S.C. § 203(a)(3) (1994). Congress retained this provision of earlier copyright law in the 1976 Act partly because of authors' weak bargaining positions "resulting in part from the impossibility of determining a work's value until it has been exploited." H.R. REP. NO. 94-1476, at 124 (1976), *reprinted in* 1976 U.S.C.C.A.N. 5740. Hence, the current dispute may repeat, on a potentially larger scale, in several decades.

123. The Copyright Act went into effect on January 1, 1978. 17 U.S.C. § 301(a) (1994). Most publishers have obtained express transfers of electronic rights from freelance authors since the *Tasini* litigation brought the issue to the fore in the early 1990s. *See* George H. Pike, *Understanding and Surviving* Tasini, INFO. TODAY, Oct. 1, 2001, at 18.

124. It is unclear whether publishers would favor providing electronic versions of entire collective works, since presumably the user would be purchasing the product to read one article, and may be reluctant to pay more than the market rate for one article. However, given the alternative of no revenue, publishers might accept this scenario as the best possible business practice.

ion, the search capabilities of electronic databases may be retained to inform researchers that relevant articles exist.[125] This result follows from the data structure of electronic database systems, which consists of the articles themselves and a file called the inverted file index.[126] The inverted file index is so named because it contains an inversion list of terms, or a list of terms with pointers to each article in which the terms occur.[127] For example, the inverted file index for a database of legal news publications might contain the terms "electronic" and "database." Each of these terms will have pointers to articles that contain that term.[128] When a user executes a Boolean search for articles containing both terms (i.e. searches for articles containing "electronic" AND "database"), the database system compares the terms' pointers in the inverted file index and returns a list of articles that appear under both terms.[129] Inverted file indices may be preserved by database providers even if the article texts are completely expunged, because they exist separately from the articles themselves and contain only author names, titles, publication names, dates, and searchable terms, all of which are not subject to copyright.[130] While this partial solution does not address researchers' efficiency concerns, since electronic versions of articles themselves will not be delivered, it at least ensures that researchers will not remain unaware of relevant articles.

IV. CONCLUSION

The Supreme Court's ruling in *Tasini* reaffirmed the importance of authors' rights in modern American copyright law. In resolving the competing rights of freelance authors and publishers of collective works, the Court initiated a long process of adjustment in the electronic database industry. Although many issues remain undecided even after the decision, the Court's identification of the user's perspective as the proper frame of

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125. *See* Barbara Quint, *Let's Stop the Trash Trucks*, INFO. TODAY, Sept. 1, 2001, at 8 (proposing that inverted file indices may be retained by database providers without risk of copyright infringement, thereby providing searchers with full search results if not full text).

126. *See* KOWALSKI, *supra* note 82, at 76-79.

127. *See id.*

128. *See id.*

129. *See id.*; *see also* Quint, *supra* note 125.

130. *See* 37 C.F.R. § 202.1(a) (2001) ("Words and short phrases such as names, titles, and slogans" are not subject to copyright); Feist Publ'ns v. Rural Tel. Serv., 499 U.S. 340, 344-45 (1991) ("The most fundamental axiom of copyright law is that 'no author may copyright his ideas or the facts he narrates.'") (quoting Harper & Row Publishers, Inc. v. Nation Enters., 471 U.S. 539, 556 (1985)); *see also* Quint, *supra* note 125.

reference enables prediction of the boundaries of infringement in electronic database cases.

Interested parties have debated the issues of *Tasini* in highly polarized terms, but many possible middle paths exist. These moderate and admittedly partial solutions—ranging from the design of noninfringing revisions to retention of database search functions—mitigate the potentially harsh consequences of the ruling.

RANDOM HOUSE V. ROSETTA BOOKS

By Caryn J. Adams

Technological developments in communications media have created new possibilities for the distribution and enjoyment of creative works, but at the same time have produced difficult problems for courts in construing the scope of preexisting contracts and licensing agreements.[1] Courts have traditionally applied recognized principles of contract law where a "new use" has developed long after the original licensing agreements were signed.[2] The results have been mixed, however, as courts have been split over how broadly to interpret old contracts in light of new technological capabilities.[3] *Random House v. Rosetta Books*,[4] which involves the distribution and publication of electronic books ("eBooks") over electronic networks, such as the Internet, is the most recent in this line of cases.

Part I of this Note discusses the technological developments involved in the *Random House* decision. Part II addresses the factual background of the case, the licensing agreements at issue, and the district court's decision. Part III then analyzes the result in *Random House* using both traditional principles of contract interpretation and the reasonableness analysis developed in the new use line of cases and concludes that the decision reached by the District court in *Random House* was arguably inconsistent with precedent in New York and the Second Circuit.

I. BACKGROUND

In many ways, the eBook represents the most significant innovation in publishing technology to emerge since World War II.[5] An eBook is a digi-

1. *See* MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT, § 10.10[B] (2001).
2. *See, e.g.*, Tele-Pac v. Grainger, 570 N.Y.S.2d 521 (N.Y. App. Div. 1991).
3. *See* NIMMER, *supra* note 1, § 10.10[B].
4. 150 F. Supp. 2d 613 (S.D.N.Y. 2001).
5. As early as 1945, authors imagined libraries capable of being accessed and read electronically:

> Consider a future device for individual use, which is a sort of mechanized private file and library .... A memex is a device in which an individual stores all his books, records, and communications, and which is mechanized so that it may be consulted with exceeding speed and flexibility. It is an enlarged intimate supplement to his memory .... Any given book of his library can thus be called up and consulted with

tal book, read on a computer screen or other electronic device, which is created by converting digitized text into a format readable by computer software.[6] Like all digital files, it cannot be accessed and read without an enabling device, such as a personal computer, personal digital assistant, or a hand-held reading appliance.[7]

The eBook is physically different from the traditional printed book.[8] Nevertheless, eBooks and traditional books share certain significant characteristics.[9] The paper book, like the eBook, presents the original text or content in its complete, full-length form.[10] Moreover, eBooks are often

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> far greater facility than if it were taken from a shelf. As he has several projection positions, he can leave one item in position while he calls up another. He can add marginal notes and comments, taking advantage of one possible type of dry photography, and it could even be arranged so that he can do this by a stylus scheme . . . .

Vannevar Bush, *As We May Think*, 176 ATLANTIC MONTHLY 101 (1945), *available at* http://www.theatlantic.com/unbound/flashbks/computer/bushf.htm (last visited Feb. 10, 2002).

6. *Random House*, 150 F. Supp. 2d at 615.

7. The Microsoft Reader with ClearType and the Adobe Acrobat eBook Reader are two examples of enabling devices. *See ReaderWorks: ePublishing tools for Microsoft Reader*, *at* http://www.overdrive.com/readerworks/ppc/ (last visited Feb 10, 2002); *eBook Central*, *at* http://www.adobe.com/epaper/ebooks/ (last visited Feb 10, 2002). The enabling device may sometimes itself be referred to as an eBook. For simplicity's sake, this Note refers to the content as the eBook and the enabling device as the enabling device or "reader."

8. For a good general introduction to eBooks, see Jamie Engle, *Reader's E-Book Primer: What's an E-Book*, *at* http://www.ebookconnections.com/ReadersPrimer/what's_an_e-book.htm (last visited Feb. 10, 2002):

> Electronic books, or e-books, are books in computer file format and read on all types of computers, including handheld devices designed specifically for reading e-books. E-Books can be as familiar as their print counterparts or as unique as the electronic medium itself.

Id.

9. *Id.* "On its simplest level, an e-book is a book just like any other book," says Phyllis Rossiter Modeland, former editor of the e-book reader electronic magazine *The RunningRiver Reader*™. "It has 'cover' art, a title page, an ISBN, a copyright notice, an editor and publisher for whom it was a labor of love—and an author who wrote it because she or he had to." *Id.*

10. *Random House*, 150 F. Supp.2d at 615 ("Included in a Rosetta ebook is a book cover, title page, copyright page and 'eforward' all created by Rosetta Books . . . the text of the ebook is exactly the same as the text of the original work."). Of course, the eBook may be enhanced by hyperlinks that supplement the original text with new content, which may be anything from definitions or commentary on the original text to links to audio or

marketed to the general public by online publishers as "books"[11] without the word "electronic" as a modifier immediately preceding the word "book."[12]

The development of eBooks and reading appliances designed to make eBooks more user-friendly realize that goal in several important ways.[13] As with traditional paper books, the reader may skim, turn "pages," and read exactly the same text as he would expect to find in his paperback or hardback version.[14] The eBook user can also highlight or "bookmark" text much as a paper book reader might.[15] Like the virtual book reader, the eBook reader may type or write, with a stylus, electronic notes in the margins to be stored for later use.[16] Unlike traditional books, however, the eBook reader can change the font of the text, use a search function to instantly find a desired passage, use hyperlinks to jump to a specific passage or bookmark, and may request the definition of any word in the text.[17] The addition of hyperlinks is especially significant because creating a book with such embedded links almost always entails the creation of works with far more content than a fixed amount of static text.[18] Depending on the

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video works. *Reader's E-Book Primer: What's an E-Book*, *supra* note 8, *at* http://www.ebookconnections.com/ReadersPrimer/what's_an_e-book.htm.

11. *See, e.g., Discover Modern Library eBooks*, *at* http://www.randomhouse.com/modernlibrary/ebooks.html ("Ebooks allow you to purchase, download, and read books through a specialized ebook device. . . .") (last visited Feb. 10, 2002); *Ballantine Books: Category: eBook*, *at* http://www.randomhouse.com/BB/ebooks.html ("An eBook is a digital version of a print book.") (last visited Feb. 10, 2002).

12. *See, e.g.*, National Writers Union, *Contract Issues Books Published Online*, *available at* http://www.nwu.org//docs/online-p.htm (last modified April 16, 1997) ("We're now at the threshold of another form of book distribution . . . .").

13. Bill N. Schilit et al., *As We May Read: The Reading Appliance Revolution*, COMPUTER, Jan. 1999, at 65, *available at* http://www.fxpal.com/PapersAndAbstracts/abstracts/sch99.htm.

14. *See Reader's E-Book Primer: What's an E-Book*, *supra* note 8, *at* http://www.ebookconnections.com/ReadersPrimer/what's_an_e-book.htm; James Sachs, *SoftbookPress: Marketing a Paperless Reading System*, INSTITUTE FOR CYBERINFORMATION (Summer 1998), *at* http://futureprint.kent.edu/articles/sachs01.htm.

15. *Random House*, 150 F. Supp. 2d at 615

16. *Id.*

17. Hyperlinks are embedded links which, when clicked with a mouse, immediately transport the reader to another part of the work or to other texts, audio, video, or other digital elements which are outside the book itself but accessible through the Internet. *See* National Writers Union, *supra* note 12, *at* http://www.nwu.org//docs/online-p.htm (last modified April 16, 1997).

18. *Id.*

enabling device and software, the eBook can even be read aloud to the user by means of a synthetic speech engine.[19]

Because eBooks are in digital format, they are particularly susceptible to copyright infringement.[20] Some eBooks, such as those sold by defendant Rosetta, incorporate security features designed to prevent copyright infringement.[21] The reader may be prevented from printing, copying, emailing, or otherwise distributing the eBook in whole or in part without first bypassing certain security features.[22] Although bypassing the eBook's security is technologically possible, to do so is a violation of the licensing agreement accompanying the software.[23]

The introduction of eBook technology to the marketplace raises questions regarding who owns the right to license eBooks under existing licensing agreements.[24] This question is especially important to those traditional publishers who have themselves moved into the e-publishing arena.[25] *Random House v. Rosetta Books* is the first case to address these questions.

II. CASE SUMMARY

A. New and Old Licensing Agreements

In 2000 and early 2001, Rosetta Books executed contracts with several authors, including Kurt Vonnegut, William Styron and Robert B. Parker, giving Rosetta the rights to publish their literary works, previously published by Random House in virtual book form, as eBooks.[26] On February 26, 2001, Rosetta Books launched its website, www.rosettabooks.com,

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19. *See, e.g., Microsoft Reader with ClearType, at* http://www.Microsoft.com/reader/accessibility.asp (last visited Feb. 10, 2002) (description of Microsoft Reader Text-To-Speech Package 1.0).

20. *See, e.g.,* Kurt Foss, *DEF CON 9'Hacker Fest' Includes Talk on eBook Security,* PLANET EBOOK (July 11, 2001), *at* http://www.planetebook.com/mainpage.asp ("There is one big problem that related with ebooks [sic] . . . . Information in electronic form could be duplicated and transmitted, and there is no reliable way to take control over that processes."); James Middleton, *eBook Hacker Brought to Book,* vnunet.com (Nov. 11, 2001), *at* http://www.vnunet.com/News/1127096 (discussing the case against Dmitri Sklyarov, the Russian programmer who broke the encryption on Adobe's eBook software).

21. *Random House,* 150 F. Supp. 2d at 615.

22. *Id.*

23. *Id.*

24. *Id.* at 614.

25. Random House is one such publisher. *See* Random House, *DiscoverModern Library eBooks at* http://www.randomhouse.com/modernlibrary/ebooks.html (last visited Feb 10, 2002).

26. *Random House,* 150 F. Supp. 2d at 614.

offering familiar titles such as *The Confessions of Nat Turner* and *Sophie's Choice* by William Styron; *Slaughterhouse-Five*, *Breakfast of Champions*, *The Sirens of Titan*, *Cat's Cradle*, and *Player Piano* by Kurt Vonnegut; and *Promised Land* by Robert B. Parker.[27]

The next day, Random House filed a complaint against Rosetta Books.[28] The complaint alleged copyright infringement and tortious interference with the contracts Random House had with Styron, Vonnegut, and Parker.[29] Random House accordingly requested that the district court grant a preliminary injunction preventing Rosetta Books from infringing Random House's copyrights.[30]

Random House's claims arise from various licensing agreements that it entered into with the three authors, all of which grant Random House the right to "print, publish and sell the work in book form."[31] The licensing agreements between Random House and Styron date back to 1961.[32] Besides granting Random House the right to "print, publish and sell the work[s] in book form," the Styron agreements also gave Random House various related rights, including the rights to license publications of reprint editions, publications of the works in whole or shortened forms in anthologies and school books, publications of the works by book clubs, and publications or broadcasts of selections from the works for publicity purposes.[33] In contrast, Random House was not granted the right to license publications in the British Commonwealth or in foreign languages.[34] Both licensing agreements also contained noncompetition clauses.[35]

Vonnegut entered into two licensing agreements with Random House in 1967 and 1970, which gave Random House similar rights, although Vonnegut specifically reserved for himself in the 1967 contract the "dramatic . . . motion picture (silent and sound) . . . radio broadcasting (including mechanical renditions and/or recordings of the text) . . . [and] televi-

27. *Id.*
28. *Id.*
29. *Id.*
30. *Id.*
31. *Id.* at 615.
32. *Id.*
33. *Id.* at 615-16. Random House also acquired the right to license without charge publication of the work for the physically handicapped (*e.g.* in Braille). *Id.* at 616.
34. *Id.*
35. *Id.*

sion rights."[36] Unlike Styron's agreements and Vonnegut's 1970 contract, Vonnegut's 1967 contract did not contain a noncompetition clause.[37]

Robert B. Parker's contract granting Dell[38] the right to publish *Promised Land* also contains a noncompetition clause which states, in pertinent part, "[t]he Author . . . will not, without the written permission of Dell, publish or permit to be published any material based on the material in the Work, or which is reasonably likely to injure its sale."[39] In other respects, Parker's agreement resembles Vonnegut's 1970 contract with Random House: both grant various rights related to the right to print and publish the book in book form to the publisher, but reserve for the author certain other important rights.[40] In Parker's case, these rights included those related to the licensing of dramatic works, motion pictures, radio broadcasting, television, and mechanical or electronic readings of the text.[41]

B. The District Court's Opinion

The district court denied Random House's motion for a preliminary injunction against Rosetta, holding that Random House "is not the beneficial owner of the right to publish the eight works at issue as eBooks," and was therefore unlikely to succeed at trial on the merits on its claim of copyright infringement.[42] The court reasoned that in order to win its motion for a preliminary injunction, Random House would have to have shown both irreparable harm and either a likelihood of success on the merits or serious questions about the merits.[43] To achieve the latter, generally, the party requesting relief must demonstrate that the dispute over the merits of the case is sufficiently serious to constitute a fair ground for litigation and that the "balance of hardships" tips in its favor.[44] Finally, the moving party, Random House, could have raised a presumption of irreparable harm by establishing a *prima facie* case of copyright infringement.[45]

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36. *Id.* (parentheses and brackets in original). Vonnegut reserved largely the same rights for himself under the 1970 contract. *Id.*

37. *Id.*

38. The Bantam Dell Publishing Group is a subsidiary of Random House, Inc. *Bantam Dell Publishing Group, at* http://www.randomhouse.com/bantamdell/ (last visited Feb 10, 2002).

39. *Random House*, 150 F. Supp. 2d at 617.

40. *Id.* at 616-17.

41. *Id.*

42. *Id.* at 624.

43. *Id.* at 617 (citing Abkco Music v. Stellar Records, 96 F.3d 60, 64 (2d Cir. 1996)).

44. *Id.* at 617.

45. *Id.*

In addressing the merits of the case, the court held that Random House could show neither irreparable harm nor a likelihood of success on the merits based on Random House's failure to establish a *prima facie* case of copyright infringement.[46] The court held with respect to all contracts at issue that Random House failed to prove the ownership of a valid copyright, one of the two elements of a *prima facie* case of infringement, with respect to the digital version of the authors' works.[47] The court further found that since Random House was not the beneficial owner of the right to publish the works as eBooks, it had no standing to institute an action for infringement.[48]

Since the word "eBook" does not appear in any of the contracts at issue, the court reached its conclusion that Random House did not have the right to publish the authors' works as eBooks by applying well established principles of contract interpretation.[49] For example, it held that the interpretation of an agreement purporting to grant a copyright license is a matter of state contract law.[50] New York law dictates that a contract be interpreted to give effect to the intentions of the parties as reasonably revealed by the contract language itself.[51] If the meaning is ambiguous, then interpretation of the contract is a question of fact for the court to determine on the basis of all evidence, including extrinsic evidence.[52]

Applying these principles, the court determined that the right to "print, publish and sell the work in book form" could not be reasonably interpreted to include the right to publish the work as an eBook.[53] First, examining the contract language, the court found that the words "in book form" have a specific meaning.[54] The court defined a book as "sheets of paper fastened or bound together within covers."[55] Moreover, the court determined that it could not be shown that the parties' intended the grant of

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46. *Id.* at 624.

47. Feist Publ'ns v. Rural Tel. Serv. Co., 499 U.S. 340, 361 (1991). The other element of a *prima facie* case is the "copying of constituent elements of the work that are original." *Id.*

48. *Random House*, 150 F. Supp. 2d at 624.

49. *Id.* at 620.

50. *Id.* at 618; *see also* Flack v. Friends of Queen Catherine, 139 F. Supp. 2d. 526, 536 (S.D.N.Y. 2001).

51. *Random House*, 150 F. Supp. 2d at 618 (citing Terwilliger v. Terwilliger, 206 F.3d 240, 245 (2d Cir. 2000)).

52. *Id.* at 618 (citing Seiden Assocs. v. ANC Holdings, 959 F.2d 425, 428 (2d Cir. 1992)).

53. *Id.* at 620.

54. *Id.*

55. *Id.* (citing the RANDOM HOUSE WEBSTER'S UNABRIDGED DICTIONARY (2001)).

rights to publish "in book form" to be all encompassing.[56] For example, specific clauses conveying to the publisher the rights to publish "book club editions, reprint editions, abridged forms, and editions in Braille" imply the exclusion of the right to publish all unmentioned types of print publications.[57]

Second, the court interpreted all the contracts as granting narrow rights to the publisher.[58] In several cases, the authors retained certain rights by drawing a line through portions of the printed contract where additional rights of the publisher were detailed.[59] Additionally, evidence was provided to show that the right to publish a work "in book form" is understood in the publishing industry to be a "limited" grant.[60] According to the court, "the publishing industry generally interprets the phrase 'in book form' as granting the publisher 'the exclusive right to publish a hardcover trade book in English for distribution in North America.'"[61]

The court also found that the presence of noncompetition clauses in some of the agreements did not mean that the authors had granted Random House the right to publish eBooks.[62] Only noncompetition clauses limited in scope are enforceable in New York.[63] Further, even if the noncompetition clauses did prevent the authors from contracting with Rosetta Books, Random House would only be a entitled to bring a breach of contract action against the authors; it would not have sufficient cause to prove a copyright infringement action against Rosetta.[64]

Finally, the court concluded that "[t]he finding that the five licensing agreements at issue do not convey the right to publish the works as eBooks accords with Second Circuit and New York case law," i.e., the prior new use case law in that jurisdiction.[65] New use cases arise where it

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56. *Id.*

57. *Id.*

58. *Id.* at 620-21.

59. *Id.* at 620.

60. *Id.* at 621-22. *See also* Field v. True Comics, 89 F. Supp. 611, 613-14 (S.D.N.Y. 1950); NIMMER ON COPYRIGHT, *supra* note 1, § 10.14[C] (citing *Field*, 89 F. Supp. at 613-14).

61. *Random House*, 150 F. Supp. 2d at 622 (quoting ALEXANDER LINDLEY, 1 LINDLEY ON ENTERTAINMENT, PUBLISHING, AND THE ARTS 1.01-1 (2d ed. 2000)). The court noted, however, that the phrase, "in book form," outside the context of a specific contract, "may include other forms of books such as book club editions, large print editions, leather bound editions, trade and mass market paperbacks." *Random House*, 150 F. Supp. 2d at 622.

62. *Id.* at 621.

63. *Id.*

64. *Id.*

65. *Id.* at 622.

is unclear whether "licensees may exploit licensed works through new marketing channels made possible by technologies developed after the licensing contract."[66] The court distinguished *Random House* from prior new use cases based on the limited scope of the contract language, existence of two separate mediums, nature of the copyrighted work, and absence of anti-progressive incentives.[67]

Characterizing the decision as "neither a victory for the technophiles nor a defeat for Luddites," the court denied plaintiff's motion for a preliminary injunction.[68] On September 13, 2001, Random House appealed the decision of the district court.[69] The Court of Appeals has not yet set a date for oral arguments.[70]

III. DISCUSSION

Random House is typical of new use cases in that it centers around the interpretation of a few words which were probably not ambiguous when the licensing agreement was written, but have become ambiguous in light of technological developments in the communications industry.[71] Specifically at issue in *Random House* is the phrase "in book form," which appears in each of the licensing agreements.[72] Under New York contract law principles, the court could have reasonably interpreted the term "in book form" either strictly, including only traditional paper-based books, as it seems to have done in *Random House*, or broadly, to include new forms of book distribution.

To the extent that the interpretation of "in book form" is an open question under these principles, the developing line of new use cases is especially instructive. Recently, the Second Circuit has tended to interpret con-

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66. *Id.* at 618 (citing Boosey & Hawkes Music Publishers v. Walt Disney, 145 F.3d 481, 486 (2d Cir. 1998)).

67. *Random House*, 150 F. Supp. 2d 622-23.

68. *Id.* at 624.

69. The appeal, reply to the appeal, and other court documents can be accessed from Rosetta Books' website *at* http://www.rosettabooks.com/pages/legal.html (last visited Feb. 10, 2002).

70. *Id.*

71. *See, e.g.*, Tele-Pac v. Grainger, 570 N.Y.S.2d 521 (1991) (interpreting "broadcasting television"); Bartsch v. Metro-Goldwyn-Mayer, 391 F.2d 150 (2d Cir. 1968), *cert. denied*, 393 U.S. 826 (1968) (interpreting the word "exhibit"); Bourne v. Walt Disney, 68 F.3d 621 (2d Cir. 1995), *cert. denied*, 517 U.S. 1240 (1996) (disputing the meaning of "motion picture").

72. *Random House*, 150 F. Supp. 2d at 615.

tracts in new use cases broadly.[73] Had the court applied this expansive approach to the facts in *Random House*, the dispute might have been resolved differently.

A. Interpreting "In Book Form"

Contract interpretation is governed by state law even though the subject matter in question may come within the scope of federal copyright law.[74] Under New York law, which governs each of the specific publishing agreements in this case, contract language, such as the phrase "in book form," must be construed in accordance with its plain and ordinary meaning.[75] Further, the written contract should be interpreted in accordance with the contracting parties' intentions as expressed by the language used in the contract itself to the greatest extent possible.[76] Any ambiguity or conflict in the language "must be resolved against the party who drew the contract," in this case Random House.[77]

The plain meaning of the contract language employed in the original licensing agreements does not limit Random House's publication rights to one specific form of book. Therefore, the pertinent question to ask is whether or not an eBook is distributed to readers "in book form." If a book is defined by its traditional physical characteristics, such as paper successively numbered and bound between two covers, then an eBook clearly falls outside this definition. There are several reasons, however, not to construe the phrase "in book form" so narrowly.

First, paper-based books and eBooks are functionally equivalent in that the reader experiences both a virtual book and an eBook in comparable ways.[78] In both cases, text is most usually read in a linear fashion, from the beginning of the story to the end. The reader may also "flip," physically or electronically, to a desired passage, thereby experiencing the book nonlinearly.[79] The reader of both the paper book and the eBook may high-

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73. *See, e.g., Bourne*, 68 F.3d at 630 (interpreting the phrase "motion picture" as including videocassettes).

74. *Bartsch*, 391 F.2d at 153-54.

75. *Tele-Pac*, 570 N.Y.S.2d at 523; *see also* W.W.W. Assoc. v. Giancontiere, 566 N.E.2d 639 (N.Y. 1990).

76. Terwilliger v. Terwilliger, 206 F.3d 240, 245 (2d Cir. 2000).

77. Certified Fence v. Felix Indus., 687 N.Y.S.2d 682, 683 (1999); Chatterjee Fund Mgmt. v. Dimensional Media Assoc., 687 N.Y.S.2d 364, 365 (1999) (any ambiguity in the contract language must be construed against plaintiff as drafter of the document).

78. An analogous situation arises in cases involving movies: the movie viewer at the theater experiences the film in a way comparable to the viewer who watches the film at home on videocassette. *See Bourne*, 68 F.3d at 630.

79. An eBook reader could accomplish this, for example, via embedded hyperlinks.

light certain passages, insert bookmarks, or make notes in the margin.[80] It is possible that as eBook technology develops even further, the differences may be even further diminished.[81]

This is not to say, however, that there are no differences between virtual books and eBooks. For example, a reader of a virtual book would be hard-pressed to find all the instances of a single word in her paperback novel, whereas an eBook reader could use a search function to accomplish this task in very little time.[82] Additionally, consumers can update and download eBooks immediately, granting them access to the most current digital encyclopedias and schoolbooks, for example.[83] However, the significant functional similarities between paper books and Rosetta's eBooks weigh in favor of treating an eBook as simply another kind of "book."

Second, one may argue that popular conceptions about what constitutes "in book form" have already expanded in publishing circles to include both compact discs containing the text and the eBook.[84] Rosetta's own marketing, while making a formal distinction between "physical" books and "virtual" books, goes on to treat both types of book the same.[85] The view that eBooks are books is supported by publishers of eBooks and eBook reading appliances, such as Microsoft Reader and Adobe, both of

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80. Of course, it is vastly easier to rid an electronic text of highlights and margin notes once the reader no longer requires them, returning the eBook to a pristine state.

81. *See, e.g.*, Douglas Boling, *The Book of the Future*, MICROSOFT INTERACTIVE DEVELOPER, Oct. 1998, *at* http://www.microsoft.com/mind/1098/flux/flux1098.htm (discussing the development of electronic books which use electronic ink "sprayed" on flexible pages).

82. This function, however, is not currently part of Rosetta's software and is therefore not offered in connection with the eBooks Rosetta sells.

83. Jamie Engle, *Reader's E-Book Primer: Benefits*, *at* http://www.ebookconnections.com/ReadersPrimer/benefits.htm (last visited Feb 10, 2002).

84. *See, e.g.*, National Writers Union, *supra* note 12 *at* http://www.nwu.org/docs/online-p.htm (last modified April 16, 1997):

> For centuries there was little doubt about what constituted a book . . . . In the past few years the definition has extended to compact discs containing audio, video, and other digital elements along with text . . . .We're now at the threshold of another form of book distribution in which only the words themselves and accompanying material are conveyed—via electronic networks. Online book publishing is still in its infancy . . . .

85. Rosetta Books, *About eBooks*, *at* http://www.rosettabooks.com/pages/about_ebooks.html (last visited Feb. 10, 2002) ("An e-book, or electronic book, is a digital book that you can read on a computer screen or electronic device.").

whom advertise that the eBook displays text in a form nearly identical to the font of a hardcover book.[86]

In contrast to this contemporary treatment of eBooks as books, the district court in *Random House* found that traditional publishing industry practice revealed that a license to print, publish, and distribute a work "in book form" bestowed merely a narrow grant of rights.[87] For example, in *Field v. True Comics*, the court held that "the sole and exclusive right to publish, print and market *in book form*," especially when the author had specifically reserved rights for himself, was "much more limited" than "the sole and exclusive right to publish, print and market the book."[88]

However, the District court's reliance on *Field* is misplaced, since the facts and the scope of the disputed contract in *Field* are significantly different from those in *Random House*. *Field* involved the question of whether the publisher had the right to publish an eight-page comic strip based on, but different from, an original work when his license granted him only the right to publish the work "in book form."[89] However, as has been stated, the content of an eBook is almost identical to the content of its paper-based counterpart.[90] Moreover, the court's narrow interpretation of the disputed contract language in *Field* is consistent with the pub-

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86. *The Microsoft eBooks Story*, *at* http://www.microsoft.com/reader/info.asp (last visited Feb 10, 2002):

> ClearType enhances display resolution by as much as 300 percent by improving letter shapes and character spacing, making them appear more detailed, more finely crafted, and more like printed fonts .... Books need not be confined to the physical qualities of their pages .... [A] book is really a magical thing that disappears when you read it. The book itself, whether it's made of ink on paper or pixels on a screen, seems to evaporate when you become immersed in the act of reading .... That's the kind of experience you can have using Microsoft Reader with ClearType.

See also Adobe Acrobat eBook Reader 2.2, *at* http://www.adobe.com/products/ebookreader/main.html (last visited Feb. 10, 2002) ("Only this reader software displays eBooks with the pictures, graphics, and rich fonts you've come to expect from printed books.").

87. Field v. True Comics, 89 F. Supp. 611, 612 (S.D.N.Y. 1950).

88. *Id.* (emphasis added). According to the district court, "the publishing industry generally interprets the phrase 'in book form' as granting the publisher 'the exclusive right to publish a hardcover trade book in English for distribution in North America.'" *Id.* (quoting LINDLEY, *supra* note 61, at 1.01-1).

89. *See* Random House v. Rosetta Books, 150 F. Supp. 2d 613, 621-22 (S.D.N.Y. 2001).

90. *See id.* at 615; *see also supra* text accompanying notes 11-13.

lisher's limited rights under the contract.[91] On the other hand, Random House's contract rights are comparatively broad.[92]

Finally, traditional analysis of industry practice usually focuses on the time the contract was formed. This analysis is less likely to be illustrative of the parties' intentions when the use in question is a new one, based on technology developed since the contract's execution.[93] For example, was a licensing agreement concerning "motion picture" rights signed in 1928 intended to include within its scope only what was technologically possible at the time, or would new forms of motion picture distribution, such as the videocassette and the DVD, fall within the scope of the contract as the technology developed?[94] If Justice Henry Friendly was right to say that "any effort to reconstruct what the parties actually intended nearly forty years ago is doomed to failure,"[95] then how *are* courts to determine such cases?

B. The New Use Cases

Where the parties' intentions with regards to new uses are not clear, courts have taken one of two approaches to the problem of contract inter-

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91. *See* Random House Reply Brief at 15, *Random House* (No. 01-1728), *available at* http://www.rosettabooks.com/casedocs/Random_House_Reply_Brief.pdf (Feb. 11, 2002):

> [S]everal of the contracts give Random House the right to publish "in such style and manner" as it "deems suitable" (1961 Styron Contract, Sarnoff Aff., Ex. A at ¶ 2; 1979 Styron Contract, Sarnoff Aff., Ex. B at ¶ 6), and several grant the right to publish the Works via forms of copying "either now in use or hereafter developed" (1967 Vonnegut Contract, Sarnoff Aff., Ex. C at ¶ 1.d; 1970 Vonnegut Contract, Sarnoff Aff., Ex. D at ¶ 1.d; Parker Contract, Sarnoff Aff., Ex. E at ¶ 1.d). Others prevent the authors from "publish[ing] or permit[ting] to be published any material in book or pamphlet form, based on material in the work" (1961 Styron Contract, Sarnoff Aff., Ex. A at ¶ 8; Parker Contract, Sarnoff Aff., Ex. E at ¶ 18).

92. *Id.*

93. *See* Boosey & Hawkes Music Publishers v. Walt Disney, 145 F.3d 481, 488 (2d Cir. 1998) ("[I]ndustry custom [is not] likely to illuminate the intent of the parties, because the use in question was, by hypothesis, new, and could not have been the subject of prior negotiations or established practice.").

94. The Second Circuit held in *Bourne v. Disney*, a recently new use case, that the phrase "motion pictures" extends to videocassettes, even if videocassette technology did not exist at the time of the contract. *See* Gayley Rosen, *The Rights to Future Technologies: Should Bourne v. Disney Change the Rules?*, 24 FORDHAM URB. L.J. 617, 618 (Spring 1997).

95. Bartsch v. Metro-Goldwyn-Mayer, 391 F.2d 150, 155 (2d Cir. 1968), *cert. denied*, 393 U.S. 826 (1968).

pretation.[96] Courts applying the first, narrow approach generally hold that a license of rights in a given medium (i.e., "motion picture rights") includes only such uses as fall within the unambiguous core meaning of the term (e.g., exhibition of motion picture film in motion picture theaters) and excludes any uses that lie within the ambiguous penumbra (e.g., exhibition of motion picture film on television or on videocassettes).[97] Thus, if the grant of rights is not expressly granted in the contract, the author retains the rights. The First and Ninth Circuits have adopted this standard.[98] To courts applying this approach, a right to publish "in book form" would most certainly include only the right to publish the work as a virtual book and not as an electronic book.

Under the alternative, dominant approach, the court would determine whether the contract language, read as to admit any reasonable interpretation, is broad enough to authorize the new use.[99] This is the approach taken by the Second Circuit in its leading new use cases, *Bartsch v. Metro-Goldwyn-Mayer, Inc.*, *Boosey & Hawkes Music Publishers, Ltd v. Walt Disney Co.*, and *Bourne v. Walt Disney Co.*[100] Further, in interpreting contracts in the light of new technology, the actual language used in the contract, not extrinsic evidence of the intent of the contracting parties at the time, is controlling.[101]

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96. As has been previously stated, new use cases, like *Random House*, involve disputes about whether licensees may exploit licensed works through new marketing channels made possible by technologies developed after the licensing contract. *See Boosey*, 145 F.3d at 486.

97. NIMMER, *supra* note 1, § 10.10[B].

98. Rosen, *supra* note 94, at 622 (citing Cohen v. Paramount Pictures, 845 F.2d 851 (9th Cir. 1988), and Rey v. Lafferty, 990 F.2d 1379 (1st Cir. 1993), as examples).

99. NIMMER, *supra* note 1, § 10.10[B]:

> [T]he licensee may properly pursue any uses that may reasonably be said to fall within the medium as described in the license. This would include uses within the ambiguous penumbra because if whether or not a given use falls within the description of the medium is ambiguous, it must, by definition, mean that it is within the medium in a reasonable sense (albeit this is not the only reasonable sense). "In other words, the question before the court is not whether he [the licensee] gave the words the right meaning, but whether or not the words authorized the meaning he gives them."

(quoting CURTIS, A BETTER THEORY OF LEGAL INTERPRETATIONS: JURISPRUDENCE IN ACTION 135, 157 (1953)).

100. *Boosey*, 145 F.3d 481; *Bartsch*, 391 F.2d 150; Bourne v. Walt Disney, 68 F.3d 621 (2d Cir. 1995), *cert. denied*, 517 U.S. 1240 (1996). The *Random House* court focused its analysis on *Boosey* and *Bartsch*. Random House v. Rosetta Books, 150 F. Supp. 2d 613, 618-19 (S.D.N.Y. 2001).

101. *Boosey*, 145 F.3d at 481.

The dispute in *Bartsch* turned on the meaning of the phrases "exhibition" and "motion picture," and specifically whether or not the right to exhibit motion pictures included the right to distribute the work as a television broadcast.[102] In 1930, the author of the play "Maytime" granted Harry Bartsch worldwide motion picture rights to the play, including the right to copyright, vend, license, exhibit, and transmit or otherwise reproduce such motion picture photoplays by the art of cinematography "or any process analogous thereto."[103] These rights were eventually assigned to Metro Goldwyn-Mayer, "MGM," which licensed its motion picture "Maytime" for television viewing in 1958.[104] Bartsch sued, claiming the right to distribute the play as a television broadcast was not within those rights granted to MGM.[105]

The *Bartsch* court found that since the contract was designed to give MGM a broad grant of motion picture rights, the clause granting the licensee the right to "exhibit" the work should also be broadly interpreted.[106] The court observed that if Bartsch or his assignors had wanted to limit their grant of rights to traditional exhibition of the play as a motion picture in a movie theater, they could have done so.[107]

The agreement at issue in *Boosey* gave the licensee the right "to record in any manner, medium or form, and to license the performance of, the musical composition [for use] in a motion picture."[108] The plaintiff, who was the assignee of Igor Stravinsky's copyrights in the musical composition "The Rite of Spring," argued that the agreement authorized the use of the musical work in the motion picture "Fantasia," but not the right to use the Stravinsky work in video format.[109] The court held, however, that the language of the grant was broad enough to authorize Disney's use of the work in video format, even though the original grant did not contemplate such a use.[110]

The court in *Bourne* addressed the role of the parties' intent at the time the contract was signed.[111] This new use case involved a dispute over

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102. *See Bartsch*, 391 F. 2d at 151.

103. *Id.* at 150, 153.

104. *Id.* at 152.

105. *See id.*

106. *Id.* at 155.

107. *Id.*

108. Boosey & Hawkes Music Publishers v. Walt Disney, 145 F.3d 481, 484 (2d Cir. 1998).

109. *Id.* at 483-84.

110. For a succinct summary of *Boosey*, see Random House v. Rosetta Books, 150 F. Supp. 2d 613, 619 (S.D.N.Y. 2001).

111. *See generally* Rosen, *supra* note 94.

whether two copyright agreements between Disney and songwriter Irving Berlin included the rights to use Berlin's music on videocassettes.[112] *Bourne* seems to hold that the parties are not required to contemplate or be aware of the possible new use at the time of original contract.[113] In fact, *Bourne* seems to indicate that the Second Circuit will read all contracts as broadly as the plain language reasonably allows *at the time of interpretation*, taking into account technological advances not in existence at the time the contract was written.[114] Moreover, broad grant language, which facilitated the courts' expansive interpretations of the *Bartsch* and *Boosey* licenses, is absent from the *Bourne* contract.[115] Therefore, the court in *Random House* could have found that, at the time the case came before the court, the publishing industry considered eBooks to be like a virtual book and interpreted the grant of rights to Random House accordingly.

Despite these precedents, the court in *Random House* distinguished the case from the Second Circuit's line of new use cases on four grounds.[116] First, the court argued that the conveying language in the *Boosey* and *Bartsch* licensing agreements was "far broader" than that in *Random House*.[117] Second, the new use in *Boosey* and *Bartsch* fell within the same medium as the original grant.[118] Third, whereas *Boosey* and *Bartsch* involved the creation of new works—where the right to display the new work is derivative of the right to create that work—the publishers in *Random House* merely displayed the words written by the author.[119] Fourth, reserving the rights to license eBooks for the authors did not implicate any anti-progressive incentives.[120]

None of these four grounds are persuasive. First, the key question in *Random House* should not involve the breadth of the granting language in the abstract, but should inquire specifically into whether the contract language used is broad enough to encompass the digital form of the work. This approach would be consistent not only with *Bartsch* and *Boosey*, but also with *Bourne*. The question of whether the phrase "in book form" is broad enough to include the publication of eBooks over the Internet turns on whether or not an eBook is a book or something else altogether. Given

112. Bourne v. Walt Disney, 68 F.3d 621, 623-24 (2d Cir. 1995), *cert. denied*, 517 U.S. 1240 (1996).

113. *See* Rosen, *supra* note 94, at 628-29.

114. *Id.* at 628 (citing *Bourne*, 68 F.3d at 630).

115. *Id.* at 630.

116. Random House v. Rosetta Books, 150 F. Supp. 2d 613, 622-23 (S.D.N.Y. 2001).

117. *Id.* at 622.

118. *Id.* at 622-23.

119. *Id.* at 623.

120. *Id.*

the functional and conceptual similarities between digital and paper books, as discussed above, a court interpreting the phrase "in book form" could reasonably include eBooks within the ambit of the contracts' language.

Second, the reasonableness of the broad interpretation should depend not on formal distinctions such as whether print books and eBooks belong to the same medium,[121] but rather on their functions and the ways in which the readers experience the works. Few will dispute that traditional print technology is vastly different from digital technology, just as few dispute that the technology involved in projecting a film reel onto a screen is different from the technology involved in viewing the same film on one's VCR. In both cases, whether a new distribution mechanism falls within the scope of the license at issue in the Second Circuit depends on "whether the 'fundamental characteristic' of the intellectual property involved—here, a faithful presentation of the author's text—remains unaltered . . . . If so, 'the physical form in which the work is fixed—film, tape, discs, and so forth—is irrelevant.'"[122]

The third prong of the court's test for distinguishing *Random House* from other Second Circuit new use cases asks whether the new use creates a new work, distinct from the original.[123] This was significant to the court because the right to display the new work is derivative of the right to create that work, as opposed to the right of the publisher to display the author's work.[124] However, the inquiry into whether a new work has been created has nothing to do with the crucial question of whether the contract language reasonably accommodates the use. Indeed, the court's preference for the creation of new works seems counter-intuitive in the new use context. It seems more logical that the *closer* the new use is in form to the original use, the more likely it will be that the contract language will be broad enough to cover the new use.

Finally, contrary to the assumptions made by the district court in *Random House*, there are no anti-progressive incentives involved in giving eBook publishing rights to Random House and similarly situated publishers. Allocating the rights in such a fashion undoubtedly raises questions

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121. Dictionary.com defines "medium" as "[a]n intervening substance through which something else is transmitted or carried on; an agency by which something is accomplished, conveyed, or transferred." *See* dictionary.com, *at* http://www.dictionary.com (last visited Feb. 10, 2002).

122. Random House Reply Brief, *supra* note 91, at 4 (quoting Bourne v. Walt Disney, 68 F.3d 621, 630 (2d Cir. 1995), *cert. denied*, 517 U.S. 1240 (1996)). *Accord* L.C. Page & Co. v. Fox Film Corp., 83 F.2d 196, 199 (2d Cir. 1936).

123. *Random House*, 150 F. Supp. 2d at 623.

124. *Id.*

concerning the fairness of the distribution, which should be answered by the reasonableness analysis already discussed. It does not, however, inherently hinder the progression of technological development. To the contrary, if electronic publishing becomes lucrative, and if traditional publishers are assigned the rights, then it seems likely that traditional publishers will be become e-publishers. In fact, Random House currently sells eBooks through Ballantine, the Modern Library, and books@Random, three of its divisions.[125] Moreover, eBook publishers are free to sign contracts for new works with authors.

IV. CONCLUSION

With the exception of *Random House*, courts have not yet widely tested the new use line of cases.[126] However, litigation in this area is likely in the near future, especially because courts remain split on the proper approach to new use issues.[127] Adoption of the Second Circuit's broad approach, which looks to the reasonableness of a particular interpretation of contract language at the time the suit is brought rather than at the time the contract was signed, would provide both courts and contracting parties with greater flexibility when addressing uses made possible by rapidly developing technology. This reasonableness analysis should take into account the important functional similarities between the proposed new use and the use covered in the contract from the perspective of the end user or consumer. Finally, the reasonableness of a given interpretation should be informed by the perception and treatment of the new use by the general public and industry members.

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125. *See, e.g.*, *The ModernLibrary: Discover ModernLibrary eBooks*, *at* http://www.randomhouse.com/modernlibrary/ebooks.html (last visited Feb 10, 2002). *But see eBooks news-briefs*, *at* http://www.artmedia.com.au/news.htm (last visited Feb 10, 2002) ("In another blow for the fledgling electronic book market, Time Warner Books announced Tuesday it was shutting down its e-publishing division, iPublish.com.").

126. Christine Lepera, *Litigating in Cyberspace*, 662 PLI/PAT 773, 794 (2001).

127. *Id.*

BONNEVILLE INTERNATIONAL V. PETERS

By Raffi Zerounian

Copyright law is a creature of technology. The invention of machines that produced direct copies of original works led to the creation of copyright law. As technology has evolved, so has copyright doctrine.[1] Copyright law strives to achieve a difficult balance between encouraging societal access to such works and encouraging authors to create them.[2] In *Bonneville International v. Peters,*[3] Judge Berle Schiller ruled that AM and FM radio stations broadcasting transmissions over the Internet are not exempt "nonsubscription broadcast transmissions," and thus have to pay a public performance royalty.

In upholding the Copyright Office's administrative "final ruling," the district court allowed the Copyright Office to make a decision unprecedented in its history. Furthermore, the district court's decision did not fully consider the policy differences between various forms of music transmission over the Internet, and the evolution of sound recording rights. Historically, sound recordings had not received copyright protection because they did not affect record sales. In 1995, the Copyright Act was amended to include a narrow digital performance right for sound recordings. This right only included transmissions of sound recordings that affected record sales because of their "on demand" or "interactive" character.

This Note first examines the Copyright Office's novel rulemaking authority.[4] The analysis then turns to the increasing complexity of Copyright law as evidenced by the contradictory provisions of the Digital Millennium Copyright Act.[5] Finally, this Note examines the policy considerations that favor an exemption for radio stations that transmit their broad-

1. *See* Sony Corp. v. Universal City Studios, 464 U.S. 417, 430 (1984) ("[I]t was the invention of a new form of copying equipment—the printing press—that gave rise to the original need for copyright protection.").

2. Twentieth Century Music Corp. v. Aiken, 422 U.S. 151, 156 (1975) ("The primary objective in conferring the Copyright monopoly is the general benefit received by the public from the work of authors. When the literal terms of the Copyright Act are rendered ambiguous, it must be construed in light of the primary objectives of conferring the Copyright monopoly.").

3. 153 F. Supp. 2d 763 (E.D.P.A. 2001).

4. *See infra* Part III.A.

5. *See infra* Part III.B.

casts over the Internet because they do not threaten the sale of recorded music.[6]

I. BACKGROUND

The following section discusses music delivery models of sound recording broadcasts over the Internet, in order to illustrate the different policy implications of each model. The evolution of musical copyrights is then described. The final section discusses the literature surrounding deference to an administrative agency in order to better understand the district court's decision to defer to the Copyright Office's "final rule."

A. The Evolution of Copyright Protection for Transmission of Sound Recordings

Copyright law has long recognized the right of public performance of a musical composition.[7] Only recently has copyright law begun to protect sound recordings embodying musical compositions. Under the 1909 Copyright Act, the public performance right for musical works was limited to performances made "for profit."[8] With the Sound Recording Act of 1971,[9] Congress extended limited federal copyright protection to sound recordings in order to counter the unauthorized duplication and sale of sound recordings that resulted from advances in duplicating technology.[10] This limited protection did not include a public performance right,[11] even though the issue had been debated extensively.[12] Congress' amendment to the Copyright Act of 1971 did not include a public performance right be-

6. *See infra* Part III.C.

7. *See* 17 U.S.C. § 106(4) (Supp. 2001).

8. SHELDON HALPERN ET. AL., FUNDAMENTALS OF UNITED STATES INTELLECTUAL PROPERTY LAW: COPYRIGHT, PATENT, AND TRADEMARK 88 (1999).

9. Pub. L. No. 92-140, 85 Stat. 391 (1971).

10. H.R. REP. NO. 104-274, at 2 (1995); S. REP. NO. 92-72, at 3 (1971) (noting that the reason for creating a limited right in sound recordings was "the pirating of records and tapes").

11. A public performance right affords the copyright owner the exclusive right to the public performance of his or her work or to charge a royalty for such a transmission. *See* 17 U.S.C. § 106(6) (Supp. 2001).

12. *See* David W. Wittenstein & M. Lorrane Ford, *The Webcasting Wars*, J. INTERNET L. (Feb. 1999), *at* http://www.gcwf.com/articles/journal/jil_feb99_2.html ("Broadcasters argued that record companies are more than adequately compensated for the use of their music by receiving free advertising in the form of their music being broadcast to mass audiences over the radio."). The recording industry replied that some musical recordings do not receive these benefits and that "performers should be compensated for the commercial use of their property." *Id.*

cause the rights granted were sufficient to "protect against record piracy."[13] Furthermore, a public performance right was not granted, in large part, because of intense lobbying from the radio broadcast industry.[14] The Copyright Act of 1976 then eliminated the "for profit" limitation, but added many specific exemptions, including licensed broadcast transmissions.[15]

1. *Digital Performance Right in Sound Recordings Act*

Public performances of sound recordings were not afforded copyright protection until the passage of the Digital Performance Right in Sound Recordings Act ("DPSRA") in 1995.[16] The DPSRA included copyright protection for public performances of sound recordings by means of digital audio transmission.[17] The legislation was narrowly crafted to address concerns about the impact of certain types of subscription and interactive audio services on record sales.[18] Furthermore, the DPSRA did not address "free over-the-air broadcast services."[19]

Under 17 U.S.C. § 114(d)(1), transmissions that were perceived to pose little threat to record sales, such as nonsubscription transmissions, were exempted from the digital performance right.[20] Subscription digital

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13. H.R. REP. NO. 104-274, at 11 (1995).

14. JOHN HAZARD, COPYRIGHT LAW IN BUSINESS AND PRACTICE § 4.04 (rev. ed. 1999) (noting that the radio broadcast industry lobbied in order to evade paying "royalties to the owners of sound recording copyrights for the right to broadcast these works"); Kevin Featherly, *Broadcasters Must Pay Webcast Royalties, Judge Rules*, NEWSBYTES, Aug. 8, 2001, *available at* http://www.newsbytes.com/news/01/168650.html (noting that "a powerful broadcast lobby many years ago successfully convinced Congress to set aside" public performance rights for radio).

15. HALPERN, *supra* note 8, at 88.

16. *See* 17 U.S.C. § 106(6) (Supp. 2001).

17. S. REP. NO. 104-128, at 17 (1995), *reprinted in* 1995 U.S.C.C.A.N. 356, 364. This performance right did not cover broadcasting or related transmissions. *Id.*

18. *Id.* at 15 (stating that the legislation was concerned with how subscription and interactive services could "adversely affect sales of sound recordings and erode copyright owners' ability to control and be paid for use of their work"). The Senate Report of 1995 reads:

> It is the Committee's intent to provide copyright holders of sound recordings with the ability to control the distribution of their product by digital transmission, without hampering the arrival of new technologies, and without imposing new unreasonable burdens on radio and television broadcasters, which often promote, and appear to pose no threat to, the distribution of sound recordings.

Id. at 14.

19. *Id.* at 15.

20. 17 U.S.C. § 114(d)(1) (Supp. 2001); H.R. REP. NO. 104-274, at 14 (1995). Requirements for exemption included: being a nonsubscription broadcast transmission, a

audio transmissions not exempt under 17 U.S.C. § 114(d)(1),[21] and not part of an interactive service, were subject to a statutory license.[22] Upon meeting certain requirements, such as not publishing advanced schedules of the recordings, the "transmitters are guaranteed a license so long as they pay royalties (at rates to be negotiated, or if necessary, arbitrated) and comply with the other provisions of section 114."[23] Transmitters that use sound recordings as part of an interactive service are required to obtain a license from the copyright holder.

2. *Digital Millennium Copyright Act*

In 1998, Congress further amended the Copyright Act with the passing of the Digital Millennium Copyright Act ("DMCA").[24] In addition to a variety of provisions aimed at limiting digital piracy,[25] Congress abrogated two exemptions that had been included in section 114(d)(1)(A) under the DPSRA.[26] This deletion was "not intended to affect the exemption for nonsubscription broadcast transmissions."[27] Contemporaneously, Con-

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retransmission of a nonsubscription broadcast transmission not willfully or repeatedly transmitted more than a radius of 150 miles from the site of the radio broadcast transmission, or a noncommercial educational broadcast station. 17 U.S.C. § 114(d)(1) (Supp. 2001).

21. Section 114(d)(1) provides exemptions for retransmissions of nonsubscription broadcast transmissions.

22. 17 U.S.C. § 114(d)(2) (Supp. 2001).

23. H.R. REP. NO. 104-274, at 21 (1995).

24. H.R. REP. NO. 105-796, at 80 (1998), *reprinted in* 1998 U.S.C.C.A.N. 639, 656. The House of Representatives Report reads:

> The amendments to sections 112 and 114 of the Copyright Act . . . bill are intended to . . . further a stated objective of Congress when it passed the . . . ("DPSRA") to ensure that recording artists and record companies will be protected as new technologies affect the ways in which their creative works are used; and second, to create fair and efficient licensing mechanisms that address the complex issues facing copyright owners and copyright users as a result of the rapid growth of digital audio services.

Id.

25. H.R. REP. NO. 105-551, at 25 (1998) ("In contrast to the analog experience, digital technology enables pirates to reproduce and distribute perfect copies of works—at virtually no cost at all to the pirate. As technology advances, so must our laws.").

26. *Id.* Congress made clear that the deleted provisions "were either the cause of confusion as to the application of the DP[S]RA to certain nonsubscription services (especially webcasters) or which overlapped with the other exemptions (such as the exemption . . . for nonsubscription broadcast transmissions)." H.R. CONF. REP. NO. 105-796, at 80 (1998), *reprinted in* 1998 U.S.C.C.A.N. 639, 656.

27. H.R. CONF. REP. NO. 105-796, at 80 (1998), *reprinted in* 1998 U.S.C.C.A.N. 639, 656.

gress expanded the category of transmissions that would qualify for a statutory license. The exemption for "nonsubscription broadcast transmission[s]" was not amended.[28]

The DMCA amendment to section 114(d)(2) extended the statutory license umbrella for subscription broadcasts to cover certain eligible nonsubscription transmissions.[29] "Eligible nonsubscription transmissions" are defined in section 114(j)(6).[30] The DMCA amendment divides section 114(d)(2) into three subparagraphs. Subparagraph 114(d)(2)(A) dictates three conditions for a statutory license applicable to all nonexempt subscription and eligible nonsubscription transmissions.[31] Subparagraph (B) includes provisions applicable only to "nonexempt subscription transmissions" made by a preexisting subscription service in the same transmission medium as was used by the service on July 31, 1998.[32] Subparagraph (C)(i) eliminates the requirements of conformity with the sound performing complement[33] for retransmissions of over-the-air broadcast transmissions "by a transmitting entity that does not have the right or ability to

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28. 17 U.S.C. § 114(d)(1)(A) (Supp. 2001).

29. *See* 2 MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT § 8.22[d][3]; *see also* 17 U.S.C. § 114(d)(2) (Supp. 2001).

30. H.R. CONF. REP. NO. 105-796, at 87 (1998), *reprinted in* 1998 U.S.C.C.A.N. 639, 663. The Conference Report requires that "[e]ligible nonsubscription transmission" meet the following criteria:

> First, the transmission must be noninteractive and nonsubscription in nature. Second, the transmission must be made as part of a service that provides audio programming consisting in whole or in part of performances of sound recordings. Third, the purpose of the transmission service must be to provide audio or entertainment programming, not to sell, advertise, or promote particular goods or services.).

Id.

31. The conditions pertinent to this discussion are that :

> retransmissions by a transmitting entity must not have the right or ability to control the programming of the broadcast station making the broadcast transmission, to the extent that such identifying information was included in the original broadcast transmission and to the extent that it is technically feasible for the transmitting entity to retransmit that information.

17 U.S.C. § 114(d)(2)(A) (Supp. 2001).

32. *Id.* § 114(d)(2)(B).

33. The "sound recording complement" is "the performance in any three-hour period of three selections from a single record album, with no more than two selections transmitted consecutively, or of four selections by a single featured artist or from a single boxed set, with no more than three transmitted consecutively." H.R. REP. NO. 104-274, at 21 (1995).

control the programming of the broadcast station making the initial broadcast transmission, subject to two limitations."[34]

The DMCA also includes an ephemeral recording exemption that permits a transmitting organization to make one copy of a sound recording without infringing any copyrights.[35]

3. *Rulemaking Authority of an Administrative Agency*

The Administrative Procedure Act ("APA") reflects a broad determination by Congress to subject the decisions of government agencies to review by the courts.[36] Although courts maintain the final word on interpretations of law, they often defer to an administrative agency's interpretation of its enabling legislation. Courts defer to an agency's interpretation particularly when Congress has empowered the agency, either implicitly or explicitly, to interpret the laws the agency enforces, and the agency has done so over a period of time.[37]

A court reviewing an agency's construction of a statute that it administers must apply the following two-prong analysis. A court must first ascertain whether "Congress has directly spoken to the precise question at issue."[38] If the intent of Congress is clear, the court's evaluation ends, and Congress' unambiguously expressed intent is given effect. "If the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute."[39] The final authority on a statute's interpretation and its applicability, whether constitutional or statutory, remains with the courts.[40]

More specifically, in determining the amount of deference courts give to an agency interpreting its own statute, "courts have looked to the degree

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34. Ronald H. Gertz, *Client Memo Re: Text of Sections 114 and 112 of the Copyright Act as Amended*, 640 PLI/PAT 75, 80 (March 12, 2001); *see also* 17 U.S.C. § 114(d)(2)(C) (Supp. 2001) (listing the two limitation to subparagraph (C)(1) as: (1) retransmissions in digital format that regularly exceed the sound recording performance complement are not eligible for a statutory license, and (2) retransmission broadcast transmissions that violate the sound performance complement on a weekly basis not be eligible for a statutory license).

35. 17 U.S.C. § 112(a)(1) (Supp. 2001). This copy can only be used "for the transmitting organization's own transmissions within its local service area, or for purposes of archival preservation or security." *Id.* § 112(a)(1)(B).

36. 5 U.S.C. § 701 (1994).

37. United States v. Mead Corp., 121 S.Ct. 2164 (2001).

38. Chevron v. Natural Res. Def. Council, 467 U.S. 837, 842 (1984).

39. *Id.* at 843.

40. 5 U.S.C. § 706 (1994).

of the agency's care, its consistency, formality, and relative expertness, and to the persuasiveness of the agency's position."[41] Implicit delegation of authority to an agency can also be apparent:

> from the agency's generally conferred authority and other statutory circumstances that Congress would expect the agency to be able to speak with the force of law when it addresses ambiguity in the statute or fills a space in the enacted law, even one about which 'Congress did not actually have an intent' as to a particular result.[42]

When the circumstances exist to give an agency rulemaking authority, a court reviewing an agency decision may not reject an agency's interpretation "simply because the agency's chosen resolution seems unwise, but it is obliged to accept the agency's position if Congress has not previously spoken to the point at issue and the agency's interpretation is reasonable."[43]

B. Webcasting Technology

Music broadcast on the Internet can be divided into three music delivery models: 1) AM/FM Radio Webcasting, 2) Internet Webcasting, and 3) Personalized Internet Webcasting.[44] Copyright law treats each music delivery model differently. Accordingly, the copyright holder's rights under each medium are different.

The first music delivery model, AM/FM Radio Webcasting, is the transmission of AM/FM radio broadcast signals over the Internet by that radio station. AM/FM Radio Webcasting is the simultaneous transmission of the identical AM/FM broadcast signal without a playlist, skip forward function, method to influence playlists,[45] or search engine.

The second music delivery model, Internet Webcasting, includes music played solely to an Internet audience and third-party broadcasts of AM and FM radio station transmissions.[46] Internet Webcasting is not interactive or on-demand. Some Internet Webcasters have a format similar to that

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41. *Id.*

42. *Mead*, 121 S.Ct. at 2171.

43. *Id.* at 2172.

44. Different commentators have used different names for these delivery models.

45. Except through traditional means, such as calling the radio station and making a "request" or "dedication."

46. A radio station website such as KIISFM.com also falls into this category. KIISFM.com offers chats with listeners, as well as videos and concert tickets, on the web. AM/FM radio stations that create Internet-only programs also fall into this category.

of an AM/FM broadcaster, which includes a predetermined format. Other Internet Webcasters have skip forward functions and playlists.[47]

Personalized Internet Webcasting, the third model, is the music delivery model closest to Professor Paul Goldstein's "Celestial Jukebox."[48] This model includes musical services which require a subscription or payment, are on-demand,[49] or are interactive.[50] For example, a user can hear a whole radio show of only one artist for a three-hour period.[51] Listen.com is an example of a subscription service that permits a user to listen to on-demand, commercial-free Internet radio programming.[52]

II. CASE SUMMARY

A. Facts and Procedural History

In *Bonneville*, AM and FM radio station broadcasters brought an action against the Recording Industry Association of America ("RIAA") and the Copyright Office.[53] Previously, the RIAA had petitioned the Copyright Office to adopt a rule "clarifying that a broadcaster's transmission of its AM or FM radio station over the Internet is not exempt from copyright

47. For example, Listen.com is broken up by genre such as electronica, country, jazz, and folk. It also contains tour dates and other information. Users who click on oldies can then choose between "Beach Boys and similar artists" or "the Doors and similar artists." *Copyrighted Webcast Programming on the Internet: Hearing Before the Subcomm. on Courts and Intellectual Prop. of the House Comm. on the Judiciary*, 106th Cong. 119 (2000) (statement of Hilary Rosen, President, Recording Industry Association of America).

48. The "celestial jukebox" is a metaphor that expresses the possibilities of the future: "a technology-packed satellite orbiting thousands of miles above Earth, a subscriber's order-like a nickel in the old jukebox, and the punch of a button-to connect him to any number of selections from a vast storehouse via a home or officer receiver." PAUL GOLDSTEIN, COPYRIGHT'S HIGHWAY: FROM GUTENBERG TO THE CELESTIAL JUKEBOX 199 (1995).

49. An "on-demand" service is a musical service that allows a user to hear a particular artist "on demand."

50. An "interactive" musical service allows a user to narrowly tailor particular music preferences.

51. Launch.com and MTVi allow users to click a button if they do not like a song; the use never has to hear the song again. Christopher Jones, *True Consciousness of Stream*, WIRED, Apr. 6, 2000, *available at* http://www.wired.com/news/technology/0,1282,35122,00.html.

52. Brad King, *Songs Arrive in the Key of Fee*, WIRED, Dec. 3, 2001, *available at* http://www.wired.com/news/mp3/0,1285,48734,00.html.

53. Bonneville Int'l v. Peters, 153 F. Supp. 2d 763 (E.D.P.A. 2001).

liability under section 114(d)(1)(A)."[54] The RIAA also contended that until the Copyright Office made such a ruling, "the parties [would] not agree on who qualifies for the Section 114 performance license" and thus who should attend the rate setting arbitration panels.[55] On March 16, 2000, the Copyright Office published a notice of proposed rulemaking, finding for the RIAA. On December 21, 2000, the Copyright Office denied the National Association of Broadcaster's ("NAB") motion to suspend the rulemaking, and announced that "a transmission by an FCC-licensed broadcaster of its AM or FM radio broadcast over the Internet is not exempt from the limited public performance right for digital transmissions under section 114(d)(1)(A)."[56]

B. The Copyright Office's Administrative "Final Rule"

Rejecting the Broadcaster's assertions that the Copyright Office's previous decisions were not as expansive as its decision in *Bonneville*,[57] the Copyright Office stated that it does have the authority to make such a final rule. Amending the rule as urged by the RIAA, the Copyright Office held that Congress intended the exemption for "nonsubscription broadcast transmission" to apply only to radio stations transmitting their signals "over the air" made within the broadcasters' local service area.[58] The Copyright Office relied on its

> responsibility to conduct CARP ["Copyright Arbitration Royalty Panel"] proceedings to establish rates and terms for the section 114 license, as provided in section 114 itself and chapter 8 of the

54. Public Performance of Sound Recordings, 65 Fed. Reg. 77,292 (Dec. 11, 2000) (codified at 37 C.F.R. pt. 201.35).

55. *Id.* Accordingly, the Copyright Office postponed the pending rate adjustment proceeding. The purpose of these proceedings "is to set the rates and terms for the public performance of a sound recording by means of digital audio transmissions under the section 114 statutory license and to establish the rates and terms for the making of an ephemeral recording in accordance with the section 112 statutory license." *Id.* The Copyright Arbitration Panel ("CARP") proceedings, which set the rates, are adversarial in nature. It is crucial that all interested parties and users are represented so that the panel can have a complete evidentiary record to render its decision. *Id.* at 77294.

56. *Id.*

57. *Id.*

58. *Id.* at 77,297. The Copyright Office construed the statute narrowly, citing Tasini v. New York Times Co., 206 F.3d 161, 168 (2d Cir. 2000), for the proposition that "any doubt must be resolved against the one asserting the exemption" to preserve the purpose of the provision. *Id.*

> Copyright Act, and the [Copyright] Office's general rulemaking authority granted by section 702 of the [Copyright] Act.[59]

According to the Copyright Office, an agency is allowed to complete its action "where the function of the agency and the particular decision sought to be reviewed involve the exercise of discretionary powers granted the agency by Congress, or require application of special expertise."[60] The Copyright Office also stated that its extensive history of administering and interpreting the Copyright Act,[61] and the necessity of a full and complete record by the CARP proceedings, required that all parties subject to section 114 be identified.[62]

Accordingly, the Copyright Office construed the meaning of "broadcast transmission"[63] to include only over-the-air transmissions made by an FCC-licensed broadcaster.[64] The term "Service" was amended by the Copyright Office to reflect its determination that "any entity that transmits an AM/FM radio station over a digital communications network is subject to the terms of the statutory license set forth in 17 U.S.C. § 114(d)(2)."[65] Dissatisfied with this outcome, the radio station broadcasters sought judicial review of the Copyright Office's administrative "final rule."[66]

C. The District Court's Decision

On appeal, the District Court of the Eastern District of Pennsylvania summarily adjudicated the case in favor of the defendants, and held that the Copyright Office did have the statutory authority to promulgate such a rule.[67] The district court ruled that the Copyright Office's rulemaking was reasonable and that the district court would have independently reached

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59. *Id.* at 77,293,294 (noting that if the "Broadcasters' position were accepted, the Copyright Office's ability to administer section 114 of the Copyright Act will be frustrated.").

60. *Id.* at 77,294 (quoting Miss Am. Org. v. Mattel, Inc., 945 F. 2d 536, 540 (2d Cir. 1991)).

61. *Id.* at 77,294. The Register of Copyrights gave as examples the "definition of gross receipts under section 111 license" and the establishment of "filing regulations for SMATV systems under section 111." *Id.*

62. *Id.* at 77,295.

63. The NAB argued that the pivotal element of the definition of "broadcast transmission" is the designation of the nature of the entity making the transmission. Since an FCC-licensed broadcast station makes the transmission, the method of transmission does not matter. *Id.* at 77,297.

64. *Id.* at 77,301.

65. *Id.*

66. Bonneville Int'l v. Peters, 153 F. Supp. 2d 763 (E.D.P.A. 2001).

67. *Id.*

the same conclusion as the Copyright Office.[68] Basing its decision on the standard set forth in *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*,[69] the district court held that Congress delegated to the Copyright Office interpretive authority over section 114 of the Copyright Act.[70]

With respect to the first prong of the *Chevron* standard,[71] the district court concluded that Congress had not directly addressed the issue of whether AM/FM Radio Webcasters are exempt from the public performance right in section 106 of the Copyright Act.[72] Thus, the district court stated that it was required to defer to Copyright Office's determination if it was reasonable.[73]

Analyzing the statutory language, the Copyright Office concluded that Congress did not intend the term "nonsubscription broadcast transmission" to include AM/FM Webcasting.[74] The court held that a facial reading of the statute, as well as the legislative history of both the 1995 and 1998 amendments to the Copyright Act, demonstrated that it was not likely that Congress even considered the streaming of AM/FM broadcasts, let alone exempted such activities from the public performance rights of section 106.[75] The court reasoned that the term "terrestrial" requires an over-the-air transmission as evinced by Congressional testimony stating that "free over-the-air broadcasts are available without subscription, do not rely on interactive delivery, and provide a mix of entertainment programming and other public interest activities to local communities to fulfill a condition of the broadcasters' license."[76] The court also concluded that the phrase "licensed as such by the [FCC]" did not refer to the nature of the transmitting entity; rather, Congress chose the words to refer to over-the-air broadcasting, a type of transmission. Examining the legislative history, the court noted that the exemption was enacted before the rise of AM/FM Webcasting, and that it was not likely that Congress foresaw such activity.[77] Furthermore, the court stated that Congress never mentioned any other type of

68. *Id.*

69. 467 U.S. 837 (1984). An implicit delegation of power to an administrative agency by Congress would allow the agency "to speak with the force of law when it addresses ambiguity in the statute." United States v. Mead Corp, 121 S.Ct. 2164, 2172 (2001).

70. *Bonneville*, 153 F. Supp. 2d at 772.

71. *See supra* notes 38-39 and accompanying text.

72. *Bonneville*, 153 F. Supp. 2d at 775.

73. *Id.* at 779.

74. *Id.* at 774.

75. *Id.* at 776.

76. *Id.* at 780 (quoting H.R. REP. NO. 104-247, at 13 (1995).

77. *Bonneville*, 153 F. Supp. 2d at 781.

transmission made by an FCC-licensed broadcaster, other than over-the-air transmissions.[78]

The court agreed with the Copyright Office that defining "nonsubscription broadcast transmission" to include streaming of AM/FM broadcasting would conflict with provisions of the DPSRA and the DMCA. Section 114(d)(1)(A) states that a retransmission of a nonsubscription broadcast cannot be retransmitted beyond a 150 mile radius from the site of the radio broadcast transmitter.[79] The court concluded that this provision demonstrates that Congress intended only local retransmission of over-the-air radio broadcasts, and not AM/FM streaming.[80] Where the statute states an exception to the 150 mile limitation,[81] the court concluded that a portion of the statute requiring FCC licensure necessarily limits the geographic area within which the retransmission can extend, and thus it cannot be global.[82]

Finding further conflicts between the contentions of the radio stations and the Copyright Act, the district court affirmed the Copyright Office's finding that a definition of "nonsubscription broadcast transmission" that includes streaming of AM/FM broadcasting is inconsistent with the Copyright Act's ephemeral recording provisions in section 112.[83] Section 112 permits a transmitting organization to make one copy of the transmission embodying the performance, so long as "the copy or phonorecord is used solely for the transmitting organization's own transmissions within its local service area."[84] The court concluded that the limitation to a local service area makes streaming around the world through the Internet incompatible with the section 112(a)(1) exemption.[85] Since a streaming broadcast is not eligible for the section 112(a)(1)(B) exemption, the court ruled that the broadcaster would have to obtain a statutory license under section 112(e) to make ephemeral copies.[86] However, a broadcaster streaming its broadcast on the Internet is also not eligible to obtain a section 112(e)

78. *Id.*

79. *Id.* at 782.

80. *Id.*

81. 17 U.S.C. § 114(d)(1)(B)(i)(I) (Supp. 2001) ("[T]he 150 mile limitation under this clause shall not apply when a nonsubscription broadcast transmission by a radio station licensed by the Federal Communications Commission is retransmitted on a nonsubscription basis by a terrestrial broadcast station, terrestrial translator, or terrestrial repeater licensed by the Federal Communications Commission.").

82. *Bonneville*, 153 F. Supp. 2d at 782.

83. *Id.*

84. *Id.*; 17 U.S.C. § 112(a)(1)(B) (Supp. 2001).

85. *Bonneville,* 153 F. Supp. 2d at 782.

86. *Id.*

ephemeral copy license. Section 112(e) ephemeral copy licenses are only available to those who meet the criteria for a section 114(f) statutory license, and are not available to those who fall under the section 114(d)(1)(A) nonsubscription broadcast transmission category.[87]

Finally, the court held that public policy considerations stated by the Copyright Office reinforce the court's finding that the section 114(d)(1)(A) exemption does not apply to broadcasters who stream their transmissions over the Internet. The court agreed with the Copyright Office's warning that allowing AM/FM radio stations to broadcast their transmissions on the Internet will give them "an unfair advantage in the webcasting market."[88] The Copyright Office also concluded that allowing AM/FM broadcasts to be streamed over the Internet would be incompatible with the goal of preserving the relationship between the record industry and broadcasters.[89]

Under the District Court's holding, the only exemption to the digital performance right is for traditional over-the-air broadcasts made by an FCC licensed broadcaster, limiting its broadcast within the geographically defined areas determined by the FCC.[90] Thus, AM/FM Radio Webcasters are subject to the statutory license set forth in section 114(d)(2).[91]

III. DISCUSSION

This Section demonstrates that, while not directly violating legal doctrine, the district court did not devote sufficient attention to the implications of its decision. Part III.A analyzes the district court's extension of *Chevron* deference to the Copyright Office without sufficient consideration of administrative law and its impact on the future of the Copyright Office, including separation of power issues. The next section illustrates that section 114 cannot be read without self-contradiction because Copyright Law has become increasingly complex. The final section suggests that section 114 should be revisited so as to exempt AM/FM Radio Webcasters.

87. *Id.*
88. *Id.* at 783.
89. *Id.*
90. *Id.*
91. *Id.*

A. It is Unclear whether the Copyright Office's Administrative "Final Rule" is binding under the *Chevron* Doctrine

Although Judge Schiller stated that he would have come to the same conclusion as the Copyright Office's administrative "final rule," it is still important to recognize the implications of this decision. If courts continue to give *Chevron* deference to Copyright Office decisions that are not customarily within the office's powers, the Copyright Office may have unilaterally created authority without sufficient legislative oversight. This may also have created separation of powers consequences.

It is not clear that the Copyright Office has been relegated the authority to interpret section 114 as it did in its administrative "final rule." In order to be binding, Congress must intend that the Copyright Office's interpretations bind the courts.[92] Furthermore, "[w]hen Congress enacts a statute to be administered by an agency, it has delegated to the agency resolution of all policy disputes that arise under that statute that Congress did not itself resolve."[93] According to Kenneth Culp Davis, the first step of the *Chevron* analysis involves deciding whether a dispute of policy, as opposed to law, exists.[94]

1. *Factors that Favor Expansion of the Copyright Office's Rulemaking Authority*

Many considerations support a reviewing court's deference to the Copyright Office's interpretation of section 114, as in *Bonneville*. The Digital Millennium Copyright Act codified the role of the Register of Copyrights as chief of the "hybrid entity that historically has performed both legislative and executive or administrative functions."[95] It is true that "Congress relies extensively on the Copyright Office to provide its technical expertise in the legislative process."[96] Congress did ask the Copyright Office to advise it during implementation of the DMCA, and gave additional rulemaking authority to the Register of Copyrights relating to the

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92. *See* Robert Anthony, *Which Agency Interpretations Should Bind Citizens and the Courts?*, 7 YALE J. ON REG. 1, 4 (1990).

93. KENNETH CULP DAVIS & RICHARD J. PIERCE JR., ADMINISTRATIVE LAW § 3.3 (3d ed. 1994).

94. *Id.* ("Like the Chevron Court, the Marbury Court recognized that issues of policy are to be resolved by the politically accountable Branches. . . . As long as the Court preserves the principle of legislative supremacy, as it did in *Chevron*, Congress can be relied upon to check the power of the Executive.").

95. H.R. CONF. REP. NO. 105-796, at 77 (1998), *reprinted in* 1998 U.S.C.C.A.N. 639, 653.

96. S. REP. NO. 101-268, 2d Sess., at 6 (1990), *reprinted in* 1990 U.S.C.C.A.N. 237, 241.

DMCA's anticircumvention features.[97] Yet, David Nimmer writes that "[t]hough courts frequently invoke their willingness to defer to Copyright Office practices, one gathers the impression that their deference ends as soon as their disagreement begins with the [Copyright] Office's position."[98] Perhaps *Bonneville* reflects a shift in the courts' thinking.[99]

2. *Case Law is Not Dispositive as to the Expansion of the Copyright Office's Rulemaking Authority*

Courts have found application of the *Chevron* doctrine to be a difficult task.[100] Case law is not dispositive as to whether a court should defer to an administrative "final rule" of the Copyright Office. Some of the Copyright Office's decisions have been afforded *Chevron* deference.[101]

No Supreme Court case, however, has held that the Copyright Office's interpretation is to be dispositive. In *De Sylva v. Ballentine*,[102] the Court did not defer to the interpretation of the Copyright Office. The Court stated that weight would ordinarily be given to the interpretation of an

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97. *See* JAY DRATLER JR., INTELLECTUAL PROPERTY LAW: COMMERCIAL CREATIVE, INTELLECTUAL PROPERTY § 5A.01 (2001) ("The DMCA's anti-circumvention provisions prohibit trafficking in measure to circumvent technological protection of copyrighted works, creating secondary liability for copyright infringement.").

98. *See* NIMMER, *supra* note 29, at § 7.26; Fonar Corp. v. Dominick, 105 F.3d 99, 105 (2d Cir. 1997); Marascalco v. Fantasy, Inc. 953 F.2d 469, 473 (9th Cir. 1991).

99. Some of the considerations set forth by the Copyright Office are not dispositive. The consequences of not having every party involved in an arbitration (CARP) is not as disastrous as made out by the district court. The fact that it is critical to a CARP that there be a full and complete evidentiary record which, if absent, would compromise the efficiency of the section 114 license, does not result in the court's finding that the Copyright Office could not exercise its duties and functions without the ability to interpret section 114. A separate CARP proceeding could be held for rates for AM/FM radio webcasters when the issue was resolved by the courts or Congress.

100. DAVIS & PIERCE, *supra* note 93, at § 3.6. ("Judges do not always agree as to its meaning and effect in a particular case but they almost invariably apply its two-step analytical framework to resolve disputes concerning the permissibly of agency construction of agency-administered statutes."). The Supreme Court sometimes "gives *Chevron* powerful effect, sometimes it ignores *Chevron*, and sometimes it characterizes the *Chevron* test in strange and inconsistent ways." *Id.*

101. For example, deciding whether a work is copyrightable, a determination the Register of Copyright makes on a daily basis. Those applying for copyright registration may obtain judicial review of the Register's decision under the Administrative Procedure Act. The Register of the Copyright Office's decisions have been given *Chevron* deference. *See, e.g.*, Custom Chrome, Inc. v. Ringer, No. 93-2634 (GK), 1995 U.S. Dist. LEXIS 9249, *12 (D.D.C. 1995); OddznOn Products, Inc. v. Oman, 924 F.2d 346 (D.C. Cir. 1991) (holding that a work of soft sculpture titled KOOSH ball did not have sufficient creativity beyond the object's basic shape to warrant copyrightability).

102. 351 U.S. 570 (1956).

ambiguous statute by the agency charged with its administration, but that in *DeSylva*, "the Copyright Office's explanation of its practice deprives the practices of any force as an interpretation of the statute, and we therefore do not rely on it in this instance."[103] On the other hand, the Court of Appeals for the District of Columbia Circuit has found "no reason to deny the Copyright Office's legitimacy in selecting, as the EPA did in *Chevron*, among those choices so long as the interpretation selected is reasonable."[104]

3. *The Expansion of the Register of Copyright's Rulemaking Authority may Create Separation of Powers Issues*

It is unclear whether the Copyright Office is an executive or legislative agency. The Copyright Office is an arm of the Library of Congress. The Register of Copyrights ("Register") is the head of the Copyright Office, and can be removed by the President.[105] However, removal by the President may not be much of a threat to the Librarian.[106]

The Fourth Circuit has found that the Librarian of Congress is an executive officer because of his appointment by the President.[107] On the other hand, some commentators have written that the Register and Librar-

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103. *De Sylva*, 351 U.S. at 577 (1956). In *De Sylva*, the district court held that the statement "the widow, widower, or children of the author if the author is not living," in 37 C.F.R. 1938 § 201.24(a), gave the widow rights before the children in renewal of a copyright after the author's death. *Id.*

104. Cablevision Sys. Dev. Co. v. Motion Picture Ass'n. of Am., Inc., 836 F.2d 599, 609 (D.C. Cir. 1988).

105. *See* Eltra Corp. v. Ringer, 579 F.2d 294, 300 (4th Cir. 1978); C.H. Dobal, *A Proposal to Amend the Cable Compulsory License Provision of the 1976 Copyright Act*, 61 S. CAL. L. REV. 699, 724 n.153 (1988) ("The Librarian is appointed by the President with the advice and consent of the Senate, and in theory may be removed by the President."). The Librarian of Congress reports to two congressional appropriations committees. *Id.* at 719.

106. Dobal, *supra* note 105, at 724 n.153 ("Yet, since 1897, Librarians have either served for life or voluntarily retired from Office.").

107. *Eltra*, 579 F.2d at 300. In *Eltra*, the court stated that the:

> Office of the Register of the Copyrights is not open to any charge that is violative of the Appointments Clause. The Register is appointed by the Librarian of Congress, who in turn is appointed by the President with the advice and consent of the Senate. By the nature of his appointment the Librarian is an 'Officer of the United States, with the usual power of such officer to appoint such inferior Officers [i.e., the Register], as [he] thinks proper.

Id.

ian are legislative officers.[108] In *Bowsher v. Synar*, the Office of the Comptroller General, was found to be unconstitutional because the Comptroller General was under the "control" of Congress.[109] Arguably, the expanded powers of the Librarian and the Register may result in Congress controlling the interpretation of the Copyright Act, a seemingly unconstitutional departure from the checks and balances system.

4. *The Copyright Office's Scope of Power Should be Defined by the Legislature*

There appears to be no statutory limit to the Register's range of duties.[110] The Copyright Act does not explicitly grant the Copyright Office the power to interpret the Copyright Act.[111] Congress should specifically authorize whether and how the Copyright Office should be afforded such rulemaking authority. The district court erred in finding that Congress has given the Copyright Office authority to interpret section 114 on the grounds that courts have deferred to the interpretation of the Copyright Office regarding issues of registration.[112]

Whether an AM/FM Radio Webcaster is exempt is not an issue of policy, but an issue of law for courts to decide. Thus, deferring to the Copyright Office on such issues of law is problematic because there does not seem to be a statutory limit on the Register's duties.[113] Nevertheless, it would be practical for the Library of Congress, as an expert agency, to have rulemaking authority over copyright issues so long as they are in accord with the intent of Congress. The future of the Copyright Office would be much more secure and stable were the legislature to define the powers, duties, and limits of the Copyright Office.

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108. Dobal, *supra* note 105, at 724 (noting that Congress views the Register and the Librarian as legislative officers, and that the Register and Librarian depend on Congress for appropriations and policy support).

109. 478 U.S. 714, 726 (1986) ("To permit an officer controlled by Congress to execute the laws would be, in essence, to permit a congressional veto."). Admittedly, in *Bowsher*, Congress had the power to remove the Comptroller General; in this case an exercise of control occurs nonetheless.

110. 17 U.S.C. § 702 (1994) ("The Register of Copyrights is authorized to "establish regulations not inconsistent with the law for the administration of the functions and duties made the responsibility of the Register under this title.").

111. Dobal, *supra* note 105, at 724 ("[T]hese powers seems to have been appropriated without legislative authority.").

112. Even though courts defer to the Copyright Office's decisions regarding registration, courts are not required to defer to Copyright Office decisions regarding unrelated matters such as the interpretation of section 114.

113. *See* 17 U.S.C. § 702 (1994).

B. Section 114 is Contradictory Regardless of How it is Read

The complexity of section 114 has been discussed by academics.[114] As a practical matter, because an AM/FM RadioWebcaster does not qualify for the "nonsubscription broadcast transmission" exemption, the decision in *Bonneville* leaves the AM/FM Radio Webcaster with four unsatisfactory alternatives: 1) qualify for a statutory license, 2) negotiate separate agreements with copyright owners, 3) allow a third party to retransmit the radio station's broadcast, or 4) cease transmitting its broadcast over the Internet.

To qualify for a statutory license, the AM/FM Radio Webcaster must not exceed the sound performance complement.[115] Thus, the AM/FM Radio Webcaster would not be able to simply retransmit its original broadcast with ease. The AM/FM Radio Webcaster would be forced to change the content of its traditional over-the-air station.[116] Furthermore, abiding by the sound recording complement will result in a radio station that cannot play the songs by the most popular musicians more than once in any three-hour period.

The second alternative, entering into voluntary negotiations, is equally burdensome. The AM/FM Radio Webcasters would be required to enter into voluntary negotiations with every recording artist whose music they want to play. This takes a great amount of time and effort. Since this is voluntary, artists may not allow a radio station to play their music or exact fees that are economically untenable.

The third alternative is for the AM/FM radio station Webcaster to license a retransmitter, such as broadcast.com, who would then have the burden of complying with the compulsory license or obtaining licenses from the performing artists. Many in the radio industry have stated that

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114. David Nimmer, *Ignoring the Public, Part I: On the Absurd Complexity of the Digital Audio Transmission Right*, 7 UCLA ENT. L. REV. 189 (2000); *see* R. Anthony Reese, *Copyright and Internet Music Transmissions: Existing Law, Major Controversies, Possible Solutions*, 55 U. MIAMI. L. REV. 237, 239 (2001).

115. The "sound recording complement" is "the performance in any three-hour period of three selections from a single record album, with no more than two selections transmitted consecutively, or of four selections by a single featured artist or from a single boxed set, with no more than three transmitted consecutively." H.R. REP. NO. 104-274, at 21 (1995).

116. *See* 17 U.S.C. § 114(d)(2)-114(d)(2)(C)(i) (Supp. 2001) ("[A]n eligible nonsubscription transmission . . . shall be subject to statutory licensing . . . if . . . the transmission does not exceed the sound performance complement.").

Congress could not have intended for this to be the practical result of the DMCA.[117]

The fourth alternative is to abandon webcasting altogether. "Many radio stations have pulled the plug on their online broadcasts, citing . . . the possibility of having to pay royalties for their music."[118] It is not likely that Congress intended to place such an onerous burden on radio stations when it manifested its intent to "provide copyright holders of sound recordings with the ability to control the distribution of their product by digital transmission . . . without imposing new unreasonable burdens on radio and television broadcasters, which often promote, and appear to pose no threat to, the distribution of sound recordings."[119]

Congress was willing to grant copyright owners full control only where there existed the risk of a loss to record sales.[120] Congress granted a public performance right, then severely limited it even when the risk of loss to record sales did not exist. This explains why nonsubscription broadcast transmissions are exempt,[121] while some are subjected to a compulsory license[122] and others only to a voluntary license.[123] The purpose of

117. *See* Ronald Gertz, *Radio Internet Streaming and the DMCA*, 2 E-COMMERCE L. REP. 8, at 3 (Feb. 2000); Bob Kohn, *A Primer on the Law of Webcasting and Digital Music Delivery*, 20 ENT. L. REP. 4 (1998).

118. John Borland, *Court Rules That Radio Must Pay Online Fees*, CNET, Aug. 2, 2001, *at* news.cnet.com/news/0-1005-200-6765199.htm.

119. S. REP. NO. 104-128, at 15 (1995), *reprinted in* 1995 U.S.C.C.A.N. 356, 366.

120. H.R. REP. NO. 104-274, at 19 ("The limited right created by this legislation reflects changed circumstances that is, the commercial exploitation of new technologies in ways that may change the way prerecorded music is distributed to the consuming public.").

121. *Id.* at 14 (noting that the DPSRA contains exemptions for "nonsubscription transmissions (i.e., transmissions not controlled or limited to particular recipients or for which no consideration is required to be paid), *such as* nonsubscription broadcast transmissions by radio and television stations . . . unless they are part of an interactive service.").

122. H.R. REP. NO. 105-796, at 85 (1998), *reprinted in* 1998 U.S.C.C.A.N. 639, 661. Subsection (f)(2) directs that rates and terms examine criteria including "the quantity and nature of the use of sound recordings, and the degree to which use of the service substitutes for or promotes the purchase of phonorecords by consumers." *Id.*

123. H.R. REP. NO. 104-274, at 14 (1995) ("The Committee believes that sound recording copyright owners should have the exclusive right to control the performance of their works are part of an interactive service, and so has excluded interactive services from these limitations on the performance right.").

the licenses and exemptions is to ensure that transmissions do not approach interactivity, which would detract from record sales.[124]

Section 114 of the Copyright Act cannot be read as a harmonious whole, regardless of how it is interpreted. The ephemeral recording exemption conflicts with other portions of section 114. For example, the legislative history is not clear on what exactly is meant by the "local service area" requirement and what mediums of transmission falls into this category. A transmitting organization may have a broadcast transmitter almost everywhere in the United States, making section 112(a)(1)(B) superfluous in some situations.[125]

Finally, the DMCA was not sufficiently debated before Congress, and was mainly a compromise between the RIAA and Digital Media Association ("DiMA"). The RIAA and DiMA had competing interests until the two groups made an effort to reach a compromise before the Register of Copyrights on July 23, 1998. The Register gave them until the end of that month to draft the legislation they were seeking. On August 31, 1998, the House of Representatives passed an amendment to the DMCA that included the groups' proposals.[126]

Congress should not fear that AM/FM Radio Webcasters would diminish record sales because they are not "interactive" or available "on demand."[127] Professor Eben Moglen stated that the National Associations of Broadcasters failed to specifically ask Congress to protect its royalty ex-

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124. *Id.* at 19 ("The limited right created by this legislation reflects changed circumstances that is, the commercial exploitation of new technologies in ways that may change the way prerecorded music is distributed to the consuming public.").

125. S. REP. NO. 105-190, at 21 (1998) ("The Committee believes that the ephemeral recording exemption should apply to broadcast radio and television stations when they make nonsubscription digital broadcasts permitted by the DP[S]RA.").

126. Kohn, *supra* note 117, at 5. Kohn notes:

> Within days, they reached an agreement that would (1) eliminate the exemption for webcasters set forth in Section 114(d)(1) of the Copyright Act, (2) add a compulsory license scheme for limited kinds of "eligible" transmissions (i.e., those made by webcasters having a profile of members of DiMA), and (3) add language to Section 112 that would make it clear that "eligible" webcasters could make ephemeral recordings of sound recordings for the purposes of facilitating their webcasts.

Id.

127. "The underlying rationale for creation of this limited right is grounded in the way the market for prerecorded music has developed, and the potential impact on that market posed by subscription and interactive services—but not by broadcasting or related transmissions." S. REP. NO. 104-128, at 13 (1995), *reprinted in* 1995 U.S.C.C.A.N. 356, 360.

emptions on the Internet.[128] The Internet community should not have fewer AM/FM Radio Webcasting stations to listen to simply because of this oversight.

C. Policy Favors an Exemption for AM/FM Webcasters

Had Congress thoroughly discussed and considered the status of AM/FM Radio Webcasters, it would have exempted them. AM/FM Radio Webcasting should be exempt from the public performance right so long as the transmission is simultaneous and does not allow for a playlist, a skipping forward function, or methods to influence playlists.[129] Such an exemption will likely benefit the recording industry in increased record sales. "[R]ecord companies spend millions of dollars on advertising and promotion to encourage broadcasters to play their records,"[130] and this mutually beneficial relationship ought to not be disturbed.[131]

The scope of the DPSRA was narrow, and transmissions that posed little threat to record sales were exempted from the sound recording performance right.[132] Upon hearing music on the radio, listeners would have to purchase phonorecords when they wanted to listen to music on demand. As had occurred with previous advances in recording devices, the DPSRA sought to curtail illegal copying. The DPSRA was enacted because of fears that digital technology posed.[133] AM/FM radio webcasters should not

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128. Featherly, *supra* note 14.

129. Except through traditional methods, such as calling the radio station and making a "request" or "dedication."

130. Scott Bain, *Federal Court Rejects FCC-Licensed Broadcasters' Claim of Copyright Exemption for Internet Streaming*, METRO. CORP. COUNS., at 9 (Sept. 2001).

131. Copyright law has a difficult task, to "achieve a finely tuned balance: providing authors and publishers enough control over their work that they are motivated to create and disseminate, while seeking to limit that control so that society as a whole benefits from access to the work." COMPUTER SCI. AND TELECOMM. BD. NAT'L RESEARCH COUNCIL, THE DIGITAL DILEMMA: INTELLECTUAL PROPERTY IN THE INFORMATION AGE (2000) [hereinafter DIGITAL DILEMMA].

132. 17 U.S.C. § 114(d)(1) (Supp. 2001); H.R. REP. NO. 104-274 at 14 (1995) ("This legislation is a narrowly crafted response to concerns that . . . subscription and interaction audio services might adversely affect sales of found recordings.").

133. H.R. REP. NO. 104-274, at 19 (1995). "The limited right created by this legislation reflects changed circumstances that is, the commercial exploitation of new technologies in ways that may change the way prerecorded music is distributed to the consuming public." DIGITAL DILEMMA, *supra* note 131, at 46. Because of these increases in technology "[i]ndividuals find themselves capable of reproducing vast amounts of information, in private, using commonplace, privately owned equipment. A single individual can now do in private what once would have required substantial commercial equipment and perhaps criminal intent." *Id.*

be covered by the DPSRA's narrow scope because AM/FM Radio Webcasts are not likely to be copied.

The DMCA's purpose is to facilitate the development of electronic commerce and maintain strong protection for intellectual property.[134] The legislative history of the DMCA does not discuss AM/FM Radio Webcasting, but it does state that the deletion of two DPSRA exemptions does not "affect the exemption for nonsubscription broadcast transmissions."[135] The DMCA also makes it a crime to circumvent technology used to protect intellectual property. Hence, it is apparent that the concern of the DMCA and DPSRA is with illegal copying of copyrightable works and not with establishing a level playing field between Internet webcasters and AM/FM Radio Webcasters.[136] The intention in securing the rights of authors and performers is to provide incentives to support the greater good, not to be an end in itself.[137]

The district court's analysis did not give sufficient attention to the differences between Internet Webcasters and AM/FM Radio Webcasters. The policy of copyright law only balances fair compensation to the author as secondary to the public benefit.[138] AM/FM radio broadcasters have as their primary market, and thus their primary concern, their "over-the-air listeners."[139] Airwaves only reach a certain distance, which results in between 20 and 50 radio stations in any particular geographic area.[140] To

134. H.R. REP. NO. 105-551, at 28 (1998).

135. H.R. CONF. REP. NO. 105-795, at 80 (1998), *reprinted in* 1998 U.S.C.C.A.N. 645, 669.

136. Ronna Abrahmson, *Court Deals Webcasters a Royal(ty) Blow*, THE STANDARD.COM, Aug. 2, 2001, *at* http://www.thestandard.com/article/0,1902,28450,00.html (noting that DiMA Executive Director Jonathan Potter stated DiMA is concerned with "the anti-competitive impact if broadcasters who were webcasting had an advantage over Webcasters that were Webcasting").

137. Feist Publ'ns v. Rural Tel. Servs., 499 U.S. 340, 349-50 (1991); Sony Corp. of Am. v. Universal City Studios, 464 U.S. 417, 429 (1984); Twentieth Century Music Corp. v. Aiken, 422 U.S. 151, 156 (1975) ("The primary objective in conferring the Copyright monopoly is the general benefit received by the public from the work of authors. When the literal terms of the Copyright Act are rendered ambiguous, it must be construed in light of the primary objectives of conferring the Copyright monopoly.").

138. *See Aiken*, 422 U.S. at 156.

139. Reese, *supra* note 114, at 239 ("Over-the-air broadcasters typically need to appeal to a large enough audience to generate significant advertising revenues; on the other hand, Webcasters may be able to target much smaller niche audiences, thus offering music that would not generally be accessible through radio broadcasting.").

140. Sue Cummings, *Internet Radio Offers a Wide Choice to a Slim Audience*, N.Y. TIMES, Oct. 25, 2000, at 35.

survive, an AM/FM radio station must cater to a broad audience[141] and receive revenue through advertising, which results in stations having a wider variety of music.[142] Thus, a listener with a particular preference in music might have to listen to music not of their choosing.[143]

With AM/FM Radio Webcasters, the incentive remains to purchase records.[144] AM/FM Radio Webcasters listeners will find themselves in the same bind of having to choose between broad spectrums of music.[145] The economics of AM/FM Radio Webcasting work the same way as they do for over-the-air broadcasting, a symbiotic relationship between the record companies and the radio stations who "promote these songs to 75 percent of Americans who listen to the radio each day."[146] If the time comes when the lines between radio and the Internet completely blur, or if AM/FM Radio Webcasting threatens to replace the sale of recorded music, this issue should be revisited.

IV. CONCLUSION

Bonneville illustrates that the increasing complexity of the Copyright Act coupled with advances in technology which require secure rights has created much uncertainty. The Copyright Act should be revisited to clarify the ambiguities discussed in this Note. As technology continues to advance, more issues will arise and possibly inhibit growth of beneficial technologies and services. The purpose and history of the Copyright Act, and the traditional, mutually beneficial relationship between radio station

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141. *See* Eric Slater, *Broadcasting on the Internet: Legal Issues For Traditional and Internet-Only Broadcasters*, 6 MEDIA L. & POL'Y 25, 37 (1997) (stating that Internet-only broadcasters are able to broadcast "more narrowly focused music formats that are not likely to appear on conventional radio, such as industrial, reggae, disco, and punk rock").

142. Reese, *supra* note 114, at 239.

143. Slater, *supra* note 141, at 40. ("In addition to programming mainstream radio formats such as country, modern rock, and classical, [Internet-only broadcasters are] cybercasting more narrowly focused music formats that are not likely to appear on conventional radio, such as industrial, reggae, disco, and punk rock."); Reese, *supra* note 114, at 238 ("'Webcasting' can provide listeners with far greater variety of music than can traditional broadcasters.").

144. Furthermore, Internet webcasters do not only play Oldies, but break this genre down to sub-genres, making it possible to cater to a particular user's tastes.

145. This rule does have exceptions, however, including small country music stations in certain parts of the country.

146. *Copyrighted Webcast Programming on the Internet: Hearing Before the Subcomm. on Courts and Intellectual Prop. of the House Comm. on the Judiciary*, 106th Cong. 140 (2000) (statement of Edward O. Fritts, President, National Association of Broadcasters).

broadcasters and the RIAA, should not be disturbed. The exemption of AM/FM Radio Webcasters would benefit the public and not impact record sales, the historical basis of protection for sound recordings.

If Copyright Office decisions are to bind courts, the legislature should define the powers, duties and limits of the Copyright Office. This would create greater stability and certainty, and ensure that the Copyright Office does not overstep any of its boundaries.

A&M RECORDS, INC. V. NAPSTER, INC.

By Lisa M. Zepeda

Copyright owners in the music industry have long feared that technological developments would transform the existing market, effectively eliminating the demand for the product or service upon which they are financially dependent.[1] In balancing the exclusive rights granted to copyright owners with the public interest in access to new technology, courts have largely weighed in favor of allowing new technologies, provided that they are capable of some legitimate use.[2]

Due to the novelty and complexity of the technology involved, *A&M Records, Inc. v. Napster, Inc.*[3] presents new problems for traditional copyright law.[4] This Note contends that the district court misapplied the substantial noninfringing use defense established by the Supreme Court in *Sony Corporation of America v. Universal City Studios, Inc.*,[5] and in effect, limited the scope of the original analysis. This Note also examines Napster's defense under the Digital Millennium Copyright Act[6] ("DMCA"), focusing on Napster's eligibility for protection under the safe harbor provisions. Last, this Note discusses possible implications *Napster* will have on the music industry's current distribution models.

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1. *See*, e.g., Ariel Berschadsky, RIAA v. Napster: A Window onto the Future of Copyright Law in the Internet Age, 18 J. Marshall J. Computer & Info. L. 755, 785 (2000) ("In the 17th century the emergence of lending libraries was seen as the death knell of book stores; in the 20th century, photocopying was seen as the end of the publishing business, and videotape the end of the movie business.").

2. *See* Jessica Litman, *Napster, Inc., v. A&M Records, Inc.: Amended Brief Amicus Curiae of Copyright Law Professors in Support of Reversal*, 645 PLI/PAT 727, 738 (2001).

3. *See* 239 F.3d 1004 (9th Cir. 2001); 114 F. Supp. 2d 896 (2000); 54 U.S.P.Q.2d 1746 (2000).

4. *See generally*, Shawn D. Chapman, *Pushing the Limits of Copyright Law and Upping the Ante in the Digital World: The Strange Case of A&M Records, Inc. v. Napster, Inc.*, 89 KY. L.J. 793, 808 (2001) (Noting that in 1999, Napster, Inc. introduced peer-to-peer file sharing, a technology that enables individuals to transfer digital music files directly to one another over the Internet). The music industry feared that Napster would allow widespread Internet-based piracy of their copyrighted works. Napster also threatened the music industry's traditional business paradigms, which have yet to embrace an Internet-based method of music distribution). *Id.*

5. 464 U.S. 417 (1984).

6. 17 U.S.C. § 512 (1998).

I. BACKGROUND

A. The Advent of Digital Audio Recording Technology

MPEG-3 (abbreviated "MP3") technology allows individual computer users to copy an audio compact disc directly onto their hard drive by compressing the information on the disc into the MP3 format.[7] This technology allows users to copy an original recording with almost no deterioration in sound quality regardless of the number of copies made.[8] The compressed format of MP3 files also enables users to rapidly transmit digital audio files from one computer to another by electronic mail, or to download files available through the Internet onto individual computer hard drives.[9] Consequently, MP3 files have become a popular mode for the distribution of digital music through the Internet.[10]

B. The Napster Peer-to-Peer File Sharing Technology

Napster, Inc., an Internet service, operates a system allowing the transmission and retention of digital audio files between and among its users.[11] Unlike previous systems that allowed transmission through a centralized server, the Napster system allows its users to connect directly to one another via the Internet.[12] In conjunction with Napster's network servers and server-side software, Napster's MusicShare software[13] allows users to make MP3 files stored on personal computer hard drives available for copying by other Napster users.[14] To transfer a copy of a requested MP3 file, the Napster server-side software directly connects the requesting and host computers and then transmits the MP3 file to the requesting computer.[15] The MP3 files transferred between users do not pass through Nap-

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7. *See* Recording Indus. Ass'n of Am. v. Diamond Multimedia Sys., Inc., 180 F.3d 1072, 1074 (9th Cir. 1999).

8. *See id.*

9. *See* Ines G. Gonzalez, *Recording Industry Association of America, Inc. v. Diamond Multimedia Systems, Inc.*, 15 BERKELEY TECH. L.J. 67, 70 (2000).

10. *Id.* at 71.

11. *See* I. Fred Koenigsberg, *Music, The Internet, and the Music Industry*, 616 PLI/PAT 117, 125 (2000).

12. *See id.*

13. *A&M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004, 1011 (9th Cir. 2001). To access the Napster system, a user must first download the MusicShare software, available free from Napster's Internet site. *Id.*

14. *Id.* at 1011.

15. *Id.* at 1012. (The Napster system facilitates the connection of the users' hard drives by providing the searching user's computer with the Internet Protocol address of the host user. The searching user's computer then uses the address information to create a

ster's servers at any point during the process, and Napster does not obtain copies of the transferred files.[16]

C. The Controversy Over MP3 and Peer-to-Peer File Sharing Technology

The music industry has expressed concern over the use of MP3 and peer-to-peer file sharing technology to create unauthorized, high-quality copies of commercially prepared recordings.[17] They fear consumers may stop purchasing commercial recordings if they can conveniently download the same music through the Internet without charge.[18] They are also concerned that these developments will curb their ability to control distribution channels[19] and introduce new artists to the consumer market.[20] MP3 and peer-to-peer file sharing technology have substantially reduced the music industry's traditional influence by allowing new artists to promote and distribute their music directly to consumers in the format of a downloadable MP3.[21] These innovations also expand consumers' choice of music because they can now locate and download music that was largely unavailable through traditional modes of distribution.[22]

D. Secondary Copyright Infringement

The Internet and related technologies have made it difficult to hold direct infringers liable for copyright infringement.[23] Since Internet systems often obscure individual user identities, copyright owners may not be able to identify infringing users, or distinguish infringers from other users.[24]

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direct connection to the host user's hard drive so that the requested file may be downloaded from the host's hard drive to the searching user's hard drive). *Id.*

16. *Id.*

17. *See* Chapman, *supra* note 4, at 804.

18. *See* Gonzalez, *supra* note 9, at 71.

19. *See* Heather D. Rafter, *Streaming Into the Future: Music and Video Online*, 611 PLI/PAT 395, 398 (2000). (In the past, a small group of large recording companies have dominated the sale of music to consumers. Five recording companies control approximately eighty percent of the popular music industry: BMG Entertainment, Sony Music, Warner Music Group, EMI Recorded Music, and Universal Music Group).

20. *See* Gonzalez, *supra* note 9, at 71.

21. *Id.*

22. *See* Note, *Exploitation Publishers, Untrustworthy Systems, and the Dream of a Digital Revolution for Artists*, 114 HARV. L. REV. 2438, 2449 (2001).

23. *See* Seth D. Greenstein, *Copyright in the Age of Distributed Applications* 9 (2000), *available at* http://www.tprc.org/abstracts00/copywriteage.pdf.

24. *Id.*

Moreover, the vast number of users and market considerations often make litigation against direct infringers an impractical method of enforcement.[25]

Copyright owners have therefore brought suit against Internet service providers ("ISPs") for assisting a third party to infringe their copyrights.[26] A defendant may be secondarily liable for copyright infringement based on the theories of contributory and vicarious infringement.[27] A contributory infringer is "one who, with knowledge of the infringing activity, induces, causes or materially contributes to the infringing conduct of another."[28] In contrast, a vicarious infringer has the right and ability to supervise the infringing activity and derives a direct financial benefit from the activity.[29]

E. Protection Under the DMCA

In 1998, Congress enacted the DMCA in response to the growing concerns of ISPs over their potential liability for the copyright infringement of their users.[30] The DMCA strives to adapt concepts of copyright law to emerging technologies that utilize and distribute copyrighted works.[31] The Act created four safe harbor provisions[32] which shelter qualifying ISPs from copyright liability when users of the service engage in infringing activities.[33] These protections extend to direct, contributory, and vicarious copyright infringement.[34] Under the safe harbor provisions, ISPs will not

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25. *Id.*

26. *Id.*

27. *Id.*

28. *A&M Records, Inc. v. Napster, Inc.*, 114 F. Supp. 2d 896, 918 (9th Cir. 2000) (quoting Gershwin Publ'g Corp. v. Columbia Artists Mgmt., Inc., 443 F.2d 1159 (2d Cir. 1971)).

29. *Id.* at 920.

30. David Nimmer, *A Riff on Fair Use in the Digital Millennium Copyright Act*, 148 U. PA. L. REV. 673, 674 (2000).

31. *See id.* at 681.

32. 17 U.S.C. § 512 (1998) (The DMCA provides four non-exclusive safe harbors for qualifying ISPs. Each provision addresses a different ISP function: (a) Transitory digital network communications: Provides protection for an ISP "transmitting, routing, or providing connections for, material through a system or network controlled or operated by or for the service provider . . . "; (b) System Caching: Limits the liability of a an ISP for caching, defined as the "temporary storage of material on a system or network"; (c) User storage: Protects an ISP who stores, at the direction of a user, material on a system controlled or operated by the ISP; (d) Information location tools: Protects an ISP for referring or linking users to an on-line location containing infringing material or activity).

33. *See generally* Jonathan A. Friedman, *Using the Digital Millennium Copyright Act to Limit Potential Copyright Liability Online*, 6 RICH. J.L. & TECH. 18 (2000).

34. 17 U.S.C. § 512 (1998).

be held liable for monetary damages and most injunctive relief pertaining to copyright infringement.[35]

To qualify for protection under the DMCA, a defendant must fit one of two definitions of service provider.[36] It must be either "an entity offering the transmission, routing, or providing of connections for digital online communications, between or among points specified by a user, of material of the user's choosing, without modification to the content of the material as sent or received,"[37] or "a provider of online services or network access, or the operator of facilities therefore. . . ."[38] The critical difference between these definitions is that an ISP qualifying under the first definition may invoke any of the four safe harbor provisions, while an ISP that only qualifies under the second definition is restricted to using provisions (b) through (d).

A defendant must also fulfill two additional conditions to qualify for protection.[39] First, the ISP must adopt, reasonably implement, and inform its users of a termination policy for users found to be repeat infringers.[40] Second, it must accommodate "technical measures that are used by copyright owners to identify or protect copyrighted works."[41]

II. CASE SUMMARY

In December 1999, several record companies and music publishers[42] filed a complaint against Napster, Inc. in the District Court for the Northern District of California alleging, among other claims, contributory and vicarious copyright infringement.[43] In response, Napster asserted the affirmative defenses of fair use and substantial noninfringing use.[44] Napster

35. *Id.*

36. John W. Belknap, *Copyright Law and Napster*, 5 J. SMALL & EMERGING BUS. L. 183, 193 (2001).

37. 17 U.S.C. § 512(k)(1)(A).

38. *Id.* at § 512(k)(1)(B).

39. *Id.* at § 512(i).

40. *Id.* at § 512(i)(1)(A).

41. *Id.* at § 512(i)(1)(B).

42. The plaintiffs include the following recording companies: A&M Records, Geffen Records, Interscope Records, Sony Music Entertainment, MCA Records, Atlantic Recording Corp., Island Records, Motown Records Co., Capital Records, La Face Records, BMG d/b/a The RCA Records Label, Universal Records, Elecktra Entertainment Group, Arista Records, Sire Records Group, Polygram Records, Virgin Records America, and Warner Bros. Records. *A&M Records, Inc. v. Napster, Inc.*, 114 F. Supp. 2d 896 (9th Cir. 2000).

43. *See id.* at 900.

44. *Id.* at 912.

also argued that the DMCA limited its liability for contributory and vicarious copyright infringement.[45]

The evidence demonstrated that the vast majority of the MP3 music files available on the Napster system were copyrighted.[46] The plaintiffs may own the copyrights to more than seventy percent of these files.[47] Napster did not own licenses to distribute, download, or to facilitate others in distributing or downloading any of the copyrighted music.[48] Consequently, the plaintiffs did not receive royalties or other forms of payment when Napster users uploaded or downloaded MP3 files to which they held the rights.[49]

A. The District Court Decision

In August 2000, the district court granted the plaintiffs' joint motion to preliminarily enjoin Napster "from engaging in, or facilitating others in copying, downloading, uploading, transmitting, or distributing plaintiffs' copyrighted musical compositions and sound recordings, protected by either federal or state law, without express permission of the rights owner."[50] The court held that the plaintiffs had established a prima facie case of direct copyright infringement by Napster users;[51] that the downloading and uploading of MP3 music files by Napster users did not constitute a fair use; and that the plaintiffs had established a likelihood of success on their contributory and vicarious copyright infringement claims.[52]

The district court rejected Napster's fair use defense, finding that all four fair use factors listed in section 107 of the Copyright Act weighed in favor of the plaintiffs.[53] The court also rejected Napster's specific claims

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45. *See id.* at 919 n.24

46. *Id.* at 902-903.

47. *Id.*

48. *Id.*

49. *Id.*

50. *Id.* at 927.

51. *Id.* at 911. The district court reasoned that the plaintiffs had sufficiently demonstrated ownership of the allegedly infringing MP3 files, and that Napster users violated two of their exclusive rights as copyright owners: the rights of reproduction and distribution. *Id.*

52. *Id.* at 920, 922.

53. *Id.* at 912. The Copyright Act provides that a fair use inquiry includes consideration of at least four factors: (1) the purpose and character of the use, including whether such use is commercial in nature or is for nonprofit educational purposes; (2) the nature of the copyrighted work; (3) the amount and substantiality of the portion used in relation to the copyrighted work as a whole; and (4) the effect of the use upon the potential market for or value of the copyrighted work. 17 U.S.C. § 107 (1994).

of fair use: sampling,[54] space-shifting,[55] and the authorized distribution of new artists' work.[56]

After establishing direct infringement by Napster users, the district court turned to the plaintiffs' contributory infringement claim.[57] First, the court found that Napster had both actual and constructive knowledge of direct infringement by its users.[58] Under the second element, the court found that Napster materially contributed to the infringing activity by providing support services that allowed its users to conveniently locate and download copyrighted files.[59]

The district court concurred with the plaintiffs' vicarious infringement claim.[60] The court determined that Napster satisfied the first element of the claim because it had the right and ability to supervise its system and block

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54. *Napster*, 114 F. Supp. 2d at 915. The district court reasoned that sampling was not a fair use in this context because it is commercial in nature and will likely have an adverse effect on the market for plaintiffs' copyrighted music. *Id.*

55. *Id.* at 915. Space-shifting occurs when a Napster user makes copies of files she already owns to facilitate their use in another medium. *Id.*

56. *Id.* at 917. The district court rejected Napster's last fair use argument, which claimed that it was engaged in the "authorized promotion of independent artists." *Id.* Instead, the court believed that music by major recording artists was the primary feature of the service, and characterized the New Artist's Program as an afterthought. *Id.*

57. *Id.* at 918. As discussed above, a claim of contributory infringement has two elements: (1) the defendant has knowledge of the direct infringement, and (2) the defendant materially contributes to the infringement. *See supra* Part I.D.

58. *See id.* Plaintiffs demonstrated that Napster had actual knowledge of direct infringement because the RIAA notified it of more than 12,000 infringing files. *Id.* The court also determined that defendant had constructive knowledge of the infringing activity, citing evidence that Napster executives had previously enforced intellectual property rights in other law suits, they had downloaded infringing files to their personal computers using the system, and they had promoted the service using lists of the infringing files available on its system. *Id.*

59. *Id* at 919. The court analogized the Napster system to the swap meet in *Fonovisa, Inc., v. Cherry Auction, Inc. Id.* In *Fonovisa*, the owner of copyrights in musical recordings brought various claims, including a claim for contributory infringement, against the operators of a swap meet based on the sales of counterfeit recordings by independent vendors at the meets. *Id.* The operators materially contributed to the infringing activity by providing support services such as space, utilities, parking, advertising, and clientele to the vendors. *Id.* at 920. In *Napster*, the district court emphasized that "Napster supplies the proprietary software, search engines, servers, and means of establishing a connection between users' computers." *Id.*

60. As previously discussed, a claim of vicarious infringement has two elements: (1) the defendant has the right and ability to supervise the infringing activity, and (2) the defendant obtains a direct financial benefit from the infringing activity. *See supra* Part I.D.

those users accused of repeat infringement.[61] However, Napster failed to exercise this ability to prevent infringing activities.[62] The court found for the plaintiffs on the second element because Napster received a direct financial benefit from the availability of copyrighted music files on its system.[63] The infringing files acted as a "draw" for users, thereby increasing the userbase and securing Napster's potential future revenues.[64]

The district court then addressed Napster's argument for protection under the DMCA in two separate opinions.[65] In the first opinion, the court denied Napster's motion for summary judgment based on the section 512(a) safe harbor provision of the DMCA.[66] For purposes of summary judgment, the court assumed, but did not hold, that Napster was an ISP under the first, broader definition of service provider.[67] However, the court determined that Napster failed to satisfy the additional requirements for protection under the DMCA.[68] First, Napster did not qualify as an ISP under section 512(a) because it did not "transmit, route, or provide connections through its system."[69] Rather, the Internet provided the connection between system users.[70] Second, the court noted that even if Napster had qualified as an ISP under section 512(a), genuine issues of material fact existed concerning Napster's compliance with section 512(i), which imposes additional requirements for protection under any of the DMCA safe harbor provisions.[71]

In the second opinion, the district court rejected Napster's argument for protection under the section 512(d) safe harbor provision.[72] The court stated that section 512(d) excludes from protection any defendant with ac-

61. *Napster*, 114 F. Supp. 2d at 920.

62. *Id.*

63. *Id.* at 921.

64. *See id.* (relying on the Ninth Circuit's vicarious liability analysis in *Fonovisa*, where the court determined that a financial benefit exists when the availability of infringing material acts as a draw for customers).

65. *See Napster*, 54 U.S.P.Q.2d 1746 (2000) (Napster's motion for summary judgment); *Napster*, 114 F. Supp. 2d 896 (2000) (district court opinion).

66. *Napster*, 54 U.S.P.Q.2d 1746.

67. *Id.* at 1749 n.5 (This definition provides that the term service provider as used in section 512(a) of the DMCA "means an entity offering the transmission, routing, or providing of connections for digital online communications, between or among points specified by a user, of material of the user's choosing, without modification to the content of the material as sent or received").

68. *See id.* at 1752.

69. *Id.*

70. *Id.*

71. *See id.*

72. *See Napster*, 114 F. Supp. 2d at 919 n.24.

tual or constructive knowledge of the infringing works or activity, and, therefore, does not shelter contributory infringers.[73] Since Napster had both actual and constructive knowledge of its users' infringing activities, the court held that it did not qualify for protection under this safe harbor provision.[74]

B. The Ninth Circuit Decision

Napster appealed the preliminary injunction to the Court of Appeals for the Ninth Circuit.[75] Although the Ninth Circuit largely affirmed the district court's rulings,[76] it diverged from the lower court's reasoning on several important issues.

Under the contributory liability analysis, the Ninth Circuit emphasized that Napster may be "capable of commercially significant noninfringing uses."[77] It reasoned that the district court improperly focused the analysis on the system's current uses, disregarding its capabilities and future uses.[78] Regarding the vicarious liability analysis, the Ninth Circuit agreed that Napster financially benefited from the availability of infringing files on its system and that it had the right and ability to supervise its system.[79] However, the Ninth Circuit noted that the architecture of the system might limit the defendant's ability to police the system since Napster does not examine the files for content.[80] Despite this limitation, it emphasized that Napster maintains the duty of policing the file name indices for infringing works.[81]

On the issue of Napster's defense under the DMCA, the Ninth Circuit concluded that the balance of hardships weighed in favor of the plaintiffs, supporting the issuance of a preliminary injunction.[82] However, it disagreed with the district court in finding that Napster's potential liability for secondary copyright infringement renders the DMCA inapplicable.[83] It

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73. *Id.*
74. *Id.*
75. *See A&M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004 (9th Cir. 2001).
76. *Id.* at 1027. The Ninth Circuit agreed that the plaintiffs would likely succeed on their contributory and vicarious copyright infringement claims, but remanded the case with instructions to reduce the scope of the preliminary injunction, which it determined was too broad. *Id.*
77. *Id.* at 1021.
78. *Id.*
79. *See id.* at 1024.
80. *Id.*
81. *Id.*
82. *Id.* at 1025.
83. *Id.*

ultimately concluded that this issue would develop more fully at trial and that significant questions remained as to the applicability of the DMCA to Napster.[84]

The Ninth Circuit remanded the case with instructions to modify the injunction.[85] The preliminary injunction was overbroad because Napster had to bear the entire burden of preventing infringing activity on its system.[86] Instead, the Ninth Circuit instructed the district court to place the burden of notification on the plaintiffs.[87] Accordingly, the plaintiffs must notify Napster of the presence of specific infringing files on its system before Napster has the duty to discontinue access to the infringing materials.[88] Napster is also required to police its system to the extent technologically possible.[89]

III. DISCUSSION

This Note discusses Napster's substantial noninfringing use defense to contributory copyright infringement. In effect, the *Napster* decision modified and limited the original *Sony* analysis[90] by applying an inappropriately narrow view of the defense, and by imposing a lack of knowledge requirement into the analysis. This Note also considers Napster's defense under the DMCA, and analyzes the scope of the protections afforded by the DMCA safe harbor provisions against contributory and vicarious copyright infringement. It examines whether Napster has complied with the DMCA's copyright compliance policy and notification requirement. Finally, this Note discusses the impact Napster may have on the direction of the music industry, which may drive music companies to alter their traditional business paradigms to accommodate an online form of distribution.

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84. *Id.*
85. *Id.* at 1027.
86. *Id.*
87. *Id.*
88. *Id.*
89. *Id.*
90. *Sony*, 464 U.S. 417 (In *Sony*, the Court decided that the manufacturers of videocassette recorders could not be held liable for contributory copyright infringement, even if they knew some consumers would use the equipment for infringing purposes, as long as the equipment also had substantial noninfringing uses.).

A. The Substantial Noninfringing Use Defense

The Supreme Court first applied the staple article of commerce doctrine[91] to copyright law in the landmark *Sony* decision.[92] In *Sony*, the owners of television program copyrights argued that the manufacturers and suppliers of home videocassette recorders ("VCRs") should be held liable for consumers' unauthorized copying of their broadcasted programs.[93] The Court refused to impose liability, despite evidence demonstrating that the VCRs were capable of being used to infringe copyrighted television programs.[94] It primarily relied on a modified staple article of commerce doctrine from the Patent Code in reaching this conclusion.[95] As applied to copyright law, when a new technology functions as an instrument for infringement but is also capable of substantial noninfringing uses, the act of providing the technology to consumers does not constitute contributory copyright infringement.[96] The defendants in *Sony* satisfied this standard by demonstrating that the VCR was capable of "private, non-commercial time-shifting in the home."[97]

1. *Narrow View of the Substantial Noninfringing Use Defense*

In *Napster*, the district court improperly restricted the *Sony* analysis to the infringing primary uses of the system, discounting the system's noninfringing capabilities.[98] The court refused to apply *Sony* to this case because the principal role of the Napster system was to facilitate the unauthorized copying and distribution of established artists' music, and was not widely used for noninfringing purposes.[99] It reasoned that the Napster system's infringing uses outweighed its noninfringing uses.[100] The court seems to have misstated the inquiry under *Sony*, which asks only whether the technology is capable of commercially significant noninfringing uses.[101] Although the Court in *Sony* did not identify what percentage of

91. *Id.* at 440 (The Patent Code explicitly states that the sale of "a staple article or commodity of commerce suitable for substantial noninfringing use is not contributory infringement.").

92. *See Sony*, 464 U.S. 417.

93. *Id.*

94. *Id.*

95. *See supra* note 91.

96. *Id.* at 442.

97. *Id.* A user is "time-shifting" when she uses a VCR to record a program in order to watch it later. *Id.*

98. *Napster*, 239 F.3d at 1021.

99. *Napster*, 114 F. Supp. 2d at 917.

100. *See id.*

101. *See Napster*, 239 F.3d at 1021.

noninfringing uses must be found commercially significant to avoid liability, the language used by the Court suggests a low threshold.[102]

In accord with *Sony*, the appropriate use analysis considers not only principal uses, but all current and future capabilities of the technology.[103] As with the VCR, Napster is capable of being used for the legitimate purpose of copying and distributing authorized recordings.[104] Making noncommercial copies of copyrighted recordings for personal use also constitutes a noninfringing fair use.[105] Although these uses may comprise a relatively small percentage of the system's actual uses, they nonetheless require consideration under the *Sony* analysis.

The district court reasoned that the injunction was consistent with the Court's holding in *Sony* because it permitted Napster to continue operating for only noninfringing uses.[106] The court emphasized that noninfringing uses of the system, such as "chat rooms or message boards, the New Artist Program or any distribution authorized by rights holders" were not covered by the injunction.[107] Again, the district court seems to have misapplied the holding in the *Sony* decision, which established that new technologies with legitimate uses should not be enjoined, even though they are capable of infringing uses.[108] As one commentator observed, "the district court's analysis is tantamount to a holding that Sony could market VCRs only if it could ensure that the VCRs were never used to commit infringement."[109] Accordingly, if on remand, the district court determines that the Napster system is capable of significant noninfringing uses, Napster should not have the burden of ensuring that its system is only used for noninfringing purposes.

2. *Lack of Knowledge Requirement*

In *Sony*, the Court refused to impute knowledge for purposes of contributory liability merely because the defendant produced equipment capa-

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102. *See Sony*, 464 U.S. at 444 (The Court in *Sony* emphasized, "Whatever the future percentage of legal versus illegal home-use recording might be, an injunction which seeks to deprive the public of the very tool or article of commerce capable of some noninfringing use would be an extremely harsh remedy, as well as one unprecedented in copyright law.).

103. *See id.*

104. *Napster*, 114 F. Supp. 2d at 917.

105. *Id.* at 915.

106. *Id.* at 917.

107. *Id.*

108. *See Sony*, 464 U.S. at 442.

109. Litman, *supra* note 2, at 749.

ble of both infringing and substantial, noninfringing uses.[110] The Court held that general knowledge of infringing uses would not support a claim of contributory infringement.[111] Under this standard, most ISPs and peer-to-peer file sharing operators lack the requisite level of knowledge, since it is nearly impossible for them to monitor all the file content located on their systems.[112] MP3 files are particularly difficult to filter since they generally lack indicators distinguishing between legitimate and infringing uses.[113] Further, even if an MP3 file does contain infringing works, a system user can easily conceal its content by assigning alternative names to the file.[114] Due to these architectural difficulties, ISPs and Napster-like systems generally do not have knowledge of specific acts of copyright infringement.

The Ninth Circuit determined that *Sony*'s holding is of "limited assistance" to Napster because it had actual and constructive knowledge of direct infringement by its users.[115] It concluded that "sufficient knowledge exists to impose contributory liability when linked to demonstrated infringing use of the Napster system."[116] However, under the *Sony* analysis, the defendant's knowledge of infringement is irrelevant if the defendant's equipment is capable of commercially significant noninfringing uses.[117] In effect, the Ninth Circuit diverged from the original analysis by inserting a lack of knowledge requirement.[118] This modification fails to acknowledge that the substantial noninfringing use doctrine establishes more than a rebuttable presumption of a lack of knowledge; rather, it is an affirmative defense to contributory infringement.[119] The Ninth Circuit's holding ultimately reduces the scope of the original *Sony* defense by requiring that ISPs demonstrate both that their systems are capable of substantial noninfringing uses, and that they lack knowledge of direct infringement by their users.

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110. *Sony*, 464 U.S. at 436.
111. *Id.*
112. *See* Greenstein, *supra* note 23, at 20.
113. *Id.*
114. *Id.*
115. *Napster*, 114 F. Supp. 2d at 918 (The district court held that Napster had actual notice of direct infringement because the RIAA had informed it of more than 12,000 infringing files.).
116. *Id.*
117. *Sony*, 464 U.S. at 442.
118. *See Napster*, 114 F.Supp.2d at 918.
119. *See* Chapman, *supra* note 4, at 821.

3. *New Technological Developments*

The decision in *Sony* suggests that courts should be cautious when using copyright law to stifle new technological developments. While peer-to-peer file-sharing technology is still in its infancy, a ruling that would suppress this development would be inconsistent with the fundamental objective of copyright law, which strives to "stimulate artistic creativity for the public good."[120] Since technology is often the means of bringing copyrighted works to the public, the public interest extends to the progress and exploitation of emerging technologies. Because one technological development generally serves as the building block for the next, a ruling that bars innovative technologies such as Napster could have far-reaching effects outside the scope of the immediate case. Moreover, copyright owners who initially view technological developments as a threat to their viability may eventually discover ways to exploit them. Although the plaintiffs in *Sony* once predicted that VCRs would destroy the market for motion pictures, the movie industry has since found ways to profit from the VCR through videocassette rentals and sales.[121] Similarly, further developments in peer-to-peer file sharing technology may enable the music industry to benefit from Napster-like systems.

B. Protection Under the DMCA

When the district court ruled on Napster's motion for summary judgment, Napster argued, and the plaintiffs agreed, that Napster qualified as an ISP under the first, broader definition of the term.[122] This finding allowed Napster to use any of the four safe harbor provisions.[123] However, to qualify for protection under the DMCA, Napster must have complied with the two preliminary requirements of the statute, and must have met each element of the relevant safe harbor provision.[124] In denying Napster's motion for summary judgment, the district court concluded that section 512(a) of the DMCA did not apply to Napster.[125] Since the safe harbor provisions are nonexclusive, whether an ISP qualifies for one safe harbor provision does not affect a determination of whether that ISP qualifies under any other provision.[126] Alternatively, Napster argued for protection

120. *Sony*, 464 U.S. at 432 (quoting Twentieth Century Music Corp. v. Aiken, 422 U.S. 151, 156 (1975)).

121. *See* Berschadsky, *supra* note 1, at 785.

122. *Napster*, 54 U.S.P.Q.2d at 1749.

123. *See* 17 U.S.C. § 512(k)(1)(A).

124. Belknap, *supra* note 36, at 193.

125. *Napster*, 54 U.S.P.Q.2d at 1753.

126. 17 U.S.C. § 512(n).

under section 512(d), which applies to information location tools, including directories, indexes, references, pointers, or hypertext links.[127] As noted by the district court, section 512(d) imposes more rigorous eligibility requirements than section 512(a).[128]

1. DMCA Protection Against Secondary Copyright Liability

The district court gave Napster's defense under section 512(d) nominal consideration in precluding the issuance of a preliminary injunction.[129] Since this section excludes qualifying ISPs with actual or constructive knowledge of the infringing activity from protection, the district court broadly concluded that section 512(d) did not shelter contributory infringers.[130] The Ninth Circuit disagreed with this per se rule, noting that Napster's eligibility for protection under the DMCA would be developed more at trial.[131]

a) Contributory Liability

Although the DMCA purportedly protects against direct, contributory, and vicarious liability, the protections afforded to ISPs by section 512(d) are, in effect, limited against claims of contributory and vicarious copyright infringement.[132] Contributory infringement requires two elements: that the defendant knows or has reason to know of direct infringement, and that the defendant materially contributes to the infringing activity.[133] However, an ISP is ineligible for protection under section 512(d) if it has actual or constructive knowledge of infringing activity and fails to promptly remove or disable access to the infringing material.[134] Consequently, if an ISP possesses the requisite knowledge to impose contributory liability, it is ineligible for protection under section 512(d). Napster may have originally chosen to classify itself under section 512(a) in order to avoid the knowledge prong of this provision. In effect, the more demanding eligibility requirements under this safe harbor provision create a disincentive for ISPs to characterize themselves under this provision.

127. *Id.* at § 512(d).
128. *Napster*, 54 U.S.P.Q.2d at 1750.
129. *See Napster*, 114 F. Supp. 2d at 919 n.24.
130. *Id.*
131. *Id.*
132. *See* 17 U.S.C. § 512(d).
133. *Id.* at 918.
134. 17 U.S.C. § 512(d)(2).

b) Vicarious Liability

Vicarious liability exists if the defendant has a financial interest in the infringing activity, and the right and ability to supervise that activity.[135] The district court and the Ninth Circuit both found that Napster had an explicit reservation of rights policy, thereby demonstrating that it had the right and ability to control the activities of its users.[136] They also determined that Napster financially benefited from the infringing activity.[137]

According to the DMCA, an ISP does not qualify for the section 512(d) safe harbor provision if it receives "a financial benefit directly attributable to the infringing activity, in a case in which the service provider has the right and ability to control such activity."[138] These elements are essentially identical to those required for the imposition of vicarious liability. Since Napster was found to satisfy both elements of vicarious infringement, this finding effectively rendered Napster ineligible for protection under section 512(d).

2. *The Copyright Compliance Policy*

Assuming that Napster qualifies as an ISP for the purposes of the DMCA, it must also demonstrate compliance with the requirements under section 512(i).[139] This section requires that ISPs adopt and implement a termination policy for users found to be repeat infringers.[140] Napster did not adopt a written copyright compliance policy until February 2000, approximately two months after the lawsuit was filed.[141] Napster, however, argued that section 512(i) does not specify when the policy must be enacted.[142]

The issue of when an ISP must adopt and implement a termination policy in order to qualify for protection under the DMCA remains unclear. As the district court noted, "Congress did not intend to require a service provider to investigate possible infringements, monitor its service or make difficult judgments as to whether conduct is or is not infringing."[143] This suggests that an ISP only loses protection if it becomes aware of and ig-

135. *Napster*, 239 F.3d at 1022.
136. *Id.* at 1023.
137. *Id.*
138. 17 U.S.C. § 512(d).
139. *Id.* at § 512(i).
140. *Id.*
141. *Napster*, 54 U.S.P.Q.2d at 1752.
142. *Id.*
143. *Id.*

nores "red flags" indicating blatant copyright infringement.[144] Since Congress has expressly stated that an ISP does not have to search its system for infringing users,[145] an ISP may not know or have reason to know that its users are engaged in infringement. In Napster's case, employing a termination policy after litigation begins is most likely insufficient proof of compliance with section 512(i). In contrast, it may be overly harsh to disallow an ISP any protection if it does not enact a termination policy at the outset of its operation. A more equitable standard may be to require ISPs to adopt and implement a termination policy only upon notification of specific infringing uses.

Section 512(i) also requires that the termination policy be "reasonable."[146] Napster had a policy of blocking an infringer's password so she could not use that password to access the system.[147] Since this policy did not bar the infringer's IP address from the system, a blocked user could access the system by changing her username and password.[148]

The plaintiffs argued that Napster should have blocked the IP addresses of known infringers.[149] This method may prove ineffective, however, since IP addresses are generally assigned at random when a user logs onto her ISP.[150] To block a user by her IP address would require blocking everyone who uses her ISP.[151] Further, a blocked user may circumvent this policy by signing up through another ISP.[152] Regardless, given that the legislature has not mandated how access should be terminated or how reasonable the policy must be to qualify for protection, Napster should not be disqualified from DMCA protection if there proves to be a more effective means of terminating repeat infringers. Therefore, Napster should be able to satisfy this requirement by blocking a user's password upon receiving proper notification.

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144. Jennifer E. Markiewicz, *Seeking Shelter from the MP3 Storm: How Far Does the Digital Millennium Copyright Act Online Service Provider Liability Limitation Reach*?, 7 COMMLAW CONSPECTUS 423, 439 (1999).

145. *See Napster*, 54 U.S.P.Q.2d at 1752.

146. 17 U.S.C. § 512(i).

147. *Napster*, 54 U.S.P.Q.2d at 1753.

148. *Id.*

149. *See* Anne Hiaring, *Copyright Infringement Issues on the Internet*, 617 PLI/PAT 455, 531 (2000).

150. *See* Berschadsky, *supra* note 1, at 780.

151. *Id.*

152. *Id.*

3. *The Notification Requirement*

In order to remedy the district court's broad preliminary injunction, the Ninth Circuit required the plaintiffs to give Napster notice of copyrighted works available on its system before Napster has the duty to disable access to the infringing content.[153] Although the plaintiffs retain the burden of notification, Napster has the burden of policing its system within the limits of the system's architecture.[154] Napster not only has the duty to remove infringing works upon receiving an explicit request to do so, but it also has the burden of monitoring its system to ensure that no additional copies of the infringing works appear.

In effect, the Ninth Circuit's decision requires ISPs to expend substantial resources to continuously monitor their systems for infringing material. This decision may have a particularly damaging effect on peer-to-peer file-sharing services, since individual users have control over the material they post and transmit over the Internet.[155] For example, users of Napster-like systems have the ability to alter the file names of copyrighted works, making the infringing files difficult to identify and subsequently remove.[156] Further, MP3 files are difficult to screen since they generally lack indicia differentiating between authorized and infringing uses.[157] The competing efforts of users and the ISP will lead to an almost endless series of policing efforts and evasive responses. Ultimately, if ISPs who maintain directories in peer-to-peer systems are assigned the responsibility of policing the use of available files and are held legally accountable for these uses, the overwhelming burden of such liability may render peer-to-peer technology infeasible.

C. Implications for the Future

While technological advances will make copyright infringement and piracy a continuing concern for the music industry,[158] one possible solution to these problems may be to adopt a new business model. Instead of challenging new technology with legal action, a more effective response may be to develop business paradigms that exploit these innovations. The music industry may be slowly moving in this direction, as evidenced by

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153. *Napster*, 239 F.3d at 1027.

154. *Id.*

155. Greenstein, *supra* note 23, at 20.

156. *Id.*

157. *Id.*

158. *See* Amy Kover, *Napster: The Hot Idea of the Year*, FORTUNE (June 26, 2000), *at* http://www.fortune.com (Several other peer-to-peer file sharing services, such as Gnutella and Freenet, have surfaced in the wake of the Napster litigation).

on-going negotiations between Napster and plaintiff Bertelsman Music Group ("BMG").[159]

In October 2000, Napster and BMG agreed to develop a new business model using the peer-to-peer network.[160] This model would amount to a "pay-for-play" service, wherein users would be able to access music files for a monthly subscription fee and owners of the copyrighted works would receive royalties for this use.[161] Although the current agreement would only allow users to access music files owned by BMG, if the other four major recording companies[162] followed in this direction, subscribers will have much of the same selection as they once did on the Napster system. Regardless of whether other major recording companies choose to participate in an agreement with Napster, they will ultimately have to devise a more attractive distribution method than the one currently in place.

IV. CONCLUSION

In spite of its relative youth, the Internet has posed significant challenges for copyright law. As *Napster* illustrates, copyright owners confronted with Internet-related technological innovations have become increasingly concerned about the protection of their intellectual property rights. In addressing these concerns, courts must formulate an approach to copyright law that reflects the reality of constant technological development.

The *Napster* decision severely limited the *Sony* substantial noninfringing use defense to contributory copyright infringement. This result is inconsistent with the Court's holding in *Sony*, where an injunction is precluded if the technology at issue is capable of legitimate uses.[163] When new technology may be used for both legitimate and infringing purposes, the balance should weigh in favor of allowing the new technology.[164] By issuing a broad injunction, the *Napster* courts failed to recognize current

159. Maggie A. Lange, *Digital Music Distribution Technologies Challenge Copyright Law*, 45 APR. B. B.J. 14, 31 (2001).

160. *Id.*

161. *See* Ryan C.Edwards, *Who Said Nothing in this World is Free? A&M Records, Inc., v. Napster, Inc.: Problems Presented, Solutions Explored, and Answers Posed*, 89 KY. L.J. 835, 877 (2001).

162. *See* Rafter, *supra* note 19, at 398 (The five major recording companies include: BMG Entertainment, Sony Music, Warner Music Group, EMI Recorded Music, and Universal Music Group.).

163. *Sony*, 464 U.S. 417.

164. *See* Litman, *supra* note 2, at 744.

and future capabilities of the system, effectively allowing the suppression of this new technology.

The applicability of the DMCA safe harbors to Napster and qualifying ISPs remains unclear. Although the DMCA allegedly protects qualifying ISPs against direct, contributory, and vicarious copyright liability, uncertainties remain as to the scope of the protection offered by the DMCA against these claims. The DMCA is also vague in other critical areas, such as the copyright compliance policy and notification requirement. The ultimate decision in *Napster* may help to clarify ambiguities in the law by establishing appropriate standards for these provisions.

ADDITIONAL DEVELOPMENTS—COPYRIGHT

ALS SCAN, INC. V. REMARQ COMMUNITIES, INC.

239 F.3d 619 (Fed. Cir. 2001)

The Federal Circuit held that, under Title II of the Digital Millennium Copyright Act ("DMCA"), an Internet service provider may not rely on a claim of defective notice to maintain the immunity defense under the DMCA safe harbor provisions when provided with notice of infringing activity that substantially complied with DMCA.

ALS Scan, which creates and markets copyrighted adult photographs, brought suit against RemarQ, an Internet service provider ("ISP"), alleging that ALS Scan violated the DMCA and unfair competition laws. Specifically, ALS Scan claimed that RemarQ, which has the ability to filter information contained in its newsgroups and prevent its members from logging onto certain newsgroups, failed to prevent its members from posting material which violated ALS Scan's copyrights. ALS Scan alleged that RemarQ possessed actual knowledge that the newsgroups contained infringing material but had "steadfastly refused to remove or block access to the material." ALS Scan also alleged that it warned RemarQ about the infringing material contained in its database. In response, RemarQ stated that it was prepared to remove articles posted in its newsgroups, if the articles were specifically identified as infringing material. RemarQ further contended that it had a defense to ALS Scan's copyright infringement claim because of ALS Scan's failure to comply with the DMCA's notice requirements.

The district court granted RemarQ summary judgment, stating that RemarQ could not be held liable for direct copyright infringement merely because it provided access to a newsgroup containing infringing material. Further, RemarQ could not be held liable for contributory infringement because ALS Scan failed to comply with the notice requirement set forth in the DMCA.

ALS Scan appealed, claiming that it substantially complied with the notification requirements of the DMCA and that RemarQ did not have a "safe harbor" defense to copyright infringement. The Federal Circuit affirmed-in-part, reversed-in-part, and remanded for further proceedings. The court stated that because RemarQ was given notice in accordance with the DMCA, it did not have a safe harbor defense. Title II of the DMCA, the "Online Copyright Infringement Limitation Act," defines the limitations of liability for copyright infringement to which ISPs might otherwise be exposed. The liability-limiting provision applicable here, 17 U.S.C. § 512(c), gives ISPs a safe harbor from liability for "infringement of copyright by reason of the storage at the direction of a user of material that resides on a system or network controlled or operated by or for the service provider," if an Internet service provider meets all three of the safe harbor requirements: (1) lacks actual or constructive knowledge; (2) receives no financial benefit; and (3) responds expeditiously to remove or disable access to infringing material after receiving notification conforming with requirements under the DMCA. The court held that ALS Scan's written notice to RemarQ met the requirements of the DMCA. The court found that the DMCA did not require ALS Scan to list every instance of infringement in its cease and desist letter as long as it provided RemarQ with a representative list.

Therefore, the Federal Circuit reversed the district court's grant of summary judgment. Because the ruling only removed the safe harbor defense, the case was remanded for further proceedings on ALS Scan's copyright infringement claims and any other affirmative defenses that RemarQ may have.

FELTEN V. RECORDING INDUSTRY ASSOCIATION OF AMERICA, INC.

Case No. CV-01-2669 (GEB) (D.N.J. 2001)

At issue in this case is whether Section 1201 of the Digital Millennium Copyright Act ("DMCA") violates the First Amendment by impermissibly prohibiting scientists and engineers from doing research and publishing their findings. Judge Garrett Brown of the Federal District Court of New Jersey dismissed the case without hearing arguments and without giving reasons for his judgment. The plaintiff will appeal to the Third Circuit.

The Secure Digital Music Initiative Foundation ("SDMI"), a multi-industry consortium established to create specifications for the secure delivery of digital music, invited the digital community to break into certain watermark technologies. Plaintiffs, as part of their normal scientific research, participated in the challenge, defeating most of the technologies. Plaintiffs then sought to publish their findings at a scientific conference. Prior to publication, the SDMI, and the Recording Industry of America Association ("RIAA") threatened suit under the DMCA.

Section 1201 of the DMCA prohibits the circumvention of technological measures used to protect a work that is copyrighted, except in the case of a noninfringing use. Reverse engineering of computer programs is permitted: (1) if a copy of the program is legitimately obtained, and (2) to identify and analyze those elements of the program that are necessary to achieve interoperability of an independently created computer program with other programs, and that have not previously been readily available to the person engaging in the circumvention. Encryption research does not violate the DMCA when: (1) the researcher lawfully obtained the encrypted copy, phonorecord, performance, or display of the published work; (2) the act of encryption is necessary to conduct encryption research; (3) the researcher made a good faith effort to obtain authorization before the circumvention; and (4) the act of encryption does not violate any other law.

University Professor Edward Felten and his research team brought a preemptive suit against the Department of Justice, Verance, SDMI, and RIAA before the district court seeking a declaration that publication of their scientific research regarding technologies used to protect digital music from copyright infringement is protected by the First Amendment, and not a violation of the Digital Millennium Copyright Act (DMCA). Felten argued that by forcing scientists to obtain the permission of companies whose business interests might be harmed by scientific publication before publishing their research, the DMCA thwarts society's First Amendment interest in the benefits of free scientific inquiry and discourse.

The Justice Department argued that the case should be dismissed because it was not ripe. It argued that because SDMI and RIAA no longer seek to bring suit and permitted the plaintiff and his team to publish portions of their research, and because the researchers did not plan to do further research in this area, that there was no valid claim.

The court agreed with the Justice Department and dismissed the case without ruling on the First Amendment issue.

SUNTRUST BANK V. HOUGHTON MIFFLIN CO.

268 F.3d 1257 (11th Cir. 2001)

The United States Court of Appeals for the Eleventh Circuit reviewed the District Court for the Northern District of Georgia's grant of a preliminary injunction enjoining the publication and distribution of the fictional work, *The Wind Done Gone*, a work alleged to infringe the copyrighted work, *Gone with the Wind.*

In an attempt to critique and comment on *Gone with the Wind* and Margaret Mitchell's depictions of slavery and the Civil-War era in the American South, Alice Randall created *The Wind Done Gone.* In creating her work, Randall appropriated characters, plot devices, and major scenes from *Gone with the Wind*, but told parts of the story through the eyes of Cyana, the illegitimate daughter of a plantation owner and the slave who cares for his children. After discovering the similarities between *The Wind Done Gone* and *Gone with the Wind*, SunTrust, the trustee of the Mitchell Trust, asked the Houghton Mifflin Company to refrain from publishing or distributing the second work. Houghton Mifflin refused, and SunTrust subsequently filed an action alleging copyright infringement and motions seeking a temporary restraining order and a preliminary injunction. Finding that *The Wind Done Gone* infringed the copyright of *Gone with The Wind*, the district court applied the four-factor fair use analysis: (1) the purpose and character of the use, (2) the nature of the copyrighted work, (3) the amount and substantiality of the portion of the copyrighted work used, and (4) the potential market harm. After applying these factors, the district court determined that *The Wind Done Gone* constituted an unauthorized sequel of the copyrighted work and did not warrant fair use protection. Based on these decisions, the district court granted a preliminary injunction enjoining the publication and distribution of *The Wind Done Gone.*

Houghton Mifflin appealed the grant of the preliminary injunction to the United States Court of Appeals for the Eleventh Circuit. The appellate court reversed and remanded the district court's decision to grant a preliminary injunction. In order to merit a preliminary injunction, the plaintiff must prove (1) a substantial likelihood of success on the merits, (2) a substantial threat of irreparable injury if the injunction were not granted, (3) that the threatened injury to the plaintiff outweighs the harm an injunction may cause the defendant, and (4) that granting the injunction would not disserve the public interest. Finding that the parodic and transformative nature of *The Wind Done Gone* would likely result in fair use, the appellate court did not believe that the plaintiffs showed a substantial likelihood of success on the merits. Further, the appellate court found that any harm suffered by SunTrust due to the publication and distribution of *The Wind Done Gone* was not irreparable because monetary damages could remedy the potential harm. Thus, the appellate court held that a lack of irreparable injury to SunTrust, together with the likelihood of a fair use defense prevailing, rendered injunctive relief improper. The decision of the district court was therefore vacated.

UNIVERSAL CITY STUDIOS, INC. V. CORLEY

273 F.3d 429 (2d Cir. 2001)

The Second Circuit addressed the constitutionality of the Digital Millennium Copyright Act's ("DMCA") anti-trafficking provisions. These provisions prohibit trafficking in computer programs which circumvent technological measures designed to secure unauthorized access to digital works that are protected by federal copyright laws. The court held that the computer code used in the programs was protected speech. Applying intermediate scrutiny, the court also found that the anti-trafficking provisions were constitutional because they were content neutral and they targeted functional aspects of speech.

The defendant posted a copy of DeCSS, a program designed to circumvent the Content Scramble System ("CSS"), the encryption technology used by motion picture studios to prevent unauthorized viewing and copying of the DVD releases of their motion pictures, on his website. Corley also included links to other web sites where copies of DeCSS could be found. Several motion picture companies sought and won injunctions against Corley in the United States District Court for the Southern District of New York. The defendants appealed to the Second Circuit, challenging the constitutionality of the DMCA's prohibitions.

The Second Circuit affirmed the district court's decision. However, the court held that computer code and programs are a form of speech and thus qualify for First Amendment protection. The court applied intermediate scrutiny and upheld the DMCA's restrictions, which were aimed at the functional aspects of DeCSS, because they were content-neutral. In addition, the court emphasized that the combination of technologies such as the Internet and DeCSS dramatically increased the amount of harm caused by copyright infringement. The court also rejected defendants' contention that the DMCA prevents the fair use of copyrighted materials such as excerpts from motion pictures on DVD.

PURDUE PHARMA L.P. V. FAULDING INC.

By Limin Zheng

In *Purdue Pharma L.P. v. Faulding Inc.*,[1] the Federal Circuit invalidated the claims of a patent for lack of adequate written description.[2] The court found that the original specification failed to describe a later-amended claim limitation as being the "important defining quality" of the invention,[3] and thus failed to convey to one skilled in the art that the inventor was in possession of the invention at the time of the original filing.[4] This is the first time that the Federal Circuit has invalidated patent claims on written description grounds when the amended limitation *narrowed*, rather than *broadened*, the scope of the challenged claims.

While the court may have had justifiable concerns about abusive amendment practice, it failed to articulate a workable standard for the written description requirement. The court used a "defining quality" test that was explicitly rejected by its predecessor and was unwarranted by the purpose of the written description requirement. The decision, perhaps itself the result of an unstructured written description jurisprudence, added to the ever growing uncertainty as to how specific one's disclosure must be to survive the written description scrutiny, especially in cases of subgenus claims. Combined with the court's repeated practice of using the written description requirement to narrow the scope of chemical and biotechnology patents, the *Purdue Pharma* decision is likely to discourage inventors in the pharmaceutical industry from seeking patent protection. Further, the court's recent decisions signal its willingness to overlook the distinction between predictable and unpredictable arts when imposing a stringent written description requirement. As such, the harm of a standardless and unworkable written description requirement goes beyond the chemical and biomedical fields, and threatens to weaken patent rights in general.

1. 230 F.3d 1320 (Fed. Cir. 2000).
2. *Id.* at 1322.
3. *Id.* at 1327.
4. *Id.* at 1324-26.

I. BACKGROUND

A. The Statutory Written Description Requirement

The goal of the U.S. patent system is to promote the progress of science and technology.[5] To that end, limited monopoly rights, in the form of patents, are granted to inventors in exchange for a full and early disclosure of the inventions.[6] To obtain a valid patent, the claimed invention must be useful, novel, nonobvious, and adequately disclosed in the patent application.[7]

The first paragraph of section 112 of the Patent Act of 1952 sets forth the statutory requirement for an adequate disclosure:

> The specification shall contain a written description of the invention, and of the manner and process of making and using it, in such full, clear, concise, and exact terms as to enable any person skilled in the art to which it pertains, or with which it is most nearly connected, to make and use the same, and shall set forth the best mode contemplated by the inventor of carrying out his invention.[8]

On its face, the statutory purpose of the written description is to allow any person skilled in the art "to make and use the same" and to "set forth the best mode" of carrying out the invention.[9]

B. Judicial Interpretation of the Written Description Requirement

1. Written Description As a Separate Disclosure Requirement Independent of Enablement

Courts, however, have interpreted the first paragraph of section 112 as mandating three distinctive requirements: (1) the written description requirement; (2) the enablement requirement; and (3) the best mode re-

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5. U.S. CONST. art. I, § 8, cl. 8.

6. A patent granted in the United States is "for a term beginning on the date on which the patent issues and ending 20 years from the date on which the application for the patent was filed." 35 U.S.C. § 154(a)(2). As of November 29, 2000, a patent application will be published "after the expiration of a period of 18 months from the earliest filing date" for a subset of patents unless the applicant opts to seek patent protection only in the United States. Act of November 29, 1999, Pub. L. No. 106-113, Div. B, § 1000(a)(9), 113 Stat. 1536 (codified as amended at 35 U.S.C. § 122(b)(1)).

7. 35 U.S.C. §§ 101-103, 112.

8. 35 U.S.C. § 112, ¶ 1.

9. *Id.*

quirement.[10] The enablement requirement ensures effective teaching of the invention to the public to avoid "undue experimentation."[11] The best mode requirement is designed to prevent a patentee from concealing part of the invention while obtaining patent protection for the whole.[12]

The purpose of the written description requirement has evolved from serving as a notice to the public to functioning as a safeguard against overreaching by the inventors.[13] Historically, the written description was to "put the public in possession of what the [inventor] claims as his own invention" so as to warn an innocent purchaser or user of her infringement of the patent.[14] Since the enactment of the Patent Act of 1952, this purpose is fulfilled by a requirement to disclose claims as set forth in the second paragraph of section 112.[15]

Although no longer necessary as a notice, the written description requirement has been assigned a second function—to preclude patentees from later claiming what they did not possess at the time they filed their applications.[16] It has been standard practice for patent attorneys to file a patent application that broadly describes an invention, and later broaden or narrow the claims through amendments to reflect the results of follow-up research and/or to include a competitor's newly-developed variants.[17] The written description requirement serves to "convey with reasonable clarity to those skilled in the art that, as of the filing date sought, [the patentee] was in possession of the invention."[18]

In *In re Ruschig*,[19] the Federal Circuit's predecessor court promulgated a separate written description requirement independent of the enablement requirement in a patent case involving chemical arts.[20] The court found that section 112 required the patentees to "convey clearly to those skilled

10. *See* 3 DONALD S. CHISUM, CHISUM ON PATENTS § 7.01 (2001).

11. *In re* Wright, 999 F.2d 1557, 1561 (Fed. Cir. 1993).

12. *See In re* Gay, 309 F.2d 769, 772 (C.C.P.A. 1962).

13. *See* Vas-Cath, Inc. v. Mahurkar, 935 F.2d 1555, 1560-61 (Fed. Cir. 1991).

14. *Id.* at 1561 (citing Evans v. Eaton, 20 U.S. (7 Wheat.) 356, 433 (1822)).

15. 35 U.S.C. § 112, ¶ 2. The earlier patent statutes did not require an inclusion of the claims. *See Vas-Cath*, 935 F.2d at 1561.

16. *See Vas-Cath*, 935 F.2d at 1561 (quoting Rengo Co. v. Molins Mach. Co., 657 F.2d 535, 551 (3d Cir. 1981)).

17. *See* ROBERT P. MERGES ET AL., INTELLECTUAL PROPERTY IN THE NEW TECHNOLOGICAL AGE 225 (2d ed. 2000).

18. *Vas-Cath*, 935 F.2d at 1563-64.

19. 379 F.2d 990 (C.C.P.A. 1967).

20. *Id.* at 995-96.

in the art" that they invented the specific chemical compound claimed.[21] Later, in *In re DiLeone*,[22] the court held that "it is possible for a specification to enable the practice of an invention as broadly as it is claimed, and still not describe that invention."[23] However, the court's subsequent decisions often intermingled the written description requirement with the enablement requirement, and were criticized for redundancy and lack of clarity.[24]

2. Vas-Cath, Inc. v. Mahurkar

In *Vas-Cath, Inc. v. Mahurkar*,[25] the Federal Circuit examined whether the drawings in the specification provided an adequate written description to support the claim limitation describing the range of sizes of a return lumen in a patent for a double-lumen hemodialysis catheter.[26] Acknowledging the confusion about "what the law of the Federal Circuit is" regarding the written description requirement,[27] the court reviewed the written description doctrine, and affirmatively stated that written description and enablement are two separate and distinct requirements.[28]

The court recognized that written description cases often stressed the fact specificity of the holdings, making the precedential value of the cases extremely limited.[29] However, the court also noted:

> [A] fairly uniform standard for determining compliance with the 'written description' requirement has been maintained throughout: 'Although [the applicant] does not have to describe exactly the subject matter claimed, . . . the description must clearly allow persons of ordinary skill in the art to recognize that [he or she] invented what is claimed.'[30]

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21. *Id.* at 996. The case involved a subgenus claim of a chemical compound. The court found that the compound was insufficiently disclosed because the general disclosure in the specification encompassed about half a million compounds. *Id.* at 993.

22. 436 F.2d 1404 (C.C.P.A. 1971).

23. *Id.* at 1405.

24. *See* Vas-Cath, Inc. v. Mahurkar, 935 F.2d 1555, 1563 (Fed. Cir. 1991) (discussing the confusion in the court's decisions concerning the written description requirement).

25. *Id.*

26. *Id.* at 1558. The catheter at issue comprised a pair of joined, semi-circular lumens designed to allow blood to be removed from an artery, processed in an apparatus that removes impurities, and returned close to the place of removal. *Id.*

27. *Id.* at 1560.

28. *Id.* at 1560-64.

29. *Id.* at 1562.

30. *Id.* at 1562-63 (quoting *In re* Gosteli, 872 F.2d 1008, 1012 (Fed. Cir. 1989)).

Because the written description requirement often comes up in cases where amendments of claims are involved,[31] the court adopted a possession test for adequate written description: whether the disclosure "'reasonably conveys to the artisan that the inventor had possession'" of the later claimed subject matter at the time of the filing.[32] The court emphasized that it is not required that the specification label what features are "novel or important."[33] However, as will be discussed in Part III.B.1, *infra*, the court has yet to provide guidance as to exactly what is needed to establish that one "had possession" of the invention at the time of the filing.

II. CASE SUMMARY

Purdue Pharma L.P. and the Purdue Frederick Company (collectively "Purdue Pharma") brought suit against Faulding Inc., Faulding Pharmaceutical Co., Faulding Services, Inc., and Purepac Pharmaceutical Co. (collectively "Faulding") in the United States District Court for the District of Delaware, alleging infringement of its United States Patent No. 5,672,360 ("the '360 patent").[34] Faulding challenged the validity of the '360 patent on the grounds of, *inter alia*, inadequate written description.[35] The district court held that the claims of '360 patent were invalid for lack of written description.[36] On appeal, the Federal Circuit affirmed.[37]

A. Facts

Purdue Pharma owned United States Patent No. 5,478,577 ("the '577 patent") for a method of treating pain using a once-a-day morphine formulation.[38] In late 1994, Purdue Pharma filed with the United States Patent and Trademark Office ("PTO") a related patent application, Serial No. 08/578688 ("the '688 application"), which disclosed sustained-release, once-a-day oral morphine formulations for long-lasting and effective pain

31. *See id.* at 1560.

32. 935 F.2d at 1563 (quoting Ralston Purina Co. v. Far-Mar-Co, Inc., 772 F.2d 1570, 1575 (Fed. Cir. 1985)).

33. *Id.* at 1565.

34. Purdue Pharma, L.P. v. F.H. Faulding & Co., 48 F. Supp. 2d 420, 423 (D. Del. 1999).

35. *Id.*

36. *Id.* at 433.

37. Purdue Pharma L.P. v. Faulding Inc., 230 F.3d 1320, 1322 (Fed. Cir. 2000).

38. *Id.* The '577 patent issued December 26, 1995. U.S. Patent No. 5,478,577.

relief.[39] In 1996, Faulding began marketing its sustained-release morphine formulation in the United States.[40] Shortly after, Purdue Pharma brought suit against Faulding for infringement of the '577 patent in the United States District Court for the District of Delaware.[41] After commencement of the suit, Purdue Pharma canceled the pending claims of the '688 application before the PTO and amended the application to add all new claims.[42] The amended application was issued as the '360 patent.[43] Thereafter, Purdue Pharma amended its complaint by dropping claims of infringement of the '577 patent and asserting instead infringement of the '360 patent.[44]

The amended claims in the '360 patent included a newly added limitation requiring that the maximum blood morphine concentration ("C submax") in a patient be more than twice the concentration at about 24 hours ("C sub24") after administration of the formulation (*C submax / C sub24 > 2*), i.e., a blood morphine fluctuation of greater than 100 percent.[45] The specification of the '360 patent did not explicitly disclose the *C submax / C sub24 > 2* limitation, or expressly describe the limitation as one of its design goals.[46] Instead, it characterized the inventive formulation as "designed to provide an initially rapid rate of rise in the plasma concentration of [the morphine]"[47] and as "having a surprisingly fast time to peak drug plasma concentration."[48] Nevertheless, the specification stated that "it has now been surprisingly discovered that quicker and greater analgesic efficacy is achieved by 24 hour oral opioid formulations, *which do not exhibit a substantially flat serum concentration curve*, but which instead provide a more rapid initial opioid release."[49] In addition, the '360 patent contained five examples of the inventive formulations exhibiting various *C submax /*

39. *See Purdue Pharma*, 230 F.3d at 1322. The '688 application was filed on November 22, 1994. *See* U.S. Patent No. 5,672,360 (issued Sept. 30, 1997) [hereinafter the '360 patent].

40. *Purdue Pharma*, 48 F. Supp. 2d at 426.

41. *Purdue Pharma*, 230 F.3d at 1322.

42. *Id.*

43. *Id.*

44. *Id.* at 1323.

45. *See Purdue Pharma*, 48 F. Supp. 2d at 428.

46. *See* the '360 patent.

47. *Id.*, col. 6, ll. 1-7.

48. *Id.*, col. 6, ll. 10-12.

49. *Id.*, col. 5, ll. 40-47 (emphasis added).

C sub24 ratios, with the lowest ratio illustrated being 1.48 and the highest being 3.43.[50]

B. The District Court's Ruling

The district court held that the claims of the '360 patent were invalid for lack of written description under section 112.[51] Specifically, the court found that the specification failed to convey that the *C submax / C sub24 > 2* requirement was encompassed in the original invention, and consequently held that Purdue Pharma was not in possession of the claimed invention at the time of the original filing.[52]

The court reasoned that the original claim language did not define the invention in terms of concentration ratios, and that the specification did not describe the *C submax / C sub24 > 2* limitation as critical to the invention.[53] The court rejected Purdue Pharma's claim that the limitation was adequately disclosed by the language in the specification describing its inventive formulation as exhibiting a not "substantially flat" concentration curve.[54] According to Purdue Pharma, a skilled artisan would understand "flat" to mean a *C submax / C sub24* ratio of greater than two.[55] However, the court found that "not substantially flat" did not necessarily mean *C submax / C sub24* ratios greater than two or refer to any precise quantifica-

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50. *Purdue Pharma*, 48 F. Supp. 2d at 430-31. *See also* the '360 patent, cols. 17-18, Tables 4 & 6; cols. 22-23, Tables 11 & 13 (the respective *C submax / C sub24* ratios that could be calculated from the data presented in the tables were 1.48, 1.56, 2.60, 2.98, and 3.43).

51. *See Purdue Pharma*, 48 F. Supp. 2d at 432-33. Faulding challenged the validity of the '360 patent on the grounds of inadequate written description, obviousness, anticipation, and public use. *See id.* at 423. Because the court found the claims invalid for lack of adequate written description, it did not address the other grounds raised by Faulding. *Id.* at 433.

52. *Id.* at 433. The court also found that the '360 patent omitted essential elements of the invention as originally filed, which in the court's view supported a finding that Purdue Pharma was not in possession of the invention at the time of the filing. *See id.* at 431 (citing Gentry Gallery, Inc. v. Berkline Corp., 134 F.3d 1473 (Fed. Cir. 1998)). The Federal Circuit avoided addressing this issue on appeal. This Note will not discuss whether the "omitted essential element" test should be used to determine the adequacy of written description. For a discussion about the omitted essential element test in *Gentry Gallery* and subsequent judicial reactions to the test, see Mark D. Janis, *On Courts Herding Cats: Contending with the "Written Description" Requirement (and Other Unruly Patent Disclosure Doctrines)*, 2 WASH. U. J.L. & POL'Y 55, 74-79 (2000).

53. *Purdue Pharma*, 48 F. Supp. 2d at 429.

54. *Id.*

55. *Id.*

tion.[56] In addition, the court found that the isolated examples of formulations with *C submax / C sub24* ratios greater than 2 were insufficient to support the claim limitation because there were also examples of formulations having *C submax / C sub24* ratios less than two.[57] The court found that collectively, the examples established a *C submax / C sub24* range between 1.48 and 3.43.[58]

C. The Federal Circuit's Ruling

The Federal Circuit affirmed the district court's finding that the term "not substantially flat" in describing a concentration curve did not refer to the peak to trough ratio of morphine concentrations, but instead referred to the feature of rapid initial morphine release, because only the latter was described in the specification as critical to the invention.[59] The court held that neither the text nor the examples set forth in the specification provided adequate written description to support the later-amended *C submax / C sub24* > 2 claim limitation.[60]

The court reasoned that nothing in the specification conveyed that the *C submax / C sub24* ratio was a critical aspect of the invention.[61] Moreover, the court concluded that a skilled artisan would not necessarily understand "flat" to mean a *C submax / C sub24* ratio of two or less.[62] Although acknowledging that a *C submax / C sub24* > 2 limitation could be derived from some of the examples,[63] the court found that nothing in the examples emphasized this ratio as "an important defining quality of the formulation," or would "even motivate one to calculate the ratio."[64] Therefore, the court found it "immaterial what range for the *C submax / C sub24 ratio* can be gleaned from the examples when read in light of the claims."[65] Consequently, the court invalidated the claims for lack of written description.[66] In doing so, the Federal Circuit in essence created a new rule that would prevent a patent applicant from narrowing the scope of her

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56. *Id.* The court noted that Purdue Pharma's own expert witness characterized a drug exhibiting *C submax / C sub24* > 2 as "flat," and at least one of the publications that Purdue Pharma relied on described a formulation with a *C submax / C sub24* ratio of 2.05 as having "low" fluctuations. *See id.*

57. *Id.*

58. *Id.* at 431.

59. Purdue Pharma L.P. v. Faulding Inc., 230 F.3d 1320, 1324 (Fed. Cir. 2000).

60. *Id.* at 1324-26.

61. *Id.* at 1324.

62. *Id.* at 1324-26.

63. *Id.* at 1326.

64. *Id.* at 1327.

65. *Id.* at 1328.

66. *Id.*

claims through amendment if the narrowing limitations were not specifically described in the original application as being critical for the invention.

III. DISCUSSION

In *Purdue Pharma*, the Federal Circuit fashioned a "defining quality" test, which requires that the specification, as originally filed, clearly identify each and every amended claim limitation as an important defining quality of the invention.[67] This test is not only at odds with the court's written description precedent, but also unjustified by the purpose of the written description requirement. The decision may be the result of an incoherent written description jurisprudence. The court's continuing use of an inconsistent and often overly-stringent written description requirement leaves inventors, especially those in the pharmaceutical industry, with little incentive to disclose, and is likely to discourage inventors from seeking patent protection. The harm of an inconsistent and unworkable written description doctrine may extend beyond the "unpredictable" arts such as chemical and biological arts, and impose a heavy toll on the patent system.

A. *Purdue Pharma* Adds Uncertainty to the Standard of Adequate Written Description

1. Purdue Pharma*'s Defining Quality Test Is Inconsistent with the Written Description Precedents*

In *Purdue Pharma*, the Federal Circuit focused on whether the specification labeled the amended claim limitation as crucial to the invention, finding inadequate disclosure because the specification did not indicate that the *C submax / C sub24* ratio was "an important defining quality of the formulation."[68] Analogizing the pharmacokinetic parameters disclosed in the '360 patent to a forest, the court remarked, "one cannot disclose a forest in the original application, and then later pick a tree out of the forest and say here is my invention."[69] Instead, "to satisfy the written description requirement, the blaze marks directing the skilled artisan to that tree must be in the originally filed disclosure."[70]

For the first time, the Federal Circuit used the written description requirement to strike down claims, the scope of which was *narrowed* through amendment during patent prosecution. Under the court's rationale,

67. *Id.* at 1327.
68. *Id.*
69. *Id.* at 1326.
70. *Id.* at 1326-27.

one cannot first disclose and claim the entire forest as one's invention, describing the general features of the trees and the surroundings in a way that would demonstrate her possession of the forest and enable others to find the forest, but later change her mind and only claim the part of the forest starting from the second row of the trees. This is particularly odd given the prevalence of dependent claims. Under *Purdue Pharma*, all the dependent claims, if amended during prosecution, must have been individually and separately described in the original application in order to maintain their validity.

Although the court never explicitly explained what kind of "blaze marks" would suffice under a high level of written description scrutiny, it seems that the court equated leaving the "blaze marks" with labeling the features as having the "defining quality." In finding adequate support only where the claim limitations were described by the specification as a "defining quality" of the invention, the court in essence required the patentee to define the invention using the specification, a test expressly rejected by the *Vas-Cath* court.[71]

In *Vas-Cath*, the claim limitation at issue was the range of sizes of a return lumen in a patent for a double-lumen hemodialysis catheter.[72] In finding that the trial court's requirement that the drawings in the specification "describe what is novel or important" constituted legal error, the court noted that the claims did not "recite *only* a pair of semi-circular lumens, or a conical tip, or a ratio at which the tip tapers, or the shape, size, and placement of the inlets and outlets," but claimed "*a double lumen catheter* having a *combination* of those features."[73] Similarly, in the instant case, the patent did not claim *only* the *C submax / C sub24 > 2* limitation, but a formulation for treating pain that had a *combination* of pharmacokinetic parameters, including the *C submax / C sub24 > 2* limitation.[74] Using the court's metaphor, the invention was the forest, which included the tree. No precedent requires that each tree be the defining quality of the claimed forest. An inventor should be free to narrow the scope of the patent, and thereby her own patent rights, by limiting the claims with nonessential elements, so long as the elements are adequately disclosed.[75] To render disclosure of a limitation adequate only when it identifies the limitation as being a critical aspect of the invention is to bar inclusion of any nonessen-

71. Vas-Cath, Inc. v. Mahurkar, 935 F.2d 1555, 1565 (Fed. Cir. 1991) (finding "the district court's concern with 'what the invention is' misplaced").

72. *Id.* at 1565-66.

73. *Id.* at 1565 (emphasis original).

74. *See, e.g.*, the '360 patent, Claim 1.

75. *See* Hyatt v. Boone, 146 F.3d 1348, 1353 (Fed. Cir. 1998).

tial elements during prosecution, a judgment that should be left to the inventor, not the court.

2. Purdue Pharma's *Defining Quality Test Is Inconsistent with the Purpose of the Written Description Requirement*

In *Purdue Pharma*, the court acknowledged that the examples provided data from which a skilled artisan could piece together the *C submax / C sub24* > 2 limitation.[76] The court also agreed that two of the formulations disclosed in the '360 patent *possessed* the limitation.[77] Nevertheless, the court considered the examples inadequate because they did not emphasize the *C submax / C sub24 ratio*.[78] The court noted that the examples would not even motivate one skilled in the art to calculate the ratio.[79] Quoting *Vas-Cath*, the court recited that an adequate disclosure must convey with reasonable clarity to those skilled in the art that the inventor was in possession of the invention,[80] but went on to define "reasonable clarity" as allowing one skilled in the art to "immediately discern the limitation at issue" from reading the specification.[81]

The purpose of the written description requirement is not to influence the conduct of the public, but to shape the behavior of the inventor.[82] It is an insurance against fraud rather than a motivation for the public to study the invention. It purports to prevent overreaching by the inventor by ensuring that the inventor "had possession, as of the filing date of the application relied on, of the specific subject matter later claimed by him."[83] The goal of an adequate written description, therefore, is to demonstrate possession by providing support for the claimed invention. To that end, it is irrelevant whether a skilled artisan would be motivated to calculate the *C submax / C sub24* ratio or how fast she could derive that ratio from the

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76. Purdue Pharma L.P. v. Faulding Inc., 230 F.3d 1320, 1326 (Fed. Cir. 2000).

77. *Id.* at 1327.

78. *Id.* at 1326.

79. *Id.* at 1327.

80. *Id.* at 1323 (quoting Vas-Cath, Inc. v. Mahurkar, 935 F.2d 1555, 1563-64 (Fed. Cir. 1991)).

81. *Id.* (citing Waldemar Link GmbH & Co. v. Osteonics Corp., 32 F.3d 556, 558 (Fed. Cir. 1994)).

82. *See* Rengo Co. v. Molins Mach. Co., 657 F.2d 535, 551 (3d Cir. 1981) (distinguishing written description requirement and definiteness requirement as the latter shapes the future conduct of persons other than the inventor).

83. *In re* Edwards, 568 F.2d 1349, 1351-52 (C.C.P.A. 1978). Whether a separate written description requirement is necessary to serve that purpose is not always clear. *See* Janis, *supra* note 52, at 69 ("Proponents of the written description requirement have yet to explain exactly what benefits the requirement provides that are not already provided by the enablement requirement.").

specification, even though that might matter for enablement purpose. What is important is that a skilled artisan would be able to find the support for the claimed ratio if she needed to. In the instant case, the support for the *C submax / C sub24* > 2 limitation could be found in two of the formulations disclosed, which, as the court acknowledged, "possessed" the desired characteristic.[84]

Possession of an invention necessarily extends to all aspects of the invention, including those noncritical characteristics. To require disclosure of each limitation and to simultaneously require labeling of each disclosed limitation as a defining quality of the invention in order to demonstrate possession are two standards that cannot easily be reconciled, especially if one were to take the view that an inventor is within her own rights to limit the scope of her invention.

Moreover, an inventor may have disclosed some inherent characteristics of an invention she possessed at the time of filing without even realizing it. For purposes of demonstrating possession, it should be irrelevant whether an inventor appreciates the value or even existence of those characteristics. Therefore, whether a patentee had possession of an invention with certain characteristics should not turn on whether the patentee recognized the importance of those characteristics at the time of the filing.

B. An Obscure Written Description Doctrine

The difficulty in finding a reasonable and well-balanced test for adequate written description perhaps lies in the unfortunately cryptic and incoherent nature of the written description jurisprudence. The Federal Circuit has yet to clearly define what "in possession" means. The written description doctrine, as it has developed, is inconsistent with some patent law doctrines and redundant with others.

1. A Standardless "in Possession" Test

Although the Federal Circuit has at instances made clear what is *not* required to demonstrate possession,[85] what *is* required is a question yet to be answered. The judicially created written description doctrine has been criticized as being "standardless."[86] Although the court's decisions have

84. *Purdue Pharma*, 230 F.3d at 1327 (stating that two of the examples "possessed" the *C submax / C sub24* > 2 characteristic).

85. *See, e.g.*, Vas-Cath, Inc. v. Mahurkar, 935 F.2d 1555, 1565 (Fed. Cir. 1991) (holding that the specification does not have to identify the novel or important features of the invention).

86. *See* Janis, *supra* note 52, at 72 ("Although the Federal Circuit nibbles around the edges of the standard, it has rarely, if ever, succeeded in giving the standard any real content.").

often recited that the test for adequate written description is whether it "reasonably conveys to the artisan that the inventor had possession at that time of the later claimed subject matter,"[87] the court has yet to breathe life and meaning into the term "in possession." To simply say that "[o]ne shows that one is in 'possession' of the invention by describing the invention"[88] provides no guidance as to how the invention should be described in order to demonstrate possession.

One uncertainty arises from the lack of consensus for what constitutes "reasonable clarity." The Federal Circuit stated that the disclosure as originally filed "does not have to provide *in haec verba* support for the claimed subject matter,"[89] but nevertheless must convey with "reasonable clarity" to one skilled in the art that the patentee was in possession of the invention.[90] On one end of the spectrum, the court used a "support" standard, requiring that the disclosure *reasonably* support the claim limitations.[91] On the other end of the spectrum, the court required that the disclosure must constitute "a full, clear, concise and *exact* description . . . of the invention claimed."[92] Although the Federal Circuit tried to reconcile the two standards as of no real distinction,[93] such a baffling characterization would only confirm that there actually is no standard for an adequate written description. In *Purdue Pharma*, the court went further to require that the disclosure must allow one skilled in the art, "reading the original disclosure, [to] *immediately discern* the limitation at issue in the claims."[94] The multiple standards for "reasonable clarity" prescribed by the Federal Circuit make the "in possession" test unworkable.

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87. *Vas-Cath*, 935 F.2d at 1563-64 (quoting Ralston Purina Co. v. Far-Mar-Co, Inc., 772 F.2d 1570, 1572 (Fed. Cir. 1985), which in turn was quotes *In re* Kaslow, 707 F.2d 1366, 1375 (Fed. Cir. 1983)).

88. Lockwood v. Am. Airlines, 107 F.3d 1565, 1572 (Fed. Cir. 1997).

89. *Purdue Pharma*, 230 F.3d at 1323 (citing Fujikawa v. Wattanasin, 93 F.3d 1559, 1570 (Fed. Cir. 1996)).

90. *Id.* (citing *Vas-Cath*, 935 F.2d at 1563-64).

91. *See Vas-Cath*, 935 F.2d at 1563 n.6 (citing various Federal Circuit cases that require specification to support the claims).

92. *In re* Wertheim, 646 F.2d 527, 538 (C.C.P.A. 1981) (emphasis added).

93. *See* Hyatt v. Boone, 146 F.3d 1348, 1354 (Fed. Cir. 1998) ("We do not view these various expressions as setting divergent standards for compliance with § 112.").

94. *Purdue Pharma*, 230 F.3d at 1323 (emphasis added) (citing Waldemar Link GmbH & Co. v. Osteonics Corp., 32 F.3d 556, 558 (Fed. Cir. 1994)). But the source of that premise is not entirely clear. *Waldemar* in turn cited *In re* Rasmussen, 650 F.2d 1212, 1215 (C.C.P.A. 1981). *Waldemar*, 32 F.3d at 558-59. *Rasmussen*, however, does not support such a proposition. In fact, *Rasmussen* represents a time when the court viewed enablement and written description as one requirement. *See Rasmussen*, 650 F.2d at 1214 ("Disclosure is that which is taught . . . .").

2. *An Overly Stringent Written Description Requirement Is Hard to Reconcile with the Established Canon That Claims Should be Read to Preserve Their Validity*

The *Purdue Pharma* decision is in keeping with the Federal Circuit's approach to patent claims involving chemical or genetic material, where the court often applied a heightened "in possession" test in examining the validity of the claims.[95] Such an unduly stringent written description requirement is at odds with the long-standing judicial practice of construing the claims "so as to sustain their validity."[96] For example, a court is to construe a claim element narrowly in order to preserve its validity over prior art.[97] And under a related rule, if a claim is subject to two viable alternative interpretations, the narrower one should apply.[98] It is a waste of the court's and the parties' resources to ask a court to go through lengthy claim construction and construe the claim narrowly to preserve its validity, but only to invalidate it later because the written description supports, in *Purdue Pharma*'s case, a broader interpretation of the claim.

3. *Redundancy of a Separate Written Description Requirement Independent of the Enablement Requirement*

The Federal Circuit has attempted to justify having a separate written description requirement on grounds ranging from a historical notice function to the contemporary role as a safeguard against overreaching.[99] However, as one commentator argues, the Federal Circuit has yet to demonstrate a compelling justification for recognizing a distinct written descrip-

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95. *See infra* notes 114-19 and accompanying text.

96. Carman Indus., Inc. v. Wahl, 724 F.2d 932, 937 n.5 (Fed. Cir. 1983) (citing *Klein v. Russell*, 86 U.S. 433, 466 (1874); Turrill v. Michigan S. & N.I.R.R. Co., 68 U.S. 491, 510 (1864)).

97. *See* Apple Computer, Inc. v. Articulate Sys., Inc., 234 F.3d 14, 24 (Fed. Cir. 2000) (acknowledging that "claims should be read in a way that avoids ensnaring prior art if it is possible to do so") (quoting Eastman Kodak Co. v. Goodyear Tire & Rubber Co., 114 F.3d 1547, 1556 (Fed. Cir. 1997)).

98. *See* Athletic Alternatives, Inc. v. Prince Mfg., Inc., 73 F.3d 1573, 1581 (Fed. Cir. 1996). The court stated:

> [W]here there is an equal choice between a broader and a narrower meaning of a claim, and there is an enabling disclosure that indicates that the applicant is at least entitled to a claim having the narrower meaning, we consider the notice function of the claim to be best served by adopting the narrower meaning.

Id.

99. *See* Vas-Cath, Inc. v. Mahurkar, 935 F.2d 1555, 1560-61 (Fed. Cir. 1991).

tion requirement.[100] The redundancy of the two disclosure doctrines may have contributed to the court's continuing struggle in separating the two in practice.[101]

A separate written description requirement independent of enablement may be at odds with the Supreme Court's decision in *Pfaff v. Wells Electronics, Inc.*[102] In *Pfaff*, the Court held that in addition to evidence of commercial marketing, the invention must be "ready for patenting" in order to invoke the statutory on-sale bar of section 102(b).[103] The latter condition may be satisfied "by proof that . . . the inventor had prepared drawings or other descriptions of the invention that were sufficiently specific to enable a person skilled in the art to practice the invention."[104] The Court found that the drawings the patentee sent to the manufacturer was sufficiently enabling, and thus "*fully disclosed* the invention," and triggered the on-sale period even though invention was not yet reduced to practice.[105] Therefore, a separate written description requirement for patentability possibly renders a claim invalid, while the same enabling specification is enough under *Pfaff* to trigger the statutory on-sale bar. This is a peculiar result.

The goal of the patent system is to promote science and technology,[106] that is, to encourage a free flow and exchange of ideas that can be readily converted into creating useful things. To that end, what the patent law should be concerned with is whether the patent effectively teaches the making and use of the useful things. In that regard, if the disclosure can enable one skilled in the art to "make and use the same,"[107] the patentee should be presumed to have possession of the invention, which may be overcome by clear and convincing evidence that the patentee had not actually thought of the invention at the time of filing.

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100. *See* Janis, *supra* note 52, at 62-69 (criticizing the distinction made by the Federal Circuit between written description and enablement as artificial).

101. *See* Harris A. Pitlick, *The Mutation on the Description Requirement Gene*, 80 J. PAT. & TRADEMARK OFF. SOC'Y 209, 222-23 (1998) (criticizing Regents of the University of California v. Eli Lilly & Co., 119 F.3d 1559 (Fed. Cir. 1997), by stating that the court "has lost sight of the real culprit lack of enablement and directed its ire at an innocent bystander the description requirement . . . [and] takes description requirement jurisprudence in an unjustifiably new and reckless direction").

102. 525 U.S. 55 (1998) (finding that an invention was offered for sale and ready for patenting because the drawings the plaintiff sent to the manufacturer fully disclosed the invention).

103. *Id.* at 67.

104. *Id.* at 67-68.

105. *Id.* at 68.

106. U.S. CONST. art. I, § 8, cl. 8.

107. 35 U.S.C. § 112, ¶ 1.

Arguably, the court may be concerned with fairness issues. It may seem unfair, as in *Gentry Gallery, Inc. v. Berkline Corp.*,[108] for a patentee to broaden the claims through amendment just to cover its competitor's products.[109] However, the final result in *Gentry* may remain the same under a rule that a patentee is presumed to have had possession of the invention under an enabling disclosure unless there is clear and convincing evidence that he had not actually thought of the invention at the time of filing. Unlike in *Purdue Pharma*, where the inventors testified that one of the specific goals was to develop a formulation that would provide a *C submax / C sub24 ratio* of greater than two,[110] in *Gentry*, the inventor admitted that he did not even think of placing the controls outside the console before he learned about the competitors' designs.[111] In addition, in *Gentry*, a related enablement argument could be made to invalidate the claim in that the disclosure did not enable one skilled in the art to make sofas with controls located other than on the console because the disclosure in effect specifically directed a skilled artisan *not* to do so.[112]

Moreover, patent law is not all about fairness. It may seem at least equally unfair that patent law gives a patentee the right to exclude those who independently come up with an identical or substantially similar invention from making and using that invention, which might even be a better one than the patentee's. But the law must compromise on fairness to achieve its constitutional goal—to promote innovation in science and technology.[113]

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108. 134 F.3d 1473 (Fed. Cir. 1998)

109. *See id.* In *Gentry*, the patent at issue involved a sectional sofa with side-by-side recliners separated by a fixed console. *Id.* at 1475. The specification disclosed that the console was to accommodate the controls for both the reclining seats, and specifically limited the control to the console as part of the objective of the invention. *Id.* at 1478. The broadest original claim was directed to a sofa comprising "control means located upon the center console." *Id.* at 1479. The claims were broadened during prosecution to include placing the controls outside the console after the inventor learned that the competitors were so locating the recliner controls. *Id.* The court invalidated the claims on grounds of written description, finding that the original disclosure did not adequately support the claims in which the location of the control was other than the console. *Id.*

110. Purdue Pharma, L.P. v. F.H. Faulding & Co., 48 F. Supp. 2d 420, 424 (D. Del 1999) (citing the transcripts).

111. *Gentry*, 134 F.3d at 1479.

112. *Id.*

113. U.S. CONST. art. I, § 8, cl. 8.

C. An Overly Stringent Written Description Requirement Is Likely to Discourage Inventors in the Pharmaceutical Industry From Seeking Patent Protection

Biotechnology and chemical patents have received more than their fair share of a harsh written description inquiry. The Federal Circuit's decisions since *Amgen, Inc. v. Chugai Pharmaceutical, Co.*[114] have applied a heightened level of scrutiny under the written description requirement to "unpredictable arts" involving DNA sequences.

Drawing a line between predictable and unpredictable arts, the court in *Amgen* required actual reduction to practice at the time of filing "when an inventor is unable to envision the detailed constitution of a gene so as to distinguish it from other materials."[115] The court found that since Genetics Institute, one of the defendants in the suit, had not actually isolated the claimed human erythropoietin DNA at the time of filing the application, a mere description of the method to isolate the DNA and a statement that the said DNA encodes human erythropoietin protein were inadequate for the purpose of the written description requirement.[116]

More recently, the Federal Circuit addressed the issue of the written description requirement for genomic patents in *Regents of the University of California v. Eli Lilly & Co.*[117] The court invalidated University of California's patent on human insulin cDNA because the specification only contained a recitation of the rat insulin cDNA sequence, even though the examples in the specification described how to isolate the human insulin cDNA.[118] The court stated that adequately describing a cDNA in a patent specification "requires the kind of specificity usually achieved by means of the recitation of the sequence of nucleotides that make up the cDNA."[119]

The court's rigid application of the written description requirement to biotechnology patents has been criticized as departing recklessly from written description precedents.[120] On the other hand, the decisions have

114. 927 F.2d 1200 (Fed. Cir. 1991).

115. *Id.* at 1206.

116. *See id.* Similarly, in *Fiers v. Revel*, 984 F.2d 1164 (Fed. Cir. 1993), the court rejected Revel's claim of priority to the DNA sequence coding for human beta-interferon on the grounds that he had not included the actual DNA sequence in his patent application. *Id.* at 1170-71.

117. 119 F.3d 1559 (Fed. Cir. 1997).

118. *Id.* at 1567-68.

119. *Id.* at 1569.

120. *See* Janice M. Mueller, *The Evolving Application of the Written Description Requirement to Biotechnological Inventions*, 13 BERKELEY TECH. L.J. 615, 649 (1998).

been viewed as necessary steps to ensure that overly broad patent rights are not granted to DNA sequences of unknown function, which may have a significant, yet unforeseeable impact on future downstream research.[121] Indeed, granting overly broad patent rights to upstream research products has raised antitrust concerns that may chill the efforts by other researchers to take multiple research paths, which are characteristic and crucial for biotechnology innovations.[122]

However, the fact remains that the effect of the Federal Circuit's recent written description cases may not stop at just narrowing the scope of the biomedical and chemical patents, but may force inventors in this area to avoid seeking patent protection entirely, thereby depriving the inventors of the most, and perhaps the only, effective protection. Although secrecy is commonly the dominant appropriability mechanism across all industries,[123] trade secret protection may be a weak form of protection, especially in this day and age, where information and communication technology makes it difficult to conceal one's research advancements within the walls of an institution. In the biotechnology and pharmaceutical industry, research efforts usually require a large amount of collaborative work. Coupled with the increased mobility of employees, trade secrecy may be hard to manage. Moreover, trade secret law does not protect against reverse engineering, which would allow a pharmaceutical company to figure out, and then legally make and use its competitor's newest drug formulations with relatively little effort and expense. Therefore, trade secret protection may not give a pharmaceutical company enough incentive to invest in research and development ("R&D").

In theory, patent law provides incentive to invest in innovation by allowing the inventor to appropriate fully the economic returns of her invention.[124] Empirical studies have shown that in some R&D intensive industries such as the pharmaceutical industry, patent protection provides the second most effective appropriability mechanism, closely trailing se-

121. *See* Margaret Sampson, *The Evolution of the Enablement and Written Description Requirements Under 35 U.S.C. § 112 in the Area of Biotechnology*, 15 BERKELEY TECH. L.J. 1233, 1259-61 (2000).

122. *See generally* Arti K. Rai, *Fostering Cumulative Innovation in the Biopharmaceutical Industry: The Role of Patents and Antitrust*, 16 BERKELEY TECH. L.J. 813 (2001); Michael A. Heller & Rebecca S. Eisenberg, *Can Patents Deter Innovation? The Anticommons in Biomedical Research*, 280 SCIENCE 698 (1998).

123. WESLEY M. COHEN ET AL., PROTECTING THEIR INTELLECTUAL ASSETS: APPROPRIABILITY CONDITIONS AND WHY U.S. MANUFACTURING FIRMS PATENT (OR NOT) 6 (Nat'l Bureau of Econ. Research, Working Paper No. 7552, 2000).

124. *See* MERGES, *supra* note 17, at 137.

crecy.[125] The same studies also indicate that one of the top reasons for not applying for a patent is the amount of information disclosed in a patent application, because it allows a competitor to easily and legally invent around the patent.[126] The approach adopted by the Federal Circuit in recent written description cases, which not only requires an extremely specific disclosure, but also limits the scope of the patent to the minimum, will undoubtedly deter pharmaceutical companies from seeking patent protection. In fact, the studies by Wesley Cohen et al. indicate that the importance of secrecy has increased dramatically in recent years, albeit the weak protection it provides.[127] Curiously, although empirical studies found that the absence of patent protection would have had little impact on the innovative efforts of a majority of firms in most industries, the pharmaceutical industry was a "clear exception."[128] Therefore, the court's almost abusive use of written description requirement against biomedical patents may have a much greater negative impact than it intended.

D. The Uncertainty Generated by an Amorphous Written Description Doctrine May Harm the Patent System

The biotechnology cases may reflect the court's unwillingness to grant broad patents to unpredictable arts. However, some commentators have suggested that *Gentry Gallery* signals that predictability of the arts may have nothing to do with how strictly the court applies the written description requirement.[129]

A poorly developed doctrine without a workable standard, the written description requirement generates grave uncertainty that would impose a huge cost to the society as well as the patent system.[130] The PTO, for example, has been burdened by the court's written description requirement, and struggled with the task of coming up with a better-defined "posses-

125. COHEN, *supra* note 123, at 6.

126. *Id.* at 14.

127. *Id.* at 3.

128. *Id.* at 2.

129. *See, e.g.*, Cynthia M. Lambert, Note, *Gentry Gallery and the Written Description Requirement*, 7 B.U.J. SCI. & TECH. L. 109, 139 (2001) (concluding that *Gentry* is perceived as unifying the standard of all arts to the stricter written description standard that was previously only applied to unpredictable arts); Laurence H. Pretty, *The Recline and Fall of Mechanical Genus Claim Scope Under "Written Description" in the Sofa Case*, 80 J. PAT. & TRADEMARK OFF. SOC'Y 469, 479-80 (commenting that it remains to be seen whether *Gentry* will become an influential precedent in permitting a stringent and limiting written description requirement in predictable arts).

130. *See* Janis, *supra* note 52, at 69.

sion" standard in its written description requirement guidelines.[131] However, as one commentator remarked, the PTO Guidelines "do little to bring the written description requirement out from the shadow of enablement."[132] And the PTO's "admirable effort to create something from nothing"[133] is unlikely to pay off. As its Director of biotechnology admitted, "Every time I think we're getting a handle on biotech, something new crops up."[134]

A more serious threat is the judges' ability to use written description as a means to serve policy ends as they see fit with little judicial restraint. The Federal Circuit has reiterated that written description inquiry "must be assessed on a case-by-case basis."[135] The court even went so far to declare that "the precedential value of cases in this area is extremely limited."[136] Given the almost unchecked freedom to make law granted by an unstructured and standardless doctrine, judges might be tempted to use the written description requirement to invalidate claims even when the facts should have been assessed on other legal grounds.

This is undesirable even if the judges have justified policy concerns. It is Congress' job to make law, not the courts'. Courts often reveal their zealousness to invalidate patents on written description grounds in cases where the patentee broadens the claims in order to exclude a competitor's product, like *Gentry*, or where the patentee narrows the claims with the intent to avoid prior art, like *Purdue Pharma*. To be sure, it is not prohibited to amend claims with an intent to exclude a competitor's product that the inventor has learned about, or to avoid prior art that the inventor has discovered during the prosecution.[137] In fact, this is what amendment prac-

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131. *See, e.g.*, Guidelines for the Examination of Patent Applications Under 35 U.S.C.§ 112, ¶ 1, "Written Description" Requirement, 66 Fed. Reg. 1099, 1101 (2001) (commenting on whether actual reduction to practice is required for demonstration of possession) [hereinafter the "Guidelines"]. *See also* Eli Loots, Note, *The 2001 USPTO Written Description Guidelines and Gene Claims,* 17 BERKELEY TECH. L.J. 117 (2002).

132. Janis, *supra* note 52, at 71.

133. *Id.*

134. Anthony Shadid, *Battle Turns Fierce Over Biotech Patents Agency Struggles Over What's Covered and What Rights are Offered*, BOSTON GLOBE, July 18, 2001, at D1 (quoting the PTO's Director of Biotechnology Division).

135. Purdue Pharma L.P. v. Faulding Inc., 230 F.3d 1320, 1323 (Fed. Cir. 2000) (citing Vas-Cath, Inc. v. Mahurkar, 935 F.2d 1555, 1561 (Fed. Cir. 1991)).

136. *Vas-Cath*, 935 F.2d at 1562 (quoting *In re* Driscoll, 562 F.2d 1245, 1250 (C.C.P.A. 1977)). This perhaps defeats the purpose of the Congress in creating the Court of Appeals for the Federal Circuit—to establish a more uniform and coherent body of patent law.

137. *See* Kingsdown Med. Consultants, Ltd., v. Hollister Inc., 863 F.2d 867, 874 (Fed. Cir. 1988).

tice is for. Undoubtedly, there are attorneys who will abuse the amendment practice. But unless the court can develop a clear and workable written description doctrine, a more prudent way for the court to channel its disapproval of such practice is to expand or redefine the scope of the inequitable conduct doctrine.

IV. CONCLUSION

Like all written description cases, *Purdue Pharma* may have little precedential value according to the Federal Circuit.[138] But that in itself does not eliminate the harm. The decision adds to the incoherency of the written description jurisprudence. Together with the recent line of cases, the decision represents judicial hostility towards amendment practice and a trend towards using the written description requirement to unduly narrow the scope of a patent. The court's willingness to expand the use of a standardless written description requirement will create great uncertainty, which in turn will impose an unjustifiably high cost on the patent system.

138. *See Vas-Cath*, 935 F.2d at 1562 (stating that the precedential value of cases in the written description area is extremely limited).

THE 2001 USPTO WRITTEN DESCRIPTION GUIDELINES AND GENE CLAIMS

By Eli A. Loots

The patent system attempts to "promote the progress of science and useful arts, by securing for limited times to authors and inventors the exclusive rights to their respective writings and discoveries."[1] In doing so, the patent system balances the goal of promoting research with the reward of offering exclusive protection of the invention. In order to ensure such a balance, a patent must meet certain requirements. The invention must be novel,[2] nonobvious,[3] useful,[4] of statutory subject matter,[5] and enable one skilled in the art to make the invention.[6] An additional requirement, embodied in section 112, is the written description of the invention.[7] The scope of the written description requirement is unclear because of apparent inconsistencies in case law.

In order to help define the written description requirement, the United States Patent and Trademark Office (USPTO) issued the Written Description Guidelines (Guidelines) to explain how the requirement should be applied to incoming patent applications. It is not clear whether the Guidelines have resolved the inconsistencies in the field of biotechnology, perhaps because of inconsistencies in other areas of patent law. This is unfortunate because the written description requirement, in its current form, does not clearly promote research in the field of biotechnology.

1. U.S. CONST. art. I, § 8, cl. 8.
2. 35 U.S.C. § 102 (1994).
3. 35 U.S.C. § 103 (1994).
4. 35 U.S.C. § 101 (1994).
5. *Id.*
6. 35 U.S.C. § 112 (1994).
7. "The specification shall contain a written description of the invention, and of the manner and process of making and using it, in such full, clear, concise, and exact terms as to enable any person skilled in the art to which it pertains, or with which it is most nearly connected, to make and use the same, and shall set forth the best mode contemplated by the inventor of carrying out his invention." *Id.*

I. BACKGROUND

A. Purpose of the Written Description Requirement

While the courts have articulated the written description requirement in slightly different ways, the factual inquiry is "whether a claim defines an invention that is clearly conveyed to those skilled in the art at the time the application was filed."[8]

Such a description ensures that the patentee has possession over the claimed invention,[9] so possession of the claimed invention will transfer to the public once the patent term has expired. In theory, the written description requirement ensures that the applicant actually invented the invention. Additionally, by forcing the inventor to describe what is claimed in the patent, we are able to ascertain if the inventor is trying to claim something that is already known.[10] To this end, the written description can serve a notice function, both providing notice to the general populace that a new invention is being claimed and providing notice to future inventors of what has being claimed.[11] Finally, since the written description requirement is examined separately from other requirements (such as enablement), it ensures that what is actually claimed is clear. The requirement prevents expansion of the claimed subject matter through later amendment by requiring that any alterations be fully described in the original application.[12]

B. Purpose of the Guidelines

The Written Description Guidelines are intended to assist USPTO personnel in the determination of whether an adequate written description has been provided in a patent application.[13] The Guidelines are derived from

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8. U.S. Department of Commerce, Manual of Patent Examining Procedures § 2163.02 (7th ed., rev. Feb. 1, 2000) [hereinafter MPEP]. In theory, this is not a high standard to meet since, when reviewing a patent application, there is a strong presumption that an adequate written description is provided. *See* In re Wertheim, 541 F.2d 257, 263 (C.C.P.A. 1976).

9. 35 U.S.C. § 112; Vas-Cath Inc. v. Mahurkar, 935 F.2d 1555, 1563-64 (Fed. Cir. 1991).

10. Evans v. Eaton, 20 U.S. 356 (1822).

11. For a historical perspective of the evolution of the written description requirement, see Janice M. Mueller, *The Evolving Application of the Written Description Requirement to Biotechnological Inventions*, 13 BERKELEY TECH. L.J. 615 (1998).

12. *See* MPEP, *supra* note 8, § 2163.

13. Guidelines for Examination of Patent Applications under the 35 U.S.C. § 112, ¶1 "Written Description" Requirement, 66 Fed. Reg. 1099, 1104 (Jan. 5, 2001) [hereinafter The 2001 Written Description Guidelines].

the USPTO's current understanding of the law and prior comments to the Interim Guidelines. Formally, the Guidelines lack any independent legal authority.[14] The Guidelines state that a rejection of a patent application is based upon the substantive law itself, not the Guidelines.[15] As such, inconsistencies within the Guidelines will result in inefficiencies, rather than a collapse of the patent system.[16] Regardless, because of its central role in educating Patent Examiners, a thorough understanding of the Guidelines is helpful to patent attorneys in overcoming the hurdle of the written description requirement. Perhaps more importantly, any differences between the Guidelines and the current state of the law should be appreciated to ensure that an invention is adequately protected should the patent later face litigation.

C. Molecular Biology of DNA

While the new Guidelines are applicable to all inventions, they are particularly relevant in the area of biotechnology because several of the decisions that prompted the Guidelines involved inventions related to DNA.[17]

The desire to patent DNA sequences has dramatically increased in the last decade. This is due in part to new advances in technology, such as superior sequencing machines, sequencing techniques, and better computers (both for analysis and for sequencing). It is also due to a large influx of businesses into the biotechnology field, both from a biological and computational aspect. Finally, the increase in interest is due to the acknowledgement that new fields, such as genomics and proteomics, can cut years of research time from traditional scientific techniques thus, the information itself is valuable regardless of the particular function of a particular piece of DNA.[18]

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14. *Id.*

15. *Id.* However, the USPTO states that, in light of the received comments to the Interim Guidelines, the present Guidelines are "believed to be fully consistent with binding precedent of the U.S. Supreme Court, as well as the U.S. Court of Appeals for the Federal Circuit and its predecessor courts." *Id.*

16. *Id.*

17. *See generally,* The 2001 Written Description Guidelines, *supra* note 13; Revised Interim Written Description Guidelines Training Materials, http://www.uspto.gov/web/menu/written.pdf (last visited Feb. 10, 2002) [hereinafter Interim Training Materials].

18. For instance, sequence comparison between various organisms relies on the concept of evolutionary conservation. As such, without knowing anything about a particular sequence, one is able to get an idea of a sequence's importance and even function, merely by its presence or absence across evolutionarily diverse species.

1. *General Composition of DNA*

A DNA sequence is a description of a series of nucleic acids or bases (adenine, cytosine, guanine, and thymine) covalently linked together.[19] For the coding DNA to produce the protein it codes for, the DNA is first transcribed into a complementary strand of RNA.[20] This piece of RNA can then be translated into the protein for which it encodes.[21] Enzymes read the sequence of nucleic acids in RNA as one might read a recipe in a cookbook, instructing the enzymes as to which amino acids need to be linked together to produce the desired protein.

2. *Properties of DNA that Make Patentability Difficult*

The largest problem with attempts to describe a DNA or protein sequence for a patent is that the sequences themselves are, on a base-by-base basis, relatively unimportant for the DNA or protein as a whole.[22]

First, the genetic code itself is degenerate.[23] This presents the formal possibility that two people could each get a patent on the same amino acid sequence of a protein if it were described by different nucleic acid sequences. In practice, this is not an issue because, with relatively few exceptions, the genetic code is universal and well-known. That is, given any set of nucleic acids, one can predict the amino acid sequences that correlate to the nucleic acid sequence.[24]

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19. Some sections of the DNA molecule encode proteins. Such coding sections are termed exons; sections that do not code for proteins (noncoding) are termed introns. However, introns are not simply void of important biological information since elements within the introns regulate the expression of the coding exons. *See* BRUCE ALBERTS ET AL., MOLECULAR BIOLOGY OF THE CELL 104-106 (3d ed. 1994).

20. *Id.*

21. *Id.*

22. This is exemplified by the practice of tryptophan and alanine scans, techniques for looking at key enzymatic sections of proteins, whereby each amino acid of a protein is progressively mutated and the properties of the protein examined for effects. The underlying assumption is that the vast majority of positions can be mutated without a substantial effect on the protein; only those unique sections of the protein which are biologically critical will alter the protein's properties. *See, e.g.*, Li-Smerin, *A Localized Interaction Surface for Voltage-Sensing Domains on the Pore Domain of a K+ Channel.* 25 NEURON 411 (2000).

23. That is, each set of three nucleic acids (a triplet or codon) only encodes for a single amino acid; however, each amino acid may have different codons that encode for it. As such, two unique nucleic acid sequences may represent an identical amino acid sequence. ALBERTS ET AL., *supra* note 19, at 106.

24. In fact, given the right reading frame, one could predict the amino acid sequence with absolute certainty. Likewise, given the amino acid sequence, one could, with ease and absolute certainty, predict every possible combination of nucleic acid sequences that

Another problem is that the function of a protein (what it does and how it does it) is determined by the protein's structure. The protein's structure is determined by the amino acid sequence of the protein. Because of this relationship, in theory, one could predict the structure and function of a protein with nothing more than the sequence of the coding DNA.[25] In fact, the state of the art has now evolved to the point where rational protein design and modification, based on fundamental properties of the individual amino acids themselves, are now possible.[26] There are many types of interactions that occur along the amino acid chain which determine the protein's structure.[27] Surprisingly, the structure of a protein is predominately produced by a very large number of weak interactions. Because of this, the removal of any one of those small interactions will have practically no effect on the structure, and thus the function, of the protein.[28] A patent on a unique sequence, nucleic acid or amino acid, has no protective value since variations that do not alter the protein's function are common and easy to make.

3. *How Those In the Art View These Properties*

It has become a routine practice to identify and classify similar proteins in different organisms, as well as the functional parts of proteins, by comparing functionally equivalent sequences from different species

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could encode the amino acid sequence. While the possible number probably would be very large, a standard table of the genetic code, found in most biology textbooks, would be all that was required. *See id.* at 106.

25. The "[s]hape of a [p]rotein [m]olecule is [d]etermined by its [a]mino [a]cid [s]equence"; "related structures often imply related functions"; and "the conformation of a newly sequenced protein domain can be guessed if it is homologous to a domain of a protein whose conformation . . . " is known. *Id.* at 111, 123. *See also* Burkhard Rost, *Review: Protein Secondary Structure Prediction Continues to Rise,* 134 J. OF STRUCTURAL BIOLOGY 204 (2001) (stating that recent advances in protein prediction have resulted in a 76% accuracy rate in predicting the secondary state of amino acids in proteins).

26. *See, e.g.*, Scott A. Ross, *Designed Protein G Core Variants Fold to Native-like Structures: Sequence Selection by ORBIT Tolerates Variation in Backbone Specification,* 10 PROTEIN SCI. 450 (2001); Christopher A. Voigt et al., *Computational Method to Reduce the Search Space for Directed Protein Evolution*, 98 PROC. OF THE NAT'L ACAD. OF SCI. U.S.A. 3778 (2001); Shannon A. Marshall et al., *Achieving Stability and Conformational Specificity in Designed Proteins via Binary Patterning,* 305 J. OF MOLECULAR BIOLOGY 619 (2001).

27. Some of these interactions are very strong, such as disulfide bonds or charge interactions; others are very weak, such as van der waals interactions or hydrophobicity. ALBERTS ET AL., *supra* note 19, at 111-12.

28. See the previous discussion on this topic, *supra* note 22 (discussing the concept of the alanine and tryptophan scans).

(orthologs).[29] Sequences (either amino acid or nucleic acid) that are required for the protein to function are conserved between species. If such a critical element were changed, the protein would not function. If the protein were required for survival, the organism would be selected against evolutionarily. While critical elements are conserved between species, unimportant elements may vary.[30] Since this is all a function of time (or breeding cycles), organisms that evolved apart long ago show sequence similarities only at positions that are critical for function. Put another way, protein and nucleic acid sequences found in different species are the result of evolution over long periods. Thus, conservation of sequences between species allows identification of key structural elements in the sequences. Because of this, a critical sequence identified in a mouse is assumed to have a functionally and structurally equivalent sequence in humans and dogs. It is generally accepted that identification of the first member of any of these groups is not only the most difficult step in discovery, but also the most valuable since the sequence can be used to discover the equivalent sequence in another organism.[31]

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29. ALBERTS ET AL., *supra* note 19 at 122 (stating that structural homologies can help assign functions to newly discovered proteins). *See* BLAST (presenting an actual tool for genomic comparisons), *at* http://www.ncbi.nlm.nih.gov/BLAST (revised Jan. 29, 2001); Systematics and Molecular Phylogenetics, *at* http://www.ncbi.nlm.nih.gov/About/primer/phylo.html (defining such a comparison and why such comparisons can be useful in other ways) (revised Nov. 31, 2001); and Molecular Modeling: A Method for Unraveling Protein Structure and Function, *at* http://www.ncbi.nlm.nih.gov/About/primer/molecularmod.html (revised Dec. 31, 2001) (describing one benefit of sequence comparison for structure determination). *See also* Tim Fergestad et al., *Targeted Mutations in the Syntaxin H3 Domain Specifically Disrupt SNARE Complex Function in Synaptic Transmission*, 21 THE J. OF NEUROSCIENCE 9142 (2001) (regarding an experiment based on amino acid conservation demonstrating key functional residues by conservation); Michael Wood et al., *Structural Conservation of Ion Conduction Pathways in K Channels and Glutamate Receptors,* 92 PROC. OF THE NAT'L ACAD. OF SCI. U.S.A. 4882 (1995) (using sequence homology to develop experiments and draw conclusions); Rosa Planells-Cases et al., *Mutation of Conserved Negatively Charged Residues in the S2 and S3 Transmembrane Segments of a Mammalian K+ Channel Selectively Modulates Channel Gating*, 92 PROC. OF THE NAT'L ACAD. OF SCI. U.S.A. 9422 (1995) (using sequence conservation to direct experimental efforts and draw conclusions).

30. *See* Martin Kreitman et al., *Coding Sequence Evolution*, 9 CURRENT OPINION IN GENETICS & DEVELOPMENT 637 (1999) ("[S]elective constraint on protein function must be the dominant mode of natural selection acting on amino acid replacement . . . .").

31. For instance, once one knows the sequence in one organism one may use segments of that sequence as a probe to find equivalent sequences in other organisms. Alternatively, if the genome is known, a simple BLAST search will reveal all similar sequences in minutes. A BLAST search can be performed by visiting the BLAST website. *See* BLAST, *supra* note 29.

D. Recent Legal Conflicts in the Written Description Requirement

Considering the mutability of DNA and amino acid sequences, sequences often need to be described in very broad terms to ensure adequate protection.[32] Thus, many in the patent field have tried to describe DNA-based inventions in broad terms, without limiting the invention to the sole embodiment that was actually reduced to practice. Recent cases have addressed these attempts in conflicting manners.[33] A brief description of the cases is helpful in understanding the challenge that the USPTO faced in developing a unified definition of the written description requirement for the new Guidelines.

1. Nonobviousness Cases

While recent conflicts over the written description requirement have emphasized some internal inconsistencies, the source of these problems may have originated in case law concerned with issues of nonobviousness.

a) *In re Deuel*

While the issue in *In re Deuel*[34] was one of "obviousness," the holding has had a profound effect on the issue of adequate written description. Deuel's invention involved a process for isolating and purifying specific DNA molecules, in the context of a method for gene cloning and a partial amino acid sequence of the protein.[35] Deuel challenged the Board of Patent Appeals and Interferences' finding of obviousness of his invention. The court held that disclosure of a particular protein's sequence does not necessarily render a DNA sequence encoding that protein obvious because of the redundancy in the genetic code.[36] Effectively, the court minimized the analytic role of "one skilled in the art" and simply required the USPTO and courts to hold DNA sequences to be nonobvious over amino acid sequences. Interestingly, the USPTO has refused to follow this in the current

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32. This is especially true since minor variations are easy to produce once the initial work is done, e.g. a single point mutation via a "Quickchange mutagenesis kit," a kit mass-produced by Strategene.

33. *See generally* Limin Zheng, Note, *Purdue Pharma L.P. v. Faulding Inc.* , 17 BERKELEY TECH. L.J. 95 (2002) (describing recent cases involving the written description requirement for biotechnology patents).

34. *In re* Deuel, 51 F.3d 1552 (Fed. Cir. 1995).

35. *Id.* at 1554-1557.

36. "[A] prior art disclosure of the amino acid sequence of a protein does not necessarily render particular DNA molecules encoding the protein obvious because the redundancy of the genetic code permits one to hypothesize an enormous number of DNA sequences coding for the protein." *Id.* at 1558.

Written Description Guidelines, instead favoring what one skilled in the art would realize from an amino acid sequence.[37]

b) *In re Bell*

Similar to Deuel, Bell challenged the USPTO's finding that his inventions, the nucleic acids of the Preproinsulin-Like Growth Factors I and II, were obvious in light of a prior amino acid sequence of the protein and an enabling method to isolate it.[38] The court rejected the idea that such a nucleic acid sequence was obvious, primarily because of the vast number of possible nucleic acid sequences that could correspond to the specified amino acid sequence.[39] Bell specifically claimed *human* insulin. As such, the "unique" DNA sequence for human preproinsulin was not obvious out of the large number of possibilities described by the amino acid sequence.[40] The USPTO has used the court's holding in *Bell* as a means for limiting the USPTO's departure from the rules suggested in *Deuel*. While one can describe a nucleic acid by describing an amino acid, the USPTO has refused to grant each possible species in such a genus to an inventor, though the genus itself is described.[41]

2. *Written Description Cases*

a) *Vas-Cath v. Mahurkar*

Mahurkar relied on drawings of his double lumen catheter in one of his previous patents as support for a range of lumen ratios for a new utility patent.[42] While the original patent only contained a single ratio, the Federal Circuit held that the drawings were sufficient for an adequate written description of a range of ratios.[43] The court held that the written description is not limited to what is literally described; rather, it includes what one skilled in the art would be aware of as limitations.[44] This opinion has served as an expansive interpretation of the written description require-

37. The 2001 Written Description Guidelines, *supra* note 13, at 1102 ("[T]he question of possession of a class of nucleotides encoding that polypeptide can be addressed as a relatively routine matter using the understanding of the genetic code . . . .").

38. *In re* Bell, 991 F.2d 781 (Fed. Cir. 1993).

39. *Id.* at 784.

40. *Id.*

41. "[T]his does not mean that applicant was in possession of any particular species of the broad genus" and "possession of a large genus did not put a person of ordinary skill in the art in possession of any particular species." The 2001 Written Description Guidelines, *supra* note 13, at 1102.

42. Vas-Cath, Inc. v. Mahurkar, 935 F.2d 1555, 1558 (Fed. Cir. 1991).

43. *Id.* at 1566.

44. *Id.*

ment, allowing one to incorporate the knowledge of one skilled in the art in fulfilling the written description requirement.

b) *Amgen, Inc. v. Chugai Pharmaceutical, Co.*

Amgen alleged that Genetics Institute and Chugai Pharmaceutical's patents infringed Amgen's patent on the DNA sequence of human erythropoietin (EPO).[45] Genetics Institute possessed a prior patent on purified human EPO that also included in the specification a disclosure (although not an enabling disclosure)[46] for obtaining and using the DNA sequence of human EPO.[47] The court suggested that an inventor might need actual reduction to practice to establish inventions such as DNA sequences.[48] The court required this because an inventor would not be able to distinguish one sequence from another without actually knowing both sequences.[49] Thus, the court found that Genetics Institute's description was not a sufficient written description of the DNA sequence.[50] Some have read *Chugai* as the first in a series of decisions tending toward a per se rule for sequence patents rather than from the perspective of one skilled in the art.[51] However, the court in *Chugai* declined to hold that a per se rule was required, stating that there might be other "characteristics sufficient to distinguish [a gene] from other genes."[52]

c) *Fiers v. Revel*

Unlike *Amgen*, where the description was not enabling, Fiers had actually described a method that enabled one skilled in the art to isolate the protein of interest (beta-interferon).[53] In an attempt to distinguish *Amgen*, Fiers asserted that *Amgen* only applies to nonenabling disclosures, and that an enabled disclosure for a method of isolation is sufficient to describe an invention.[54] The court disagreed with Fiers' assertion and stated that allowing such a policy would allow would-be inventors to obtain patents before they had invented anything.[55] Such a policy would promote the dis-

45. Amgen, Inc. v. Chugai Pharmaceutical, Co., 927 F.2d 1200, 1203 (Fed. Cir. 1991).
46. *Id.* at 1207.
47. *Id.* at 1204-6.
48. *Id.* at 1206.
49. *Id.*
50. *Id.*
51. *See* Mueller, *supra* note 11, at 631, n.92 (1998).
52. *Id.* at 1206.
53. Fiers v. Revel, 984 F.2d 1164 (Fed. Cir. 1993).
54. *Id.* at 1169.
55. *Id.*

closure of research plans, rather than inventions.[56] Additionally, a second patent applicant, Revel, attempted to claim the DNA sequence by stating that it was part of the invention and including a reference for obtaining the DNA.[57] However, the court reemphasized its initial rejection of Fiers' application, stating that the inventor was required to produce a description of the DNA itself.[58]

The third applicant, Sugano, did have an adequate written description of the DNA. Sugano's application disclosed the entire sequence of beta-interferon in addition to containing an enabling disclosure of how to obtain the sequence.[59] The court seemed to be requiring an actual reduction to practice even where the inventor had provided enabling disclosures.

d) *Regents of the University of California v. Eli Lilly & Co.*

In 1977, the University of California (U.C.) discovered and patented the cDNA of insulin using the DNA sequence of rat insulin.[60] The patent also claimed "mammalian" and "vertebrate" insulin, and it provided enabling methods for obtaining such sequences.[61] The patent did not provide sequences themselves.[62] The University of California then filed suit against Eli Lilly for its production of human insulin.[63] Relying on *Fiers*, the court stated that enabling an invention is not synonymous with an adequate written description.[64] The court suggested that possession is not demonstrated without the complete sequence of the cDNA, since one skilled in the art would not recognize the invention without such an actual reduction to practice of the DNA sequence.[65]

While the amino acid sequence of human insulin was disclosed in the U.C. patent, the court used *Deuel* to state that a DNA sequence is, by definition, nonobvious in light of an amino acid sequence. The court went even further, however, stating that even if a description makes an invention obvious, it may not suffice for the written description requirement.[66] As such, it appears that even if something is obvious and enabled, one

56. *Id.*
57. *Id.* at 1170.
58. *Id.*
59. *Id.* at 1172.
60. Regents of the University of California v. Eli Lilly & Co., 119 F.3d 1559, 1569 (Fed. Cir. 1997).
61. *Id.* at 1563.
62. *Id.* at 1562-3.
63. *Id.* at 1562.
64. *Id.* at 1567.
65. *Id.* at 1568.
66. *Id.* at 1567.

may not have actually described it. The court found such a situation acceptable since the "level of skill in the art" was very low.[67]

Generally, the USPTO has interpreted *Lilly* to mean that a description by function is not sufficient for a DNA claim.[68] In order to avoid any appearance of conflict between *Vas-Cath* and *Lilly*, the USPTO has stated that Lilly "explains that a chemical compound's name does not necessarily convey a written description . . . particularly when a genus of compounds is claimed."[69] In effect, one skilled in the art cannot "visualize or recognize the identity of the members of the genus."[70] Presumably this is so because of the "unpredictability" or low "level of skill in the art," a factor the court and the USPTO seem to have interpreted as determinative of all other facts in the written description requirement.

II. THE GUIDELINES

The new Guidelines outline a three-step process for analyzing a written description. First, one must determine what the claim covers as a whole.[71] Second, one must examine the application to determine *how* support is provided for the claimed invention.[72] Finally, one determines whether the written description is sufficient to inform one skilled in the art that the applicant possessed the invention as a whole at the time the application was filed.[73] Possession can be demonstrated by: (a) reduction to practice;[74] (b) a clear depiction;[75] or (c) a disclosure of relevant, distin-

67. *Id.* at 1568.

68. The 2001 Written Description Guidelines, *supra* note 13, at 1110, n.43.

69. *Id.* at 1100.

70. *Id.* (quoting Regents of the University of California v. Eli Lilly & Co., 119 F.3d 1559, 1568 (Fed. Cir. 1997)).

71. *Id.* at 1105. Additionally, each claim must be given its broadest reasonable interpretation in view of the written description. *Id.*

72. *Id.* This includes an examination of the specific embodiments, figures, and sequence (nucleotide or amino acid) listings. It is at this point that one must determine which field and what level of skill is present in the art of the invention. The Guidelines note that information that is well known in the art need not be described in detail. *Id.* Accordingly, there is a lower requirement for a description in technologies with a high level of skill in the art, while there is a higher requirement for technologies that have a lower amount of knowledge and skill. *Id.*

73. *Id.* at 1105-6.

74. *Id.* at 1105.

75. *Id.* A clear depiction can be achieved by detailed drawings and structural formula. *Id.*

guishing, and identifying characteristics.[76] At this point, one considers whether there is sufficient evidence of possession.[77]

The USPTO specifically indicates that in technologies that are mature, the written description requirement is met, even if the description only discloses a method of manufacturing the invention and the function of the invention.[78] For young or unpredictable technologies, however, more evidence is required to show possession.[79] This heightened standard also applies if the invention is characterized by factors which are not reasonably predictable. In order to determine the maturity of the art or the level of skill in the art, the USPTO uses patents and printed publications.[80]

The USPTO also describes the requirements for obtaining a claim on a genus, a core claim for many DNA claims. In addition to the previous three requirements, the claim must describe a "representative number of species."[81] A claim describes a representative number of species when the described species "are representative of the entire genus."[82] For instance, in a genus that encompasses widely variant species, disclosure of a single species is insufficient.[83] However, the level of description for the species does not have to be so great as to provide support for each species individually.[84]

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76. *Id.* Identifying characteristics include, physical/chemical properties, functional characteristics combined with a structure/function correlation, and complete or partial structures (either amino acid or nucleic acid). *Id.* at 1106.

77. In situations where a complete structure is disclosed, the written description requirement is satisfied. If a complete structure is not disclosed one considers such factors as, level of skill in the art, partial structures, physical/chemical properties, functional characteristics, functional characteristics with additional structure/function correlations, and the method for making the invention. "Disclosure . . . of such identifying characteristics that distinguish the claimed invention from other materials and would lead one of skill in the art to the conclusion that the applicant was in possession of the claimed species is . : ." the requirement that the above factors must demonstrate. *Id.* For a full description of such scenarios, see *Id.*

78. *Id.* at 1106 (citing *In re Hayes Microcomputer Products, Inc.*, 982 F.2d 1527, 1534-35 (Fed. Cir. 1992)).

79. *Id.*

80. *Id.*

81. *Id.*

82. *Id.* Additionally, the USPTO specifically notes that there may be situations where a single species represents an entire genus. *Id.* at 1110, n.55. However, the USPTO specifically prohibits this for DNA descriptions. *Id.* at 1111, n.56.

83. *Id.* at 1106.

84. *Id.* at 1106. "For example, in the molecular biology arts, if an application disclosed an amino acid sequence, it would be unnecessary to provide an explicit disclosure of nucleic acid sequences that encoded the amino acid sequence." *See Id.* at 1111 n.57.

III. DISCUSSION

A. Inconsistencies between the Guidelines and Prior Case Law

Since the prior case law upon which the Guidelines are based may be inconsistent,[85] it is not surprising that the new Guidelines can be interpreted as conflicting with prior case law. This is most noticeable in the area of biotechnology involving DNA sequences. While the court in *Lilly* held that claiming a nucleic acid sequence by describing an amino acid sequence was not an adequate description of the invention,[86] the Guidelines suggest otherwise.[87] Additionally, while the court in *Lilly* held that stating the name of a DNA sequence is not an adequate description,[88] the Guidelines allow descriptions of sequences in terms of percent identity,[89] a description arguably equivalent to stating a name.[90] This differs from the prior case law not only by allowing a functional term to define the sequence, but also because the use of percent identity results in potentially huge numbers of sequences that are described by the patent.[91] Such a deviation starts to erode the per se rule of nonobviousness that cases such as *Bell*[92] and *Deuel*[93] have suggested.

One manner in which the USPTO can attempt to justify these differences is that the "level of knowledge in the art" of biotechnology when the patent in *Lilly* was issued was low, and thus the patent required more description than is required of a biotechnological invention of today.[94] This

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85. See discussion, *supra* Part I.D.

86. Regents of the University of California v. Eli Lilly & Co., 119 F.3d 1559, 1567 (Fed. Cir. 1997).

87. The 2001 Written Description Guidelines, *supra* note 13, at 1102 (stating that nucleic acid sequences can be determined from amino acid sequences).

88. *Lilly*, 119 F.3d. at 1567 ("[T]he name cDNA is not itself a written description of that DNA. .").

89. "[T]here is no basis for a per se rule . . . limiting DNA claims to only the sequence disclosed." The 2001 Written Description Guidelines, *supra* note 13; *see also*, Interim Training Materials, Ex. 14, *supra* note 17, at 53-55.

90. For instance, one might consider the statements 1) sequence X is 80% identical to proteins that are of group Y, and 2) a sequence belonging to the group Y (which consists of proteins that are 80% identical), to be equivalent.

91. For instance, there are 5^20 permutations of a 100 amino acid sequence with 95% identity.

92. *In re* Bell, 991 F.2d 781 (Fed. Cir. 1993).

93. *In re* Deuel, 51 F.3d 1552 (Fed. Cir. 1995).

94. Some suggest "that, with regard to biotechnological inventions, as the general knowledge and skill in this art improves, the PTO will allow increasingly broader claims. . . . This position reflects the argument that while the state of DNA inventions was once unpredictable, today the state of the art has advanced to the point where isolating nucleotide sequences is routine to persons skilled in the art, and therefore predict-

concept is in keeping with part of the *Lilly* decision and is reiterated in the Guidelines as the factor of the "level of skill and knowledge in the art."[95] However, many believe that the "level of skill in the art" at the time of the filing of the *Lilly* application was sufficiently high that "one of skill in the art" would have understood what U.C. meant by its description of mammalian insulin in its original patent.[96] While debatable, the USPTO suggests that regardless of the changes that may have occurred in the art of biotechnology over the last two decades, such changes are not sufficient to render the claims in *Lilly* as adequately described, even at today's "level of skill in the art" of biotechnology.[97]

Many have seen *Lilly* as a departure from the fact-based standard of what one skilled in the art would recognize, to a legal rule that some written descriptions are per se inadequate.[98] Concerning biotechnology, many have viewed *Lilly* as requiring the recitation of the literal nucleic acid sequence for an adequate written description. Because of this requirement, commentators have suggested that *Lilly* "reflect[s] an increasingly-widening gulf between the norms of the business and scientific community and those of the United States patent system."[99] Given this interpretation of *Lilly*, the USPTO's allowance of claims using amino acids and percent homology are in conflict with the court's requirement, as in *Lilly*, that the application recite a sequence.[100]

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able." Margaret Sampson, *The Evolution of the Enablement and Written Description Requirements Under 35 U.S.C. 112 in the Area of Biotechnology,* 15 BERKELEY TECH. L.J. 1233, 1267 (2000).

95. The 2001 Written Description Guidelines, *supra* note 13, at 1106.

96. "Persons skilled in the art of recombinant DNA technology were very likely to have understood that by making the rat insulin cDNA, the UC inventors conceptually possessed the human insulin cDNA (if not all mammalian cDNAs)." Mueller, *supra* note 11, at 652 (1998). For instance, the genetic code which allows one to predict (in a functional manner) nucleic acids from amino acids was known long before the U.C. patent was written in 1979. *See* Marshall Nirenberg & Christian Wunsch, *RNA Codewords and Protein Synthesis*, 145 SCIENCE 1399 (1964). In addition, homology is a concept that has been ingrained in biology from the first days of taxonomy and was acknowledged specifically on the protein level before the *Lilly* decision as well. *See* Marshall Needleman & Philip Leder, *A General Method Applicable to the Search for Similarities in the Amino Acid Sequence of Two Proteins,* 48 J. MOL. BIOL. 443 (1970).

97. Interim Training Materials, Ex. 17, *see supra* note 17, 61-64.

98. "The *Lilly* court's per se rule that a claim to a cDNA must be described in terms of its specific nucleotide sequence fails to address fact-specific questions concerning the state of the art and the level of skill among art workers, from whose perspective the written description inquiry must be answered." Mueller, *supra* note 11, at 651.

99. *Id.* at 652.

100. This is emphasized by the USPTO's statement that there is no per se rule concerning the requirements for patenting a DNA sequence. The 2001 Written Description

B. Inconsistencies within the Guidelines

Despite the progressive nature of some of the requirements, the Guidelines are not as broadening as one might first suspect. For instance, while the Guidelines depart from prior case law in a fairly permissive manner,[101] the comments in the Guidelines also state that a genus claimed by name is not sufficient because one cannot identify the members of the genus.[102] Additionally, descriptions consisting only of the function of the invention are insufficient to achieve an adequate written description if they only indicate what the composition does, rather than what it is.[103] Finally, the factor of the "level of skill in the art" limits any relaxation of the written description requirement. In effect, the ability to ignore what one skilled in the art may know, because the Examiner has declared that some element in the field is too uncertain,[104] allows the Examiner to require actual reduction to practice.[105]

The implementation of the rules in the training examples makes the inconsistencies clear. For instance, according to the USPTO, if a scenario similar to *Lilly* occurred today, the USPTO would reject the application for failing to satisfy the written description requirement.[106] A comparison of the Examples in the training materials, in particular the *Lilly* Hypothetical in Example 17 and the more progressive Examples, may be helpful in describing these inconsistencies.[107]

Guidelines, *supra* note 13, at 1101. Even more impressive is the USPTO's statement regarding the requirements to claim a genus of DNA sequences by describing an amino acid sequence. The 2001 Written Description Guidelines, *supra* note 13, at 1101-1102.

101. There is no "per se rule requiring disclosures of complete DNA sequences or limiting DNA claims to only the sequences disclosed." *Id.* at 1101. Amino acid sequences appear to be sufficient for claiming the equivalent nucleic acid sequence. *Id.* at 1102. There is even an admission that a single species would be sufficient to claim a genus "when the description of the species would evidence to one of ordinary skill in the art that the invention includes the genus." *Id.*

102. Although a search of the National Center for Biotechnology Information's database by a single protein's name would yield a genus of sequences with regions of conservation. Presumably, the regions of conservation would automatically identify the critical structural elements of the protein that one skilled in the art would recognize as critical for that particular protein.

103. The 2001 Written Description Guidelines, *supra* note 13, at 1101.

104. Uncertainty can arise either in the art itself or in the features that define the claim.

105. The 2001 Written Description Guidelines, *supra* note 13, at 1101.

106. This is also the strongest evidence that the differences between the Guidelines and *Lilly* cannot be attributed to a change in the level of skill in the art since the USPTO is still claiming that such a claim would not be sufficient.

107. Interim Training Materials, *supra* note 17, at 61-64.

C. Example 17 Demonstrates the Guideline's Inconsistencies

Example 17 of the training materials presents a fact scenario identical to *Lilly*. As in *Lilly*, the patent recites a sequence for rat cDNA of proinsulin,[108] as well as a method for determining other cDNA sequences.[109] In analyzing the adequacy of the description, the Example discusses four factors: 1) the absence of human insulin cDNA; 2) variability of insulin cDNA; 3) the absence of evidence concerning how the structure of rat cDNA could provide structural evidence of human cDNA, based on rat cDNA; and 4) the absence of evidence that the rat cDNA had a known structural relationship to the human cDNA. The Example then concludes that the written description requirement is not met.[110] This decision concurs with the holding in *Lilly*.[111] However, it is unclear how this result is justified when each of the four factors is satisfied under the new Written Description Guidelines.

1. No species of human insulin cDNA is disclosed

While no human cDNA is literally defined in Example 17, one skilled in the art could equate the given human amino acid sequence with the genus of nucleic acid sequences claimed.[112] The Guidelines explicitly recognize this.[113] Additionally, by sequence comparison of the given rat and human sequences, it is possible to obtain an idea of the percent identity (and thus sequence) of even the missing elements that encode the "pre" aspect of the pre-proinsulin.[114] Finally, the Guidelines suggest that an

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108. Proinsulin is a biological precursor of insulin. The example also includes pre-proinsulin, a precursor of proinsulin.

109. Interim Training Materials, *supra* note 17 at 61-64. Additionally, the example stipulates that the amino acid sequence of human proinsulin is known. However, it is stated that the human insulin sequence may vary, and that insulin is post translationally modified. There is a genus claim directed to isolated human cDNAs which encode insulin. *Id.*

110. *Id.* at 64.

111. Interestingly, while the facts and outcome are identical, the "level of skill in the art" is not since the field has had 20 years to develop since the U.C. patent in *Lilly*. As such, the theory that the result in *Lilly* would not occur today, because there is a higher level of skill in the art, is not consistent with the USPTO's Interim Training Materials.

112. See previous discussion on this topic, *supra* note 24.

113. The 2001 Written Description Guidelines, *supra* note 13, at 1102 ("[P]ossession of a class of nucleotides encoding that [amino acid sequence] can be addressed as a relatively routine matter . . . ").

114. For instance, a quick comparison of the amino acid sequences of the rat and human insulin protein by BLAST may yield a percent identity of 84% (88% similarity). *Supra* note 29. In theory, assuming that the functional aspects of the protein should be conserved and that the pre and pro elements of insulin are functional, one should also

amino acid sequence would suffice for a genus claim of the nucleic acids.[115]

2. *Variation among individuals*

Variability of proteins across individuals should be allowed in the written description requirement. The USPTO rejects the idea that sequences can only be claimed by a literal recitation of the sequence.[116] All that is required is that the species be representative of the structures of the entire genus.[117] As noted by Example 9[118] and Example 14,[119] there are multiple methods for demonstrating genus claims with a *single* species, even if it is a piece of DNA. The important element is that the structurally functional features of the genus (the common element in each species) are described to one of skill in the art, keeping in mind that unimportant elements need not be described.[120] Such a description is present here (constructively) because the amino acid sequences of rat and human insulin allow one to predict the critical structural elements of the protein, and thus of the cDNA for insulin.[121] Additionally, variation among individuals is not a relevant concern because such variations, presumably, do not alter the underlying invention.[122]

3. *Lack of a structure/function relationship*

The remaining factors, the lack of a structure/function relationship between the rat and human cDNA, simply ignore the knowledge of one

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have an idea of the percent homology of the pre and pro regions of the human cDNA (84/88%) from the rat sequence.

115. 2001 Written Description Guidelines, *supra* note 13, at 1102.

116. *Id.* at 1101.

117. *Id.* at 1106.

118. *Interim Training Materials*, *supra* note 97, at 35-37 (demonstrating a description of a genus with a single species by using stringent hybridization conditions).

119. *Id.* at 53-55 (using percent identity to describe a genus with a single species).

120. 2001 Written Description Guidelines, *supra* note 13, at 1106.

121. Additionally, since a BLAST search results in a rat to human comparison of 84%, the phrase, "human insulin cDNA" includes the DNA sequence that has "84% identity to rat cDNA." See BLAST, *supra* note 29. Because of this functional equivalence, it could be argued that there should be no difference between the use of an agreed upon name or scientifically agreed upon percentage.

122. For example, assuming insulin functions the same in each human, or even in mammals, variations in the cDNAs between the organisms are not necessary for the operation of the protein. Since these variations aren't part of the invention, the variations may be defined as irrelevant features of the invention. Since irrelevant features of an invention never need to be disclosed, these variations need not be described in the written description.

skilled in the art. The simplest comparison[123] between amino acid sequences of the two organisms will demonstrate conserved areas in the sequences. Presumably these areas are conserved because they are required for protein function. Conservation thus defines the structurally significant areas of the nucleic acid sequences of both the rat and human cDNA.[124] As such, the critical structural relationships between the human and rat amino acid sequence, and constructively the nucleic acid sequence, would be routine for one skilled in the art to determine, and thus need not be disclosed. The assertion that there may be substantial variation among the species is meaningless. It is evident that the key structures for the desired functions are conserved between species since insulin protein function is conserved across a wide range of organisms.[125] Since the sequences that make the protein function are conserved, the unique sequences of the possible variations of insulin do not need to be described because these highly variable sequences are not elements that are essential to the invention.

Thus, it appears that the knowledge of one skilled in the art has been deemed lacking in this scenario. Presumably, this is for the same reason that the court in *Lilly* found, that the "level of skill and knowledge in the art" was too low to allow such a claim.

D. Per se Rules are the Source of the Inconsistencies

Some conflict between patent prosecution and patent litigation is inevitable. However, the current conflict has been recognized as a widening gulf between the norms of the scientific community and those of the legal system.[126] As such, the USPTO and the courts seem willing to treat the written description requirement as a legal issue,[127] as opposed to a

123. For instance, the use of a program such as BLAST is a common method of analyzing sequences. *See* BLAST, *supra* note 29.

124. *See, e.g.*, J. Michael Conlon, *Evolution of the Insulin Molecule: Insights into Structure-Activity and Phylogenetic Relationships*, 22 PEPTIDES 1183 (2001) (applying such a comparison for fifty sequences of insulin).

125. Additionally, for an item such as insulin where there is a long history of cross species equivalence of the protein between various organisms, one skilled in the art would take the structural similarities between the insulin proteins of various organisms to be highly conserved, without additional evidence. *See* ALBERTS ET AL., *supra* note 19, at 122.

126. "Since the addition of Lilly to the Fiers v. Revel decision, scholars and commentators alike have argued that the rulings are a radical departure from traditional description requirement jurisprudence." Lisa A. Karczewski, *Biotechnological Gene Patent Applications: The Implications of the USPTO Written Description Requirement Guidelines on the Biotechnology Industry*, 31 MCGEORGE L. REV. 1043, 1064-5 (2000). One reason for such a gulf may be due to the fact that the requirements for something to be "obvious" in a legal sense do not accurately reflect what is scientifically "obvious." *See* MUELLER, *supra* note 11, at 615 (1998).

written description requirement as a legal issue,[127] as opposed to a question of fact.

In the particular instance of DNA technology, it seems that the origin of the current problems may be traced back to courts' decisions in *In re Bell*[128] and *In re Deuel.*[129] While these decisions may have been technically correct as far as the nonobviousness analysis were concerned, these holdings promote patenting previously discovered sequences by simply altering a single amino or nucleic acid. While greatly limiting the protection that many of the DNA inventions received,[130] the holdings of *Bell* and *Deuel* had a larger negative impact—the development of per se rules.

E. Per se Rules and the "Level of Skill in the Art" are Self-Defeating for Promoting Certain Research in Biotechnology

A system that ignores the ability of one skilled in the art by using per se rules may actually inhibit downstream product optimization research while also removing the incentive for upstream, basic research.[131] This is particularly relevant in biotechnology. The combination of the reduction of informational barriers, an emphasis on granting patent protection only to optimized products, and the certainties of FDA testing costs, result in a scenario where downstream research is the only area encouraged. However, there is little protection for getting to, or finding value in, the final product.

1. Informational barriers protecting drug optimization are disappearing

A patent is traditionally a reward for a completed invention, not a license to hunt for one.[132] While this may have been the proper role of a patent in biotechnology in the past, it is not clear that an overly strict application of this idea is appropriate now. The amount of information that is available to the skilled artisan has dramatically increased in the biotech-

127. For example, the development of per se rules concerning the obviousness of DNA sequences or the USPTO's deferring to the court's holding in *Lilly* in Example 17 of the Interim Training Materials. Interim Training Materials, *supra note* 17, at 61-64.

128. *In re* Bell, 991 F.2d 781 (Fed. Cir. 1993).

129. *In re* Deuel, 51 F.3d 1552 (Fed. Cir. 1995).

130. Often to a point of uselessness, as for example, limiting the invention to rat insulin as in *Lilly. See* Regents of the University of California v. Eli Lilly & Co., 119 F.3d 1559 (Fed. Cir. 1997).

131. Whether this information is ignored simply for per se rules or because the USPTO has declared that the "level of skill in the art" is low, may not matter because the key factor for this analysis is that "one skilled in the art" is able to avoid another's patent without an inventive step.

132. Brenner v. Manson, 383 U.S. 519, 536 (1966).

nology field, primarily because of progress in the sequencing of entire genomes. Requiring a reduction to practice because of a low "level of skill in the art," as in *Lilly,* also increases the amount of information available to the practitioner.[133] The availability of this information reduces the initial barrier for entering the field of drug design, as well as the amount of protection that trade secrets can provide late in that area. The result may be that the financial risk in drug development has now been shifted from discovery to optimization of a target drug.[134] Such a shift is consistent with the general goals of the court in *Lilly* because only disclosure of the *final species* is sufficient. It is not clear that drug design will actually be encouraged by this shift.

2. *Per se rules discourage pioneering work but favor optimization*

The patent system has traditionally granted broad protection to pioneers in a field.[135] The courts and the USPTO have changed this by granting less protection to pioneers in uncertain fields (i.e., fields with a "low level of skill in the art"). This is a disincentive for pioneering work, but may be an incentive for optimizing existing inventions.[136] This is particularly true with regard to the current written description requirement, because inventions may be obvious and enabled, but may still escape protection.[137]

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133. For instance, patents could fully enable but not protect obvious targets for downstream inventions. *See* Regents of the University of California v. Eli Lilly & Co., 119 F.3d 1559 (Fed. Cir. 1997) (holding that enablement of an invention does not provide an adequate description of the invention and that a description which renders something obvious may not provide an adequate written description).

134. Interestingly, this early part of the process usually involves shifting from animal to human models, a process obviously not encouraged by the court's decision in *Lilly*. *See id.* (holding that a description which is adequate for rat insulin is not adequate for human insulin).

135. *See generally* Boyden Power Brake Co. v. Westinghouse, 170 U.S. 537, 569 (1898). *See also* 5A DONALD S. CHISUM, CHISUM ON PATENTS §18.02[2] (1998).

136. For instance, people may choose optimization because: a) it is relatively easy compared to pioneering work, and b) it is the only area in which they can get patent protection.

137. For instance, following the court's decision in *Lilly*, there is no longer an incentive for the U.C. to disclose the sequence of a rat protein and a method for obtaining the same sequence from humans, because another entity, with more resources, can use the disclosed information to obtain the literal sequence first.

3. *Drug optimization is discouraged without adequate upstream protection*

While optimization may be an appropriate goal of the patent system, promotion of research at this point in the research stream may not be adequate to encourage downstream research, such as optimization of drug technologies, in biotechnology. If initial patent protection is too narrow and competitors can readily identify and create alternative, but equivalent, embodiments of the invention, it is safe to assume they will.[138] While this may initially attract researchers to the point in the research stream where drug candidates are being selected (since a "new" invention can be easily obtained),[139] this is a disincentive in the development of further downstream research or optimization of the drug. The existence of numerous alternative but equivalent drug candidates is a guarantee that the value of the drug will be much less when it enters the market, because the drug will hit the market at approximately the same time as its equivalents.[140]

Adequate protection for biotechnology inventions may be required further upstream than adequate protection for many other fields because of the huge and relatively certain costs of FDA approval and the ease of making equivalent variants that are, per se, nonobvious.

IV. CONCLUSION

The individual differences between prior case law and the Guidelines, as well as inconsistencies within the Guidelines themselves, may be due to the USPTO's attempt to combine both per se rules and factors such as "the level of skill in the art" with the actual knowledge and ability of one skilled in the art. To the extent that the Guidelines encourage the analysis of the written description requirement as an issue of fact, the purposes behind the patent system will be well served.

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138. This may be exacerbated if the patent system itself is encouraging improvement patents over pioneering patents, guaranteeing that inventions with minor modifications will be given as much protection as any other invention.

139. For example, by introducing a point mutation or finding the gene's ortholog in another organism, "novel" but functionally identical inventions may be readily "discovered."

140. In effect, allowing generics to enter the market when the original enters.

ADDITIONAL DEVELOPMENTS—PATENT

AMAZON.COM V. BARNESANDNOBLE.COM, INC.

239 F.3d 1343 (Fed. Cir. 2001)

By Tiffany Weeks

In *State Street* Bank & Trust Co. v. Signature Financial Group Inc., 149 F.3d 1368 (Fed. Cir. 1998), the Federal Circuit broadened the scope of patentable subject matter under 35 U.S.C. § 101 ("section 101"). The decision extended the scope of patentable subject matter to encompass business methods as a class. The patent in suit in *Amazon.com, Inc. v. Barnesandnoble.com, Inc.* was the first internet business method patent to be litigated and thus provided the Federal Circuit an opportunity to implement its holding in *State Street.*

In 1995, the online market was beginning to explode. Yet, a large population of online consumers could not be reached due to wide-spread fear of the potential security risks associated with online credit card purchases. In an effort to realize full revenue potential, both retailers and credit card companies began to introduce a variety of remedies to calm consumers' fears.

Around May 1997, online retailer Amazon.com ("Amazon"), introduced the "1-Click" solution to address the long-standing problem faced by all online retailers—the abandonment of approximately 65% of online shopping carts. By whittling the required purchase steps down to one click, as opposed to the several confirmation steps employed by the more traditional shopping models, Amazon's ordering system sought to capitalize on the impulsive nature of buyers.

United States Patent No. 5,960,411 ("the '411 patent") issued on September 28, 1999, and is assigned to Amazon. In the '411 patent, the 1-Click method assigns each customer a unique customer identifier ("cookie") that allows the customer to automatically be recognized without requiring them to log on. The item to be purchased is chosen from a visual display. The method requires only one click for an order to be generated, as the customer's credit card and shipping information has been previously entered and stored. The customer information is retrieved from a second server, where it has been stored and scrambled for added security. The order does not require any further confirmation from the customer. Amazon's patent explicitly disclaims the "shopping cart" model which was the standard method for online shopping prior to 1-Click

Wanting to capture a share of the market that Amazon was able to tap, BarnesandNoble.com implemented its "Express Lane" ordering feature in May 1998. The Express Lane feature allowed customers to purchase a displayed product with a single click of a mouse. Less than one month after the '411 patent issued, Amazon filed suit against BarnesandNoble.com (hereinafter "BN") for infringement its patent. Amazon moved for a preliminary injunction to enjoin BN's use of the Express Lane method.

I. LEGAL BACKGROUND

A. Preliminary Injunction Requirements

Four elements must be met for a court to order a preliminary injunction: (1) a reasonable likelihood of success on the merits at trial; (2) a showing that the party would suffer irreparable harm if the preliminary injunction was *not* granted; (3) the balance of hardships had been determined to tip in the movant's favor; and (4) the preliminary injunction sought was in the public interest. 35 U.S.C. § 283.

In the patent infringement context, the trial court is required to make a preliminary determination as to patent validity before injunctive relief can properly be granted. This construction is compatible with and subsumed under the first prong of the preliminary injunction standard. *See* Sofamor Danek Group v. Depuy-Motech, 74 F.3d 1216 (Fed. Cir. 1996). Despite the strong presumption of validity under 35 U.S.C. § 282, the party seeking relief may still establish a "likelihood of success on the merits." If the accused infringer, however, raises a substantial question as to the validity of a patent on anticipation or obviousness grounds, the burden then shifts to the patent holder to provide sufficient evidence to rebut these attacks. *See* Amazon.com, Inc. v. Barnesandnoble.com, Inc., 73 F. Supp. 2d 1228, 1239 (W.D. Wash. 1999). If the patent holder has sustained this burden, then the injunction should issue. Genentech, Inc. v. Novo Nordisk, A/S, 108 F.3d 1361, 1364 (1997). Thus, the decision on whether or not issue a preliminary injunction entails an assessment of validity, including questions of obviousness. *See* We Care, Inc. v. Ultra-Mark Int'l Corp., 930 F.2d 1567 (Fed. Cir. 1991).

To reverse a preliminary injunction that has been granted the Federal Circuit must make a clear showing that the district court committed legal or factual error. New England Braiding Co. v. A.W. Chesterton Co., 970 F.2d 878, 882 (Fed. Cir. 1992). Additionally, case law has held that no one factor is "'dispositive' [but] the absence of an adequate showing with regard to any one factor may be sufficient, given the weight or lack of it assigned the other factors, to justify the denial." Chrysler Motor Corp. v. Auto Body Panels of Ohio, 908 F.2d 951, 953 (Fed. Cir. 1990). Therefore, before a reversal of an injunction can be ordered, the Federal Circuit *must* engage in a balancing test to support its decision.

B. Invalidity

In assessing validity, the court must construct the claims of the patent to determine if the patent was anticipated by prior art. For a patent to be invalid for a lack of novelty, every element of the patent must be present in a single prior art reference. Merck & Co., v. Mylan Pharms., 19 F. Supp. 2d 334, 345 (1998). Each individual element within both the prior art and the patent in question must be present. If this happens to be the case, then the patent is said to anticipate the prior art and it will be held invalid. If the patent in question incorporates additional elements or there are missing elements, the patent will withstand the anticipation examination and the inquiry for a validity determination will a proceed to a an obviousness determination under 35 U.S.C. § 103.

Section 103 requires the court to consider additional factors before a patent may be issued: (1) the nature of the problem to be solved; (2) the teachings of prior art; and (3) the knowledge of persons of ordinary skill in the art (where this is a hypothetical legal construction).

In 1966, the Supreme Court decided *Graham v. John Deere Co. of Kansas City*, 383 U.S. 1 (1966). Two principles emerged from the Court's decision: (1) the *differences*

between the invention and the prior art must be assessed *as a whole*; and (2) courts may not determine validity in hindsight. Thus, in determining the obviousness of a patent, courts must make a determination as to what a person of ordinary skill in the art, at the time, would have considered obvious.

In addition, the Supreme Court looked at other objective indicia in determining the obviousness of the patent. These considerations—commercial success of the invention, long-felt need, and failure of others—were used as further measures of the patent's validity. These secondary considerations have continued to evolve within the federal courts and additional objective factors have been incorporated into the obviousness analysis over time. In *Weatherchem Corp. v. J.L. Clark, Inc.*, 163 F.3d 1326 (Fed. Cir. 1998), the Federal Circuit formally incorporated secondary considerations as the fourth prong of the obviousness test.

If a single prior art reference does not render the patented invention obvious, and therefore invalid, the main inquiry shifts to obviousness in light of a combination of references. Here, the inquiry is whether the combination was "taught, suggested or motivated through prior art" *or* if someone of ordinary skill in the art would have found the combination obvious. If a motive to combine exists or a combination is obvious to one skilled in the art, the patented invention is obvious in light of the combined references. Nevertheless, a patent that combines elements from several prior art references may be found to be nonobvious where the prior art "teaches away from" the combination. Winner Int'l Royalty Corp. v. Wang, 202 F.3d 1340 (Fed. Cir. 2000).

II. CASE SUMMARY

A. The District Court Opinion

During the preliminary injunction hearing, BN raised the affirmative defenses of anticipation and obviousness under 35 U.S.C. §§ 102-103. The district court found these defenses lacking in merit and granted a preliminary injunction on December 1, 1999.

BN argued that the 1-Click patent was anticipated, or at least rendered obvious, by five prior art references not considered by the patent examiner, and was thus invalid. BN later re-introduced these five prior art references to the Federal Circuit for consideration. Amazon's 1-Click method shared common elements with each of the references. *Web Basket,* like Amazon, used a unique customer identifier ("cookie") to identify the customer and stored this data on a server. It did not, however, use a one click method in a strict sense, as it did not employ a purchasing method that was shopping cart independent. The *Netscape Merchant* reference is used interchangeably with *"Creating the Virtual Store,"* by Magdalena Yesil. Both identify the same reference. The reference, in total, consists of four lines of excerpted text and reads: "*Instant Buy Option*. Merchants also can provide shoppers with an Instant Buy button for some or all items, enabling them to skip check out review. This provides added appeal for customers who already know the single item they want to purchase during their shopping excursion."

The *Oliver's Market* reference was also submitted by BN. Like, 1-Click, *Oliver's Market* also made use of u cookies and employed a server to store customer information. Although it spoke of a "one click" method, it was not shopping-cart independent as claims 1 and 11 of the '411 patent specifically require. The '780 reference was also submitted by BN in their defense. BN argued that the '780 reference used a "single action ordering method." The '780 patent covers a shopping cart-independent method that also happened to use the world wide web.This reference, unlike the 1-Click method, may re-

quire that a person "log on" before they are recognized by the navigating system.The method does not, however, involve any "ordering" per se. A debate as to the definition of "order" and the similarity of this method to the 1-Click method ensued. The district court ultimately rejected this reference as not having any bearing upon the validity of the 1-Click method. Finally, BN cited the CompuServe reference. CompuServe shares elements in common with 1-Click in that it also uses a single action ordering component. Compuserve, however, did not display items that could be purchased (as claims 1-8 and 11-26 of the '411 patent require) and was not used on the world wide web, but through a direct modem connection. Additionally unlike the 1-Click method, Compuserve sent an order confirmation to the user. The district court concluded that these five references did not anticipate the '411 patent under § 102, as no single references possessed all of the elements of the '411 patent.

BN also argued that the prior art at least rendered the patent obvious under 35 U.S.C. § 103. The court concluded that, although there were similarities, none of the prior art had utilized an "ordering" component consisting of a single action. Pivotal to the court's decision was its conceptualization of the four line excerpt of the *Netscape Merchant* publication. The court concluded that, considered within its context, the *Netscape Merchant* reference did not render Amazon's 1-Click patent obvious. The court's secondary considerations analysis also weighed in favor of the validity of the '411 patent.

The district court concluded that BN failed to meet its burden of proffering "clear and convincing" evidence as to the invalidity of the 1-Click patent. The court also concluded that societal interest tipped in Amazon's favor and thus enjoined BN from using its Express Lane feature. On appeal to the Federal Circuit, BN argued that the district court construed key claim limitations inconsistently and misunderstood the teachings of prior art references. Amazon aligned itself with the district court, arguing that the court was correct both in its claim construction and in its understanding of the prior art.

B. The Federal Circuit Decision

In *Amazon*, the Federal Circuit adopted a two-step inquiry for scrutinizing the district court's grant of a preliminary injunction. First, the Federal Circuit analyzed whether Amazon would likely prove that BN had infringed the '411 patent. Second, the Federal Circuit considered whether Amazon's infringement claim would "likely withstand BN's challenge to [the '411 patent's] validity." The Federal Circuit found that Amazon had demonstrated it would likely succeed in proving that BN infringed at least all four independent claims of the '411 patent.

The Federal Circuit first reviewed the construction of the key claim limitation "single action" ordering technology. In light of the plain meaning, specification and prosecution history, the Federal Circuit agreed with Amazon in construing all four independent claims (i.e., claims 1, 6, 9, and 11) to call for the "single action" to be performed "immediately after a display of information about an item, and without any intervening action, but not necessarily immediately after the first display or every display." Given this construction of the "single action" limitation, the Federal Circuit held that BN's Express Lane feature would likely infringe the '411 patent.

The Federal Circuit also rejected BN's argument that the Express Lane feature did not infringe claim 2 of the '411 patent because it was a shopping-cart model as defined and explicitly disclaimed by the patent. The court found that Express Lane feature could infringe claim 2 because, unlike the shopping-cart methods defined in the '411 patent, it did not require additional checkout or confirmation steps before a request to order an item

was sent to the server. For similar reasons, the court held that BN had failed to raise a substantial question of non-infringement for claim 11.

The second phase of the Federal Circuit's analysis focused on "whether the district court correctly determined that BN failed to mount a substantial challenge to the validity of the claims in the '411 patent." The Federal Circuit criticized the district court's fact-finding, stating that the district court had committed clear factual error by misreading the five prior art references and by failing to recognize that BN had raised a substantial question of invalidity.

While the Federal Circuit did not find that any one prior reference anticipated the invention in the '411 patent, the court did find that the '411 patent would likely be found obvious in light of the prior art. In conducting the obviousness analysis, the Federal Circuit concluded that it was enough that the elements Amazon used in the 1-Click method were known or had previously existed in some form within prior art.

The Federal Circuit did not consider evidence supporting the proposition that the 1-Click method had been "taught away from" by the prior art, thus indicating nonobviousness. *United States v. Adams*, 383 U.S. 39 (1966) was one of the first cases to apply an invention's combination being "taught away from," as evidence of the nonobviousness of the invention. At the time of Amazon's invention, the e-commerce community advocated a process that led the consumer through the purchase and confirmation steps slowly in order to reduce consumer anxiety and simultaneously increase consumer confidence with regard to security. Thus, the prior art in the e-commerce industry "taught away from" the quick purchase method that the 1-Click patent claimed. Amazon offered additional evidence to support the proposition that the 1-Click method was a radical departure from the traditional approach. Though the district court cited these reasons as offering "direct evidence of nonobviousness," the Federal Circuit declined to consider evidence offered by Amazon and industry experts to show that Amazon's method had been "taught away from." The Federal Circuit found that the five prior art references did not fully anticipate or teach the Amazon 1-Click method, but reasoned that the person of ordinary skill could easily "fill in the gaps" in the prior art to come up with the Amazon method.

In its obviousness analysis, the Federal Circuit found that Amazon failed to submit any evidence of commercial success, though Amazon had presented testimony that millions of customers utilize the 1-Click method in the district court proceedings. The Federal Circuit did not consider the commercial value that BN had placed upon the 1-Click method. Additionally, the court explicitly rejected other secondary considerations which would have weighed in Amazon's favor. Unlike the district court, the court did not consider other secondary considerations—copying, success and the "problem to be solved"—as indicators of the nonobviousness of Amazon's invention.

Thus, the court found that BN had "cast enough doubt on the validity of the '411 patent to avoid a preliminary injunction." Accordingly, the Federal Circuit reversed the preliminary injunction.

III. CONCLUSION

In the aftermath of *State Street*, the Patent and Trademark Office experienced an incredible surge in the number of business method patents being applied for and, issued. The legal system and patent law, in particular, are still attempting to wrestle out the legal ramifications that both a rapid technological advancement and subsequent legal uncertainties have introduced.

APOTEX USA, INC. V. MERCK & CO., INC.

254 F.3d 1031 (2001)

The issue presented to the United States Court of Appeals for the Federal Circuit was whether defendant Merck "suppressed" or "concealed" a patented process under 35 U.S.C. § 102(g).

Merck manufactures and commercially sells enalapril sodium ("VASOTEC") for use in the treatment of high blood pressure. While Merck owns patents covering the treatment compound in the U.S. and Canada, it does not own a patent on the process it uses to manufacture VASOTEC. In 1991, Merck sued Apotex's Canadian affiliate for patent infringement of the enalapril sodium compound. During this trial, Merck officials described the process used to make VASOTEC. Soon after explanation, Apotex conceived and patented the method used to make VASOTEC. Apotex then filed suit against Merck alleging Merck's infringement of the process patent. The United States District Court for the Northern District of Illinois granted Apotex's motion for summary judgment on the issue of infringement, but also granted Merck's cross-motion for summary judgment of invalidity because it found that Merck invented the claimed process within the United States and did not abandon, suppress or conceal the invention within the meaning of section102(g).

Apotex appealed from the district court's grant of summary judgment of invalidity. In affirming the decision of the district court, the Federal Circuit clarified that actions taken outside of the United States provide sufficient evidence of an absence of suppression or concealment. The Federal Circuit further clarified the burdens of proof for demonstrating suppression or concealment under section 102(g) in a patent infringement suit. First, a party asserting patent invalidity under §102(g) must prove facts by clear and convincing evidence establishing prior invention. Once the challenger of a patent has proven that the invention was "made in this country by another inventor," the burden of proof shifts to the patentee to produce evidence sufficient to create a triable issue of material fact as to whether the prior inventor suppressed or concealed the invention. The party defending the patent does not have to demonstrate actual suppression or concealment because to require such proof would undermine the presumption of patent validity under 35 U.S.C. § 282. Once the patentee satisfies the burden of production of a material fact of suppression or concealment, the party alleging invalidity under section 102(g) must rebut the alleged suppression or concealment with clear and convincing evidence. In this case, Apotex produced enough evidence of suppression or concealment to shift the burden to Merck because Merck kept its process of producing VASOTEC private for 5 years. However, Merck successfully rebutted this presumption because it "resumed activity" before Apotex entered into the market. Merck resumed activity by making the process public before Apotex's entrance into the market. Merck made the process public by discussing it at trial and by publishing the ingredients of the drug in its product monograph and the French dictionary. Because Merck took these steps before Apotex entered the market, the court concluded that it could be deemed to have suppressed or concealed the invention within the meaning of section 102(g).

BAYER AG V. HOUSEY PHARMACEUTICALS, INC.

169 F. Supp. 2d 328 (D. Del. 2001)

The United States District Court for the District of Delaware addressed whether the scope of 35 U.S.C. § 271(g) infringement claims extends to patented nonmanufacture processes and whether substantial royalties demanded by the patentee could conceivably constitute a patent misuse claim.

Defendant Housey Pharmaceuticals, Inc. owned four patents, U.S. Patent Nos. 4,980,281, 5,266,464, 5,688,655, and 5,877,007 (collectively, "the ICT patents"). The patents, which generally related to research methods used by pharmaceutical companies for discovering drugs, enabled companies to screen substances for active compounds that indicated a potential for pharmaceutical development. Plaintiffs filed an action against defendant Housey Pharmaceuticals and sought a declaratory judgment that the ICT patents were invalid and unenforceable. Plaintiffs alleged that the defendant's misuse of the ICT patents was twofold: (1) defendant required plaintiffs to pay substantial royalties throughout the patents' life for any products derived from research and development that utilized the patented technology in drug development, and (2) defendant licensed the patents with terms that they knew went beyond the claims of the patents. Defendant then filed a counterclaim of infringement. Defendant alleged that plaintiffs infringed the ICT patents under 35 U.S.C. § 271(g) whenever plaintiff sold an inhibitor or activator drug identified through the patented methods in the United States. Defendant Housey Pharmaceuticals, Inc. also alleged infringement whenever the plaintiff imported into or used within the United States knowledge or information reflecting the identification or characterization of a drug acquired from using the patented methods. Both parties filed motions to dismiss. Plaintiffs' motion sought to dismiss defendant's infringement claim on the theory that section 271(g) is inapplicable to patents claiming research methods. Defendant's motion sought to dismiss plaintiffs' claim of patent misuse.

The district court granted plaintiffs' motion to dismiss defendant's infringement claim and denied defendant's motion to dismiss plaintiffs' claim of patent misuse. The court concluded that, because section 271(g) only addresses products derived from patented manufacturing processes and the method claims of the ICT patents describe processes of identification and generation of data that are not steps in the manufacture of final drug products, section 271(g) was inapplicable to the case at hand and defendant's infringement claim must accordingly be dismissed. The court further held that, if the statute were applicable to patents claiming screening methods or methods of use, any products subjected to those methods in foreign countries would have infringed those patents upon importation to the United States. The court concluded that plaintiffs sufficiently stated a claim of patent misuse because a rational factfinder could conceivably conclude that defendant misused the patents, given that: (1) arrangements in which a patentee effectively extends the term of its patent by requiring post-expiration royalties constitute per se patent misuse, and (2) the practices could not reasonably relate to subject matter within the scope of the patent claims.

BREED V. HUGHES AIRCRAFT CO.

253 F.3d 1173 (9th Cir. 2001)

The Ninth Circuit ruled on the issue of appellate jurisdiction in actions arising in part under the patent law.

Breed, an inventor who performed consulting work for Hughes, brought suit against Hughes after Hughes allegedly breached an oral agreement. The suit was originally filed in state court of Texas, and later transferred to the United States District Court for the Central District of California. The complaint made thirteen California state law claims relating to breach of contract and misappropriation of trade secret, and one patent law claim for "Omission of Inventor" under 35 U.S.C. § 256. As to the section 256 claim, Breed requested that the district court issue an order requiring the amendment of the patent at issue to reflect that Breed was a co-inventor. The district court's jurisdiction was based both on diversity and on 28 U.S.C. § 1338(a), jurisdiction over a "civil action arising under any Act of Congress relating to patents." The district court granted summary judgment to Hughes on all claims. As to the omission of inventor claim, the district court found a further order from the court unnecessary because the parties had already begun the process of including Breed's name in the patent as a co-inventor.

Breed appealed. The Ninth Circuit, *sua sponte*, found that it lacked jurisdiction because the Federal Circuit had exclusive jurisdiction over appeal in actions arising under the patent law. The court noted that 28 U.S.C. § 1295(a) conferred to the Federal Circuit, exclusive jurisdiction over the entire case "if the jurisdiction of [the district] court was based, in whole or in part, on section 1338 of this title." 28 U.S.C. § 1295(a). Therefore, in a well-pleaded complaint, the presence of even a single claim arising under the patent law, regardless of its significance to the litigation or how rigorously it was pursued, acts as an "on switch" for Federal Circuit jurisdiction. The court noted an exception to this rule: where a district court grants the plaintiff's unopposed motion to voluntarily dismiss a patent claim early in the litigation, the Federal Circuit does not have jurisdiction over the appeal. However, because Breed never moved to dismiss the patent claim in the district court, the exception did not apply. Although Breed tried to abandon the co-inventor claim after the court raised jurisdiction issue, the court found it irrelevant whether the claim was abandoned or even appealed. The court was also aware of the hardship to the parties if the appeal were to be transferred to the Federal Circuit, but noted that it was not a factor to be considered when deciding subject matter jurisdiction. The court cautioned that litigants should be mindful of the pleading pitfall occasioned by the Federal Circuit's jurisdiction statute while drafting a complaint.

FESTO CORP. V. SHOKETSU KINZOKU KOGYO KABUSHIKI CO.

234 F.3d 558 (Fed. Cir. 2000) (en banc)

In this en banc decision, the Federal Circuit held that an amendment to a patent claim element made for any reason related to patentability completely bars application of the doctrine of equivalents to that element.

Festo Corp. sued Shoketsu in the United States District Court for the District of Massachusetts, alleging infringement of two patents on magnetically coupled rodless cylinders. After several trials and appeals, the Federal Circuit chose to hear the case en banc and addressed five questions.

First, the court considered whether, for prosecution history estoppel purposes, an amendment made for "a substantial reason related to patentability," as defined in *Warner-Jenkinson Co. v. Hilton-Davis Chemical Co.*, 520 U.S. 17 (1997), is limited to amendments made to overcome rejections under 35 U.S.C. § 102 or § 103. The court ruled that prosecution history estoppel applies not only to amendments made for reasons related to novelty and nonobviousness under sections 102 and 103, but also to amendments related to patentable subject matter or utility under 35 U.S.C. § 101, or the disclosure requirements of 35 U.S.C. § 112.

Second, the court considered whether a "voluntary" claim amendment could create prosecution history estoppel. The court ruled that the doctrine of prosecution history estoppel applied equally to "voluntary" amendments as to those required by a patent examiner.

Third, the court considered whether prosecution history estoppel would serve as a complete bar to a finding of infringement under the doctrine of equivalents. In ruling that amendments related to patentability completely bar the a finding of infringement under the doctrine of equivalents, the court attempted to reconcile two divergent lines of Federal Circuit authority. In *Hughes Aircraft Co. v. United States*, 717 F.2d 1351 (Fed. Cir. 1983), the court had adopted a flexible bar that allowed a limited range of equivalents. In contrast, the court in *Kinzenbaw v. Deere & Co.*, 741 F.2d 383 (Fed. Cir. 1984), held that prosecution history estoppel completely barred any range of equivalents for a claim element amended for reasons related to patentability. While most decisions have followed the flexible bar approach of *Hughes*, the court found that the notice function of patents and the need for greater certainty in patent litigation favor the complete bar approach.

Fourth, the Federal Circuit considered what range of equivalents, if any, is available for a claim element that is amended with no explanation, thus invoking the presumption of prosecution history estoppel under *Warner-Jenkinson*. The majority ruled that the doctrine of equivalents is not available for amendments that are not explained in the file history.

Finally, the Federal Circuit reached the question of whether application of the doctrine of equivalents in *Festo* would violate the "all elements" rule of *Warner-Jenkinson*. The court held that it was unnecessary to decide the issue in light of the available record. The court proceeded to apply its holding to the facts in *Festo*, and reversed the grant of summary judgment and jury verdict of infringement under the doctrine of equivalents.

On June 18, 2001, the United States Supreme Court granted *certiorari*. The Court heard oral arguments on January 8, 2002. At the time of publication, the Court had not yet issued its decision.

GROUP ONE, LTD. V. HALLMARK CARDS, INC.

254 F.3d 1041 (Fed. Cir. 2001)

The United States Court of Appeals for the Federal Circuit ruled on whether negotiations to sell an invention that do not rise to the level of a formal offer to sell trigger the on-sale bar rendering a patent invalid under 35 U.S.C. § 102(b). The court held that for an offer to be considered for an on-sale bar, it must constitute a commercial offer for sale under generally understood contract law.

Before filing a device and method patent application for producing pre-curled ribbon, the plaintiff attempted to generate interest in its product by commencing a series of communications with Hallmark. Hallmark expressed some interest, but the nature of the communications between the parties was indefinite because Hallmark never signed the agreed upon Confidential Disclosure Agreement. Additionally, no specific terms such as price or quantity were discussed. Hallmark then went on to develop its own pre-curled ribbon. When Group One sued for patent infringement, Hallmark argued that its patent was invalid because the patented ribbon-curling machine and method had been "on sale" more than one year prior to the filing date of the application. The trial court found that, while the communications between Group One and Hallmark did not constitute a formal offer for sale in the contractual sense, they did constitute an offer for sale within the context of section 102(b). Section 102(b) states that "[a] person shall be entitled to a patent unless . . . (b) the invention was . . . on sale in this country, more than one year prior to the date of the application for patent in the United States." In reaching this decision, the court relied upon dicta from *RCA Corp. v. Data General Corp.*, 887 F.2d 1056 (Fed. Cir. 1989), stating that the requirements for an on-sale bar may be met by activities that do not rise to the level of a sale under traditional contract law. The district court therefore held the patents were invalid and dismissed the patent infringement claims.

Group One appealed this decision, arguing that the trial court erred in declaring its patents invalid under the on-sale bar. The Federal Circuit agreed, specifically holding that any offer to sell must rise to the level of an offer for sale in the contract sense to trigger the section 102(b) on-sale bar. The appellate court's decision was strongly influenced by the need to have a uniform national rule regarding the on-sale bar. To hold otherwise would potentially mean that a patent could be invalid in one state, when the patentee's actions amounted to an offer under the laws of that state, and valid in a second state, when the same actions did not amount to an offer under the laws of that second state. Further, the court found this outcome more desirable because courts are quite accustomed to and comfortable with determining whether a particular communication or series of communications amounts to an offer in the contract sense, and that type of determination is well established in the law. In contrast, a holding which allowed something less than a formal commercial offer to trigger the on-sale bar, would open up a "vast sea of uncertainty, and requires a whole new method of analysis, whose parameters remain ill-defined." The decision of the trial court was therefore reversed and remanded for further proceedings.

J.E.M. AG SUPPLY, INC. V. PIONEER HI-BRED INTERNATIONAL, INC.

122 S.Ct. 593 (2001)

In a case for patent infringement, the United States Supreme Court held that newly developed plant breeds are subject to utility patent protection under 35 U.S.C. § 101.

Respondent Pioneer Hi-Bred International, Inc. held seventeen utility patents related to plant breeds. Petitioner J.E.M. Ag Supply, Inc. purchased patented hybrid seeds from Pioneer, subject to a license agreement prohibiting resale of the seeds. J.E.M. resold the bags of seed. When sued for patent infringement, J.E.M. argued that two statutes, the Plant Patent Act of 1930 ("PPA") and the Plant Variety Protection Act ("PVPA"), provided the exclusive statutory means for patent protection of plant life. The District Court for the Northern District of Iowa granted summary judgment to Pioneer, holding that neither the PPA nor the PVPA removed plant life from the subject matter of section 101. The District Court relied on *Diamond v. Chakrabarty*, 447 U.S. 303 (1980), in holding that section 101 was intended to include plant life.

The Federal Circuit affirmed the district court's judgment. The Supreme Court granted certiorari and affirmed. With respect to the PPA, the Court reasoned that the state of plant breeding at the time of its passage in 1930 explains both the PPA's limited applicability to asexually reproduced plants and the absence of the explicit mention of plants within section 101. The Court also agreed with the lower court's reliance on *Diamond* as to the implicit inclusion of plants in section 101. With respect to the PVPA, the Court noted the lower requirements and protection provided by the PVPA compared to a utility patent, and held that some overlapping coverage between the two statutes is acceptable, so long as each statute reaches some distinct cases.

LITTON SYSTEMS, INC. V. HONEYWELL INC.

238 F.3d 1376 (Fed. Cir. 2001)

The Federal Circuit decided whether an amendment in response to a "regards his invention" rejection during patent prosecution served as a complete bar to application of the doctrine of equivalents to the amended limitation.

In 1979, Litton obtained United States Patent No. 4,142,958 ("the '958 patent") claiming a process for making multi-layer optical films using an ion beam. In 1985, Litton sought reissue because the '958 patent was invalidated for obviousness reasons. Litton proposed an amendment to the '958 patent such that the multiple layers would have different refraction indexes. The examiner twice rejected the reissue application on obviousness grounds, and conditioned allowance on Litton's amendment of its claims to limit them to what Litton regarded as its invention—use of the Kaufman-type ion beam source rather than any ion beam source. United States Reissue Patent No. 32,849 ("the '849 reissue patent") was issued following the required amendment. After the expiration of a consulting agreement, one of Litton's prior employees, Louderback, provided Honeywell with mirrors made a method similar to that described in the '958 patent. In 1990, Litton sued Honeywell, Louderback, and Ojai Research in the United States District Court for the Central District of California, alleging infringement of the '849 reissue patent, breach of licensing and consulting agreements, intentional interference with contractual relations, and intentional interference with prospective economic advantage.

The jury found the patent both valid and infringed, and found for Litton on the tort claims. The district court entered judgment as a matter of law ("JMOL"), finding that the patent was not infringed and was unenforceable for inequitable conduct, and that Litton failed to established its state-law claims, and in the alternative, granted new trial on damages. The Federal Circuit reversed the grant of JMOL, but affirmed the grant of a new trial on damages. The United States Supreme Court vacated and remanded for reconsideration in light of *Warner-Jenkinson Co. v. Hilton Davis Chem. Co.*, 520 U.S. 17 (1997). On remand, the Federal Circuit held that Honeywell's processes (which used a hollow cathode or radio frequency ion beam) did not literally infringe the '849 reissue because they were not identical to the claimed Kaufman-type ion beam. The Federal Circuit remanded the case to the district court for consideration of infringement under the doctrine of equivalents. The court interpreted *Warner-Jenkinson* as consistent with the proposition that prosecution history estoppel did not completely bar the application of doctrine of equivalents. Because the jury may have relied on patent infringement as the wrongful means supporting the tort claims, the Federal Circuit vacated the jury verdict and remanded for further proceedings on the state-law tort claims. On remand, the district court granted summary judgment and JMOL of noninfringement of the '849 reissue patent. The district court found that prosecution history estoppel precluded infringement under the doctrine of equivalents. The district court also granted JMOL in favor of Honeywell on the state-law tort claims. Litton appealed.

The Federal Circuit, in a majority opinion, affirmed in part and reversed in part. The court affirmed the finding of noninfringement under the doctrine of equivalents. The court ruled that Litton was barred by prosecution history estoppel from asserting infringement under the doctrine of equivalents. The court found that Litton's amendment of the claim limitation "ion beam source" to "Kaufman-type ion beam source" was a direct response to a rejection under 35 U.S.C. § 112, ¶ 2 that the examiner issued for failing to claim what Litton regarded as its invention. Relying on *Festo Corp. v. Shoketsu Kinzoku*

Kogyo Kabushiki Co., 234 F.3d 558, 574 (Fed. Cir. 2000), the court held that Litton's narrowing amendment was related to the patentability of the claims and therefore acted as a complete bar to the application of doctrine of equivalents to the amended limitation. The court acknowledged that in its previous decision it had articulated a flexible-bar approach, stating that an amendment during prosecution did not foreclose all application of the doctrine of equivalents, but only narrowed the scope of application. The court noted that *Festo* expressly repudiated that approach. Because of this change in controlling legal authority, the court found that the law of the case doctrine, which precluded reconsideration of an issue decided at an earlier stage of litigation, did not apply.

The court reversed the judgment on the state-law tort claims and remanded for further proceedings. The court noted that although Litton could not rely on the patent infringement claims as the wrongful means to support its tort claims, the district court should have submitted the tort claims to a jury to resolve the factual issue of whether other wrongful means existed.

LOCKHEED MARTIN CORP. V. SPACE SYSTEMS/LORAL, INC.

249 F.3d 1314 (Fed. Cir. 2001)

The Federal Circuit construed a means-plus-function claim limitation and ruled on whether the accused satellites infringed, either literally or under the doctrine of equivalents, a patent for an apparatus and method for steering a satellite.

Lockheed Martin Corporation ("Lockheed") was the assignee of United States Patent No. 4,084,772 ("the '772 patent"), which claimed a structure and method for reducing the pointing errors of a satellite via a second momentum wheel centered on the yaw axis. Particularly relevant to the instant case was limitation [b] of claim 1 of the '722 patent. Limitation [b] described the invention as "means for rotating said wheel in accordance with a predetermined rate schedule which varies sinusoidally over the orbit at the orbital frequency of the satellite whereby" achieving certain results. Lockheed brought a patent infringement suit against Space Systems/Loral, Inc. ("SSL") in the United States District Court for the Northern District of California, alleging that SSL's Intelsat VII satellites infringed claim 1 of the '772 patent. The district court granted SSL's motion for summary judgment based on a finding that limitations [b] and [f] (a limitation not considered in the present decision) were not present in the accused satellites, either literally or under the doctrine of equivalents. The district court construed the phrase "varies sinusoidally" to mean "a sine-shaped variation that passes through zero and changes direction." Accordingly, the court ruled that the SSL satellites did not literally infringe claim 1 because the speed of the accused L-Wheel did not slow to zero and reverse direction. Applying the "function-way-result" standard, the district court also ruled that the SSL satellites did not infringe claim 1 under the doctrine of equivalents because the L-Wheel did not operate in substantially the same way as the claimed invention.

On appeal, the Federal Circuit affirmed. The court noted that the first step in analyzing a means-plus-function claim limitation was to identify the claimed function. The court held that the function was properly identified as the language after the "means for" clause and before the "whereby" clause. The court next construed the meaning of the words used to describe the claimed function and upheld the district court's construction of the phrase "varies sinusoidally" as "a variation in a sine-shaped curve that passes through zero." As the final step in a means-plus-function limitation analysis, the court examined the written description to identify the structure corresponding to the function. The court characterized the sine generator and wheel electronics disclosed in the '772 patent as the structures corresponding to the function of limitation [b].

The court found that there was no literal infringement of limitation [b] because the accused L-Wheel rotated about a nonzero bias speed and therefore did not perform the identical function of limitation [b]. The court further found that Lockheed was barred from asserting infringement of limitation [b] under the doctrine of equivalents by prosecution history estoppel. The court noted that limitation [b] was amended twice during the prosecution of the '772 patent to overcome the examiner's rejection on obviousness grounds. Lockheed argued that the prosecution history did not act as a complete bar to the application of the doctrine of equivalents as to limitation [b] because the amendment merely sought to distinguish from the prior references the period over which the sinusoidal variation occurred, rather than the nature of the sinusoidal variation. The court rejected Lockheed's argument. Quoting *Festo Corp. v. Shoketsu Kinzoku Kogyo Kabushiki Co.*, 234 F.3d 558, 574 (Fed. Cir. 2000), the court held that "prosecution history estoppel

acts as a complete bar to the application of the doctrine of equivalents when an amendment has narrowed the scope of a claim for a reason related to patentability."

MYCOGEN PLANT SCIENCE INC. V. MONSANTO CO.

252 F.3d 1306 (Fed. Cir. 2001)

Mycogen owned U.S. Patent No. 5,380,831 ("the '831 patent"), entitled "Synthetic Insecticidal Crystal Protein Gene" and claiming synthetic plant insecticidal genes using plant-preferred codons. Mycogen also owned the progeny of the '831 patent, U.S. Patent Nos. 5,567,600 and 5,567,862. Mycogen brought suit against Monsanto in the United States District Court for the Southern District of California claiming infringement of the '831 patent. The district court granted Monsanto's motion for summary judgment, finding the '831 patent invalid under 35 U.S.C. § 102(g), due to prior work done by scientists at Monsanto. The district court also found that Monsanto did not infringe the process claims under 35 U.S.C. § 271(g) because the charged process was performed prior to the issuance of the '831 patent, and that Mycogen could not assert infringement of the product claims under doctrine of equivalents due to prosecution history estoppel.

Mycogen appealed. The United States Court of Appeals for the Federal Circuit reversed summary judgment of invalidity, but affirmed the findings of noninfringement. The court found that genuine issues of material fact remained as to invalidity, and thus remanded the case.

The Federal Circuit found that Monsanto was not liable for infringement under 35 U.S.C. § 271(g) for selling products containing synthetic insecticidal genes made before the '831 patent was issued. The court stated that the plain meaning of the language of section 271(g), "a product which is made by a process patented in the United States," suggested that to establish infringement, the process must be patented at the time the product was made. Further, the court noted that the legislative history of the statute supported the conclusion that section 271(g) did not apply to products made by a process that was not patented at the time the products were made, even though the products were sold after the issuance of the patent. Therefore, the court held that the patent must be issued and in force at the time the process was practiced and the product made for infringement to be found under 35 U.S.C. § 271(g).

The court held that Mycogen was estopped from asserting infringement under the doctrine of equivalent by statements made during the prosecution of the '831 patent. The court noted that, although the product claims at issue were not a result of amendment of the original claims, they were nevertheless used to replace the cancelled initial claims that defined the synthetic gene by a more broadly specified DNA sequence. The court stated that canceling and replacing claims should be treated as analogous to amending them, and therefore the prosecution history estoppel rule established in *Festo Corp. v. Shoketsu Kinzoku Kogyo Kabushiki Co.*, 234 F.3d 558 (Fed. Cir. 2000), applied.

MYLAN PHARMACEUTICALS, INC. V. THOMPSON

268 F.3d 1323 (Fed. Cir. 2001)

The United States Court of Appeals for the Federal Circuit ruled on Mylan Pharmaceutical's ("Mylan") ability to seek an injunction requiring Bristol-Myers Squibb Co. ("Bristol") to de-list its patent from the FDA's "Orange Book."

Under 21 U.S.C. § 355(a), pharmaceutical companies seeking to manufacture a new drug must file a New Drug Application (NDA) for consideration by the Food and Drug Administration ("FDA"). If the FDA approves the NDA, it publishes a listing of the drug and patents on the drug's approved aspects in Approved Drug Products with Therapeutic Equivalence Evaluations (also known as the Orange Book). Once an NDA is approved, other pharmaceutical companies wishing to market generic versions of the previously approved drug may submit an abbreviated new drug application (ANDA) pursuant to the Drug Price Competition and Patent Term Restoration Act of 1984, 21 U.S.C. §§ 355, 360cc. ANDAs may rely on the previous manufacturer's NDA by submitting data demonstrating the generic product's bioequivalence. Importantly, parties filing an ANDA must certify that (i) no relevant patent exists or was submitted to the FDA; (ii) any relevant patent has expired; (iii) the patent is set to expire on a certain date; or (iv) that the patent is invalid or not be infringed by the manufacture, sale or use of the new generic drug. Bristol owned a patent directed towards the treatment of anxiety through buspirone hydrochloride. Mylan submitted an ANDA certifying the expiration date of Bristol's patent. On the expiration date of Bristol's patent, it hand-delivered a patent that issued earlier that day to the FDA that effectively nullified the expiration date of the previous patent in the Orange Book for the purposes of ANDA filings. The United States District Court for the District of Columbia held that Mylan was entitled to declaratory relief. The district court ordered Bristol to take steps to de-list the second patent from the Orange Book and directed the FDA to approve Mylan's ANDA. Bristol appealed this order.

The United States Court of Appeals for the Federal Circuit reversed the district court's order because Mylan did not have a recognized action against Bristol. Under 21 U.S.C. § 337(a), "all such proceedings for the enforcement, or to restrain violations, of this chapter shall be by and in the name of the United States." In order for its declaratory relief action to be allowable, Mylan needed to assert a defense against a hypothetical patent infringement claim by Bristol. However, Mylan did not assert noninfringement of Bristol's patent. Instead, Mylan sought to litigate whether Bristol is barred from listing its new patent in the Orange Book because Bristol did not properly comply with the listing requirements of the FFDCA. Because Mylan's action against Bristol was in essence an attempt to assert a private right of action for "de-listing" under the FFDCA, it was not allowable. Private rights of action are precluded under the FFDCA.

RAPOPORT V. DEMENT

254 F.3d 1053 (Fed. Cir. 2001)

The Federal Circuit construed the term "treatment of sleep apneas" to decide whether a method for treatment of sleep apneas was unpatentable on grounds of anticipation by prior publication.

Rapoport appealed from a final decision of the Board of Patent Appeals and Interferences of the United States Patent and Trademark Office ("BPAI") awarding judgment of priority in favor of the respondents Dement et al., and entitling Dement el al. to a patent containing claims 1 through 13 of the U.S. Patent Application No. 07/695,325 ("the '325 application"). Rapoport alleged that the claims were not patentable on the grounds that they were anticipated and/or rendered obvious by a prior art reference authored by Rapoport, and published in Family Practice Recertification ("the FPR publication").

The Federal Circuit affirmed the Board's decision. The court ruled that the term "treatment of sleep apneas" should be narrowly construed as limited to treatment of the underlying sleep apnea disorder, rather than including treatment of anxiety and other secondary symptoms associated with sleep apnea. The court reasoned that the plain language of the term "treatment of sleep apneas" did not include treatment of anxiety associated with sleep apneas. In addition, the court noted that the written description of the '325 application defined "sleep apneas" as comprising symptoms other than anxiety, and the description of administration of the drug "at the hour of sleep" was consistent with treatment of the underlying sleep apnea disorder, but inconsistent with treatment of anxiety and other secondary symptoms commonly associated with sleep apnea. Further, the court noted that a general description of the invention specifically disclosed the inventive method as for "treating sleep apneas comprising obstructive, central and mixed apneas," and the discussion about the effectiveness of the treatment was limited to its effect on the underlying sleep apnea disorder, and did not include any effect on secondary symptoms associated with sleep apnea.

Having construed the term "treatment of sleep apneas," the court held that the FPR publication did not render the '325 application anticipated because the publication did not disclose administration of the drug to patients for the purpose of treating sleep apnea, but focused on the treatment of anxiety. The court acknowledged that such an explicit intent was not necessary as long as the publication described administration of the drug to a patient with sleep apnea in a therapeutically effective amount, but found that the publication lacked such description. The court rejected Rapoport's assertion that the therapeutically effective dosage of about 20 to 40 mg of the drug at the hour of sleep, as disclosed by the '325 application, was encompassed by the FPR publication, which disclosed a dosage of 10 mg of the drug three times a day, and therefore the FPR publication inherently anticipated the '325 application. The court noted that the patients who received the 10 mg dosage three times a day were not suffering from sleep apnea. Furthermore, the court held that inherency may not be established by mere speculation. The court found that Rapoport's inherency argument was based on the speculative assumptions that a treatment regimen of three doses a day necessarily included an administration of the drug at the hour of sleep, and that administering two 10 mg doses of the drug at unspecified hours throughout the day in conjunction with a 10 mg dose at bedtime necessarily resulted in a therapeutically effective amount for treating sleep apnea.

ROBOTIC VISION SYSTEMS INC. V. VIEW ENGINEERING, INC.

249 F. 3d 1307 (Fed. Cir. 2001)

Robotic Vision Systems ("Robotic") is the assignee of a patent for a method that scans the leads on integrated circuit devices by the entire tray, rather than row by row. Robotic filed suit against View Engineering ("View"), claiming that View's three-dimensional scanning machines infringed its patent. The district court and Federal Circuit upheld View's claim that Robotic's patent was invalid under the two part test of *Pfaff v. Wells Electronics, Inc.*, 525 U.S. 55 (1998).

The first prong of the *Pfaff* test requires the device to have been on sale for more than one year prior to patenting. This requirement was uncontested in the present case. At issue was the second prong, which considered whether the invention was also then ready for patenting. Under *Pfaff*, the inventor need not have absolute confidence that the invention will work for it to be considered ready for patenting; a device may be ready for patenting without such confidence, or without being reduced to practice, if the invention is conceptually complete.

Robotic contended that the "internal" disclosure of the invention to a co-worker should not have indicated that the device was ready for patenting and thus trigger the on-sale bar. The Federal Circuit held that a disclosure of the invention that is sufficient to enable a person skilled in the art to practice the invention would satisfy the second prong of the *Pfaff* test. The court found that it was irrelevant whether the software required to implement the scanning method existed at the time of the disclosure, so long as the invention could have been reduced to practice before the critical date (i.e., one year before the filing date).

S3 (SONIC BLUE) INC. V. NVIDIA CORP.

259 F.3d 1364 (Fed. Cir. 2001)

The Federal Circuit ruled that a claim is definite if a person skilled in the art can understand it with the aid of the specification. The court also held that the patent does not have to provide a technical explanation that can be understood by person experienced in the field.

Plaintiff S3 owns U.S. Patent No. 5,581,279 ("the '279 patent") which claims an integrated circuit for use in computer video color displays. The '279 patent claims a novel monolithic circuit in which a programmable clock signal generator circuit, a VGA controller circuit, and a combination random-access memory/digital-to-analog converter are integrated on a single chip. The '279 patent described two modes of operation. In the "direct color" mode, pixel data is transmitted directly from the VGA controller to a digital-to-analog converter ("DAC") for display. In the "indexed" mode, the data output from the controller is input in a random access memory ("RAM") array structured as a look-up table.

The United States District Court for the Northern District of California granted summary judgment in favor of nVIDIA, holding that claims 1-4 and 9-11 of the '279 were invalid for claim indefiniteness. The district court held that the patent was indefinite because it was inconsistent for the '279 patent to use the term "video information stream" to describe both the information DAC receives directly from the VGA that which is processed by RAM before moving to the DAC. Further, the district court held that the claim limitation "means. . .for selectively receiving" was indefinite because the "structure claimed by the 'selectivity' limitation is not disclosed in the specification."

S3 appealed. The Federal Circuit reversed and remanded for further proceedings. The court found both claim elements, the video information date stream and selector, to be sufficiently definite. Federal Circuit noted that the purpose of the claim is not to explain the technology or how it works, but to state the legal boundaries of the patent. A claim is not indefinite simply because it is hard to understand when viewed without the benefit of the specification. The court found that the specification explained that VGA produces "video information data stream," and RAM receives it and produces "video display information data stream." The court concluded that a person skilled in this field would understand the meaning and scope of the data streams as set forth in the claims. Therefore, it was not indefinite. The Federal Circuit held that patents need not include subject matter that is known in the field of the invention or in the prior art, because patents are written by and for persons experienced in the field of invention. The court noted that to hold otherwise would require every patent to include a technical treatise for the unskilled reader. The uncontested evidence indicated that a selector is a well-known electronic structure that performs a common electronic function and is readily implemented from the description in the specification. Thus, the Federal Circuit held the claims of the '279 sufficiently definite.

THE FIRST WAVE OF CASES UNDER THE ACPA

By Jian Xiao

The Anticybersquatting Consumer Protection Act ("ACPA" or "the Act"),[1] creates a new civil action against a person who, with "bad faith intent to profit" from the mark, registers, traffics in, or uses a domain name that is identical or "confusingly similar" to a trademark that was distinctive or famous at the time the domain name was registered.[2] While the ACPA significantly expands the application of trademark law in the context of the Internet, it is properly limited to acts with a bad faith intent to profit from others' marks.

This Note surveys the first wave of cases decided under the ACPA and identifies issues that consistently arise in courts' applications of the ACPA. Although most courts properly apply the ACPA to cybersquatting cases, some courts have broadly interpreted the ACPA to reach cases beyond its scope. This Note cautions that when courts apply the ACPA, they should consider the ACPA merely as a special tool aimed at cybersquatting practices, not as a weapon to replace or expand trademark law.

I. BACKGROUND

A. The Problem of Cybersquatting

As the Internet has become an important medium for business and communication, it has become critically important to have the right domain name. A simple and inexpensive registration process, combined with the low cost of maintaining domain name rights,[3] however, has provided many people with the opportunity to engage in "cybersquatting."[4] In general, cybersquatting is the practice of registering or using a domain name in which others have legitimate interests, and then attempting to sell the name either to the trademark owner or to the highest bidder.[5] This practice has caused serious problems for many legitimate trademark holders who

1. 15 U.S.C. § 1125(d) (Supp. 2001).
2. *Id.* § 1125(d)(1)(A).
3. For example, VeriSign charges $29 per year for .com domain name registrations. VeriSign Web Address Registration, *at* http://www.netsol.com/en_US/ (last visited Feb. 10, 2002).
4. S. REP. NO. 106-140, at 4 (1999).
5. *Id.*

seek to establish a web presence that is readily identifiable with their trademarks.[6]

B. Legal Protections Prior to the ACPA

Before the enactment of the ACPA, domain name disputes were addressed primarily through trademark infringement or dilution actions.[7] Trademark infringement actions focused on the traditional "likelihood of confusion" test.[8] Dilution actions applied only to famous marks.[9] For a plaintiff to succeed in either of these two actions, a defendant must have made a "commercial use" of the mark.[10]

The trademark infringement approach proved problematic because most cybersquatters did not offer goods or services in connection with the domain names that would lead to consumer confusion.[11] Thus, there was little or no chance of finding cybersquatters liable for trademark infringement under the traditional "likelihood of confusion" test. Recognizing this unique problem in cybersquatting cases, some courts held that the brief "initial interest confusion" which lured the users to defendant's website was actionable, even if there was no transaction.[12] This approach, however, has been widely criticized.[13]

Given the limitations of trademark infringement actions in cybersquatting cases, many trademark owners relied on dilution claims to combat

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6. *Id.* at 5.

7. *See, e.g.*, Brookfield Communications, Inc. v. West Coast Entm't Corp., 174 F.3d 1036 (9th Cir. 1999) (applying trademark infringement analysis in a domain name dispute); Intermatic, Inc. v. Toeppen, 947 F. Supp. 1227 (N.D. Ill. 1996) (applying dilution analysis in a domain name dispute).

8. The "likelihood of confusion" test considers factors such as the strength of the senior user's mark, similarity of the marks, similarity of the goods/services, channels of trade, sophistication of consumers, wrongful intent, actual confusion, and whether the challenged use is within the senior user's zone of natural expansion. *See* Polaroid Corp. v. Polarad Elecs. Corp., 287 F.2d 492, 495 (2d Cir. 1961).

9. *See* Federal Trademark Dilution Act, 15 U.S.C. § 1125(c)(1).

10. *Id.* §§ 1125(a) and (c)(1).

11. S. REP. NO. 106-140, at 7 (1999).

12. *See, e.g.*, Interstellar Starship Servs. v. Epix, Inc. 184 F.3d 1107, 1111-12 (9th Cir. 1999) (holding that initial interest confusion is actionable in the domain name context); Planned Parenthood Fed'n of Am. v. Bucci, No. 97 CIV. 0629, 1997 WL 133313, *1 (S.D.N.Y. Mar. 24, 1997), *aff'd*, 152 F.3d 920 (2d Cir. 1998) (holding that domain names are "external labels that, on their face, cause confusion among Internet users.").

13. *See, e.g.*, Hasbro, Inc. v. Clue Computing, 66 F. Supp. 2d 117, 125 (D. Mass. 1999) (explicitly repudiating the initial interest confusion approach); *see also* Bryce J. Maynard, *The Initial Interest Confusion Doctrine and Trademark Infringement on the Internet*, 57 WASH. & LEE L. REV. 1303 (2000) (arguing that the initial interest confusion doctrine does not serve the goals of trademark law).

cybersquatters. The critical issue in these claims was to determine whether the mark at issue was famous.[14] Early cases set a low threshold of fame, and dilution, in order to reach cybersquatters.[15] Over time, however, courts have become reluctant to stretch the famousness test, and have limited dilution actions to claims involving truly famous marks.[16] The Second Circuit has gone even further, ruling that dilution actions apply only to marks that are both famous and inherently distinctive.[17] In light of these recent limitations, the number of marks protectable through dilution actions is likely to be reduced.[18]

Commercial use of domain names is also difficult to prove in most cybersquatting cases.[19] Most cybersquatters merely registered domain names to interfere with trademark owners' abilities to use their marks on the Internet; they never used the domain names as actual website addresses.[20] While courts generally hold that the mere registration of a domain name does not constitute commercial use as traditionally defined, per se,[21] some courts have found commercial use in situations where cybersquatters reserved domain names with the intent to sell the domain names to trademark owners.[22] This approach was limited in its effectiveness, however, because many cybersquatters simply waited for mark owners to make an initial purchase offer.[23]

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14. 15 U.S.C. § 1125(c)(1).

15. *See, e.g.*, Archdiocese of St. Louis v. Internet Entm't Group, Inc., 34 F. Supp. 2d 1145, 1146 (E.D. Mo. 1999).

16. *See* Avery Dennison Corp v. Sumpton, 189 F.3d 868 (9th Cir. 1999) (finding that defendant's use of avery.net as e-mail address was not dilutive of plaintiff's Avery and Dennison marks).

17. TCPIP Holding Co. v. Haar Communication Inc., 244 F.3d 88, 101 (2d Cir. 2001) (holding that the mark Children's Place was not entitled to protection under the Federal Trademark Dilution Act ("FTDA") because it is a descriptive mark).

18. *See* Sally M. Abel, *eVolution or Revolution? Trademark Law on the Internet* (June 18, 2001), *at* http://www.fenwick.com/pub/ip_pubs/Trademarks_&_Internet /main2.htm.

19. S. REP. NO. 106-140, at 7 (1999).

20. *Id.*

21. *See, e.g.*, Panavision Int'l L.P. v. Toeppen, 141 F.3d 1316, 1324 (9th Cir. 1998); Lockheed Martin Corp. v. Network Solutions, Inc., 985 F. Supp. 949 (C.D. Cal. 1997), *aff'd*, 194 F.3d 980 (9th Cir. 1999).

22. *See, e.g.*, Intermatic, Inc. v. Toeppen, 947 F. Supp. 1227, 1239-40 (N.D. Ill. 1996) (finding that defendant's "business" was the capture and ransom of a domain name).

23. Jason Kaplan, *The Anticybersquatting Consumer Protection Act: Will it End the Reign of the Cybersquatter?*, 8 UCLA ENT. L. REV. 43 (2000).

C. The Anticybersquatting Consumer Protection Act

Congress enacted the ACPA to clarify the rights of trademark owners in response to concerns about the limitations of existing trademark law in dealing with cybersquatters.[24] Congress designed the Act to balance the property rights of trademark owners with the First Amendment interests of Internet users.[25]

Under the ACPA, a defendant is liable if, with "bad faith intent to profit", he registers, traffics in, or uses a domain name that is identical or "confusingly similar to" a mark that is either distinctive or famous at the time the domain name is registered.[26]

The ACPA expands trademark law in the Internet context.[27] For example, the ACPA does not require commercial use of a mark—the mere act of registering a domain name can violate the Act.[28] The ACPA also applies to either distinctive or famous marks, eliminating the fame threshold required under dilution actions.[29] Finally, the Act applies to domain names that are "confusingly similar" to a distinctive or famous mark, a standard that is easier to satisfy than the traditional "likelihood of confusion" standard.[30]

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24. S. REP. NO. 106-140, at 7 (1999) (stating that cybersquatting cases are growing dramatically "because there is no clear deterrent and little incentive for cybersquatters to discontinue their abusive practices."). The Uniform Domain Name Dispute Resolution Policy ("UDRP"), which was created by the ICANN and adopted by major domain registrars by January 3, 2000, is another important means for trademark owners to combat cybersquatters. While the UDRP is cheaper and preferred in straightforward domain name disputes, the ACPA is sometimes favored for several reasons. First, the ACPA allows trademark owners to stop the domain name uses immediately by requesting temporary restraining orders. Second, the ACPA allows discovery, which parties generally prefer in complex cases. Furthermore, the possibility of getting statutory damages atop traditional damages makes it more attractive to go through judicial resolutions than through UDRP proceedings. Importantly, the ACPA can be used to overrule a UDRP decision. *See* Sallen v. Corinthians Licenciamentos LTDA, No. 01-1197, 2001 WL 1518455 (1st Cir. 2001). For a detailed analysis on the UDRP, see Patrick Kelley, Note, *Emerging Patterns in Arbitration Under the Uniform Domain-Name Dispute-Resolution Policy*, 17 BERKELEY TECH. L.J. 181.

25. S. REP. NO. 106-140, at 9 (1999). *See also* H.R. REP. NO. 106-464, at 109 (1999).

26. 15 U.S.C. § 1125(d)(1)(A).

27. *See* P. Wayne Hale, Note, *The Anticybersquatting Consumer Protection Act &* Sporty's Farm L.L.C. v. Sportyman's Market, Inc., 16 BERKELEY TECH. L.J. 205 (2001).

28. 15 U.S.C. § 1125(d)(1)(A).

29. *Id.* However, only famous marks are protected against domain names that are dilutive. *See* 145 CONG. REC. S. 10513-20 (daily ed. Aug. 5, 1999) (Statements of Sens. Hatch, Abraham, and Leahy).

30. *See infra* Part II.A.

The ACPA also contains procedural and remedial provisions that make it an easier and more effective means to combat cybersquatters than traditional trademark law.[31] For example, the Act allows a trademark owner to bring an *in rem* action against the domain name itself.[32] The *in rem* provision applies when the domain name violates the owner's substantive trademark right, and the cybersquatter is either beyond the personal jurisdiction of the court or cannot be located despite the trademark owner's exercise of due diligence.[33] The Act also provides that trademark owners may seek statutory damages ranging from $1000 to $100,000 per domain name.[34]

In spite of these "expansions" of trademark law in the Internet context, ACPA actions are limited to bad-faith registrations or uses of others' marks by persons seeking to profit unfairly from the marks.[35] The ACPA provides nine nonexclusive factors to guide courts in determining bad faith intent.[36] The Act also includes a safe harbor provision, stating that bad faith intent "shall not be found in any case in which the court determines that the person believed and had reasonable grounds to believe that the use of the domain name was a fair use or otherwise lawful."[37] Additionally, the Act expressly retains traditional defenses, such as the parody defense.[38]

The ACPA has received mixed reviews. Proponents stress that the ACPA eliminates loopholes in traditional trademark law by creating a legal tool aimed specifically at cybersquatters.[39] Others voice concern that the ACPA significantly broadens traditional trademark law and serves as a weapon for big corporations to attack innocent individual domain name registrants.[40] This Note analyzes the first wave of cases decided under the

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31. *See* S. REP. NO. 106-140, at 10 (1999); *see also id.* at 7 (stating that the difficulty of obtaining damages in standard trademark infringement and dilution actions are significant obstacles for legitimate trademark holders).

32. 15 U.S.C. § 1125(d)(2).

33. *Id.*

34. *Id.* § 1117(d). Statutory damages are not available in *in rem* actions.

35. *Id.* § 1125(d)(1). *See also infra* Part II.B. (discussing the bad faith intent requirement).

36. *Id.* § 1125(d)(1)(B). *See infra* note 54 for a list of the nine factors.

37. *Id.* § 1125(d)(1)(B)(ii).

38. *Id.* § 1051. *See also* S. REP. NO. 106-140, at 11 (1999).

39. *See, e.g.*, Allon Lifshitz, *Cybersquatting*, 38 HARV. J. ON LEGIS. 529 (2001); Jennifer Alvey, *Trademarks: Trademark Interests Welcome Cybersquatting Law, Others See New Dispute Policy Derailed*, BNA PATENT, TRADEMARK & COPYRIGHT LAW DAILY NEWS, December 10, 1999.

40. *See, e.g.*, Gregory B. Blasbalg, *Masters of Their Domains: Trademark Holders Now Have New Ways to Control Their Trademarks in Cyberspace*, 5 ROGER WILLIAMS

ACPA. It further examines whether the ACPA has been effective in fighting cybersquatting, and whether courts have expanded the ACPA beyond Congressional intent.

II. ANALYSIS OF THE CASES

The first wave of cases decided under the ACPA have addressed several recurring issues: (1) determining whether a domain name is identical or "confusingly similar" to a distinctive or famous mark; (2) finding a "bad faith intent to profit"; (3) applying the parody defense, and; (4) interpreting the *in rem* provision. Courts have exercised broad discretion in dealing with these issues, and have sometimes misinterpreted the ACPA to reach their desired result.

A. Identical or "Confusingly Similar"

The threshold requirement for an ACPA action is for a plaintiff to show that the domain name at issue is identical or "confusingly similar" to its distinctive or famous mark.[41]

Determining whether a domain name and a mark are identical has been relatively straightforward. For example, courts have noted that the presence of a top-level domain name is inconsequential.[42] Furthermore, because domain names normally do not contain apostrophes and ampersands, the mere absence of such characters in a domain name is insufficient to distinguish the name from the mark.[43] Accordingly, the domain

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U. L. REV. 563 (2000); Justin Graham et al., *Cybersquatting: the Latest Challenge in Federal Trademark Protection*, 2001 DUKE L. & TECH. REV. 9 (2001); Kaplan, *supra* note 23. Some commentators also express concerns that the ACPA will create chilling effects on freedom of speech. *See, e.g.*, Eric D. Paulsrud, *The First Amendment on the Internet: Challenges in a New Media*, 27 WM. MITCHELL. L. REV. 1637 (2001).

41. Courts used traditional trademark law definitions to decide whether a mark is distinctive or famous. *See, e.g.*, Prime Publishers, Inc. v. American-Republican, Inc. 160 F. Supp. 2d 266, 278 (D. Conn. 2001) (holding the mark Voices distinctive because it is at least suggestive of a newspaper); Mattel, Inc. v. Adventure Apparel, No. 00 CV. 4085, 2001 WL 1035140 (S.D.N.Y. Sept. 7, 2001) (holding the mark Barbie famous under the FTDA definition).

42. *See* Sporty's Farm L.L.C. v. Sportsman's Market, Inc., 202 F.3d 489, 497-98 (2d Cir. 2000). A domain name is made up of a top-level domain and a secondary-level domain. *Id.* at 492-93. For instance, in www.disney.com, ".com" is the top-level domain name, and ".disney" is the second-level domain name.

43. *See, e.g.*, *id.* at 497-98; Morrison & Foerster LLP v. Wick, 94 F. Supp. 2d 1125, 1130 (D. Colo. 2000).

name sportys.com is identical to the Sporty's mark,[44] and the domain name morrisonfoerster.com is identical to Morrison & Foerster.[45]

If the domain name and the mark are not identical, they must be "confusingly similar" for the ACPA to apply. While some courts use the "likelihood of confusion" test to analyze the "confusingly similar" element,[46] most courts simply compare the domain name with the mark to determine whether they are similar in appearance. Under this "similar in appearance" approach, courts have held that misspelled marks meet the confusingly similar standard.[47] Adding a generic or geographic term to a distinctive mark, moreover, has also proven insufficient to distinguish the domain name from the mark.[48]

The "similar in appearance" approach to the "confusingly similar" analysis suggests a lower standard than that used in a "likelihood of confusion" test. This lower standard is consistent with the plain language of the ACPA, which explicitly states that parties' goods or services are irrelevant to a cybersquatting claim.[49] Furthermore, Congress intended that the ACPA reach cases where parties register domain names without any intention to use them in commerce.[50] Thus, requiring a showing of "likelihood of confusion" in ACPA cases would narrow the scope of the ACPA and undermine Congressional intent.

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44. *Sporty's*, 202 F.3d at 497-98.

45. *Morrison & Foerster*, 94 F. Supp. 2d at 1130.

46. *See* Victoria's Cyber Secret Ltd. P'ship v. V Secret Catalogue, Inc., 161 F. Supp. 2d 1339, 1350-53 (S.D. Fla. 2001) (invoking traditional likelihood of confusion test to find the domain name victoriasexsecret.com confusingly similar to the Victoria's Secret mark); *see also* Advanced Magazine Publishers Inc. v. Vogue Intern., 123 F. Supp. 2d 790, 799 (D.N.J. 2000) (holding that a number of the "likelihood of confusion" factors suggest domain names teenvogue.com and vogueinternational.com are "confusingly similar" to the Vogue mark).

47. *See, e.g.*, Shields v. Zuccarini, 254 F.3d 476, 483 (3d Cir. 2001) (holding domain names containing misspelling variations of Joe Cartoon confusingly similar); *Morrison & Foerster*, 94 F. Supp. 2d. at 1130 (holding domain names containing misspelling variations of Morrison & Foerster confusingly similar).

48. *See, e.g.*, Harrods Ltd. v. Sixty Internet Domain Names, 157 F. Supp. 2d 658, 677 (E.D. Va. 2001) (finding domain names consisting of the word "harrods" and another generic or geographic term confusingly similar to plaintiff's Harrods trademark); Ford Motor Co. v. Lapertosa, 126 F. Supp 2d 463 (E.D. Mich. 2001) (holding domain name fordrecalls.com confusingly similar to the famous mark Ford). *But see* Lucent Techs. Inc. v. Lucentsucks.com, 95 F. Supp. 2d 528, 535 (E.D. Va. 20000) (finding in *dictum* that lucentsucks.com is not confusingly similar to the Lucent mark because average consumers would understand that the domain name was a parody of Lucent and would not be confused).

49. 15 U.S.C. § 1125(d)(1) .

50. S. REP. NO. 106-140, at 7 (1999).

On the other hand, courts should ensure that the "confusingly similar" analysis is not arbitrary and overly broad.[51] For instance, courts should be careful in assessing domain names which are not similar to the mark in appearance, but are nonetheless similar in either sound or meaning.[52] Courts should also be consistent with their application of the "confusingly similar" standard to provide domain name registrants some certainty about the legitimacy of their domain names.

B. "Bad Faith Intent to Profit"

While the ACPA expands traditional trademark law by requiring a low "confusingly similar" standard, its scope is significantly narrowed by the bad faith intent element.[53] The central issue in most ACPA cases to date is whether the defendant acted with a bad faith intent to profit from the plaintiff's mark.

1. Applying the Nine Statutory Factors

The ACPA provides nine nonexclusive factors to guide courts in determining bad faith intent.[54] The first four factors focus on the domain

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51. *See* Virtual Works, Inc. v. Volkswagen of Am., Inc., 238 F.3d 264, 271 (4th Cir. 2001) ("The ACPA was not enacted to give companies the right to fence off every possible combination of letters that bears any similarity to a protected mark.").

52. In *West Licensing Corp. v. Eastlaw, L.L.C.*, No. 00-2645, 2001 WL 501200 (D. Minn. May 9, 2001), Westlaw sued the registrant of the domain name eastlaw.com under the ACPA. The case was dismissed on other grounds, but raised an interesting issue whether the domain name eastlaw.com is "confusingly similar" to Westlaw.

53. S. REP. NO. 106-140, at 8-10 (1999).

54. The relevant section of the ACPA states:

> (B)(i) In determining whether a person has a bad faith intent described under subparagraph (a), a court may consider factors such as, but not limited to—
>
> (I) the trademark or other intellectual property rights of the person, if any, in the domain name;
>
> (II) the extent to which the domain name consists of the legal name of the person or a name that is otherwise commonly used to identify that person;
>
> (III) the person's prior use, if any, of the domain name in connection with the bona fide offering of any goods or services;
>
> (IV) the person's bona fide noncommercial or fair use of the mark in a site accessible under the domain name;
>
> (V) the person's intent to divert consumers from the mark owner's online location to a site accessible under the domain name that could harm the goodwill represented by the mark, either for commercial gain or with the intent to tarnish or disparage the mark, by creating a likelihood of confusion as to the source, sponsorship, affiliation, or endorsement of the site;

name holder's legitimate rights, such as trademarks, legal names, prior use of the domain names, or legitimate noncommercial fair use of the mark.[55] The presence of these factors suggests an absence of bad faith.[56] The next four factors focus on typical cybersquatting behaviors, such as creating a likelihood of confusion with the trademark, offering to sell the domain name, providing false contact information, or "warehousing" numerous domain names.[57] The presence of these factors favors a finding of bad faith intent.[58] The ninth factor, focusing on the extent to which the mark is or is not distinctive and famous, can be used to establish either the presence or the absence of bad faith intent.[59] The more distinctive or famous a mark is, the more likely that the defendant has a bad faith intent.[60] In contrast, the fact that a mark is not well known may suggest a lack of bad faith intent.[61] While some of the factors incorporate traditional infringement and dilution analyses,[62] Congress intended courts to weigh the facts of each case against all the nine statutory factors in order to balance

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> (VI) the person's offer to transfer, sell, or otherwise assign the domain name to the mark owner or any third party for financial gain without having used, or having an intent to use, the domain name in the bona fide offering of any goods or services, or the person's prior conduct indicating a pattern of such conduct;
>
> (VII) the person's provision of material and misleading false contact information when applying for the registration of the domain name. The person's intentional failure to maintain accurate contact information, or the person's prior conduct indicating a pattern of such conduct;
>
> (VIII) the person's registration or acquisition of multiple domain names which the person knows are identical or confusingly similar to marks of others that are distinctive at the time of registration of such domain names, or dilutive of famous marks of others that are famous at the time of registration of such domain names, without regard to the goods or services of the parties; and
>
> (IX) the extent to which the mark incorporated in the person's domain name registration is or is not distinctive and famous within the meaning of subsection (c)(1) of this section.

15 U.S.C. § 1125(d)(1)(B).

55. *Id.* § 1125(d)(1)(B)(i)(a)(I)-(IV).

56. H.R. REP. NO. 106-464, at 100 (1999).

57. § 1125(d)(1)(B)(i)(a)(V)-(VIII). "Warehousing" refers to the act of "register[ing] multiple domain names—sometimes hundreds, even thousands—that mirror the trademarks of others." S. REP. NO. 106-140, at 16 (1999).

58. H.R. REP. NO. 106-464, at 100 (1999).

59. § 1125(d)(1)(B)(i)(a)(IX).

60. H.R. REP. NO. 106-464, at 112 (1999).

61. *Id.*

62. § 1125(d)(1)(B)(i)(a)(V) and (IX).

trademark owners' property rights with Internet users' legitimate interests.[63]

a) A typical cybersquatting case

In *Shields v. Zucarrini*,[64] defendant registered thousands of domain names that were misspellings of trademarks or celebrities' names. Among these domain names were misspellings of plaintiff's Joe Cartoon mark.[65] A web user who reached defendant's websites would be "mousetrapped" in the sites and thus could not exit these sites without clicking on a succession of advertisements.[66] The court found defendant's conduct clearly satisfied a number of the nine statutory factors, and consequently held that there was a bad faith intent to profit.[67] The court noted that "typosquatting," registering domain names that were intentional misspellings of distinctive or famous names, was exactly the type of behavior Congress intended to prohibit under the ACPA.[68]

b) Cases requiring careful balancing of the factors

In most ACPA cases, the evidence of bad faith is not as clear as the evidence in *Shields*. Courts have therefore exercised great discretion in applying and balancing the nine statutory factors.[69] Some courts have even stretched the meanings of the factors to reach their desired results.[70]

In *Northern Light Technology, Inc. v. Northern Lights Club*,[71] plaintiff owned the Northern Light service mark and operated a search engine at the website northernlight.com. Defendant registered thousands of "catchy" domain names that contained famous marks.[72] Defendant additionally reg-

63. S. REP. NO. 106-140, at 12-16 (1999).

64. 254 F.3d 476 (3d Cir. 2001).

65. The domain names were joescartoon.com, joecarton.com, joecartons.com, joescartoons.com, and cartoonjoe.com. *Id.* at 483.

66. Defendant received between ten to twenty-five cents from advertisers for each click. *Id.* at 480.

67. *Id.* at 485.

68. *Id.*

69. *See, e.g.*, Northern Light Tech., Inc. v. Northern Lights Club, 236 F.3d 57 (1st Cir. 2001); Mattel, Inc. v. Adventure Apparel, No. CV. 4085, 2001 WL 1035140 (S.D.N.Y. Sept. 7, 2001); Harrods Ltd. V. Sixty Internet Domain Names, 157 F. Supp. 2d 658 (E.D. Va. 2001); Hartog & Co. v. Swix.com, 136 F. Supp. 2d 531 (E.D. Va. 2001).

70. *See, e.g.*, Prime Publishers, Inc. v. American-Republican, Inc. 160 F. Supp. 2d 266 (D. Conn. 2001); Ford Motor Co. v. Lapertosa, 126 F. Supp. 2d 463 (E.D. Mich. 2000).

71. 236 F.3d 57 (1st. Cir. 2001).

72. *Id.* at 65. These domain names included rollingstones.com, evinrude.com, givenchy.com.

istered the domain name northernlights.com, which contained an unfamous mark, on behalf of an unincorporated association called "Northern Lights Club."[73] Soon after the registration, defendant licensed the name to an e-mail service, and provided e-mail accounts under northernlights.com through that service.[74] Two years later, plaintiff approached defendant about purchasing northernlights.com, but negotiations were unsuccessful and plaintiff filed suit under the ACPA.[75]

In analyzing bad faith intent, the First Circuit placed great emphasis on the fact that defendant was "warehousing" domain names.[76] The court explained that although the Northern Light mark itself was not famous, defendant's well-established pattern of registering multiple domains names containing famous trademarks was highly relevant to the determination of bad faith intent.[77] Thus, even though defendant had been using northernlights.com as an e-mail domain name for two years, and had been reluctant to sell the domain name, the court found bad faith intent.[78]

In *Prime Publisher, Inc. v. American-Republican, Inc.*,[79] plaintiff published a local tabloid newspaper called "Voices."[80] Defendant published a competing tabloid newspaper, "Countrylife", in a market that overlapped with that of "Voices."[81] Plaintiff brought suit against defendant, alleging that defendant's registration and use of the domain name ctvoices.com violated the ACPA.[82]

The court applied the nine statutory factors to the case, and found that defendant registered the domain name with a bad faith intent to profit. Most importantly, the court found it was likely that business advertisers and Internet users could be confused as to the source, sponsorship, affiliation, or endorsement of the website.[83] To support a finding of bad faith intent, the court stretched the meaning of a number of the statutory factors. For example, the court found the factor directed to the typical behavior of

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73. The Northern Lights Club's stated mission was to bring together devotees of the Northern Lights, or *aurora borealis*. *Id.* at 59. There were no actual club members at the time of domain name registration. *Id.*

74. *Id.*

75. *Id.* at 60.

76. *Id.* at 65.

77. *Id.*

78. *Id.* The court ultimately decided that it was unnecessary to decide the case under the ACPA because defendant was liable for trademark infringement. *Id.* at 67.

79. 160 F. Supp. 2d 266 (D. Conn. 2001).

80. *Id.* at 269. .

81. *Id.* at 270.

82. *Id.* at 276.

83. *Id.* at 280.

domain name warehousing cut against defendant, even though defendant only registered a single domain name.[84] Furthermore, the court held that because the Voices mark was not merely descriptive of a newspaper, the factor directed to the extent to which the mark is or is not distinctive or famous also supported an inference of bad faith intent.[85]

Interestingly, the *Prime Publisher* court also held that defendant's use of plaintiff's Voices mark in its domain name constituted trademark infringement.[86] The court nevertheless decided that this case was better resolved under the ACPA, and chose to stretch the meaning of several statutory factors to find bad faith intent.

A similar problem occurred in *Ford Motor Company v. Lapertosa*.[87] Ford Motor Company sued a website operator who used the domain name fordrecalls.com to sell pornography.[88] The court found bad faith intent primarily because defendant used the famous Ford mark without any legitimate reason.[89] This raises the issue of whether it is better to decide the case under the dilution statute, or under the ACPA and subsequently infer bad faith intent from the famousness of the mark.[90]

c) Comments

While the ACPA was enacted to remedy the ineffectiveness of traditional trademark law in fighting cybersquatters, it is not intended to replace traditional trademark law in all domain name disputes. Because it is possible to obtain large statutory damage awards under the ACPA, however, parties may have a strong incentive to invoke the ACPA even in non-

84. *Id.* at 273. ("Although the statutory factor refers to the registration of 'multiple' domain names, we find that the registration of a single domain name with the knowledge that it incorporates a competitor's mark similarly informs an inference of bad faith intent.").

85. Since "voices" is such a commonly used word, the court's rationale in applying this factor only makes sense when both parties conduct business in the same field.

86. *Prime Publisher,* 160 F. Supp. 2d at 283.

87. 126 F. Supp. 2d 463, 465-66 (E.D. Mich. 2000).

88. *Id.* at 464. The court found fordrecalls.com confusingly similar to the Ford mark. *Id.* at 466.

89. *Id.* at 466. *But see* Virtual Works, Inc. v. Volkswagen of Am., Inc., 238 F.3d 264, 269 (4th Cir. 2001) (holding that the mere fact that one mark is famous and that defendant has no prior use of the domain name is circumstantial evidence which alone could not establish a bad faith intent).

90. Indeed, other courts have addressed cases involving the use of someone else's famous mark to sell pornography under trademark dilution. *See, e.g.*, Hasbro, Inc. v. Internet Entm't Group, Ltd., No. C96-130 WD, 1996 WL 84853 (W.D. Wash. Feb. 9, 1996) (holding that an online adult entertainment service using the domain name candyland.com was dilutive of the famous Candyland mark).

cybersquatting cases. When called upon to resolve domain name disputes, courts should be aware of the narrow scope of the ACPA, and apply the ACPA only in cases involving registration or use with a bad faith intent to profit.

The nine statutory factors provide guidance for a court to make the critical determination of bad faith intent, and allow a court to carefully balance the property interest of trademark owners with the legitimate interests of Internet users. While courts inevitably have to exercise their discretion in applying these factors, they should not interpret them too broadly. In cases where the ACPA is not appropriate, courts should simply acknowledge the limits of the statute, rather than stretch its meaning to reach their desired results.

2. *Unique Circumstances of the Cases*

Since the nine statutory factors are nonexclusive, some courts have looked beyond these factors in their bad faith intent analyses to consider the unique circumstances of the cases. While some courts have only considered those unique circumstances that involve direct evidence of bad faith intent,[91] other courts have considered circumstances that are only remotely indicative of bad faith intent.[92] These approaches have provided courts with more discretion and flexibility than merely applying the statutory factors in cybersquatting cases.

a) Cases involving direct evidence of bad faith intent to profit

In *Sporty's Farm L.L.C. v. Sportsman's Market, Inc.*,[93] plaintiff owned the Sporty's trademark for its aviation catalogue sales business.[94] Defendant registered the domain name sportys.com after deciding to enter into direct competition with plaintiff.[95] Applying the nine statutory factors, the First Circuit found that there was more than enough evidence to establish bad faith intent.[96] The court, however, emphasized that the most important basis for finding bad faith intent was the unique circumstance of the case: defendant planned to compete directly with plaintiff and registered the

91. *See, e.g.*, Virtual Works, Inc. v. Volkswagen of Am., Inc., 238 F.3d 264, 268-69 (4th Cir. 2001); Sporty's Farm L.L.C. v. Sportsman's Market, Inc., 202 F.3d 489, 499 (2d Cir. 2000).

92. *See, e.g.*, Morrison & Foerster LLP v. Wick, 94 F. Supp. 2d. 1125, 1133 (D. Colo. 2000); Prime Publisher, Inc. v. American-Republican, Inc., 160 F. Supp. 2d 266, 281 (D. Conn. 2000).

93. 202 F.3d 489 (2d Cir. 2000).

94. *Id.* at 493.

95. *Id.* at 494.

96. *Id.* at 499.

domain name for the primary purpose of depriving plaintiff of the domain name.[97]

In *Virtual Works, Inc. v. Volkswagen of America, Inc.*,[98] Virtual Works registered the domain name vw.net.[99] At the time of registration, Virtual Works recognized the possibility of confusion between its name and Volkswagen's VW mark, and that it might be able to sell the domain name to Volkswagen.[100] After using vw.net for two years, Virtual Works negotiated with Volkswagen to sell the domain name.[101] During the negotiation, Virtual Works threatened to sell the domain name to the highest bidder.[102] Failing to reach a sales agreement with Virtual Works, Volkswagen sued Virtual Works under the ACPA.[103]

In determining whether Virtual Works acted with bad faith intent to profit, the Fourth Circuit decided that it was unnecessary to even consider the nine statutory factors. Instead, the court held, "the most important grounds for finding bad faith 'are the unique circumstances of th[e] case, which do not fit neatly into the specific factors enumerated by Congress but may nonetheless be considered under the statute.'"[104] The Court found that Virtual Works acted with a bad faith intent to profit, especially in light of Virtual Works' knowledge of the possible confusion of vw.net with the VW mark, its hope to profit from selling the domain name to Volkswagen, and its statement that it might sell the domain name to the highest bidder.[105] Although the court noted that any particular piece of the evidence might not have been dispositive on the issue, it held that Virtual Works had demonstrated bad faith intent under the totality of the circumstances.[106]

b) Cases without direct evidence of bad faith intent to profit

In *Morrison & Foerster LLP v. Wick*,[107] Morrison & Foerster sued defendant, who registered several domain names containing the Morrison &

97. *Id. Cf.* Harrods Ltd. v. Sixty Internet Domain Names, 157 F. Supp. 2d 658 (E.D. Va. 2001) (finding that an intent to compete with the trademark owner invokes a number of the nine statutory factors).

98. 238 F.3d 264 (4th Cir. 2001).

99. *Id.* at 266.

100. *Id.*

101. *Id.* at 267.

102. *Id.*

103. *Id.*

104. *Id.* at 268 (citing *Sporty's Farm*, 202 F.3d at 499).

105. *Id.* at 269-70.

106. *Id.*

107. 94 F. Supp. 2d 1125 (D. Colo. 2000).

Foerster mark or its misspelling variations.[108] In concluding that defendant acted with bad faith intent, the court found that "the most persuasive reason," which did not fit neatly into the enumerated factors, was defendant's intent to use its website to parody corporate America and law firms.[109]

In *Primer Publisher, Inc. v. American Republican, Inc.*,[110] defendant registered the allegedly infringing domain name several months after summary judgment was entered against it in its copyright suit against plaintiff.[111] The court took this evidence into consideration in its finding of bad faith intent.[112]

c) Comments

In considering the unique circumstances of the cases in their bad faith intent analyses, courts should be particularly careful not to go beyond the scope of the ACPA. Relying too much on the unique circumstances of a case would allow a court to establish bad faith intent based on evidence that only tangentially relates to the practice of cybersquatting.[113] Given the low standard for the other elements of the ACPA,[114] a relaxed standard for the bad faith intent element would make the ACPA a powerful weapon for trademark owners in many types of domain name disputes. To maintain the narrow scope of the ACPA that Congress intended, courts should focus only on facts that show direct evidence of bad faith intent in considering the unique circumstances of the cases.

3. The Safe Harbor Provision

The safe harbor provision of the ACPA provides that "bad faith intent . . . shall not be found in any case in which the court determines that the person believed and had reasonable grounds to believe that the use of the domain name was a fair use or otherwise lawful."[115] Congress inserted the

108. *Id.* at 1129. The domain names included morrisonfoester.com, morrisonandfoerster.ccm, morrisonforster.com, and morrisonandforster.com. *Id.* at 1127.

109. *Id* at 1133.

110. 160 F. Supp. 2d 266 (D. Conn. 2000).

111. *Id.* at 281.

112. *Id.*

113. *See also* Jonathan Ward, *The Rise and Fall of Internet Fences: the Overbroad Protection of Anticybersquatting Consumer Protection Act,* 5 MARQ. INTELL. PROP. L. REV. 211 (2001) (cautioning that the ad hoc approach to bad faith intent would make the nine statutory factors superfluous, and could ultimately be detrimental to the certainty of outcomes under the ACPA).

114. *See supra* Parts I.C and II.A.

115. 15 U.S.C. § 1125(B)(ii) .

safe harbor provision to protect domain name holders without bad faith, whose actions might otherwise satisfy the requirements of the ACPA.[116]

a) Cases refusing to apply the safe harbor provision

In *Virtual Works*, the court refused to apply the safe harbor provision to excuse a defendant who knew its domain name strongly resembled a famous mark, but nonetheless registered the name with intent to sell the name.[117] The court reasoned that since it was easy for any cybersquatter to put forth at least some lawful motives for his behavior, broadly applying the safe harbor provision would frustrate Congress' purpose by artificially limiting the statute's reach.[118]

Several courts have followed the reasoning in *Virtual Works* and refused to construe the safe harbor provision broadly.[119] For example, in *Harrods Limited v. Sixty Internet Domain Names*,[120] defendants invoked the safe harbor provision, arguing that it reasonably believed that registering domain names that contained its own trademark was lawful. The court refused to apply the safe harbor provision, however, finding the evidence of defendant's bad faith intent to profit overwhelming.[121] Similarly, the court in *People for the Ethical Treatment of Animals v. Doughney*[122] refused to use the safe harbor provision to relieve a defendant who believed he was within his First Amendment rights to parody plaintiff's organization.[123] The court explained that in order for the safe harbor provision to apply, defendant not only had to believe his use of the domain name was lawful, but also needed to have reasonable grounds for his belief.[124]

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116. *See* J. THOMAS MCCARTHY, 4 MCCARTHY ON TRADEMARKS AND UNFAIR COMPETITION § 25: 78 (2000) (calling the safe harbor provision a "reasonable belief defense" provision).

117. *Virtual Works*, 238 F.3d at 266.

118. *Id.* at 270.

119. *See, e.g.*, Harrods Ltd. v. Sixty Internet Domain Names, 157 F. Supp. 2d 658, 679 (E.D. Va. 2001); People for the Ethical Treatment of Animals v. Doughney, 263 F.3d 359, 369 (4th Cir. 2001).

120. 157 F. Supp. 2d at 679.

121. *Id.*

122. 263 F. 3d at 369.

123. *Id.* at 369.

124. *Id. See also* Northern Light Tech., Inc. v. Northern Lights Club, 236 F. 3d 57, 65 (1st Cir. 2001) (holding that "defendants' oft-changing explanations for the purpose of [its] website evince a lack of subjective belief in the domain name's fair use").

b) Cases applying the safe harbor provision

The cases that have applied the safe harbor provision considered the provision only after first determining that there was no bad faith intent.[125] For example, in *Chatam International, Inc. v. Bodum, Inc.*,[126] plaintiff owned the trademark Chambord for food products. Plaintiff sued defendant, who owned the same mark for coffee makers, under the ACPA for using the domain name chambord.com to advertise coffee makers. The court refused to conduct a bad faith intent analysis, first noting that "the Act leaves open the present combination of circumstances—in which both parties can invoke legitimate grounds for the registration of the same domain name for their respective products."[127] The court then found that defendant's act also fit into the ACPA's safe harbor provision because it had reasonable grounds to believe that its use of the mark was lawful.

c) Comments

The *Virtual Works* court broadly stated that "[a] defendant who acts even partially in bad faith in registering a domain name is not, as a matter of law, entitled to benefit from the Act's safe harbor provision."[128] If one reads this statement literally to suggest that a defendant acting even partially in bad faith was not entitled to the safe harbor protection, then the safe harbor provision would seem useless. Curiously, courts have only applied the safe harbor provision in cases in which plaintiff could not establish bad faith intent.[129] It is therefore unclear when the safe harbor provision would be useful.

In deciding whether or not to apply the safe harbor provision in future cases, courts should not read the safe harbor provision so narrowly as to render the provision meaningless. On the other hand, courts should be careful not to read the provision so broadly as to undermine Congress' sole intent to fight cybersquatting.

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125. *See* Chatam Int'l, Inc. v. Bodum, Inc. 157 F. Supp. 2d 549 (E.D. Pa. 2001); Hartog & Co. v. Swix.com, 136 F. Supp. 2d 531, 540-541 (refusing to find bad faith intent based on the nine statutory factors and further because of the safe harbor provision).

126. *Chatam,* 157 F. Supp. 2d at 551.

127. *Id.* at 554.

128. Virtual Works, Inc. v. Volkswagen of Am., Inc., 238 F.3d 264, 270 (4th Cir. 2001).

129. *See supra* Part II.B.2.b).

C. Parody Defense

The ACPA does not affect traditional trademark defenses, such as the parody defense.[130] Some courts suggest that if a defendant uses a website for a parody, he would not be found liable under the ACPA.[131] Most courts, however, have held that a defendant will violate the ACPA unless the domain name itself conveys a parodic message.[132]

In *Morrison & Foerster*, defendant argued that his use of morrisonfoerster.com and other similar websites to parody the law firm Morrison & Forester was protected under the First Amendment.[133] The court rejected this argument, pointing out that to be recognized as parody, the expression in the domain name must convey two simultaneous and contradictory messages: "that it is the original, but also that it is not the original and is instead a parody."[134] Unfortunately for defendant, the court determined that the disputed domain names conveyed only the first message, and were therefore not protected by a parody defense.[135]

Similarly in *Doughney*, an organization bearing the name "People Eating Tasty Animals" established a website with the domain name peta.org.[136] The name of defendant's organization was clearly a parody of the animal rights organization "People for the Ethical Treatment of Animals" ("PETA"), and the website contained sarcastic commentaries about PETA's philosophies.[137] Defendants' parody defense failed, however, because the domain name peta.org itself did not convey the parodic message.[138]

Holding that a domain name user is not entitled to parody defense unless the domain name itself suggests a parody is consistent with the ACPA's purpose of curtailing cybersquatting.[139] Most cybersquatters reg-

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130. 15 U.S.C. § 1051. *See also* S. REP. NO. 106-140, at 11 (1999).

131. *See, e.g.*, Mattel, Inc. v. Adventure Apparel, No. 00 CV. 4085, 2001 WL 1035140 (S.D.N.Y. Sept. 7, 2001) (stating that if the website is really a parody, it would have been protected); Shields v. Zuccarini, 254 F.3d 476, 485-86 (3d Cir. 2001) (suggesting that if defendant had been using the website to criticize plaintiff prior to the lawsuit, it might be protected).

132. Morrison & Foerster LLP v. Wick, 94 F. Supp. 2d 1125 (D. Colo. 2000); People for the Ethical Treatment of Animals v. Doughney, 263 F.3d 359 (4th Cir. 2001).

133. *Morrison & Foerster*, 94 F. Supp. 2d at 1131.

134. *Id.* at 1134.

135. *Id.*

136. *Doughney*, 263 F.3d at 362-63.

137. *Id.*

138. *Id.*

139. Domain names that do convey a parody message are not per se protectable, however. *See* Lucent Techs. v. Johnson, No. CV. 00-05668, 2000 WL 1604055 (C.D.

ister domain names without intending to provide any goods or services on the website. It would therefore be easy for a cybersquatters to put some sort of a parody on their websites as a shield against ACPA actions.[140] Furthermore, the fact that a website contains a parody is already a factor to consider in the bad faith intent analysis.[141] If the parody on the website alone can be a valid defense against an ACPA claim, it would seem redundant for Congress to include it as a factor in determining bad faith.

D. The *In Rem* Provision

Prior to the ACPA, many cybersquatters were able to elude trademark enforcement actions either because they were located in foreign countries and were beyond the *in personam* jurisdictions of U.S. courts, or because they provided false contact information to domain name registrars and could not be found.[142] To address these problems, Congress included an *in rem* provision in the ACPA.[143]

Under the *in rem* provision, a trademark owner can hold a domain name "hostage" in the judicial district in which the domain name registrar, domain name registry, or other domain name authority that registered or assigned the domain name is located.[144] Courts have upheld the validity of this provision, holding that domain names are a kind of property sufficient to form a basis for an *in rem* action.[145]

Cal. Sept. 12, 2000). Thus, in order to invoke the parody defense against an ACPA claim, both the domain name and the website's content must convey the parodic message.

140. S. REP. NO. 106-140, at 9 (1999) ("To recognize such an exemption would eviscerate the protections of the bill by suggesting a blueprint for cybersquatters who would simply create criticism sites in order to immunize themselves from liability despite their bad-faith intentions.").

141. See 15 U.S.C. § 1125(d)(1)(B)(i)(IV); Northland Ins. Cos. v. Blaylock, 115 F. Supp. 2d. 1108 (D. Minn. 2000) (holding that defendant's using its website to criticize an insurance company tipped the balance against the finding of bad faith). *Contra* Morrison & Foerster LLP v. Wick, 94 F. Supp. 2d 1125, 1133 (D. Colo. 2000) (holding that an intent to parody corporate America was "the most persuasive reason for finding a bad faith").

142. S. REP. NO. 106-140, at 10 (1999).

143. 15 U.S.C. § 1125(d)(2)(A) .

144. *Id. See also* FleetBoston Fin. Corp. v. Fleetbostonfinancial.com, 138 F. Supp. 2d 121 (D. Mass. 2001) (holding that the *in rem* provision of the ACPA can be invoked only in the judicial district where the domain registrar, registry, or other authority is located).

145. *See, e.g.*, Caesars World, Inc. v. Caesars-Palace.com, 112 F. Supp. 2d 502 (E.D. Va. 2000); Cable News Network L.P. v. Cnnews.com, 162 F. Supp. 2d 484 (E.D. Va. 2001) (holding that the ACPA *in rem* action is a true *in rem* action, rather than a quasi *in rem* action). *But see* NSI v. Umbro Int'l Inc., 529 S.E. 2d 80 (Va. 2000) (holding that a registrant's interest in a domain name was merely contractual and hence cannot be garnished).

The *in rem* provision contains a substantive prong and a procedural prong. The substantive prong requires the trademark owner to prove that the accused domain name "violates any right of the owner of a mark registered in the Patent and Trademark Office, or protected under" 15 U.S.C. §1125(a) or (c).[146] The procedural prong requires a mark owner to show that he is either unable to obtain personal jurisdiction against the domain name holder, or cannot find the domain name holder after exercising due diligence.[147] In both situations, the owner must show that the domain name holder "would have been a defendant in a civil action under paragraph (1)", the *in personam* provision of the Act.[148]

1. *Courts' Interpretations of the Two Prongs*

Courts have taken inconsistent approaches in interpreting the two prongs of the *in rem* provision. Some courts have held that trademark owners must prove every element in the *in personam* provision in order to satisfy the procedural prong in the *in rem* provision.[149] Others have ignored the fact that the *in rem* provision mentions the *in personam* provision twice. Rather, these courts have held that the *in rem* provision and the *in personam* provision are completely separate provisions, and that the elements of the *in personam* provision are inapplicable in an *in rem* action.[150]

McCarthy seems to have taken a middle ground in his treatise. He suggests that the fact that the procedural prong in the *in rem* provision mentions the *in personam* provision does not add any substantive requirement.[151] Nevertheless, the elements in the *in personam* provision can be the basis for violation of the substantive prong of the *in rem* provision.[152]

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146. 15 U.S.C. § 1125(d)(2)(A)(i).

147. *Id.* § 1125(d)(2)(A)(ii).

148. *Id.* § 1125(d)(2)(A).

149. *See, e.g.*, Harrods Ltd. v. Sixty Internet Domain Names, 110 F. Supp. 2d 420, 425 (E.D. Va. 2000).

150. *See, e.g.*, Jack in the Box v. Jackinthebox.org, 143 F. Supp 2d 590, 592 (E.D. Va. 2001) (refusing to "borrow" the terms from the *in personam* provision to an *in rem* action).

151. MCCARTHY, *supra* note 116, § 25:79 (suggesting that "the person who would have been a defendant in a civil action under paragraph (1)" in the procedural prong merely defines the proper defendant in an *in rem* proceeding and "does not add an extra requirement of a substantive violation").

152. According to McCarthy, the trademark owner can assert four possible substantive violations in an *in rem* proceeding: Lanham Act § 32(1) for infringement of a registered mark; Lanham Act § 43(a) for infringement of an unregistered mark; Lanham Act § 43(c) for dilution of a famous mark; and Lanham Act § 43(d) for cybersquatting of a registered mark. *Id.*

2. *Bad Faith Intent Requirement*

Because of their different approaches in interpreting the *in rem* provision, courts have also been inconsistent in deciding whether plaintiffs must prove that the domain name registrant had a bad faith intent to profit from plaintiff's mark in an *in rem* action.

Most courts have held that bad faith intent was a substantive element in an *in rem* action.[153] These courts based their conclusions on several grounds. First, the procedural prong of the *in rem* provision makes two explicit references to the *in personam* provision. Therefore, the elements of the *in personam* provision, including the bad faith intent element, are incorporated into the *in rem* provision.[154] Second, Congress intended to use the bad faith intent element to narrow the breadth of the statute. Eliminating the bad faith intent requirement in an *in rem* proceeding would extend the ACPA beyond its intended scope.[155] In responding to challenges that bad faith intent could not be established in default proceedings, these courts have held that the mere act of registering a domain name with false contact information could lead to a finding of bad faith intent.[156]

The court in *Jack in the Box v. Jackinthebox.org*[157] took a different approach. Plaintiff Jack in the Box sued under the *in rem* provision to seek the transfer of the domain names jackinthebox.org and jackinthebox.net, both of which were registered by unknown parties who never used the domain names. Contrary to the majority of cases, the court held that it was unnecessary to consider bad faith intent in this *in rem* action, because the "plain terms" of the ACPA clearly states that the bad faith intent element only applies to *in personam* actions.[158] Instead of relying on the elements in the *in personam* provision, the court found that the domain names infringed plaintiff's trademarks because the mere act of registering domain names constituted "commercial use" and caused "likelihood of confusion."[159]

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153. *See* Hartog & Co. v. Swix.com, 136 F. Supp. 2d 531 (E.D. Va. 2001); Harrods Ltd. v. Sixty Internet Domain Names, 110 F. Supp. 2d 420 (E.D. Va. 2000); Broadbridge Media L.L.C. v. HyperCD.com, 106 F. Supp. 2d 505 (S.D.N.Y. 2000).

154. *See, e.g., Harrods*, 110 F. Supp. 2d at 425; *Broadbridge*, 106 F. Supp. 2d at 511.

155. *See Broadbridge*, 106 F. Supp. 2d at 511.

156. *See, e.g., Harrods*, 110 F. Supp. 2d at 426. *But see* S. REP. NO. 106-140, at 9 (1999) (stating that "the fact that a defendant provided erroneous information in applying for a domain name registration. . .does not necessarily show bad faith").

157. 143 F. Supp. 2d 590 (E.D. Va. 2001).

158. *Id.* at 597.

159. *Id.* at 595. The holding that the act of registration alone constitutes commercial use is clearly inconsistent with courts' general recognition that registration of a domain name alone is not commercial use.

3. *Comments*

The inconsistent approaches to the *in rem* provision stem from the ambiguity of the statutory language.[160] On the one hand, the substantive prong of the *in rem* provision seems to suggest that one can bring an *in rem* action on trademark infringement or dilution grounds, which does not require proof of bad faith intent.[161] On the other hand, eliminating the bad faith intent requirement in an *in rem* action would greatly broaden the scope of the ACPA. It is also unclear how an *in rem* action based on trademark infringement or dilution grounds would further the ACPA's goal to deter cybersquatting. Taken together, it seems more appropriate to limit *in rem* actions to cases where a plaintiff can plead and prove bad faith intent.

Congress should amend the statute to eliminate the ambiguity of the statutory language, and clarify the requirements of the *in rem* action. In so doing, Congress should keep in mind that the ACPA is a special tool created to fight cybersquatting, not a weapon to replace or expand well-established trademark law.

III. CONCLUSION

While the ACPA has proven effective in typical cybersquatting suits, it is not suitable to resolve every dispute arising within the Internet context. Because of the procedural and remedial advantages of an ACPA action, however, some parties have invoked the ACPA even when the case is better resolved under traditional trademark principles. In deciding these cases, some courts have interpreted the ACPA broadly in order to reach their desired result. This Note has stressed, however, that the ACPA is a tool created specifically to deter cybersquatters. Accordingly, courts should limit the application of the ACPA to cases when there is clear evidence of bad faith intent.

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160. At least one court has pointed out the ambiguity of the statute. *See* Cable News Networks L.P. v. Cnnews.com, No. 00-2022-A, 2001 WL 1657492 (E.D. Va. Dec. 21, 2001) (noting that the *in rem* provision is ambiguous because its terms give rise to more than one meaning).

161. *See* MCCARTHY, *supra* note 116, § 25:79. *But see* Harrods Ltd. v. Sixty Internet Domain Names, 110 F. Supp. 2d 420, 422-23 (E.D. Va. 2000) (explicitly rejecting trademark infringement and dilution actions brought *in rem*).

EMERGING PATTERNS IN ARBITRATION UNDER THE UNIFORM DOMAIN-NAME DISPUTE-RESOLUTION POLICY

By Patrick D. Kelley

The Uniform Domain-Name Dispute-Resolution Policy ("UDRP")[1] provides a mechanism for resolving disputes between domain name owners and trademark holders who claim that a domain name infringes their trademark.[2] Designed to provide a relatively quick, efficient, low cost alternative to initiating infringement or dilution litigation, the UDRP allows a trademark holder to challenge any domain name deemed confusingly similar or identical to his mark.[3] Before the UDRP went into effect, most trademark-based domain name disputes could only be resolved by agreement, court action, or arbitration.[4] Disputes over allegations of infringement can now be resolved under the UDRP when the trademark owner files a complaint with an approved dispute resolution service provider.[5]

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1. ICANN, *Uniform Domain Name Dispute Resolution Policy, at* http://www.icann.org/udrp/udrp-policy-24oct99.htm (Oct. 24, 1999) [hereinafter *UDRP*].

2. ICANN, *Uniform Domain-Name Dispute-Resolution Policy, General Information, at* http://www.icann.org/udrp/ (last modified Feb. 5, 2002) [hereinafter *UDRP General Information*].

3. Sally M. Abel, *eVolution or Revolution? Trademark Law on the Internet, at* http://www.fenwick.com/pub/ip_pubs/Trademarks_&_Internet/Trademark_&_Internet.htm (Jun. 18, 2001).

4. J. Kevin Gray, *UDRP - The First Nine Months, at* http://www.jgsolutions.com/material/articles/udrphist.pdf (last visited Feb. 8, 2002).

5. *Id. See also* ICANN, *Approved Providers for Uniform Domain-Name Dispute-Resolution Policy, at* http://www.icann.org/dndr/udrp/approved-providers.htm (last modified Feb. 5, 2002) [hereinafter *Approved Providers*] (providing a list of ICANN-approved dispute resolution service providers. Approved providers include: the National Arbitration Foundation ("NAF"); CPR Institute for Dispute Resolution ("CPR"); and the World Intellectual Property Organization ("WIPO")); *eResolution Leaves Worldwide Domain Name Dispute Resolution Behind, at* http://www.mediate.com/adrassociates/pg208.cfm (Dec. 2001) [hereinafter *eResolution*] (discussing eResolution's decision to end its participation as a dispute resolution service provider for the UDRP); ICANN, *ICANN Announces New Dispute Resolution Service Provider in the Asia Pacific Region, at* http://www.icann.org/announcements/announcement-03dec01.htm (Dec. 3, 2001) [hereinafter *New Provider*] (announcing that a new provider, the Asian Domain Name Dispute Resolution Centre (ADNRC), was recently approved and will begin accepting disputes on February 28, 2002); ICANN, *Information Concerning Approval Process for Dispute-Resolution Service Providers, at* http://www.icann.org/udrp/udrp-provider-approval-

Implemented by the Internet Corporation for Assigned Names and Numbers ("ICANN") on January 3, 2000, the UDRP appears to be a success based on results over the last two years.[6] Some commentators maintain that the UDRP has exceeded expectations, by providing a quick method for fairly resolving domain name disputes at a relatively low cost.[7] In spite of its apparent success, the UDRP has been the subject of significant criticism on a variety of issues.[8] The most common criticism of the UDRP is that the policy is biased in favor of trademark owners ("the Complainants"), giving them an unfair advantage over the domain name

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process.htm (last modified Feb. 5, 2002) [hereinafter *Approval Process*] (detailing the application process to obtain provisional approval as a UDRP dispute resolution service provider. The application must show, among other things that: (1) the applicant has sufficient experience to competently deal with the clerical aspects of alternative dispute resolution proceedings; (2) the applicant has at least twenty well qualified individuals willing to serve as neutral panelists; and (3) the provider's supplemental rules and internal procedures reflect an understanding of the workings of the policy and its rules).

6. ICANN, *Timeline for the Formulation and Implementation of the Uniform Domain-Name Dispute-Resolution Policy, at* http://www.icann.org/udrp/udrp-schedule.htm (last modified Feb. 5, 2002) [hereinafter *Timeline*]. *See* ICANN, *Statistical Summary of Proceedings Under Uniform Domain Name Dispute Resolution Policy, at* http://www.icann.org/udrp/proceedings-stat.htm (last modified Feb. 20, 2002) [hereinafter *Statistical Summary*] (providing a numerical breakdown of the results of all UDRP disputes filed in the last two years). As of February 20, 2002, less than six and one-half percent of the 5,277 administrative proceedings initiated under the UDRP are still pending. Approximately eighty-two percent of all proceedings were disposed of by a decision, while just over ten and one-half percent were settled or dismissed. These proceedings have led to the resolution of disputes involving 8,966 domain names. Roughly seventy-nine percent of all decided cases resulted in at least one domain name being transferred to the Complainant. The Respondent prevailed in less than twenty percent of the decided cases. Although the UDRP allows either party to file a lawsuit at anytime during the proceeding and up to 10 days after the proceeding if a domain name is ordered transferred or canceled, this option has rarely been exercised. *Id. See also* Patrick L. Jones, *Complete List of UDRP Challenges in Court, at* http://www.udrplaw.net/UDRPappeals.htm (last modified Feb. 8, 2002) (providing a database of forty-two UDRP decisions that are being challenged or were challenged in U.S. courts, news articles on the outcomes of these cases, and a link to the UDRP decision that resulted in the lawsuit).

7. Gray, *supra* note 4. *See also,* M. Scott Donahey, *The UDRP—Fundamentally Fair, but Far from Perfect*, 6 Electronic Com. & L. Rep. 937 (Aug. 29, 2001), *available at* http://pubs.bna.com/ip/BNA/EIP.NSF/23d9e82d7d25950885256743006e3012/8c885f12f946fe8285256ab5007e1b1f?OpenDocument (noting that the UDRP is a fundamentally fair system, despite its flaws).

8. *See, e.g.*, Michael Geist, *Fair.Com?: An Examination of the Allegations of Systematic Unfairness in the ICANN UDRP, at* http://aix1.uottawa.ca/~geist/geistudrp.pdf (Aug. 2001); A. Michael Froomkin, *ICANN's "Uniform Dispute Resolution Policy"—Causes and (Partial) Cures, at* http://www.law.miami.edu/~froomkin/articles/udrp.pdf (Nov. 19, 2001).

owners ("the Respondents").[9] According to these critics, it is this bias that allows Complainants to win over eighty percent of all UDRP disputes.[10] Additional criticism has been directed at the UDRP's processes and procedures.[11] Proponents of this line of criticism have called for the addition of an appellate process to provide an alternative to challenging UDRP decisions in court and deal with split precedents that have resulted in inconsistent decisions in cases with similar underlying facts.[12]

This Note seeks to examine the validity of these criticisms in light of the decisions produced under the UDRP and propose potential solutions to these problems. Foremost among these proposals is the implementation of a UDRP-based appellate process to provide a mechanism for challenging UDRP decisions without resorting to the court system.[13] This Note discusses how several UDRP-based dispute resolution policies have handled the implementation of an appellate process, and outlines the parameters of a model appellate process under the UDRP. In addition, this Note details proposed revisions to UDRP procedures that would require the majority of all UDRP disputes to be heard by three-member panels. The Note will ultimately propose a model for fixing problems with the current policy in order to ensure that the UDRP remains a viable and effective medium for resolving domain name ownership disputes in the future.

I. UDRP POLICIES AND PROCEDURES

The UDRP provides expedited administrative proceedings for the resolution of domain name disputes purportedly arising from abusive registrations of domain names.[14] A UDRP proceeding is initiated when a trademark owner files a complaint with an ICANN-approved dispute resolution service provider.[15] There are currently three[16] ICANN-approved dispute

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9. *Id.*

10. *Id. See also Statistical Summary*, *supra* note 6.

11. *See* Justin Kelly, *ICANN Panelist Floats Appeals Process For Domain Arbitrations*, Jan. 12, 2001, *at* http://www.adrworld.com/opendocument.asp (subscription required); *see generally* Froomkin, *supra* note 8.

12. *Id.*

13. Froomkin, *supra* note 8, at 49-56, 66-68 (discussing the difficulties of challenging UDRP decisions in court).

14. *UDRP*, *supra* note 1, at § 4(a).

15. *Id.*

16. Until November 30, 2001, there were four ICANN-approved service providers; however, eResolution recently ended its participation as a dispute resolution service provider for the UDRP. *eResolution*, *supra* note 5. ICANN recently authorized a new dispute resolution service provider, The Asian Domain Name Dispute Resolution Centre

resolution service providers—the National Arbitration Foundation ("NAF"), CPR Institute for Dispute Resolution ("CPR"), and the World Intellectual Property Organization ("WIPO").[17] The dispute resolution service provider is usually selected by the Complainant, who also typically pays the service provider's fees.[18] The only remedies available to the Complainant are the cancellation or transfer of the domain name registration.[19]

If a complaint is filed against a domain name owner, the owner is required to submit to these proceedings under the terms of its domain name registration agreement.[20] Complainants and Respondents may alternatively choose to settle their disputes by mutual agreement, arbitration, or through court proceedings.[21] The UDRP requires that most trademark-based domain name disputes be resolved by one of these methods before a registrar[22] will cancel, suspend, or transfer a domain name.[23] The UDRP is followed by all registrars in the .biz, .com, .info, .name, .net, and .org top-level domains.[24]

Under the UDRP, domain name owners are required to submit to mandatory administrative proceedings if a third party claims that the: (1) domain name is confusingly similar or identical to its trademark or service mark; (2) owner has no rights or legitimate interests in the domain name; and, (3) domain name was registered and is being used in bad faith.[25] The Complainant is required to prove that each of these elements is present in order to prevail.[26] Accused domain name owners can demonstrate their rights and legitimate interests by providing evidence of any of the following: (1) use or demonstrable preparations for use of the domain or a name

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(ADNRC). The ADNRC will begin accepting disputes on February 28, 2002. *New Provider*, *supra* note 5.

17. *Approved Providers*, *supra* note 5.

18. *UDRP supra* note 1, at § 4(d), 4(g).

19. *Id.* at § 4(i).

20. *Id.* at § 4.

21. *UDRP General Information*, *supra* note 2.

22. A registrar is the organization with which the domain name has been registered. ICANN, *Rules for Uniform Domain Name Dispute Resolution Policy, at* http://www.icann.org/udrp/udrp-rules-24oct99.htm (Oct. 24, 1999) [hereinafter *Rules*].

23. *UDRP General Information*, *supra* note 2. Trademark-based domain name disputes involving domain names registered with registrars that do not follow the UDRP are not subject to these terms. Disputes involving these registrars' domain names are instead subject to whatever terms the registrar chooses to impose.

24. *Id.*

25. *UDRP*, *supra* note 1, at § 4(a). *See also id.* at § 4(b) (discussing circumstances indicative of bad faith registration and use of a domain name).

26. *Id.* at § 4(a).

corresponding to the domain name in connection with a legitimate offering of goods and services before the domain owner was notified of the dispute; (2) common knowledge of the owner being known under the domain name, even absent trademark or service mark rights; or (3) a legitimate noncommercial or fair use of the domain name, with no intent for commercial gain to misleadingly divert consumers or tarnish the Complainant's trademark or service mark.[27]

The institution of a UDRP proceeding does not prevent either party from filing a lawsuit to resolve the dispute in a court of mutual jurisdiction before, during, or after the administrative proceeding.[28] The UDRP defines a court of mutual jurisdiction as a court in either the jurisdiction in which the main office of the Registrar is located,[29] or the jurisdiction in which the domain name owner resides according to the registration of the domain name in the Registrar's Whois database[30] at the time the complaint is filed.[31]

If a UDRP administrative panel ("panel") orders a domain name to be transferred or canceled, the owner is given ten business days to provide official documentation indicating that he has filed a lawsuit.[32] If he does not file within ten days, the decision will be implemented.[33] If documentation of the lawsuit is received within the ten day period, no further action will be taken until: (1) satisfactory evidence of a resolution is presented; (2) the lawsuit is dismissed or withdrawn; or, (3) the court dismisses the lawsuit or orders the owner to cease using the domain name.[34]

II. CRITICISMS OF THE UDRP

With over four thousand domain name dispute resolutions to its credit,[35] the UDRP appears, at least on the surface, to be a rousing suc-

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27. *Id.* at § 4(c).

28. *Id.* at § 4(k).

29. Provided the domain name owner agreed to submit to that jurisdiction for disputes over domain name use at the time the domain name was registered. *Rules*, *supra* note 22.

30. The Registrar's Whois Database contains records of the names and addresses of the owners of each domain name registered with that particular registrar. *See* Verisign, *WHOIS Command Overview*, *at* http://www.netsol.com/en_US/faq/whois/whois-learnmore.jhtml (last visited Feb. 8, 2002).

31. *Rules*, *supra* note 22.

32. *UDRP*, *supra* note 1, at § 4(k).

33. *Id.*

34. *Id.*

35. *Statistical Summary*, *supra* note 6.

cess.[36] In spite of these numbers, the UDRP has been the subject of significant criticism on a number of fronts.[37] Perhaps the most vocal critics of the UDRP are those who feel the current policy gives trademark holders an unfair advantage over domain name owners.[38] Much of this criticism has been directed at the structure and processes of the UDRP.[39] These commentators argue that there is a need for an appellate process to help ensure the fairness of panel decisions and aid in the creation of a body of consistent precedent.[40]

A. Claims that the UDRP is Biased in Favor of Trademark Holders

A number of critics have claimed that the UDRP is biased in favor of trademark holders, who are typically the Complainants in domain name disputes.[41] Proponents of this line of criticism point to ICANN's own figures, which show that Complainants emerge victorious in over eighty percent of all UDRP disputes.[42] Some argue that this trend is temporary, that it merely reflects a weeding out of obviously infringing domain names, and should level off once most of the blatant cybersquatting cases have been decided.[43] Those critical of the UDRP, however, maintain that this trend is not merely a result of Complainants having stronger cases, but is rather caused by a system which gives Complainants a significant advantage by allowing them to choose the dispute resolution service provider that will ultimately decide their case.[44] They assert that this system creates a competitive environment in which Complainants pick the arbitration service provider that appears most likely to rule in their favor.[45]

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36. *See, e.g.*, Gray, *supra* note 4 (arguing that the UDRP has proven to be an extremely productive system that produces fair results quickly and at a low cost); Donahey, *supra* note 7.

37. *See, e.g.*, Rod Dixon, *The Arbitral Forum: Why ICANN'S Uniform Dispute Resolution Process Must Undergo Reform*, Oct. 9, 2000, *at* http://www.domainnotes.com/news/article/0,,3371_480291,00.html; Geist, *supra* note 8; Froomkin, *supra* note 8.

38. *E.g.*, Geist, *supra* note 8; Froomkin, *supra* note 8.

39. *Id.*

40. *See, e.g.*, Kelly, *supra* note 11.

41. *See* Justin Kelly, *ICANN Board Member Calls for End to Domain Dispute Policy*, Oct. 23, 2000, *at* http://www.adrworld.com/opendocument.asp?Doc=RLAb9bVdD0&code=TvqDOdFE (subscription required); Geist, *supra* note 8.

42. *Statistical Summary*, *supra* note 6.

43. Gray, *supra* note 4.

44. Geist, *supra* note 8, at 3-8.

45. *Id.*

1. *The Distribution of Complaints Among Service Providers*

WIPO and NAF have handled the majority of the disputes, with fifty-eight and thirty-four percent of all cases respectively.[46] Based on raw statistical evidence, WIPO and NAF are also much more likely to rule in favor of Complainants than the other two providers, eResolution and CPR.[47] Complainants are successful in approximately eighty-two percent of WIPO proceedings and in eighty-three percent of NAF proceedings, but are only successful approximately sixty-three percent of the time with eResolution and fifty-nine percent of the time with CPR.[48] eResolution, which generally produced the least favorable outcomes for Complainants, handled just seven percent of all cases, while CPR handled less than one percent.[49] Critics of the UDRP maintain that Complainants do not choose service providers based on cost, noting that WIPO, which is the most popular provider, is the second most expensive ($US 1500 for a single complaint).[50]

Based on the apparent correlation between successful outcomes for Complainants and selection of dispute resolution services, those who believe the UDRP is biased in favor of trademark holders argue that the likelihood of success plays a major role in which provider is ultimately chosen.[51] This "forum shopping" was cited as one of the main factors in eResolution's decision to cease its participation as a dispute resolution

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46. *Id.* at 6. Until eResolution's November 30, 2001 decision to end its participation as a UDRP service provider, there were four active ICANN certified dispute resolution service providers. This data was collected while eResolution was still an active service provider.

47. *Id.*

48. *Id.*

49. *Id.*

50. *Id.* at 3-4. *See also* World Intellectual Property Organization, *Schedule of Fees under the ICANN Policy, at* http://arbiter.wipo.int/domains/fees/index.html (Aug. 15, 2001) (detailing WIPO fees for UDRP proceedings); National Arbitration Forum, *Uniform Domain Name Dispute Resolution Policy "UDRP" Fees, at* http://www.arbforum.com/domains/UDRP/fees.asp (Feb. 1, 2002) (detailing NAF fees for UDRP proceedings); CPR Institute for Dispute Resolution, *CPR'S Supplemental Rules and Fee Schedule, at* http://www.cpradr.org/ICANN_RulesAndFees.htm (last visited Feb. 8, 2002) (detailing CPR fees for UDRP proceedings).

51. Geist, *supra* note 8, at 7. *See also* Laurence R. Helfer & Graeme B. Dinwoodie, *Designing Non-National Systems: The Case of the Uniform Domain Name Dispute Resolution Policy*, 43 WM. & MARY L. REV. 141, 211-13 (2001) (discussing problems created by the actions of some dispute resolution service providers that have created a public perception that "some dispute settlement providers are more complainant friendly than others").

service provider.[52] In a press release, the company maintained that its perception as the provider least likely to rule in favor of Complainants had led to a significant reduction in its market share.[53] Concerns over potential "forum shopping" have prompted some commentators to make allegations of potential bias on the part of service providers.[54] These critics have expressed concern that service providers might deliberately assign panelists they believe are likely to rule in favor of Complainants.[55]

2. *Respondent Default*

Respondent default occurs when a Respondent fails to respond to the complaint before the time limit expires.[56] When a default occurs, the UDRP proceeding continues towards a decision, and the panel is allowed to consider the Respondent's default in reaching its decision.[57] Given that respondents default in fifty to sixty percent of all proceedings,[58] the fact that Complainants emerge victorious in over eighty percent of these disputes[59] seems somewhat less shocking than when Complainant victories are considered on their own. It has been argued that Complainants win the majority of these cases on the merits, and that a significant percentage of UDRP cases, especially in the early days, dealt with blatant cases of cybersquatting where the Respondents were clearly in the wrong.[60] Unfortunately, since Respondents default in approximately half of these disputes,[61] it is all but impossible to form concrete conclusions based on these numbers alone.

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52. *eResolution*, *supra* note 5 (detailing eResolution's decision to end its participation as a dispute resolution service provider). Karim Benyekhlef, eResolution's president argued that "forum shopping" is a common occurrence, noting that Complainants chose WIPO, the provider statistically most likely to rule in their favor, far more often than eResolution, which produced less favorable results for Complainants. Benyekhlef claims this is one of the main reasons that eResolution's market share shrunk to the point where the proceeds no longer covered the cost of maintaining the service. *Id.*

53. *Id.*

54. Geist, *supra* note 8, at 7-9.

55. *Id.*

56. John G. White, *ICANN's Uniform Dispute Resolution Policy In Action*, 16 BERKELEY TECH. L.J. 229, 235-36 (2000).

57. *Id. See also Rules*, *supra* note 22.

58. Donahey, *supra* note 7, at 2; White, *supra* note 566, at 236-37.

59. *Statistical Summary*, *supra* note 6

60. Gray, *supra* note 4.

61. Donahey, *supra* note 7, at 2; White, *supra* note 566, at 236-37.

3. *Differing Results from One and Three-Member Panels*

Three-member panels are responsible for only ten percent of all decisions, with Respondent's defaulting in twenty-four percent of those disputes.[62] While the overall Complainant win percentage rests at just over eighty percent, that number decreases to sixty percent for cases decided by a three-member panel.[63] As expected, Complainants emerged victorious in all but one of the three-member panel cases in which the Respondent defaulted.[64] When default cases are excluded, however, Complainants win only forty-five percent of three-member panel cases.[65]

Interestingly, Complainants appearing before three-member panels receive favorable outcomes at roughly the same rate regardless of which provider they use.[66] This is in stark contrast to the overall figures encompassing results from both one- and three-member panels, which indicate that WIPO and NAF find in favor of Complainants at a much higher rate than eResolution and CPR.[67] Despite the fact that Complainants have a better success rate with one-person panels than with three-member panels, Complainants request three-member panels more frequently than Respondents.[68]

One critic argues that this pattern occurs because having three panelists limits the possibility of a single panelist misinterpreting the policy and prevents incorrect decisions.[69] In the end, while the UDRP as a whole might provide an unfair advantage to Complainants, three-member panels statistically appear to produce more even results, with Complainants winning only sixty percent of disputes before three panelists in contrast to just over eighty percent when the dispute is heard by one panelist.[70] While it is all but impossible to conclude that three-member panels are inherently

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62. Geist, *supra* note 8, at 18-20.

63. *Id; Statistical Summary, supra* note 6.

64. *Id.*

65. *Id.*

66. *Id.* at 18-22.

67. *Id.*

68. *Id.* at 20 (indicating that Complainants requested the three-member panels sixty-two percent of the time).

69. *Id.* at 18-22 (explaining these figures by noting that Respondents may see the entire system as biased and unfair, and choose the three-member panel in hopes of receiving a more equitable decision; while Complainants with strong cases may be concerned that a single panelist will misinterpret the policy and decide a case they feel they should win in favor of the Respondent).

70. *Id; Statistical Summary, supra* note 6.

more fair than one-member panels,[71] these statistics have created a perception of increased fairness in three-member panels.[72]

4. *Additional Criticisms Alleging UDRP Bias Towards Trademark Holders*

Allegations of bias in favor of trademark holders have not been limited to the process for selecting a dispute resolution provider.[73] Among the most common criticisms of the UDRP is that it fails to ensure that domain owners actually receive notice that a complaint has been filed against them.[74] It has also been argued that in providing the option of challenging UDRP decisions in court, the policy actually limits the availability of the judicial system to those who lose UDRP disputes.[75] In addition, it has been alleged that the UDRP gives service providers too much freedom to add supplemental rules that may bias the dispute resolution process.[76] Some commentators also maintain that the UDRP allotted twenty-day response period fails to provide sufficient time for domain owners to respond to complaints.[77]

B. Claimed Problems with the UDRP's processes and procedures

1. *Using the Legal System to Overturn Panel Decisions*

Critics of current UDRP procedures have called for the addition of an appellate process to ensure the quality and fairness of panel decisions.[78] Under current UDRP procedures, the only alternative available to the losing party in a UDRP proceeding is to file a lawsuit to overturn the panel's decision.[79] Once the panel reaches a decision, the losing party has only ten business days to file suit in a court of mutual jurisdiction, otherwise the

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71. Concluding that three-member panels are more fair than one-person panels would require a detailed analysis of each case handled by both types of panels, which is impossible because complete records are not available for UDRP decisions.

72. *See id.* at 18-29 (providing a detailed statistical analysis of the results produced by both three- and one- person panels, and arguing that using only three-member panels would limit the potential for bias in favor of trademark holders).

73. Froomkin, *supra* note 8 (providing an in-depth discussion and analysis of each of these criticisms as well as an additional look at issues surrounding the selection and composition of the UDRP's administrative panels).

74. *Id.* at 64-65.

75. *Id.* at 66-67.

76. *Id.* at 45.

77. *Id.* at 64.

78. Kelly, *supra* note 11.

79. *UDRP supra* note 1, at § 4(k).

panel's decision will be implemented.[80] Although this is the only way a UDRP decision can be overturned, relatively few UDRP decisions have been challenged in court.[81] Those decisions that have been challenged have produced mixed results.[82] Critics of the UDRP argue that jurisdictional obstacles, the limited amount of time a losing party has to file a lawsuit, and the uncertainty on the part of courts as to how these cases should be handled appears to have limited the usefulness of courts as a medium for appealing UDRP decisions.[83] Critics of the current policy maintain that creating a means to appeal UDRP panel decisions without filing a lawsuit would make it easier to challenge panel decisions and ultimately improve the quality of these decisions.[84]

To date, relatively few United States ("U.S.") courts have considered what role UDRP panel decisions should play in the American legal system.[85] The most publicized court case involving a UDRP decision was *Weber-Stephen Products Co. v. Armitage Hardware and Building Supply, Inc.*,[86] in which the U.S. District Court for the Northern District of Illinois held that neither the UDRP nor its governing rules dictate what weight courts should give to a panel's decision.[87] The court declined, however, to determine the exact standard by which it might ultimately review the result of a UDRP proceeding, and what, if any, deference a panel decision would be entitled to.[88] Overall, the results of UDRP-based cases before U.S. courts have varied widely, with no consistent body of precedent emerging.[89] The absence of legal precedent relating to domain name dis-

80. *Id.*

81. *Jones*, *supra* note 6 (summarizing over forty UDRP decisions that are being challenged or were challenged in U.S. courts).

82. *Id.*

83. Froomkin, *supra* note 8, at 49-56, 66-68 (detailing how jurisdictional problems and other obstacles have limited the availability of court proceedings to losing parties in UDRP disputes). *See also* Helfer & Dinwoodie, *supra* note 51, at 203-04 (discussing potential obstacles to challenging UDRP decisions in court caused by the "extremely short ten-day window" respondents have to file suit once the panel has reached a decision).

84. Kelly, *supra* note 11.

85. Jones, *supra* note 6.

86. 54 U.S.P.Q.2d (BNA) 1766 (N.D. Ill. 2000).

87. *Id.* at 1768; *see also* Abel, *supra* note 3.

88. *Weber*, 54 U.S.P.Q.2d (BNA) at 1768.

89. *See, e.g.*, *Weber*, 54 U.S.P.Q.2d (BNA) 1766; Patrick Jones, *Federal Court Overturns UDRP Decision For NCAA*; *NCAA Also Wins ACPA Case Against Internet Gambling Operator*, Sept. 2, 2001, *at* http://www.udrplaw.net/ExclusiveNews.htm (discussing the *NCAA* case where the district court gave plaintiff NCAA rights to twelve domain names WIPO had granted to defendant NCAAbasketballodds.com); Virtuality L.L.C. v. Bata Ltd., Civil No. H-00-3054 (D. Md. Apr. 2, 2001), *available at* http://www.mdd.uscourts.gov/Opinions152/Opinions/bata.pdf (denying Bata's motion to

putes in general, and UDRP decisions in particular, is not unique to the United States.[90] Domain name disputes remain a relatively novel concept for the court systems of most countries.[91] In fact, most countries have yet to hear any domain name disputes in their courts.[92]

Unlike other problems with the UDRP, making changes to the current policy is not likely to solve problems relating to the interaction of UDRP decisions with the court systems. Aside from extending the ten-business day limit for filing a lawsuit after a panel decision has been rendered, there is relatively little ICANN or the dispute resolution service providers can do to bring about a direct solution to this problem. The UDRP allows either party to file suit in any court of mutual jurisdiction.[93] Absent a complete harmonization of international trademark laws, the end result of this policy will be decisions that widely vary depending on where the lawsuit is filed.

2. *The Role of Precedent in UDRP Proceedings*

Under the UDRP, panels are allowed to use prior decisions to guide them in resolving disputes, but these decisions do not serve as binding precedent.[94] Thus, panels are not bound by previous decisions, regardless of similarity.[95] Critics of the UDRP maintain that this policy has resulted in numerous situations in which incorrect decisions are used as precedent in deciding cases of a similar nature, resulting in a continuous stream of erroneous decisions.[96] The only option currently available to parties who feel their case has been incorrectly decided is to file a lawsuit challenging the panel decision.[97] The absence of any internal mechanism for reviewing panel decisions has led critics of the current policy to call for the institu-

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dismiss Virtuality's federal trademark claim, finding that it had jurisdiction over this claim); Parisi v. Netlearning, Inc., 139 F. Supp. 2d 745 (E.D. Va. 2001) (holding that the Federal Arbitration Act, which limits the review of arbitration awards, does not apply to UDRP decisions); Sallen v. Corinthians Licenciamentos LTDA, 273 F.3d 14 (1st Cir. 2001) (reversing the district court's dismissal, for lack of jurisdiction, of a Respondent's challenge to a UDRP decision to transfer his domain name).

90. Diane Cabell, *Foreign Domain Name Disputes 2000,* 17 COMPUTER & INTERNET LAW. 5 (2000), *available at* http://www.mama-tech.com/foreign.html.

91. *Id.*

92. *Id.*

93. *Rules, supra* note 22.

94. Helfer & Dinwoodie, *supra* note 51, at 235-36; Froomkin, *supra* note 8, at 69.

95. *Id.*

96. Froomkin, *supra* note 8, at 56.

97. *Rules, supra* note 31.

tion of an appellate process to help correct erroneous decisions and prevent them from being used as precedent in future proceedings.[98]

An examination of panel decisions also reveals an increasing number of split precedents in which divergent lines of case law are followed by different panels, resulting in vastly disparate holdings in cases with similar underlying facts.[99] UDRP critics argue that a method for sorting out inconsistent precedents is needed to provide UDRP panels with a uniform body of precedent to aid in the resolution of disputes.[100] One notable example of split precedent can be found in cases where the Respondent defaults.[101] When a default occurs, the UDRP proceeding continues, and the panel is allowed to consider the Respondent's default in reaching its decision.[102] Some panels use a literal interpretation of the policy and rules to shift the burden of proof on all issues to Complainants.[103] Other panels take a broader approach, placing the burden of proof on the Respondent.[104] Because respondents default in fifty to sixty percent of all proceedings,[105] the use of these two different methods is cause for concern.

III. PROPOSED SOLUTIONS AND IMPROVEMENTS FOR THE UDRP'S PROBLEMS

Despite the criticisms levied against it, the UDRP remains the best mechanism for resolving disputes over domain name ownership. There are, however, a number of flaws with the current policy, which limit both its effectiveness and its ability to produce consistently fair, high quality decisions.[106] To that end, critics of the current policy have made a number of recommendations aimed at improving the UDRP.[107] Based on these criticisms, it seems clear that a mechanism for appealing panel decisions under the UDRP could reduce problems with dueling lines of precedent and erroneous decisions. A requirement that three-member panels hear all UDRP disputes, except those in which the Respondent defaults, would also help to correct some of the weaknesses of the current policy.

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98. *Id.*
99. Kelly, *supra* note 11.
100. *Id.*
101. White, *supra* note 566, at 239-40.
102. *Id. See also Rules*, *supra* note 31.
103. White, *supra* note 566, at 239-40.
104. *Id.*
105. *See supra* note 58 and accompanying text.
106. *See generally* Geist, *supra* note 8; Froomkin, *supra* note 8.
107. *See, e.g.*, Kelly, *supra* note 11; Geist, *supra* note 8; Froomkin, *supra* note 8.

A. Making Three-Member Panels the Standard for UDRP Dispute Resolution

Based on the more equitable results produced by three-member UDRP panels, limiting the availability of single-person panels to cases in which the Respondent defaults, and requiring that all other disputes be decided by three-member panels, would lend an increased perception of fairness to UDRP proceedings.[108] Under this proposed policy, the Complainant and Respondent would each select one panelist.[109] The dispute resolution service provider would select the third panelist from a list of panelists, taking into consideration the preferences of both parties in making that selection.[110] Complainants would be required to bear the full cost of the proceeding.[111] Additional fees received from using only three-member panels could potentially allow service providers to hire more panelists, thereby eliminating any potential concerns regarding a lack of panelists to staff the three-member panels. As with the current policy, decisions would require a majority vote from the panel.[112] This process would significantly reduce the perception that providers are assigning panelists they believe are more likely to find in favor of Complainants, providing a solution to one of the most common criticisms of the UDRP.[113]

B. Implementing a UDRP-Based Appellate Process

The need for an appellate process finds support in a variety of factors. Foremost among these are the divergent lines of precedent for some key issues[114] that serve as the basis for vastly different decisions by UDRP

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108. Geist, *supra* note 8, at 26-29 (arguing for mandatory three-member panels). *See also*, Helfer & Dinwoodie, *supra* note 51, at 194 (stating that "[i]n international commercial arbitration, use of a three-member panel is the accepted norm, and often a default rule if the parties fail to specify a different selection method" and that "[t]hree-member panels also promote confidence in the arbitral process and thus generate fewer challenges to the panel's final decision").

109. Geist, *supra* note 8, at 26-29 (proposing rules identical to those currently used by ICANN for selecting the members of a three-member panel); *see also Rules*, *supra* note 22.

110. *Id.*

111. *Id.* (arguing that the Complainant should be required to bear the full cost of the mandatory three-member panel, in contrast to the current policy, in which the Complainant only pays the entire cost for the three-member panel if he elects to use it).

112. *Rules*, *supra* note 22, at § 15(c).

113. Geist, *supra* note 8, at 7-9.

114. For example, the two different approaches used by administrative panels in deciding how to deal with cases in which the Respondent is in default. *See supra* notes 101-105 and accompanying text; *see also* White, *supra* note 566, at 239-240.

panels on cases with essentially the same facts.[115] It is unclear what, if any, role the UDRP intends previous panel rulings to play in a panel's decision-making process.[116] Panelists are not bound by prior decisions, but they may consider them in resolving disputes.[117] UDRP panels have varied in their interpretation of this rule, with some panels treating prior decisions as binding precedent, and others choosing to completely ignore them.[118] Most analysts see the development of a body of precedent as a positive tool that will ultimately improve the efficiency and quality of decisions, as many disputes involve similar issues and facts.[119]

The addition of an appellate process to supplement current UDRP procedures would create an entity to reconcile divergent bodies of precedent, and allow panelists to rely on appellate decisions as the model for resolving a particular class of disputes. A UDRP-based appellate system would also play an important role in correcting rulings in which incorrect rules were applied or incorrect decisions were made. Although modifying the UDRP is unlikely to produce a solution to the jurisdictional wrangling and inconsistent decisions plaguing the court system, the addition of an internal appeals process may lessen the impact of these problems by improving the quality of UDRP decisions and providing an alternative avenue for disputing the results of UDRP proceedings. Because challenging UDRP decisions in court has proven to be a difficult and uncertain proposition,[120] a UDRP appellate process would present a more accessible forum for parties who feel their cases were decided incorrectly. If parties feel their dispute was correctly and fairly decided, which is what a UDRP appellate process would strive to promote, they may be less likely to challenge the decision in court. Clear and concise panel decisions based on consistent applications of the UDRP will make things easier for courts reviewing panel decisions.

1. Competing Models for a UDRP Appellate Process

a) The U.S. Supreme Court Model

The key obstacle for the creation of a UDRP appeals process is finding a way to implement a fair and effective process without defeating the efficiency and cost effective benefits of the UDRP.[121] One approach is to cre-

115. Kelly, *supra* note 11.
116. Helfer & Dinwoodie, *supra* note 51, at 235-36; Froomkin, *supra* note 8, at 69.
117. *Id.*
118. Helfer & Dinwoodie, *supra* note 51, at 235-36; Kelly, *supra* note 11.
119. *See* Kelly, *supra* note 11.
120. Froomkin, *supra* note 8, at 49-56, 66-68.
121. Kelly, *supra* note 11.

ate a system similar to the U.S. Supreme Court.[122] An appellate body consisting of nine panelists would typically hear appeals from panel decisions in groups of three, with the possibility of an *en banc* hearing before the entire panel in certain special cases.[123] In this model, arbitrators would be appointed either by the service providers or directly by ICANN.[124] Members of the appeals board would have discretionary review over all panel decisions, with the bulk of their caseload coming from cases with similar facts that are decided differently.[125] Under this proposal, appeals would be financed either by charging the appealing party, adding a small fee to domain name registrations, or attaching a new fee to any complaint filed under the UDRP.[126]

While this proposal presents a potentially workable appellate process based on a well-tested model, it is likely to face many of the same problems found in the appellate systems of American courts. Overcrowded dockets, a significant increase in costs to the parties involved, and significant delays between panel decisions and appellate decisions would significantly limit the usefulness of this system.[127] Although this model would adequately settle many of the problems with inconsistent bodies of precedent, the delays and higher costs that would likely result would run counter to the UDRP's goal of providing an inexpensive and efficient means for dispute resolution.

b) The Keyword Dispute Resolution Policy Model

A second model stems from the Keyword Dispute Resolution Policy ("KDRP") enacted by RealNames to settle ownership disputes over its Internet Keywords System.[128] The provisions of the KDRP are almost identical to the UDRP with the exception of several modifications in the KDRP addressing many of the UDRP's most criticized problems.[129] One of the key differences between the two policies is that the KDRP provides

122. *Id.*
123. *Id.*
124. *Id.*
125. *Id.*
126. *Id.*
127. *Id.* (summarizing Michael Froomkin's criticisms of this proposal).
128. *See* Keywords, *at* http://www.realnames.com/Eng/Eng_Corporate_RealNames Homepage.asp (last visited Feb. 9, 2002) (describing the RealNames Keyword System, designed to provide an alternative to traditional domain names, by allowing the user to find a web page simply by typing the name of a company, product, or website in the Internet Explorer address bar). *See also* RealNames, *Keyword Dispute Resolution Policy, at* http://www.realnames.com/Virtual.asp?page=Eng_Policy_DisputeResolution (last visited Feb. 9, 2002) [hereinafter *RealNames KDRP*].
129. *RealNames KDRP*, *supra* note 1288.

for a limited appellate process in which a losing party can apply for "reconsideration" of its case.[130] The KDRP allows either party to move for reconsideration of the ruling, so long as they do so within two months of the panel's decision.[131] If the moving party can demonstrate "manifest injustice," then the motion will be granted.[132] Every effort will be made to have the motion heard by the same panelists who adjudicated the original complaint, unless the motion alleges that one of the panelists was not impartial.[133] Absent a showing of manifest injustice, the Complainant is forbidden from initiating an administrative proceeding involving the same Respondent and Keyword Registration within two years of a previous panel decision.[134]

The key feature of the KDRP appellate process is that appellants must provide considerable justification as to why their case deserves appellate consideration.[135] This requirement makes it unlikely that the appellate board would be forced to consider unwarranted appeals. Applying this mechanism to the UDRP would enable it to retain its efficiency while providing a mechanism for appealing wrongly decided cases and harmonizing inconsistent precedent. Requiring that parties show "manifest injustice" if their appeal is to be heard would likely prevent unwarranted appeals from overwhelming the system and hindering the efficiency of the appellate process. However, an unfortunate side effect of such a potentially stringent justification requirement[136] is that some cases that warrant appellate review may not meet the eligibility requirements. While review would likely be granted in cases of blatant error under the manifest injustice standard, it is unclear whether this standard would allow review of cases involving split precedent.

c) Nominet's United Kingdom Model

A third model for an appellate system comes from the recently implemented Dispute Resolution Service for the .uk top level domain ("TLD"). While most nations have elected to use the UDRP to resolve domain name disputes for their TLDs, Nominet, the body managing the .uk TLD, has

130. *Id.*
131. *Id.*
132. *Id.*
133. *Id.*
134. *Id.*
135. *Id.*
136. To date, no Keyword disputes have been filed, thus the KDRP and its appellate mechanism remain untested. It remains unclear what the term "manifest injustice" means, as RealNames has not taken any steps to define this term.

chosen to create its own dispute resolution policy loosely based on the UDRP.[137]

The Nominet policy contains two features not present in the UDRP.[138] First, it requires the parties to engage in an informal mediation, within three days of the complaint being filed.[139] It also adds an appeals process, through which either party to a dispute can challenge the ruling in the case.[140] Under this policy, parties must submit an appeal within five days after the decision has been rendered.[141] Once an appeal has been submitted, a panel of three of Nominet's experts will rule on it as soon as possible.[142] The appeals panel considers appeals on two grounds: (1) that a matter needs to be re-examined on the facts; or (2) that procedure has not been followed correctly.[143] Appellate panel decisions will be published, but they do not serve as binding precedent for future decisions, and do not affect any decisions previously made under the Dispute Resolution Service.[144] Experts are, however, allowed to consider the persuasive value of appellate rulings in making future decisions.[145] During the appellate process, both parties remain free to submit their dispute to a court of competent jurisdiction.[146]

The primary advantage of this model appears to be its focus on correcting errant decisions, misinterpretations of policy, and other situations where the facts of the case do not seem to support the outcome. Unfortunately, the Nominet model does not seem to offer a solution to the problem of divergent precedent for similar cases. The Nominet policy states that appellate decisions do not serve as binding precedent for future

137. UDRPLaw.Net, *Nominet Releases New Dispute Resolution Service For .UK Domain Names,* Sept. 27, 2001, *at* http://www.udrplaw.net/cctldDisputes.htm.

138. Nominet UK, *Dispute Resolution Service Procedure*, *at* http://www.nic.uk/ref/drs-procedure.html (last visited Feb. 9, 2002) [hereinafter *Nominet Procedure*].

139. *Nominet Procedure*, *supra* note 1388, at § 7 (detailing the mediation process: Nominet reserves complete discretion over how the mediation proceeds, negotiations are kept secret so as not to affect either party's position if the mediation fails, details of the negotiations can only be released by court order, and if the dispute is not resolved within ten days, the mediation period comes to a close and an expert is appointed to hear the case).

140. *Id.* § 18.

141. *Id.*

142. *Id.*; *see also* Nominet UK, *Dispute Resolution Service Policy*, *at* http://www.nic.uk/ref/drs-policy.html (last visited Feb. 9, 2002) [hereinafter *Nominet Policy*] (defining an "expert" as a person Nominet appoints to hear disputes who serves essentially the same role as a UDRP panelist).

143. *Nominet Policy*, *supra* note 142, at § 9.

144. *Id.*

145. *Id.*

146. *Id.*

that appellate decisions do not serve as binding precedent for future decisions.[147] The UDRP uses essentially the same approach for panel decisions, which can be considered by future panels in deciding disputes, but do not act as binding precedent.[148] Under the Nominet model, even with the potential for appellate review, the absence of binding precedent would still allow panels to resolve similar cases in different ways. While the losing party in these split precedent cases could likely appeal, it seems somewhat inefficient that the appellate body would potentially resolve the same issue numerous times. Further, there is no guarantee that the appellate body would even reach the same decision each time it heard an appeal on that issue.

2. *Suggested Model for a UDRP Based Appellate Process*

Based on an analysis of these three models, it seems clear that no single model fully addresses all of the major problems UDRP critics have identified.[149] An optimal UDRP-based appeals process must provide a system for challenging incorrectly decided cases and harmonizing inconsistent bodies of precedent, while adding to the perceived fairness of the overall UDRP process. It is equally important that this appellate system not lose sight of the UDRP's original purpose of providing quick, efficient resolutions to disputes over domain name ownership.[150]

One model for an optimal appellate system would require that the party seeking an appeal show: (1) that the panel's decision was clearly erroneous; or (2) that the decision involved a situation or issue for which competing bodies of precedent exist. This standard would allow the UDRP appeals process to correct erroneously decided cases, while providing a

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147. *Id.*

148. Helfer & Dinwoodie, *supra* note 51, at 235-36; Froomkin, *supra* note 8, at 69.

149. In addition to the three models discussed *infra*, the JAMS Optional Arbitration Appeal Procedure was considered in constructing the model UDRP appellate system. JAMS is an organization that provides a full range of alternative dispute resolution ("ADR") services throughout the U.S. and abroad. JAMS, *About JAMS, at* http://www.jamsadr.com/who_we_are.asp (last visited Feb. 9, 2002). *See also* JAMS, *ADR Tools & Processes, at* http://www.jamsadr.com/adr_tools_index.asp (last visited Feb. 9, 2002) (for an overview of different types of ADR and the ADR services offered by JAMS); JAMS, *JAMS Optional Arbitration Appeal Procedure, at* http://www.jamsadr.com/optionalArbAppeal.asp (June, 2000) [hereinafter *JAMS Appellate Procedure*] (detailing the optional appeals procedure available under certain circumstances to parties using JAMS dispute resolution services).

150. Kelly, *supra* note 11 (quoting Michael Froomkin who criticizes the U.S. Supreme Court model as hindering the efficiency and cost effectiveness of the UDRP).

mechanism for harmonizing divergent lines of precedent.[151] Appellate review of clearly erroneous decisions allows for a case-specific review of instances where the wrong rule was applied to the facts of the case or the policy guideline used in reaching its decision was misinterpreted.[152] The appellate panel would determine the correct method of resolving the issue, ensuring that cases involving similar facts and issues would not be decided differently.

The appellant would bear the burden of showing that his case warrants an appeal, and would submit a petition for review to a preliminary appellate review board that would determine whether the case meets either of the requirements for appellate review.[153] If the Respondent defaults, the case would not be eligible for appellate review. If the requirements for an appeal were met, a panel of five arbitrators would hear the appeal. Appellate review of proceedings that meet the appeal requirements would be mandatory. If the appellant fails to meet these requirements, then his petition would be denied and the appealing party would have ten days to file suit in a court of competent jurisdiction before the original panel decision goes into effect.

The appealing party would be required to file an intent-to-appeal notice within five days of the issuance of the panel's decision and would then have an additional fourteen days to file the actual appeal.[154] Upon receipt of the intent-to-appeal notice, implementation of the panel decision would be delayed until twenty-five days after the date the intent-to-appeal was mailed. If the appealing party fails to file the appeal within the allotted time period, the panel decision would be implemented immediately.

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151. This standard would appear to be somewhat more flexible than the KDRP standard in that it guarantees review for cases involving issues of split precedent. Until the KDRP process is tested, however, it remains unclear how it's "manifest injustice" standard for appeals will be interpreted and what types of cases will warrant an appeal under the manifest injustice standard. *See* Froomkin, *supra* note 8, at 56 (discussing problems created by incorrectly decided cases that have been continually cited as precedent); Kelly, *supra* note 11 (arguing that incorrect decisions and inconsistent treatment of cases with similar underlying facts have created a need for a UDRP appellate process).

152. Froomkin, *supra* note 8; Kelly, *supra* note 11.

153. The purpose behind the preliminary review board is to weed out cases that do not warrant appellate review. This feature of the model appellate process is designed to prevent the system from becoming bogged down with unwarranted appeals and help maintain the efficient dispute resolution the UDRP was created to provide. *See* Kelly, *supra* note 11.

154. Like the JAMS Optional Arbitration Appeal Procedure, the model UDRP appellate system gives the appellant fourteen days to file the appeal. The model system differs from the JAMS approach, however, in that JAMS does not require the appellant to file an intent-to-appeal notice. *See* JAMS Appellate Procedure, *supra* note 149, at § (B)(i).

Once the appeal is received, the panel decision would not be implemented while the preliminary appellate review board is considering the appeal.[155] Upon receipt of the appeal, the appellee would be notified that an appeal has been filed. If the appellee fails to respond, he would be in default and the appeals process would continue with the preliminary review board and the appeals board allowed to consider the appellee's default in making their decisions.[156] If the preliminary review board decided a case warranted an appellate hearing, the domain name would not be transferred until ten days after the appellate decision has been issued.[157]

The appeals board would be controlled directly by ICANN rather than by the individual service providers. This structure should promote the institutional validity of the process, and should prevent complaints that service providers assign panelists inclined to rule in favor of trademark holders.[158] ICANN would field a board of ten panelists that would be divided into two groups of five to hear appeals.[159] ICANN would attempt to reach an agreement with both parties to the appeal regarding which five mem-

155. *See* JAMS Appellate Procedure, *supra* note 149, at § (C) (noting that under the JAMS policy, "once an appeal has been timely filed, the Arbitration Award is no longer considered final for purposes of judicial enforcement, modification or vacating pursuant to the applicable JAMS Arbitration Rules.").

156. *See Rules*, supra note 22, at § 14. *See also* JAMS Appellate Procedure, *supra* note 149, at § (E) (detailing the consequences if one of the parties refuses to participate in the appeal procedure).

157. The time periods allotted for filing appeals was selected to provide adequate time for filing the appeal without excessively slowing down the overall UDRP process. Requiring an intent-to-appeal notice allows service providers to go forward with implementing panel decisions in cases where an appeal is not going to be filed without having to wait twenty-five days. At the end of the appellate process, the losing party has only ten days to file suit before the decision is implemented. At this point, both parties have had adequate time to prepare to file a lawsuit should they choose to do so. *See* Froomkin, *supra* note 8, at 64-65 (arguing that the UDRP does not allow Respondents sufficient time to prepare an adequate response to the complaint). *See also* UDRP, *supra* note 1, at § 4(k).

158. *See* Geist, *supra* note 8, at 3-9 (discussing potential bias among service providers and detailing the possibility that providers may appoint panelists more likely to find in favor of Complainants); Froomkin, *supra* note 8, at 57-58 (arguing that service providers may have a tendency to be biased in favor of Complainants to encourage future Complainants to use their service by creating a perception that they produce Complainant-friendly outcomes).

159. JAMS uses an appellate panel made up three members, or in special cases, only one member. Since UDRP disputes can initially be heard by three member panels, the suggested model provides for appeals to be heard by five panelists so as to provide additional perspectives on the case under review). JAMS Appellate Procedure, *supra* note 149, at § (A).

bers of the appeals board would hear the appeal.[160] If the parties are unable to come to an agreement on the makeup of the appellate board within seven days, ICANN would decide which five board members would preside.[161] The preliminary appellate review process would be handled by a separate group of nine arbitrators selected by ICANN, working in groups of three. The nineteen arbitrators participating in the appellate process would primarily be retired judges, academics, and practitioners, creating a staff of arbitrators at the appellate level with similar qualifications to those serving on the panels.[162]

Appeals would be reviewed by a mini-board of three panelists who would determine if an appeal meets the requirements for an appellate hearing. Funding for the appellate process would come primarily from fees for filing the appeal, coupled with a nominal increase in the cost of domain registration. Like UDRP proceedings, the appellate process would be entirely paper-based, with no in-person arguments from either party. The appeals board would essentially perform a de novo review of each case. Neither party would be permitted to submit additional facts that were not presented to the panel.[163] The board would not be required to give deference to the panel's interpretation of the facts, however, and could ask either party to provide any additional information deemed necessary for the fair resolution of the appeal.[164] Absent exceptional circumstances, the appeals board would have fourteen days to review the case.[165] Upon receipt of the board's decision, ICANN would have three days to forward the decision to

160. *See id.* (detailing the process for selecting the members of the appellate panel under the JAMS policy).

161. *See id.*

162. *See also* Froomkin, supra note 8, at 46 (arguing that service providers need to diversify their roster of panelists to exclude trademark lawyers and include people from a more diverse selection of backgrounds).

163. *See* JAMS Appellate Procedure, *supra* note 149, at § (B)(iii) (stating the rule for composition of the record on Appeal under the JAMS policy).

164. *See id.*

165. JAMS allows its appeals panel twenty-one days to reach a decision. Because JAMS tends to hear cases involving more complex issues than most UDRP disputes, the JAMS appeals panel may require more time to resolve appeals. Given that UDRP disputes involve a relatively narrow subject matter, fourteen days should be sufficient for the appeals board to reach a decision. *See* JAMS Appellate Procedure, *supra* note 149, at § (D). *See also* Kelly, *supra* note 11 (detailing Michael Froomkin's argument regarding the importance of maintaining the quick, cost effective resolution that the UDRP was designed to provide).

both parties involved in the dispute. Service of the decision would be considered effective five days after its deposit in the U.S. Mail.[166]

Decisions made by the appeals board would be binding precedent for future administrative hearings, although the preliminary review board's denial of an appeal request would not been seen as a comment on the merits of the issue. Decisions of panels on issues that have not been reviewed by the appeals board could be considered by other panels, but would not be binding.[167] Either party to a UDRP appellate proceeding would retain the right to file suit in a court of mutual jurisdiction while the appeal is pending. Once a decision has been made at the appellate level, the losing party would have ten days from the day the decision became effective to file suit before the domain name would be transferred.

The appellate system described in this model provides a mechanism for correcting errant decisions and harmonizing divergent bodies of precedent that would likely add an increased perception of fairness to the existing process.[168] Appellate review of panel decisions would ultimately produce decisions that are more consistent.[169] This result would not only add to the perceived fairness of the process, but would make judicial review of UDRP decisions easier. Courts would be able to examine panel decisions without having to wonder if another panel would have reached a different conclusion on the same issue. At the same time, the creation of a preliminary review board to decide what cases are worthy of an appeal would likely ensure that the UDRP system does not become bogged down with appeals, which would render it incapable of providing the efficient dispute resolution for which it was designed.[170]

IV. CONCLUSION

Despite the criticism it has received, the UDRP remains the best solution for resolving domain name ownership disputes in a fast, efficient, and inexpensive fashion. This does not mean, however, that criticisms of the policy are without merit. While the UDRP remains the best choice for this purpose, it is a system in need of improvement. Eliminating single person

166. *See* JAMS Appellate Procedure, *supra* note 149, at § (F) (detailing JAMS procedure for serving the appellate decision on the parties).

167. *See* Froomkin, *supra* note 8, at 56 (discussing the continued problems created by incorrectly decided cases that have been continually cited as precedent); Kelly, *supra* note 11 (arguing that incorrect decisions and inconsistent treatment of cases with similar underlying facts have created a need for a UDRP appellate process).

168. *See id.*

169. *See id.*

170. Kelly, *supra* note 11.

UDRP panels in favor of mandatory three-member panels for cases where the Respondent does not default and implementing an appellate process would go a long way towards solving many of the UDRP's problems. By making these changes, ICANN will significantly improve the perceived fairness of UDRP proceedings, while taking significant steps towards ensuring the long-term viability of the UDRP as the primary system for resolving domain name ownership disputes.

TRAFFIX DEVICES, INC. V. MARKETING DISPLAYS, INC.

By Kerry S. Taylor

It is a well-established tenet of trademark law that functional product features are not entitled to trade dress protection.[1] This principle can lead to unfortunate consequences for producers and consumers who have come to rely on a functional feature to identify the source of a product. The exclusion of functional features from trade dress protection, however, is based on sound policy rationale because patent law serves to protect useful innovations and it encourages copying of useful items for public use.[2]

In refining the rule for functionality, the Supreme Court in *TrafFix Devices, Inc. v. Marketing Displays, Inc.*[3] held that a feature is functional when it is essential to the use or purpose of the article or if it affects the cost or quality of the article.[4] Further, when the product feature was the subject of an expired utility patent, there is a strong evidentiary inference of functionality, and the patent owner bears the burden of showing that such a feature was not a useful part of the invention, but was instead arbitrary, incidental or ornamental.[5]

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1. Qualitex Co. v. Jacobson Prods. Co., 514 U.S. 159, 164 (1995); Two Pesos, Inc. v. Taco Cabana, Inc., 505 U.S. 763, 775 (1992). *See also* 15 U.S.C. §§ 1052(e), 1064(3) and 1091(c).

2. *See, e.g.*, J. THOMAS MCCARTHY, MCCARTHY ON TRADEMARKS AND UNFAIR COMPETITION § 7:63 (4th ed. 2001), Judith Beth Prowda, *The Trouble with Trade Dress Protection of Product Design*, 61 ALB. L. REV. 1309, 1323-30 (1998); Theodore H. Davis, *Copying in the Shadow of the Constitution: The Rational Limits of Trade Dress Protection*, 80 MINN. L. REV. 595, 596-609 (1996).

3. 121 S. Ct. 1255 (2001).

4. *Id.* at 1263. "Whether a utility patent has expired or there has been no utility patent at all, a product design which has a particular appearance may be functional because it is 'essential to the use or purpose of the article' or 'affects the cost or quality of the article.'" (citing *Inwood Labs., Inc. v. Ives Labs., Inc.*, 456 U.S. 844, 850 n.10 (1982)).

5. *Id.* at 1260. "Where the expired patent claimed the features in question, one who seeks to establish trade dress protection must carry the heavy burden of showing that the feature is not functional, for instance by showing that it is merely an ornamental, incidental, or arbitrary aspect of the device." *Id.* at 1262. "In a case where a manufacturer seeks to protect arbitrary, incidental, or ornamental aspects of features of a product found in the patent claims, such as arbitrary curves in the legs or an ornamental pattern painted on the springs, a different result might obtain."

The *TrafFix* decision represents the Supreme Court's latest refinement of the scope of trade dress protection, limiting trade dress protection by eliminating economic considerations in functionality determinations. This holding narrowly interprets *Qualitex Company v. Jacobson Products Company, Inc.*,[6] the previous Supreme Court decision on functionality. The *TrafFix* ruling decreases potential overlap of patent and trademark protection for the same subject matter. But by eliminating economic inquiries, the rule may exclude some nonfunctional product features from trade dress protection, particularly nonfunctional product features that were once the subject of patent protection.

I. BACKGROUND

A. Protection of Trade Dress

Trade dress developed under unfair competition as a protection for distinctive packaging and design of goods.[7] It protects consumers from confusion by ensuring that they can distinguish between differently packaged products, and can associate packaging or product design with a particular producer. Trade dress also benefits consumers by protecting a manufacturer's good will in its uniquely designed or packaged products, thereby encouraging producers to continue to produce high quality goods.

Trade dress protection has been available under federal law since 1946 under Section 43(a) of the Lanham Act.[8] Currently, the Lanham Act serves as the principle means of trademark and trade dress protection.[9] Under this Act, registration is available on the Supplemental Register[10] for "any trademark, symbol, label, package, configuration of goods . . . capa-

6. 514 U.S. 159 (1995).

7. MCCARTHY, *supra* note 2, at § 7.15.

8. 15 U.S.C. § 1125(a) (1994).

9. JEROME GILSON, 2 TRADEMARK PROTECTION & PRACTICE § 7.02[1], 7-12—7-17 (2001).

10. The United States Patent and Trademark Office (PTO) provides for registry of marks used in commerce under two categories: the Principal Register and the Supplemental Register. The Principal Register is available to marks used in commerce that are either inherently distinctive or are descriptive and have developed secondary meaning. Characteristics of goods that are not inherently distinctive and have not acquired secondary meaning are not registrable on the Principal Register, but can be registered on the Supplemental Register if they might in the future develop secondary meaning and thereby serve to distinguish the applicant's goods from those of others. *See generally* ROBERT P. MERGES ET AL., INTELLECTUAL PROPERTY IN THE NEW TECHNOLOGICAL AGE (2d ed. 2000).

ble of distinguishing the applicant's goods or services."[11] Further, trade dress can be registered on the Principal Register if the product dress identifies the applicant's goods and distinguishes the goods from those of others.[12]

Traditional trade dress law protects product packaging and labeling.[13] But over the past 20 years, courts have extended trade dress protection to the overall image of the product, which includes features such as size, shape, smell, color and texture.[14] The courts have also expanded the scope of trade dress to include product design features and product configurations as classes of trade dress.[15] This expansion results in trade dress protection that encompasses traditional product packaging such as the Coca-Cola bottle, and extends as far as to include the design of a restaurant.[16]

B. The Role of Functionality in Trade Dress

For decades, common law did not permit trademark protection for product features that were functional, despite the lack of a statutory basis for this position.[17] Courts excluded functional features from trademark protection for public policy reasons and to promote free competition by

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11. 15 U.S.C. § 1091(c) (1994).

12. *See, e.g.*, *Ex parte* Haig & Haig Ltd. 48 TMR 1031 (Comm'r 1958), and *In re* Duro-Test Corp. 53 TMR 105 (T.T.A.B. 1962).

13. Prowda, *supra* note 2, at 1315-18.

14. *See, e.g.*, Vaughan Mfg. Co. v. Brikam Int'l Inc., 814 F.2d 346 (7th Cir. 1987); LeSportsac, Inc. v. K-Mart Corp., 754 F.2d 71 (2d Cir. 1985); John H. Harland Co. v. Clarke Checks, Inc., 711 F.2d 966 (11th Cir. 1983); Warner Bros., Inc. v. Gay Toys, Inc., 658 F.2d 76 (2d Cir. 1981).

15. Bradley K. Groff, *Bare-Fisted Competition or Palming Off? Protection of Product Design as Trade Dress Under the Lanham Act*, AM. INTELL. PROP. L. ASS'N Q.J. (Winter 1995). Note, however, that not all commentators have supported this expansion of the definition of trade dress. *See, e.g.*, Glynn S. Lunney, Jr., *The Trade Dress Emperor's New Clothes: Why Trade Dress Does Not Belong on the Principal Register*, 51 HASTINGS L. J. 1131 (2000); Melissa R. Gleiberman, Note, *From Fast Cars to Fast Food: Overbroad Protection of Product Trade Dress Under Section 43(a) of the Lanham Act*, 45 STAN. L. REV. 2037 (1993).

16. *See, e.g.*, Marya Lenn Yee & Orrie Dinstein, *Artistic Style Is Given Trade Dress Protection*, NAT'L. L.J., Jan. 24, 1994, at S10; Two Pesos v. Taco Cabana., 505 U.S. 763 (1992). Note, however, that the Supreme Court, in *Wal-Mart Stores, Inc. v. Samara Bros., Inc.*, 529 U.S. 205 (2000), halted the expansion of trade dress protection by ruling that product design cannot be inherently distinctive, and, therefore, must attain secondary meaning in order to be entitled to trademark protection. *Id.* at 212. This ruling underscores the distinction between product packaging, which can be inherently distinctive, and product design, which cannot be inherently distinctive.

17. MCCARTHY, *supra* note 2, at § 7.63.

preventing the monopolization of functional product features.[18] In 1998, Congress codified the common law position by including functionality in §§ 7:84, 19:75, 20:21 and 20:56.1 of the Lanham Act as a ground for ex parte rejection, opposition, cancellation of registration, and defense for an incontestably registered mark.[19]

C. Separating Functional and Design Elements

Two rationales support excluding functional features from trade dress protection. First, in a competitive economy, patent law is the only source of exclusive rights for functional features. Second, competitors should be allowed to copy functional features to compete effectively.[20] The underlying public policy goal is to promote competition through trademark law by protecting a firm's reputation and preventing consumer confusion while encouraging innovation of new and useful products which will, after expiration of the patent term, enter the public domain and thereby be freely used, copied and improved.[21]

Unfortunately, in implementing these rationales to define functionality, courts have provided varied and inconsistent tests, particularly with regard to whether the existence of an expired utility patent is *per se* evidence of functionality.[22] The exact formulation of the functionality definition will determine whether or not a particular patented feature should also be entitled to trade dress protection, and, thus, address a fundamental question of what happens when patent law and trademark law overlap.[23]

D. Recent Supreme Court Treatment of Functional and Design Elements

In recent years, the Supreme Court has considered several issues defining the scope of trade dress protection. Two decisions addressed the role of functionality in trade dress. In *Bonito Boats, Inc. v. Thunder Craft*

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18. *See, e.g.*, *Two Pesos*, 505 U.S. at 769; Qualitex Co. v. Jacobsen Prods. Co., Inc., 514 U.S. 159, 165 (1995). *See also* MCCARTHY, *supra* note 2, at § 7.63 and Judith Beth Prowda, *supra* note 2, at 1324 n.62.

19. Pub. L. No. 105-330, 112 Stat. 3064 (Oct. 30, 1998).

20. MCCARTHY, *supra* note 2, at § 7.63; *Qualitex* 514 U.S. 159 at 165.

21. MCCARTHY, *supra* note 2, at § 7.64; Theodore H. Davis, *supra* note 2, at 507-609; Sylvania Elec. Prods., Inc. v. Dura Elec. Lamp Co., 247 F.2d 730 (3d Cir. 1957).

22. Prowda, *supra* note 2, at 1324; Michael S. Perez, *Reconciling the Patent Act and the Lanham Act: Should Product Configurations Be Entitled to Trade Dress Protection After the Expiration of a Utility or Design Patent?*, 4 TEX. INTELL. PROP. L.J. 383, 410-412 (1996).

23. WILLIAM E. LEVIN, TRADE DRESS PROTECTION § 25 (1996); MCCARTHY, *supra* note 2, at § 7.63; Prowda, *supra* note 2, at 318-325; Perez, *supra* note 22, at 397-399.

Boats, Inc.,[24] a boat manufacturer sought to enjoin a competitor from duplicating its unpatented boat hull design using a direct molding process. The manufacturer was attempting to apply a Florida statute prohibiting use of a direct molding process to duplicate unpatented boat hulls. The Supreme Court held that a state may regulate circumstances where designs are used to prevent consumer confusion,[25] however, a law that interferes with use of a utilitarian conception contravenes "the centerpiece of federal patent policy."[26] The Court noted that Congress has considered legislation for protecting industrial designs, but has refrained from altering the present system to provide such protection.[27] Thus, the Court held, except by congressional act, a state law cannot supercede the patent act and protect a utilitarian product.[28]

In *Qualitex Company v. Jacobson Products Company, Inc.*[29] plaintiff Qualitex registered its unique green-gold colored dry cleaning press pads as a trademark and sued the defendant, a competitor, for trademark infringement.[30] The Court held that a color could be the subject of a valid trademark. The Court stated that a design is functional if it is "essential to the use or purpose of the article or if it affects the cost or quality of the article."[31] The Court then looked to past jurisprudence and to the Restatement (Third) of Unfair Competition, stating that the "ultimate test of aesthetic functionality is whether the recognition of trademark rights would significantly hinder competition."[32] According to this reasoning, a design

24. 489 U.S. 141 (1989).
25. *Id.* at 154.
26. *Id.* at 157.
27. *Id.* at 167.
28. *Id.* at 168.
29. 514 U.S. 159 (1995).
30. *Id.* at 161.
31. *Id.* at 165 (citing *Inwood Labs, Inc. v. Ives Labs., Inc.*, 456 U.S. 844, 850 (1982)).
32. *Id.* at 170 (citing RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 17, cmt. c (1993)). In general, there are two categories of functionality under the common law: utilitarian functionality and aesthetic functionality. Although the definitions of these two categories of functionality vary, the basic definition of utilitarian functionality refers to product features that improve the purpose or performance of the goods. McCarthy, *supra* note 3, § 7:69. Aesthetic functionality generally applies when the appearance of product design or packaging has a significance that is not easily duplicated with substitute designs or packaging. MCCARTHY, *supra* note 2, at § 7:79. For the purposes of this paper, the term "functionality" is equivalent to utilitarian functionality, and references to aesthetic functionality will be specifically indicated. In *Qualitex*, the Court makes only one reference to aesthetic functionality, and the Court does not clarify the relation between the term "aesthetic functionality" and the term "functionality" which is used throughout the

is functional if the design's aesthetic value "lies in its ability to 'confe[r] a significant benefit that cannot practically be duplicated by the use of alternative designs.'"[33]

II. CASE SUMMARY

A. Facts

Marketing Displays, Inc. ("MDI") manufactured and sold stands for temporary road signs that used two springs to keep the signs upright in high winds.[34] MDI held two utility patents for a mechanism based on this "dual-spring design."[35] The dual-spring design of MDI's stands was visible near the base of the sign, and MDI claimed that this design was recognizable to buyers and users of the stands.[36] After the expiration of the utility patents, TrafFix Devices, Inc. ("TrafFix") copied MDI's dual-spring design and sold sign stands that looked like those of MDI.[37]

B. Procedural History

MDI brought suit against TrafFix, alleging trademark infringement, trade dress infringement and unfair competition.[38] TrafFix responded with unfair competition and antitrust counterclaims.[39]

The district court awarded MDI summary judgment, holding TrafFix liable for trademark infringement, but not for trade dress infringement or unfair competition, and finding MDI not liable for the antitrust claim.[40] In a two-part judgment, it held that "no reasonable trier of fact could determine that MDI had established secondary meaning in its alleged trade

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remainder of the decision. *Qualitex,* 514 U.S. at 170. This ambiguity between terms played an important role in the issues discussed in the *TrafFix* decision.

33. *Qualitex,* 514 U.S. at 170 (citing RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 17, cmt. c (1993)).

34. Brief for Respondent at 2, TrafFix Devices, Inc. v. Marketing Displays, Inc., 121 S. Ct. 1255 (2001) (No. 99-1571).

35. U.S. Patent Nos. 3,646,696 (issued March 7, 1972), 3,662,482 (issued May 16, 1972).

36. Brief for Respondent at 18, *TrafFix* (No. 99-1571).

37. Brief for Petitioner at 6, TrafFix Devices, Inc. v. Marketing Displays, Inc., 121 S. Ct. 1255 (2001) (No. 99-1571).

38. Marketing Displays, Inc. v. TrafFix Devices, Inc., 967 F. Supp. 953, 956 (E.D. Mich. 1997).

39. *Id.*

40. *Id.* at 965.

dress."[41] Second, it held the dual-spring design was a functional element of the sign stand, and trade dress protection could not be granted for a functional element regardless of whether secondary meaning had developed around that functional element.[42] To overcome the district court's holding of functionality, MDI bore the burden of demonstrating that the dual-spring design was nonfunctional, but MDI did not provide such evidence.[43]

On appeal, the Sixth Circuit upheld the trademark and antitrust holdings and reversed the trade dress holding.[44] It held that MDI had presented a genuine issue of material fact regarding the secondary meaning of the dual-spring design. The Court of Appeals further held that in order to deny trade dress protection on functionality grounds, the defendant must show that "[e]xclusive use of a feature must 'put competitors at a significant non-reputation-related disadvantage.'"[45] In so holding, the court stated that in order for a competitor to use the dual-spring design, the competitor must develop a noninfringing design such as a tri- or quad-spring design or a hidden dual-spring design.[46] The court did note, however, that appellate courts were split on whether the existence of a utility patent prevented the patentee from claiming trade dress protection.[47]

C. Supreme Court Decision

The Supreme Court reversed the Court of Appeals, holding that trade dress protection will not be granted to product features that are functional, and that a patent holder must overcome a "strong evidentiary inference of functionality based on the disclosure of the dual-spring design in . . . the expired patents."[48] Justice Kennedy, writing for the Court, reasoned that federal trade tress protection serves to prevent confusion of the origin of the product, and thus promotes competition.[49] Further, laws that aim to preserve a competitive economy do not necessarily discourage copying

41. Marketing Displays, Inc. v TrafFix Devices, Inc., 971 F. Supp. 262, 269 (E.D. Mich 1997). Note that this portion of the judgment was in response to MDI's motion to reconsider the initial judgment.

42. *Id.*

43. *Id.*

44. Marketing Displays, Inc. v TrafFix Devices, Inc., 200 F.3d 929 (6th Cir. 1999).

45. *Id.* at 938-39 (quoting *Qualitex Co. v. Jacobson Prods. Co.*, 514 U.S. 159, 165 (1995)).

46. *Id.* at 940.

47. *Id.* at 939.

48. TrafFix Devices, Inc. v. Marketing Displays, Inc. 121 S. Ct. 1255, 1260 (2001).

49. *Id.* at 1259.

goods and products.[50] He cited 15 U.S.C. § 1125(a)(3),[51] which indicates that a person seeking trade dress protection must prove that the feature to be protected is not functional.[52] Thus, trade dress protection is not available to prevent a functional element of a product from being copied.[53]

After establishing that trade dress protection is not available to functional features of a product, Justice Kennedy went through the analysis of how to determine the functionality of a product feature. Specifically, he stated that an expired utility patent is "strong evidence" of functionality.[54] A feature is considered functional until proven nonfunctional by demonstrating, for example, that the feature is an "ornamental, incidental, or arbitrary aspect of the device."[55]

Justice Kennedy then evaluated MDI's representations of its patented dual-spring design. First, he examined MDI's statements made during prior patent infringement litigation, where it argued that the alleged infringer's device had springs that were equivalent to the devices claimed in the patents held by MDI.[56] Further, the specification of the patents described the dual-spring design as an improvement over signs without springs that topple in strong winds[57] or single-spring signs that twist in the wind and thereby incur damage.[58] Similarly, during the course of patent prosecution, MDI described the dual-spring design as an improvement over single-spring signs. Justice Kennedy concluded that such characterizations of the dual-spring design demonstrated the functionality of the design.[59]

Justice Kennedy then examined the test for determining whether a product feature is functional. He indicated that the Court of Appeals' test for functionality was incorrect because it determined whether the particular product configuration is a competitive necessity.[60] Further, Justice

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50. *Id.* at 1260.

51. *TrafFix*, 121 S. Ct. at 1259.

52. The text of 15 U.S.C. § 1125(a)(3) (Supp. V 1994) states:

In a civil action for trade dress infringement under this chapter for trade dress not registered on the principal register, the person who asserts trade dress protection has the burden of proving that the matter sought to be protected is not functional.

53. *TrafFix*, 121 S. Ct. at 1260.

54. *Id.*

55. *Id.*

56. *Id.* (referring to the patent infringement litigation in *Sarkisian v. Winn-Proof Corp.*, 697 F.2d 1313 (1983)).

57. U.S. Patent No. 3,662,482, col. 1 (issued May 16, 1972).

58. U.S. Patent No. 3,646,696, col. 3 (issued March 7, 1972).

59. *TrafFix*, 121 S. Ct. at 1261.

60. *Id.*

Kennedy did not support the appellate court's position that the competitor should attempt other design possibilities.[61] He stated that such alternative designs are not required if the feature in question is functional.[62] A more appropriate test is that a product feature is functional when "it is essential to the use or purpose of the article or if it affects the cost or quality of the article."[63]

Justice Kennedy declared that when the feature was previously the subject of patent claims, the patent owner bears the responsibility of showing that it was not a useful part of the invention, but was instead "arbitrary, incidental or ornamental."[64] In determining the role of the claimed feature, inquiry can be made into the patent and its prosecution history.[65] A high standard of proof is required to insure that patent law, and not trademark law, provides manufacturers with rewards for innovations.[66] Thus, regardless of how recognizable a functional feature is to consumers, such a feature should not be the subject of trade dress protection.[67]

III. DISCUSSION

This analysis will explore the policy rationale used in evaluating the overlap between patent and trademark law and the history of Supreme Court rulings in cases involving such an overlap. The present test for addressing this overlap is the test for functionality of a product feature. The definition for functionality in the Court's *TrafFix* decision represents a narrow interpretation of the scope of trade dress protection provided by the functionality test in *Qualitex*. Although the *TrafFix* functionality test is not egregiously limiting, it will likely result in denial of trademark protection for some deserving product features.

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61. *Id.*
62. *Id.* at 1262.
63. *Id.* at 1261 (quoting Qualitex *Co. v. Jacobson Prods. Co., Inc.*, 514 U.S. 159, 165 (1995), which quoted *Inwood Labs., Inc. v. Ives Labs., Inc.*, 456 U.S. 844, 850, n.10 (1982)).
64. *Id.* at 1262.
65. *Id.*
66. *Id.*
67. *Id.* at 1263.

A. The Tension Between Patent and Trademark Law

1. *Fundamental Tension.*

Patent law seeks to encourage innovation.[68] As a reward for a significant innovation, a patentee is granted exclusionary rights for a limited time, after which the innovation passes into the public for copying and improvement.[69] Awarding a patentee exclusionary rights of unlimited duration, as is provided by trademark protection, would be incompatible with the underlying justification and Constitutional basis for patent law.

Trademark law, in contrast, seeks to protect the consumer and promote competition and quality goods in the marketplace.[70] The consumer does not benefit if a competitor copies a product, thereby misleading the consumer.[71] As a result, trademark protection is properly granted to a product mark for as long as the product is sold in commerce, which can extend trademark protection into perpetuity.[72]

When a useful innovation also provides the consumer with information as to the source of the product, a tension arises. Patent law advocates dedicating innovations to the public, while trademark law favors perpetual protection for innovations in order to prevent consumer confusion. The present system favors patent law over trademark law when an overlap between the two arises.[73]

There are several reasons for favoring patent law over trademark law. First, overextending subject matter entitled to trademark protection to include innovative but functional product features can impede competition by limiting the opportunities for others to make competing products.[74] As a result, the public would be deprived of the benefit of such technological

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68. U.S. CONST. art. 1, § 8, cl. 8. For a discussion of the interplay between the Constitution, patent law and trademark law. *See generally* Prowda, *supra* note 2; Gwendolyn Gill, *Through the Back Door: Attempts to Use Trade Dress to Protect Expired Patents*, 67 U. CIN. L. REV. 1269 (1999); Andrea Falk, *Harmonization of the Patent Act and Federal Trade Dress Law: A Critique of* Vornado Air Circulation Systems v. Duracraft Corp., 21 IOWA J. CORP. L. 827 (1996); David W. Opderbeck, *Form and Function: Protecting Trade Dress Rights in Product Configurations*, 20 SETON HALL LEGIS. J. 1 (1996); and Theodore H. Davis, *supra* note 2.

69. *See, e.g.*, DONALD S. CHISUM, CHISUM ON PATENTS § 1.01; Gwendolyn Gill, *supra* note 68, at 1273-76.

70. *See, e.g.*, MCCARTHY, *supra* note 2, §§ 2:2, 2:3; Prowda, *supra* note 2, at 318-25.

71. *See, e.g.*, MCCARTHY, *supra* note 2, §§ 2:4, 2:33.

72. *See, e.g.*, *Id.* at § 6:8; Gwendolyn Gill, *supra* note 68, at 1277-80.

73. *See, e.g.*, MCCARTHY, *supra* note 2, § 6:10; Prowda, *supra* note 2, at 318-28.

74. *See, e.g.*, Falk, *supra* note 68, at 829-35.

innovations. Second, the manufacturer of an innovative product can communicate to the consumer using a variety of distinguishing features such as product labeling or ornamental packaging, and is not limited to solely establishing product distinctiveness by virtue of the innovative feature.[75] Because public policy compels dedicating useful innovations to the public and manufacturers can use non-functional labeling or packaging to distinguish their products, patent protection is more appropriate than trademark protection for protecting functional product innovations.

2. Singer *and One-Hundred Years of Supreme Court Jurisprudence*

During the 19th century, the Supreme Court recognized the dominance of patent law over trademark law for protecting functional innovations. In *Singer Manufacturing Company v. June Manufacturing Company*, [76] a sewing machine manufacturer copied a competitor's product which contained features that had been the subject of an array of patents.[77] The Court declared that patented subject matter should pass into the public domain after the patent term expires.[78]

Throughout the 20th century, the Supreme Court consistently refused to extend the monopoly for subject matter that was either previously protected by patent law or deemed to be unpatentable for reasons such as lack of novelty. For example, in *Kellogg Company v. National Biscuit Company*, the Court refused to grant trademark protection for a pillow-shaped shredded wheat biscuit which had been protected by an expired patent because "upon expiration of the patents, the form . . . was dedicated to the public."[79] In *Scott Pater Company v. Marcalus Manufacturing Company*,[80] the Court considered whether a patentee could restrict the use of an expired patent. The Court ruled that a patentee cannot continue its monopoly by registering as a trademark "any particular descriptive matter appearing in the specification, drawings or claims of the expired patent,

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75. *See, e.g.*, Prowda, *supra* note 2, at 318-25.
76. 163 U.S. 169 (1896).
77. *Id.* at 170.
78. *Id.* at 185.

> It follows as a matter of course, that on the termination of the patent there passes to the public the right to make the machine in the form in which it was constructed during the patent . . . The public having the right, on the expiration of the patent, to make the patented article, and to use its generic name, to restrict this use . . . would be to admit the right, and at the same time destroy it.

79. Kellogg Co. v. Nat'l Biscuit Co., 305 U.S. 111, 119-120 (1938).
80. 326 U.S. 249 (1945).

whether or not such matter describes essential elements of the invention or claims."[81]

Later, in two accompanying cases, the Supreme Court considered whether a product could be protected under state unfair competition law after U.S. patent protection was denied.[82] In the first of these cases, *Sears Roebuck & Company v Stiffel Company*, the defendant copied a lamp design covered by an invalidated patent.[83] The Court stated that "the right to make the article—including the right to make it in precisely the shape it carried when patented—passes to the public."[84] Attempts by a state to protect such a product under unfair competition laws would "give protection of a kind that clashes with the objectives of the federal patent laws."[85] In the second case, *Compco Corporation v. Day-Brite Lighting*, the defendant copied an unpatented fluorescent light fixture that had cross-ribs which gave "both strength and attractiveness to the fixture."[86] The Court's opinion paralleled the opinion in *Sears*, stating that to forbid copying of the light fixture would go against the spirit of the Constitution and federal patent laws.[87]

While this line of cases indicated a possible *per se* rule for product features, that patentable subject matter did not qualify for trademark protection,[88] the Court limited this rule in *Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*[89] The Court acknowledged that protection under a state's unfair competition laws could, to some extent, apply to patentable subject matter since the broad scope of patentable subject matter could potentially include "'anything under the sun that is made by man.'"[90] The Court further asserted that the Lanham Act strikes a balance with patent law, and indicated that "nonfunctional aspects of a product which have been shown to identify source" could be protectable under the Lanham Act.[91] This decision redirected the balancing test between patent and trademark law from an inquiry into whether a product feature might be patentable subject

81. *Id.* at 256.

82. Sears, Roebuck & Co. v. Stiffel Co., 376 U.S. 225 (1964); Compco Corp. v. Day-Brite Lighting Inc., 376 U.S. 234 (1964).

83. *Sears, Roebuck & Co.*, 376 U.S. 225, 226 (1964).

84. *Id.* at 230.

85. *Id.* at 231.

86. *Id.* at 234.

87. *Id.* at 237.

88. *See generally Symposium, Product Simulation: A Right or a Wrong?*, 64 COLUM. L. REV. 1178 (1964).

89. 489 U.S. 141 (1989).

90. *Id.* at 154 (quoting *Diamond v. Charkrabarty*, 447 U.S. 303, 309 (1980)).

91. *Id.* at 166.

matter (the "Sears-Compco rule"[92]) to an inquiry into whether the product feature is functional.

B. The Functionality Test

1. *Traditional Meaning of Functionality*

Under *Bonito Boats*, the key to establishing trademark protection for a product feature was demonstrating a lack of functionality. As a traditional common law doctrine, functionality has developed a variety of meanings. In general, these meanings can be separated into two categories: physical functionality and economic functionality. Under physical functionality, the product feature is functional when it plays a role in the operation or cost of the product. Under economic functionality, a feature is functional when competitors would be put at a competitive disadvantage if they were excluded from using the product feature.

The First Restatement of Torts stated that a product feature is functional if it affects the product's "purpose, action or performance, or the facility or economy of processing, handling or using" the product.[93] The Restatement, Third, of Unfair Competition defines functional as a property that "affords benefits in the manufacturing, marketing, or use of the goods or services with which the design is used . . . that are important to effective competition by others and that are not practically available through the use of alternative designs."[94] Professor J. Thomas McCarthy identifies two basic rationales supporting rules for functionality: (1) accommodating patent law as the regime for protecting utilitarian features; and (2) preserving free and effective competition by ensuring that competitors can copy necessary features.[95] The Circuit courts have been split between a physical, patent-like functionality definition and an economic competition functionality definition.[96] One circuit attempted to construct a rule that considers both physical and economic utility by looking for a "significant inventive aspect" to the feature.[97] This definition, however, was not widely ac-

92. 1 J. THOMAS MCCARTHY, TRADEMARKS AND UNFAIR COMPETITION § 7:24 (1st ed. 1973).

93. RESTATEMENT (FIRST) OF TORTS § 742 (1924). No equivalent section appears in the Second Restatement of Torts, as unfair competition law was not included in the Second Restatement.

94. RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 17 (1993).

95. MCCARTHY, *supra* note 2, at § 7:68.

96. For a thorough survey of the positions taken in the Circuits, see generally STEPHEN F. MOHR & GLENN MITCHELL, FUNCTIONALITY OF TRADE DRESS: A REVIEW AND ANALYSIS OF U.S. CASE LAW (2d ed. 1994).

97. Vornado Air Circulation Sys. Inc. v. Duracraft Corp., 58 F.3d 1498, 1510 (10th Cir. 1995). *Vornado* rejected the *per se* rule of a patent representing functionality, and

cepted.[98] The Patent and Trademark Office ("PTO") has followed a line of cases from the Court of Customs and Patent Appeals, in which the key inquiry for functionality by the PTO rests on whether the design is inherently superior to other available designs.[99]

In applying these definitions, a product feature is more likely to be found functional if the physical definition is used rather than the economic definition. For example, a large number of product features can be important for the operation or cost of the product, and thereby considered functional under the physical functionality test. But under the economic functionality test, even if a product feature is patented and plays a role in the operation or cost of the product, it may not be functional if there are economic alternatives to the feature.

2. *Evolution of the Supreme Court's Definition*

In *TrafFix*, Justice Kennedy outlined the development of the Supreme Court's definition of functionality under two previous decisions. In the first case, *Inwood Laboratories, Inc. v Ives Laboratories, Inc.*, the color of medicinal pills were found to be functional because they helped patients differentiate their medicines. The Supreme Court stated that "[i]n general terms, a product feature is functional if it is essential to the use or purpose of the article or if it affects the cost or quality of the article."[100] Thus, the *Inwood* definition for functionality falls into the category of physical functionality. In the second case, *Qualitex Company v. Jacobson Products Company, Inc.*,[101] the Supreme Court moved toward an economic definition of functionality by holding that the particular color of a dry cleaning press pad is not functional. The Court expounded on the rule in *Inwood*, stating that a product feature is functional "if exclusive use of the feature

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instead held that a "significant inventive aspect" was a configuration that "without it the invention could not fairly be said to be the same invention . . . even if the configuration is nonfunctional."

98. *See* MCCARTHY, *supra* note 2, at § 7:68 and citations therein.

99. *In re* Morton-Norwich Products, Inc., 671 F.2d 1332 (C.C.P.A. 1982); *In re* Deister Concentrator Co., 289 F.2d 496 (C.C.P.A. 1961). In *Morton-Norwich*, the CCPA provided four factors to consider in determining whether a feature is functional: (1) the existence of a utility patent disclosing utility of the feature; (2) advertising touting the utilitarian advantages of the feature; (3) the existence of alternative designs; and (4) design result from a simple method of manufacture. *Morton -Norwich Products, Inc.*, 671 F.2d at 1340. Of these factors, the most important is the third consideration because "the effect on competition 'is really the crux of the matter.'" *Id.* at 1341 (quoting HARRY D. NIMS, UNFAIR COMPETITION AND TRADE-MARKS (4th ed. 1947)).

100. Inwood Labs., Inc. v. Ives Labs., Inc., 456 U.S. 844, 851 n.10 (1982).

101. Qualitex Co. v. Jacobson Prods. Co., Inc., 514 U.S. 159 (1995).

would put competitors at a significant nonreputation-related disadvantage."[102]

In *TrafFix*, the plaintiff relied on the *Qualitex* definition of functionality, arguing that many economic equivalents of the dual-spring design were available as demonstrated by the products made by other manufacturers, and, therefore, exclusive use of their particular configuration would not put competitors at a significant disadvantage.[103] Justice Kennedy, however, rejected application of the *Qualitex* rule to functionality in all cases, limiting it to cases concerning aesthetic functionality, such as the function of the color of a laundry press pad.[104] In cases of utilitarian functionality, Justice Kennedy declared that the rule in *Inwood* should be applied.[105]

Thus, the rule as recited in *Inwood* represents the test for utilitarian functionality. But Justice Kennedy did not go as far as to equate this rule with a *per se* rule that patented subject matter is functional. He stated that a patent creates a "strong evidentiary inference of functionality" which a patentee must overcome.[106] This inference can be overcome, for example, by a demonstration that the product features are arbitrary, incidental or ornamental, despite being present in patent claims.[107]

3. *Test case: Cigarette Lighter*

A recent case brought before the Trademark Trial and Appeal Board ("TTAB") is helpful in evaluating the functionality rule set forth in *TrafFix*.[108] In *In re Zippo*, the patentee was seeking trade dress registration for a lighter design that, at one point, had been the subject of a patent.[109] In a 1963 court ruling, the feature at issue was found to be functional because it made the lighters cheaper and easier to manufacture.[110] In subsequent years, many different lighter designs were developed which competed ef-

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102. *Id.* at 165.

103. Brief for Respondent at 26, TrafFix Devices, Inc. v. Marketing Displays, Inc., 121 S. Ct. 1255 (2001) (No. 99-1571).

104. TrafFix Devices, Inc. v. Marketing Displays, Inc. 121 S. Ct. 1255, 1262 (2001). For an explanation of aesthetic functionality, see *supra* at note 32.

105. *TrafFix Devices, Inc.*, 121 S. Ct. at 1262. For an explanation of utilitarian functionality, see *supra* at note 32.

106. *Id.* at 1260.

107. *Id.* at 1262.

108. *In re* Zippo Mfg., Co., 50 USPQ2d 1852 (Trademark Tr. & App. Bd. 1999).

109. *Id.* at 1852.

110. Zippo Mfg., Co. v. Rogers Imports, Inc. 216 F.Supp. 670 (SDNY 1963). The feature at issue was the shape of the lighter, specifically its rounded corners, beveled edges and a curved top. *Id.* at 672.

fectively with Zippo's design.[111] The TTAB ruled that, in view of the development of different designs subsequent to the 1963 court ruling, granting registration would not hinder competition, and, therefore, that Zippo was entitled to registration.[112]

Under the ruling in *TrafFix*, however, it is unclear whether the TTAB should have granted Zippo registration of the lighter design. The rounded shape of Zippo's lighter was probably never essential to the use or purpose of the lighter, but it did previously affect the cost of the lighter. Even though the shape presently no longer affects the cost of the lighter, the *TrafFix* rule requires that when any product feature has been patented, an applicant must overcome an inference that the feature is functional. The only apparent guidance from *TrafFix* with regard to overcoming this inference is to present evidence that the feature is "arbitrary, incidental or ornamental." Here, the shape is not arbitrary or incidental since it originally had a functional purpose.[113] The applicant may be able to demonstrate that the shape is ornamental. However, the shape may also have been ornamental in earlier years when it was still functional. Consequently, to overcome the presumption of functionality, it will not suffice to show that the feature is ornamental. An applicant must show that the feature is *solely* ornamental. But showing that a product feature is solely ornamental requires demonstrating that the feature is ornament and not functional, which returns the inquiry to the original question of functionality. Thus, it is uncertain that Zippo could overcome the strong evidentiary inference of functionality of the lighter design that it would face under a post-*TrafFix* examination.

Whether the denial of trademark registration in this case is the proper outcome depends on the degree to which patent law and trademark law should overlap. For those who would create a *per se* rule of exclusivity between patent law and trademark law, denial of trademark registration is proper, regardless of whether or not the patented subject matter had later become obsolete. For Justice Kennedy, "[t]he Lanham Act does not exist to reward manufacturers for their innovation in creating a particular de-

111. The applicant presented thirty alternative lighter designs that had been developed. *Id.* at 1853.

112. *Id.* at 1855.

113. Both arbitrary and incidental imply that there was no particular reason for originally using a specific product feature. The Zippo lighter design did originally have a reason for its use. But this reason is no longer relevant. However, the inquiry into whether a product feature is arbitrary or incidental can produce different results if the inquiry is not directed to the original reason for the product feature, but instead to the present reason for using the product feature.

vice; that is the purpose of the patent law."[114] Although this quotation is not dispositive, Justice Kennedy's decision in *TrafFix* does not provide a policy basis for why the public would wish to provide trademark protection in instances such as the Zippo lighter, where the patented subject matter has become obsolete.

Under the reasoning of the Restatement, Third, of Unfair Competition:

> The freedom to copy goods . . . is fundamental to the operation of a competitive economy. . . The rule excluding functional designs from the subject matter of trademark law is an attempt to identify situations in which the public and private interest in avoiding confusion is outweighed by the anticompetitive consequences of trademark protection.[115]

With thirty alternative lighter designs available in the marketplace, there does not seem to be an anticompetitive consequence of trademark protection. The number of alternatives also suggests that the public will not suffer if trademark protection removes this design from the public realm. Justice Kennedy made it clear in *TrafFix*, however, that the availability of other designs is not relevant to the test for functionality.[116] But under the facts of *Zippo*, where the functional feature had lost its useful properties, the public policy rationale supporting the functionality bar from trademark protection does not clearly explain why the physical functionality rule, and not an economic functionality rule, will arrive at the proper result.[117]

In view of public policy concerns, Professor J. Thomas McCarthy suggests that a court should strike a balance between a physical functionality test and an economic functionality test.[118] While it is clear from Justice

114. TrafFix Devices, Inc. v. Marketing Displays, Inc., 121 S. Ct. 1255, 1262 (2001).

115. RESTATEMENT (THIRD) UNFAIR COMPETITION § 17 cmt. a (1993).

116. *TrafFix*, 121 S. Ct. at 1262.

117. This rationale, as discussed above, *supra* note 115, states that functional features of a product should not be entitled to trademark protection because competitors should not be prevented from using something that would influence the quality of the product. However, when a product feature becomes obsolete, any copying of this feature is more likely to be with the intent to palm off a copy of the original rather than to take advantage of an obsolete feature.

118. MCCARTHY, *supra* note 2, at § 7:68. Note, however, that aside from stating that both tests should be considered by courts, no specific guidance is provided for how the two tests could be balanced. For example, in *TrafFix*, the district court emphasized the physical functionality test (Marketing Displays, Inc. v TrafFix Devices, Inc., 971 F.Supp. 262, 269 (E.D. Mich 1997)) while the circuit court emphasized the economic functionality test (Marketing Displays, Inc. v TrafFix Devices, Inc., 200 F.3d 929, 939 (6th Cir. 1999)). Clearly, emphasis on one test or the other can often lead to opposite conclusions.

Kennedy's opinion that the *Inwood* physical functionality rule is the proper rule for functionality, there may be occasions when an economic functionality test can still be applied. According to *TrafFix*, the existence of a patent claiming a product feature establishes a strong evidentiary inference of functionality for the manufacturer to overcome. Thus, the existence of a patent for a product feature creates an inference that the feature is "essential to the use of purpose of the article" or "affects the cost or quality of the article."[119]

It may not be possible to present economic evidence to demonstrate that a product feature is no longer essential to the use or purpose of the article, but it is possible to present economic evidence to demonstrate that a product feature no longer affects the cost or quality of the article. In the case of the Zippo lighter, the presence of a large number of alternative designs demonstrates that the previously patented feature, the lighter shape, no longer affects the cost or quality of the device. Thus, at least in the narrow instance of a patented feature that was functional by virtue of its effect on the cost of a product, economic evidence such as the presence of alternative designs should be capable of overcoming an inference of functionality.

This proposed refinement of the rule in *TrafFix* is not so broad that it would uproot the *TrafFix* decision and revert to a broad interpretation of *Qualitex*. For example, the holding in *TrafFix* would remain the same because the presence of alternative designs is not sufficient to overcome the inference that MDI's dual-spring design was essential to the use of purpose of the article. Nevertheless, the Zippo lighter example demonstrates that under some circumstances, it would be appropriate to permit economic evidence, such as the presence of alternative designs, to overcome an inference of functionality. As the *TrafFix* test for functionality is applied in the courts, examples such as *In re Zippo* will highlight the somewhat restrictive nature of the *TrafFix* test and identify instances where economic considerations should be reintroduced into determinations of functionality.

IV. CONCLUSION

Product features that were at one time subject to patent protection will normally have useful properties. Such product features are properly excluded from trade dress protection to avoid excessive overlap with patent law, and to prevent unreasonable limitations on competitors copying the

119. Inwood Labs., Inc. v. Ives Labs., Inc., 456 U.S. 844, 850 (1982).

patented product features. However, there will be instances when a product feature that was protected by a patent no longer serves a functional purpose.

The Supreme Court in *TrafFix* rightly avoided a *per se* rule that would prohibit trade dress protection for any product feature once covered by a patent. In its effort to limit the extent of trade dress protection, however, the Court supported a definition for functionality that may exclude some product features that deserve trade dress protection. Moreover, by creating a strong inference of functionality for product features that were subject to patent protection, nonfunctional patented product features are unlikely to enjoy trade dress protection.

ADDITIONAL DEVELOPMENTS—TRADEMARK

AMERICA ONLINE, INC. V. AT & T CORPORATION

243 F.3d 812 (Fed. Cir. 2001)

The key issue in this case was whether a certificate of registration from the United States Patent and Trademark Office ("PTO") indicates that a descriptive mark has secondary meaning. The Federal Circuit ruled that a PTO certificate was not entitled to deference, but that it served as powerful evidence that the mark was not generic in the eyes of the public and, if the mark was descriptive, that there was secondary meaning.

American Online, Inc. ("AOL") brought suit against AT & T Corp. ("AT&T"), alleging infringement of three trademarks in connection with its Internet service—"Buddy List," "You Have Mail," and "IM." Since 1997, AOL had used and extensively promoted "Buddy List" and "IM" to describe features of its Internet real-time communication ("chat") service. Since 1992, AOL had used the phrase "You Have Mail" to notify its subscribers that they had received new e-mail. AOL also obtained a certificate of registration with respect to "Buddy List" from the PTO.

The dispute centered on whether the mark "Buddy List" was generic. AOL claimed that the certificate of registration was *prima facie* evidence that the mark was at least descriptive with secondary meaning. AT&T, on the other hand, claimed that this was not sufficient proof that the mark was generic, and that there was therefore no infringement. The district court found that "the only reasonable conclusion which could be drawn from the evidence points to generic usage" and entered summary judgment in favor of AT&T with respect to each mark, concluding that the alleged marks were generic and AOL could not enforce them as trademarks.

In a split decision, the Federal Circuit affirmed the district court's ruling with regard to the terms "IM" and "You Have Mail," but vacated the district court's grant of summary judgment with respect to the term "Buddy List." The court rejected AOL's argument that the certificate of registration for "Buddy List" should be accorded deference under *Chevron v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). The court reasoned that *Chevron* only instructed a court to defer to the reasonable interpretations of expert agencies to fill the gaps in the statutes they administer when the statutory language is silent or ambiguous with respect to the question at issue, but did not direct a court to defer to an adjudication of the PTO. The court noted that Congress expressly vested the power to "determine the right to registration" in federal courts and made clear that the PTO's decisions regarding registrations fall under the supervision of federal courts. 15 U.S.C. § 1119. Moreover, the court noted that Congress plainly stated that a certificate of registration, while it must be received into evidence, only serves as "prima facie evidence of the validity of the registered mark." 15 U.S.C. §§ 1057(b), 1115(a).

Although not entitled to deference, the court found that a certificate of registration from the PTO constituted powerful evidence that the mark was not generic in the eyes of the relevant public, and that the mark was not merely descriptive, but also suggestive of a secondary meaning. Accordingly, the court found that the prima facie evidence provided by the certificate in the instant case was sufficient to establish a question of material fact which could not be resolved on summary judgment.

CHATAM INTERNATIONAL, INC. V. BODUM, INC.

157 F. Supp. 2d 549 (E.D. Penn. 2001)

In this case, the Eastern District Court of Pennsylvania decided how to resolve claims of trademark infringement, trademark dilution, and the violation of the Anticybersquatting Consumer Protection Act ("ACPA"), 15 U.S.C. § 1125, between two legitimate owners of an identical mark, where one party uses the mark in the traditional sense and the other uses it as a domain name to sell the same product. The court granted the defendant's motion for summary judgment on all claims and dismissed this action.

Plaintiff had used the trademark "Chambord" for fruit, preserves, chocolates, and cakes since October 31, 1975, and registered the mark "Chambord Liqueur Royale" for liquer on February 8, 1977. The trademark certificate for "Chambord Liqueur Royale" states that it "expressly asserted no claim" to the individual word "Chambord." However, in 1984, it registered the mark "Chambord" for liqueur and for milk chocolate and, in 1986 and 1988, for fruit preserves and cake. Defendant registered the mark "Cafetiere Chambord" for non-electric coffee makers on May 17, 1983, noting that commercial use had first occurred on September 8, 1980. In a previous consent decree arising out of a dispute between the two parties, the defendant was prohibited from using the mark "Chambord" for the sale of coffee, but was granted the right to continue to use the mark in connection with its sales of coffee makers. In 1996, the defendant's affiliate registered the domain name www.chambord.com, and used the name for a website that advertised defendant's coffee and tea markers. Plaintiff brought suit against the defendant, alleging violation of the ACPA, trademark infringement, and trademark dilution.

The court held that the defendant did not register the domain name in bad faith. The defendant's act fit into the ACPA's safe harbor provision, which states that "[b]ad faith intent . . . shall not be found in any case in which the court determines that the [registrant] believed and had reasonable grounds to believe that the use of the domain name was a fair use or otherwise lawful." 15 U.S.C. § 1125 (d)(1)(B)(ii). The defendant reasonably believed that its use was lawful because it was limited to coffee and tea makers, and was thus consistent with the consent decree. The court noted that "the Act leaves open the present combination of circumstances—in which both parties can invoke legitimate grounds for the registration of the same domain name for their respective products."

The court focused on the initial interest confusion doctrine in deciding the trademark infringement claim. Because the parties were not competitors, and the goods and services were dissimilar, the court decided that the plaintiff would not be harmed by any initial interest confusion. The court found that "a consumer attempting to access an upscale liqueur product is unlikely to be dissuaded, or unnerved, by the sight of coffee markers and other housewares, having first brought up the coffee maker's screen." Thus, there was no likelihood of confusion that would make the defendant liable for trademark infringement.

With respect to the dilution claim, the court focused on one of the statutory elements of the Federal Trademark Dilution Act ("FTDA"), which requires that the defendant's use of the mark occur after the mark becomes famous. The plaintiff claimed that the registration and use of the domain name www.chambord.com constituted a new and different use that arose after plaintiff's mark purportedly became famous. The court disagreed, however, noting that the Internet was merely a new avenue of communication, not a new commercial use. Because plaintiff's mark "Chambord" did not become famous until after defendant's first use of the mark, plaintiff could not prevail in its dilution action.

COOPER INDUS., INC. V. LEATHERMAN TOOL GROUP, INC.

532 U.S. 424 (2001)

The Supreme Court ruled on the standard of review applied to a district court's holding in determining the constitutionality of punitive damages award.

Leatherman Tool Group, Inc. developed a multi-function pocket tool that improved on the "Swiss army knife" design. Leatherman's tool, the Pocket Survival Tool ("PST") enjoyed significant market success. In 1995, Cooper Industries Inc. decided to develop a multifunction tool that would compete with the PST. Cooper's tool, the ToolZall, was substantially similar to the PST. Cooper prepared promotional material for the ToolZall to present at a hardware show in 1996. Cooper did not yet have a prototype of the ToolZall, and instead created a prototype by making modifications to a Leatherman PST. Cooper also prepared advertisements by retouching photographs of the PST. Leatherman filed suit alleging trade-dress infringement, unfair competition and false advertising. The district court issued a preliminary injunction to prohibit Cooper from marketing the ToolZall. At trial, a jury found that despite trade-dress infringement, Leatherman incurred no damages from this alleged wrong. The jury held Cooper guilty of false advertising and unfair competition, and awarded $50,000 in compensatory damages. The jury then awarded Leatherman $4.5 million in punitive damages based on its determination that Cooper had acted with outrageous indifference to Leatherman's rights. The Ninth Circuit set aside the district court's preliminary injunction, holding that the PST was not protectable under trademark law because the copied features were functional. With regard to punitive damages, the Ninth Circuit held that the district court did not abuse its discretion in finding that Cooper's due process rights were not violated.

Cooper appealed. The Supreme Court vacated the judgment, holding that courts of appeal should apply a de novo standard when reviewing district courts' determination of the constitutionality of punitive damage awards. The Court reasoned that punitive damages are private fines levied by juries to punish reprehensible conduct, and the role of the trial judge is to determine whether the verdict is within the confines of state law. If no constitutional issue is raised, the appellate court should review the trial court under the abuse-of-discretion standard. Nevertheless, a defendant's Constitutional rights are violated when a punishment is grossly disproportionate to the gravity of the defendant's offenses. The Fourteenth Amendment makes the Eighth Amendment's prohibition against excessive punishments applicable to the states. The Court held that gross excessiveness should be subject to de novo review for three reasons: (1) it is a fluid concept that requires a context-specific assessment; (2) independent review is necessary to control and clarify legal principles; and (3) de novo review stabilizes the law.

The Court further reasoned that because punitive damages are not determined by a jury, courts should evaluate them in view of the three criteria established in *BMW of North America, Inc. v. Gore*, 517 U.S. 559 (1996). These three criteria are: (1) the reprehensibility of defendant's conduct, (2) the disparity between harm suffered and punitive damages, and (3) the difference between punitive damages awarded and the civil penalties of comparable cases. The Court noted that only the first *Gore* criterion has an element of factual determination; the second and third criteria are appropriate subjects of appellate review.

GUCCI AMERICA, INC. V. HALL & ASSOCIATES

135 F. Supp. 2d 409 (S.D.N.Y. 2001)

The United States District Court for the Southern District of New York ruled on the issue of whether Internet Service Providers ("ISPs") can be held liable for trademark infringement arising out of information posted on their website by a third party user of the Internet service. The court held that neither the First Amendment nor the Communication Decency Act of 1996 barred the plaintiff's action.

Defendant Mindspring Enterprises, Inc. ("Mindspring") provided web page hosting services to codefendant Hall & Associates and Denise Hall ("Hall"), which allegedly used the website to advertise jewelry bearing (and infringing) the Gucci trademark. Mindspring was aware of Hall's infringement, but failed to remove the infringing website. Gucci America, Inc. sued Mindspring for direct and contributory trademark infringement. Mindspring moved to dismiss the claims on two grounds: (1) that section 230 of the Communication Decency Act of 1996 immunized Mindspring from liability for information posted on Hall's website; and (2) that the plaintiff's theory of trademark infringement was barred by the First Amendment.

In denying Mindspring's motion to dismiss, the court rejected Mindspring's argument that it was immune from liability because section 230(c)(1) states that "[n]o provider or user of an interactive computer service shall be treated as the publisher or speaker of any information provided by another information content provider." The court held that section 230(e)(2) of the statute unambiguously constrained the court to construe the section in a manner that would neither "limit [n]or expand any law pertaining to intellectual property." Thus, the plain language of statute precluded Mindspring's claim of immunity. The court distinguished the present case from previous cases that successfully invoked section 230(c)(1) as a defense against defamation and other common-law tort claims, because none of the prior cases involved intellectual property rights.

The court also rejected Mindspring's First Amendment argument that accepting Gucci's claims would subject Mindspring to "strict liability" if it did not summarily restrict online speech, thereby creating a "trademark plaintiff's veto." The court held that the First Amendment did not bar Gucci's claims of trademark infringement, because the challenged speech was "allegedly infringing commercial speech used to identify the source of a product." Furthermore, the Lanham Act's "innocent infringer defense" in 15 U.S.C. §1142(2), which required a trademark plaintiff show "actual malice" to recover damages, and the requirement that Gucci demonstrate "knowledge" under the contributory infringement doctrine, adequately protected the constitutional rights of parties like Mindspring.

TCPIP HOLDING CO. V. HARR COMMUNICATION INC.

244 F.3d 88 (2d Cir. 2001)

The Second Circuit Court of Appeals ruled on the issue of whether descriptive marks were protected under the Federal Trademark Dilution Act ("FTDA"). Only marks that are both famous and inherently distinctive are protected by the FTDA; descriptive marks which have acquired secondary meaning are not entitled to protection because they are not inherently distinctive.

TCPIP Holding Company, Inc. ("TCPIP") operates a chain of stores selling children's clothes and accessories under the registered trademark "The Children's Place" in the United States. The more than 200 chain stores enjoy annual revenues of almost $300 million and have become somewhat famous in eastern states. In the fall of 1998, defendant developed the idea of creating a webpage which would provide information and links about a broad range of child-related products and services. The defendant subsequently registered the domain name www.thechildrensplace.com, and sixty-six other domain names containing variations of the words "children" and "place." The plaintiff brought trademark dilution and infringement claims against the defendant, and filed a motion for preliminary injunction. The district court found that defendant's domain names were likely to infringe and dilute plaintiff's trademark, and preliminarily enjoined defendant from using all sixty-seven domain names.

On appeal, the Second Circuit performed a detailed statutory analysis, concluding that the Act had a dual requirement of famousness and inherent distinctiveness. It vacated the injunction based on the FTDA dilution claim. The court held that "The Children's Place" designating stores selling children's merchandise, was highly descriptive. Such descriptive marks, "which possessed no distinctive quality, or at best a minimal degree, do not qualify for the Act's protection." The court reasoned the requirement that the mark be significantly distinctive was consistent with the statutory language and policies rooted in trademark law that has always disfavored descriptive marks. Furthermore, because the FTDA granted the trademark owners a greater scope of exclusivity than traditional trademark law, it mandated that the Act accord "its special, broad protection only to marks that have significant degree of distinctiveness." The court further held that even assuming that plaintiff's mark has acquired secondary meaning, it would still not qualify for dilution, because it was not "inherently distinctive." As to whether plaintiff's mark was "famous," the Second Circuit interpreted the FTDA as conferring protection on marks "only if they carried a substantial degree of fame," and found that the plaintiff failed to establish such fame. The court held that plaintiff's mark failed to satisfy the dual requirement of the FTDA, and did not qualify for the Act's protection.

The court sustained the injunction for at least nine of the domain names based on the trademark infringement claim. The court reasoned that the domain names "so closely resemble the plaintiff's mark as to give rise to a high likelihood of confusion." The court instructed the district court on remand to review all the other domain names with regard to the trademark infringement issue. Finally, the court rejected defendant's argument that its actions constituted fair use. It held that the fair use provision only applied where the name was used descriptively "other than as a mark." The defendant's use of the domain name as the "address, or name, of its website" was not a descriptive use.

BERNIER V. MERRILL AIR ENGINEERS

By C. Rachal Pugh

Confidential proprietary information can afford tremendous competitive advantages to businesses.[1] As Sir Francis Bacon stated in 1597, "knowledge itself is power."[2] Courts recognize the value of confidential proprietary information and frequently prevent its disclosure.[3] Importantly, they often protect confidential proprietary information even when it does not rise to the level of a trade secret.[4]

Courts rely on a variety of rationales to protect information that does not qualify for trade secret protection (such as breach of fiduciary duty, unfair competition, unjust enrichment, and conspiracy).[5] The judicial enforcement of contractual nondisclosure agreements ("NDAs") provides an alternative approach.[6] This Note will argue that NDAs are preferable to the other methods listed above because they allow parties to define confidential information, thereby providing certainty in an otherwise murky and fact-specific area of the law.[7] The appellate court in *Bernier v. Merrill Air*

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1. Robert Unikel, *Bridging the "Trade Secret" Gap: Protecting "Confidential Information" Not Rising to the Level of Trade Secrets*, 29 LOY. U. CHI. L.J. 841, 841 (1998).

2. FRANCIS BACON, MEDITATIONES SACRAE (1597), REPRINTED IN XIV THE WORKS OF FRANCIS BACON 95 (James Spedding et al. eds., Scholarly Press 1969). Unikel, *supra* note 1, at 841.

3. Unikel, *supra* note 1, at 843.

4. *Id.*

5. *Id.* at 858-66.

6. *See* Robert G. Bone, *A New Look at Trade Secret Law: Doctrine in Search of Justification*, 86 CAL. L. REV. 241, 246 (1998).

7. *See* Robert T. Neufeld, Note, *Mission Impossible: New York Cannot Face the Future Without a Trade Secret Act*, 7 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 883, 918 (1997) ("Reliance on the Restatement and common law in New York has created ambiguous trade secret law, leaving trade secret owners uncertain of the protection available."); Miles J. Feldman, Comment, *Toward a Clearer Standard of Protectable Information: Trade Secrets and the Employment Relationship*, 9 HIGH TECH. L.J. 151, 170-71 (1994) (highlighting uncertainty of trade secret law by describing different outcomes based on similar fact patterns); Linda B. Samuels & Bryan K. Johnson, *The Uniform Trade Secrets Act: The States' Response*, 24 CREIGHTON L. REV. 49, 50-52 (1990) (noting that trade secret protection varies widely from state to state); Stephen J. Davidson & Robert L. DeMay, *Application of Trade Secret Law to New Technology - Unwinding the Tangled Web*, 12 WM. MITCHELL L. REV. 579, 600 (1986) (describing how this area of law is "clouded").

Engineers[8] adopted this approach, holding a former employee liable for breaching an NDA that protected "confidential or secret" information, despite the fact that the information at issue did not qualify for trade secret protection.[9] Before turning to the details of the *Bernier* decision, however, it is important to review the history and doctrine of trade secret law.

I. LEGAL BACKGROUND

A. Trade Secret Law

1. Purpose of Trade Secret Law

The purpose of trade secret law is to encourage invention and foster the sharing of information in business settings.[10] Trade secret protection serves as a catalyst in the business world by allowing companies to share information without fear of losing their proprietary information and its corresponding advantages. Trade secret law protects such information in part so that companies may share information more freely with their employees, thereby maximizing internal efficiency.[11] Without such protection, companies might be compelled to guard their proprietary information too closely, thus making business operations less efficient.[12] By upholding standards of commercial ethics, trade secret law attempts to ensure that companies do not unjustly forfeit time and money spent invested in the development of valuable information through misappropriation of their proprietary information.

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8. Bernier v. Merrill Air Engineers, 770 A.2d 97, 100 (Me. 2001).

9. *Id.* at 100. *See also* Den-Tal-Ez, Inc. v. Siemens Capital Corp., 566 A.2d 1214, 1224 (Pa. Super. Ct. 1989) (discussing how certain information protected by agreement may be protected only by agreement, since it will not necessarily qualify as a "trade secret," noting that "the terms 'confidential information' and 'trade secrets' 'do not equate,' and may in fact refer to entirely different bodies of information"); Revere Transducers, Inc. v. Deere & Co., 595 N.W.2d 751, 765 (Iowa 1999) (holding that former employer did not have to prove that confidential information qualified as a trade secret in the presence of a reasonable NDA).

10. Kewanee Oil Co. v. Bicron Corp., 416 U.S. 470, 481-82 (1974). *See* RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 39 cmt. a (1995) (facilitating disclosure to employee); Davidson & DeMay, *supra* note 8, at 583-84. *See generally* ROBERT MERGES ET AL., INTELLECTUAL PROPERTY IN THE NEW TECHNOLOGICAL AGE, 36-37 Ch. 2 (2d ed. 2000).

11. *Kewanee Oil*, 416 U.S. at 485-87. *See* Painton & Co. v. Bourns, Inc., 442 F.2d 216, 223 (1971) ("the upholding of private agreements for the sharing of trade secrets on mutually acceptable terms lends against the owner hoarding them.").

12. *Kewanee Oil*, 416 U.S. at 485-87.

2. *Development of Trade Secret Law*

a) Common Law

Trade secret law developed from state common law.[13] The Massachusetts Supreme Judicial Court crystallized the law of trade secrets in 1868.[14] The court specifically held:

> It is the policy of the law, for the advantage of the public, to encourage and protect invention and commercial enterprise. If a man establishes a business and makes it valuable by his skill and attention, *the good will of that business is recognized by the law as property.*[15]

Decisions such as this based trade secret law and the protection of secret information on pre-existing property doctrines. Due to its intangible nature, however, secret information did not fit easily into established property doctrines regarding tangible property.[16]

Courts ultimately succeeded in carving out a niche in property law for secret information by focusing on the property doctrine of exclusive control.[17] Intangible information could be considered property so long as the information remained in the owner's exclusive control.[18] The only way an owner could retain exclusive control of information was to keep it secret.[19] Therefore, once secrecy was destroyed, the information was no longer under the owner's exclusive control and could no longer be considered property. As a result, any protection afforded by trade secret law necessarily ended when information lost its secrecy.

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13. Bone, *supra* note 6, at 247.

14. *Id.* at 252.

15. Peabody v. Norfolk, 98 Mass. 452, 457 (1868) (emphasis added).

16. *See* Bone, *supra* note 6, at 254. For a classic discussion of property law's emphasis on exclusive control, see Pierson v. Post, 2 Am. Dec. 264 (N.Y. 1805).

17. Bone, *supra* note 6, at 254.

18. *See* Haskins v. Ryan, 64 A. 436, 438 (N.J. Ch. 1906), *aff'd*, 75 N.J. Eq. 623 (1909) (noting undeveloped ideas cannot be treated as property because the originator cannot control it as a secret and use it for his own good without involving others in its development); Bristol v. Equitable Life Assurance Soc'y of New York, 30 N.E. 506, 507 (N.Y. 1892) (holding undeveloped ideas unprotectable because exclusive ownership cannot be easily preserved).

19. *See* Stewart v. Hook, 45 S.E. 369, 370 (Ga. 1903) (stating that the information holder must maintain the secrecy and control of information to retain protection); Eastman Co. v. Reichenbach, 20 N.Y.S. 110, 116 (1892) ("The whole world is at liberty to discover [secret information], . . . and, when discovery is thus made, . . . the inventor's or manufacturer's property . . . is gone").

The doctrine underlying trade secret law evolved as later decisions dismissed property-based theories of the law and instead focused on the wrongfulness of the defendant's conduct as the true basis for liability.[20] Justice Holmes articulated this shift in the justification for trade secret law:

> Whether the plaintiffs have any valuable secret or not, the defendant knows the facts, whatever they are, through a special confidence that he accepted. *The property may be denied* but the confidence cannot be. Therefore the starting point for the present matter is not property or due process of law, but that the defendant stood in confidential relations with the plaintiffs. . . .[21]

By focusing on the relationship between the parties, twentieth century courts associated trade secret law more closely with contract and tort law than with property law.[22]

b) Unified Doctrine of Trade Secret Law

The First Restatement of Torts ("First Restatement") extracted the first unified definition of a trade secret from the common law.[23] It defined a trade secret as "any formula, pattern, device or compilation of information which is used in one's business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it."[24] The Uniform Trade Secrets Act ("UTSA") provides the most accepted current definition of a trade secret.[25] The UTSA defines a trade secret as

> information, including a formula, pattern, compilation, program, device, method, technique, or process, that: (i) derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by other persons who can obtain economic value from its

20. Bone, *supra* note 6, at 258. *See* Vulcan Detinning Co. v. Am. Can Co., 67 A. 339, 343 (1907) (finding too much emphasis placed on secrecy of information and not enough emphasis placed on the wrongfulness of defendant's conduct); Note, *Equity - Trade Secrets - Duty of Non-Disclosure by Fiduciary Relation*, 37 YALE L.J. 1154, 1155 (1927) ("Many courts grant relief . . . on the basis of the "property right' theory. More modern decisions, however, in the absence of an express contract, place the protection afforded on the basis of a contract implied in law.").

21. E. I. duPont deNemours Powder Co. v. Masland, 244 U.S. 100, 102 (1917) (emphasis added).

22. Bone, *supra* note 6, at 260.

23. *See id.* at 247.

24. RESTATEMENT (FIRST) OF TORTS § 757 cmt. b (1939).

25. *See* MERGES, *supra* note 10, at 34 (noting the UTSA's importance).

> disclosure or use, and (ii) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.[26]

Forty-three jurisdictions (42 states and the District of Columbia) have enacted statutes codifying the law of trade secrets based on the UTSA.[27]

The UTSA definition of a trade secret differs from the First Restatement definition in that the UTSA omits the requirement that the information be "used in one's business."[28] The UTSA also adds the requirement that reasonable efforts be taken to maintain the secrecy of the information.[29] These differences allow for the protection of a broader class of information as long as the information is adequately protected.[30]

To establish liability for trade secret misappropriation under the UTSA, a plaintiff must show that (1) the information qualifies as a trade secret;[31] and (2) the defendant acquired, used, or disclosed the information in breach of confidence or by other improper means.[32] The UTSA's two-prong analysis therefore retains a property analysis under the first prong, and a contract or tort analysis under the second prong.[33] Under the first property prong of the analysis, the information must qualify as a trade secret to justify the extension of property rights to such information. Under

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26. UNIF. TRADE SECRETS ACT § 1(4) (1985).

27. Benjamin A. Emmert, Comment, *Keeping Confidence with Former Employees: California Courts Apply the Inevitable Disclosure Doctrine to California Trade Secret Law*, 40 SANTA CLARA L. REV. 1171, 1177 (2000).

28. *Compare* RESTATEMENT (FIRST) OF TORTS § 757 cmt. b (1939) *with* UNIF. TRADE SECRETS ACT § 1(4) (1985).

29. UNIF. TRADE SECRETS ACT § 1(4) (1985). Some states, including California, do not include the "readily ascertainable" language in the definition of a trade secret. CAL. CIVIL CODE § 3426.1 (1997). MERGES, *supra* note 10, at 35 n. 7.

30. *See* Religious Tech. Ctr. v. Lerma, 908 F. Supp. 1362, 1368-69 (E.D. Va. 1995) (holding religious materials protectable as a trade secret).

31. UNIF. TRADE SECRETS ACT § 1(4) (1985).

32. *Id.* § 1(1) (1985); MERGES, *supra* note 10, at 35-36. Improper means include theft, bribery, misrepresentation, breach or inducement of a breach of a duty to maintain secrecy, or espionage through electronic or other means. UTSA § 1(1) (1985).

33. Complete secrecy is no longer required, but the requirement that the information be not generally known remains. Further, THE RESTATEMENT (THIRD) OF UNFAIR COMPETITION (1995) provides the most recent effort to organize trade secret law. Importantly, THE RESTATEMENT (THIRD) ON UNFAIR COMPETITION §§ 39-45 rejects the wrongfulness of the defendant's conduct as the true basis for liability and focuses instead on an initial determination of whether the information merits protection as a trade secret. This Restatement, therefore, rejects the contractual and tortious aspects of trade secret law in favor of its property justifications. However, legislatures and jurisdictions have not yet adopted or applied this Restatement. It nonetheless remains important to consider in an analysis of whether or not the supplementation of trade secret law through contractual NDAs is appropriate.

the second contract or tort prong, a defendant must improperly acquire the information to be liable for its disclosure. Importantly, the presence of an NDA expressly provides for the existence of a confidential relationship thereby ensuring that the second prong of the UTSA analysis is met if an employee wrongfully discloses proprietary information.

B. Contractual Nondisclosure Agreements (NDAs)

When an employee's duties center on the use of secret or confidential information, the presence of an NDA can restrict that employee's ability to seek alternative employment.[34] Traditionally, courts viewed any type of contractual, post-employment restraint as an unacceptable restraint on trade.[35] However, as courts realized the importance of specialized knowledge to economic development, and recognized workplace knowledge as a firm asset, they began to accept reasonable post-employment restraint agreements.[36] As a result, the *per se* invalidity of post-employment restraint agreements gave way to a reasonableness inquiry.[37]

Currently, the law disfavors post-employment restraint agreements, including NDAs, and courts routinely subject such agreements to "strict reasonableness inquiries."[38] Under this inquiry, courts enforce NDAs only when the agreement is reasonable and necessary to protect an employer's interests.[39] Further, the NDA must balance the interests of the employer

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34. *See, e.g.,* American Broadcasting Cos. v. Wolf, 420 N.E.2d 363, 368 (N.Y. 1981) (underlying the strict treatment of post-employment restraints are "the general public policy favoring. . .the powerful considerations of public policy which militate against sanctioning the loss of a man's livelihood") (quoting Purchasing Assocs. v. Weitz, 196 N.E.2d 245, 247 (1963)). *See also* Maureen B. Callahan, *Post-Employment Restraint Agreements: A Reassessment*, 52 U. CHI. L. REV. 703, 712 (1985)

35. Dyer's Case, Y.B. 2 Hen. 5, pl. 26 (1414); Colgate v. Bacheler, 78 Eng. Rep. 1097 (Q.B. 1602). *See* Callahan, *supra* note 34, at 707.

36. Catherine L. Fisk, *Working Knowledge: Trade Secrets, Restrictive Covenants in Employment, and the Rise of Corporate Intellectual Property, 1800-1920*, 52 HASTINGS L.J. 441, 442 (2001).

37. *See, e.g.,* Mitchel v. Reynolds, 24 Eng. Rep. 347, 352 (Ch. 1711) ("To conclude: In all restraints of trade, where nothing more appears, the law presumes them bad; but if the circumstances are set forth, that presumption is excluded, and the Court is to judge of those circumstances, and determine accordingly; and if upon them it appears to be a just and honest contract, it ought to be maintained."); Callahan, *supra* note 34, at 709.

38. *See* Orkin Exterminating Co. v. Dewberry, 51 S.E.2d 669, 675 (1949) ("While it is the general rule that a contract in general restraint of trade is void, a contract only in partial restraint may be upheld, 'provided the restraint be reasonable . . . .'" quoting Kutash v. Gluckman, 20 S.E.2d 128, 130 (Ga. 1942); Kadis v. Britt, 29 S.E.2d 543, 545 (1944) (post-employment restraints are void unless shown to be reasonable).

39. *See Orkin Exterminating Co.*, 307 S.E.2d at 916 ("Covenants against competition which are contained in employment contracts . . . will be upheld only if they are

with the interests of the departing employee.[40] While the departing employee or her new employer should not be unjustly enriched through the use of confidential information, the employee must be permitted to use the general skill and knowledge gained during her previous employment.[41] Thus, courts disregard NDAs if the employee's interest in pursuing her profession outweighs the employer's interest in restricting disclosure.

States have not applied this balancing approach to NDAs uniformly.[42] While the vast majority of states require that an NDA be reasonable, the definition of "reasonable" varies.[43] For example, in Michigan, an NDA is considered reasonable if it does not go beyond what is reasonably necessary to protect confidential information.[44] Likewise, courts in Georgia consider an NDA reasonable if it is written so that confidentiality is reasonably related to the protection of information.[45] Illinois, however, finds an NDA reasonable if it is not injurious to the public, will not cause undue hardship to the employee, and is not broader than necessary to protect the *interests* of the employer.[46] Therefore, while Illinois adds an injury to the public inquiry suggesting a stricter approach to reasonableness, it also potentially protects a broader range of the employer's interests.[47]

Confidentiality agreements should simultaneously strive to protect the employer's interests and limit employee disclosures while maintaining the employee's ability to earn a living. The most common test used to evaluate the reasonableness of an NDA requires that the NDA (1) not impose undue hardship upon the employee; and (2) be no wider in scope than is reasonably necessary to protect the employer.[48] Another common test asks whether the restriction is (1) necessary to protect the employer's business; (2) unreasonably restrictive of the employee's rights; and (3) prejudicial to

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strictly limited in time and territorial effect, and are otherwise reasonable considering the business interest of the employer sought to be protected and the effect on the employee.").

40. *Id. See also* Harwell Enters., Inc. v. Heim, 173 S.E.2d 316, 318-19 (1970) (applying balancing-of-interests analysis).

41. Gary Van Zeeland Talent, Inc. v. Sandas, 267 N.W.2d 242, 248 (Wis. 1978); Carol M. Bast, *At What Price Silence: Are Confidentiality Agreements Enforceable?*, 25 WM. MITCHELL L. REV. 627, 635-36 (1999).

42. Bast, *supra* note 41, at 639.

43. *Id.*

44. *See* Follmer, Rudzewicz & Co. v. Kosco, 362 N.W.2d 676, 683 (Mich. 1984).

45. *See* Durham v. Stand-By Labor, Inc., 198 S.E.2d 145, 150 (Ga. 1973).

46. *See* Tower Oil & Tech. Co. v. Buckley, 425 N.E.2d 1060, 1065 (Ill. App. Ct. 1981).

47. For a more thorough review of state's inquiries into the reasonableness of NDAs, see Bast, *supra* note 41, at 639-42.

48. *See* Bernier v. Merrill Air Engineers, 770 A.2d 97, 103 (Me. 2001).

the public interest.[49] Yet a third test suggests that courts should consider (1) the parties' reasonable expectations; (2) the potential loss to the employer if the agreement is not enforced; (3) the protectability of the information as a trade secret or as proprietary information; (4) the substantial adverse effects on third parties; (5) the exacerbation of the adverse effects if the confidentiality agreement is not enforced; and (6) the possibility for limited disclosure when determining whether an NDA is reasonable.[50] These similar approaches outlined in the three tests above reflect the modern emphasis of balancing employer and employee interests. This balancing was addressed by the court in *Bernier v. Merrill Air Engineers*, as discussed in the next Section.

II. CASE SUMMARY

A. Facts

Plaintiff Robert Bernier provided engineering services for defendant, Merrill Air Engineers ("Merrill"). During his employment with Merrill, Bernier constantly worked with highly proprietary and confidential information.[51] Because Bernier worked with such confidential information, Merrill required that he sign an NDA. The NDA specifically stated that:

> The Employee agrees that he or she shall not, during the term of employment . . . or at anytime thereafter, divulge, use, furnish, disclose or make accessible to anyone other than Tristar [Merrill's holding company] or other than in Tristar's usual course of business, any knowledge or information with respect to (i) confidential or secret processes, plans, formulae, programs, devices or material relating to the business, services or activities of Tristar, (ii) any confidential or secret development or other original work of Tristar, (iii) any other confidential or secret aspect of the business, products, or activities of Tristar . . . . All records, materials, and information obtained by the Employee in the course of his or her employment are confidential and shall remain the exclusive property of Tristar.[52]

While employed at Merrill, Bernier managed the engineering and design aspects of a proposal to build a dryer for Henry Molded Products

49. *See* Revere Transducers, Inc. v. Deere & Co., 595 N.W.2d 751, 762 (Iowa 1999).

50. Bast, *supra* note 41, at 709.

51. *Bernier*, 770 A.2d at 102.

52. *Id.*

("HMP"). This proposal contained highly proprietary design information, and was classified as a confidential document.[53] After HMP made a preliminary commitment to purchase the dryer, Bernier resigned from Merrill and contacted HMP about potential job openings. Thereafter, Bernier accepted a job with HMP, and HMP cancelled the dryer order they had placed with Merrill.[54] Within one year, HMP completed the design and manufacture of its own dryer under Bernier's supervision.[55]

After leaving Merrill, Bernier brought an action against it to recover commissions earned for the sale of products he engineered during the course of his employment.[56] Merrill, in turn, counterclaimed that Bernier breached the NDA of his employment contract and misappropriated trade secrets by providing dryer design engineering services for HMP.[57]

B. Decision And Procedural History

1. Trial Court's Findings

The trial court held that Merrill owed Bernier commissions earned during the course of his employment.[58] Finding Merrill's argument unreasonable, the court rejected its contention that the payment of commissions to engineers was contingent on cash availability. The trial court further found that Bernier did not misappropriate trade secrets because Merrill failed to prove that the information at issue qualified for trade secret protection.[59] While Bernier did not misappropriate trade secrets, he did breach his contractual obligation not to disclose proprietary information.[60] Finding it more likely than not that HMP would have ordered the dryer from Merrill had Bernier not breached his contract, the court awarded Merrill damages equaling the profits it would have made from the design, construction and sale of the dryer.[61]

2. Trial Court's Analysis

The trial court concluded that Merrill's information did not qualify for trade secret protection based on its application and analysis of five factors

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53. *Id.*
54. *Id.*
55. *Id.*
56. *Id.* at 100. At Merrill, engineers earned a three percent commission on the sale of products that they engineered. *Id.*
57. *Id.* at 103.
58. *Id.* at 100.
59. *Id.* at 103.
60. *Id.*
61. *Id.*

outlined in *Spottiswoode v. Levine*.[62] These factors include (1) the value of the information to the plaintiff and to its competitors; (2) the amount of effort or money the plaintiff expended in developing the information; (3) the extent of measures the plaintiff took to guard the secrecy of the information; (4) the ease or difficulty with which others could properly acquire or duplicate the information; and (5) the degree to which third parties have placed the information in the public domain or rendered the information "readily ascertainable" through patent applications or unrestricted product marketing.[63]

The court addressed each factor in turn.[64] In its analysis, the court found that the first factor did not weigh in favor of trade secret protection.[65] Merrill's information was not valuable enough to warrant protection because its designs were not inherently superior to the designs of its competitors.[66] Similarly, the court found that the second factor did not weigh in favor of trade secret protection.[67] Although Merrill had expended some effort and money in developing the information, the evidence supporting such expenditures was not sufficient to support trade secret protection.[68] The court also found that the fourth and fifth factors did not favor trade secret protection.[69] Once on the market, interested parties could easily reverse engineer a Merrill dryer.[70] Further, because the parts of the dryer could be purchased from distributors, the information was readily ascertainable to those who might be interested in it.[71] The court's analysis of the third factor, however, favored trade secret protection because Merrill undertook sufficient measures to guard the secrecy of its information.[72] On balance, therefore, the court held that the disputed information did not qualify for trade secret protection.[73]

Although Merrill's information did not qualify for trade secret protection, the trial court nonetheless awarded the company damages based on Bernier's breach of the nondisclosure clause of his employment contract.[74]

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62. *Id.* at 106 (citing Spottiswoode v. Levine, 730 A.2d 166, 174 n.6 (1999)).
63. *Id.* (citing Spottiswoode, 730 A.2d at 174).
64. Id at 107-108.
65. *Id.* at 107.
66. *Id.*
67. *Id.*
68. *Id.*
69. *Id.* at 108.
70. *Id.*
71. *Id. See supra* note 29 and accompanying text.
72. Bernier v. Merrill Air Engineers, 770 A.2d 97, 108 (Me. 2001).
73. *Id.* at 108-09.
74. *Id.* at 103.

The trial court found the NDA reasonable because of its limited scope; it only prohibited Bernier from using "particularized, highly specialized proprietary protected original work that was custom designed for a particular prospect."[75] Further, the agreement did not impose undue hardship on Bernier because it did not prohibit him from using the general skills or knowledge he obtained while working at Merrill.[76]

3. Appellate Court Review

The appellate court agreed with the trial court's determination that the information was not a trade secret.[77] It disagreed, however, with the trial court's application of the fourth *Spottiswoode* factor.[78] In its analysis of factor four, the trial court held that "[o]nce a Merrill dryer is on the scene, it doesn't take a great deal of effort" to understand the design of the dryer.[79] The appellate court agreed with Merrill that Bernier could not "properly" reverse engineer the dryer because he did not acquire the information to do so through proper means; Bernier "acquired" the information at issue when he breached the nondisclosure clause of his contract.[80] Therefore, the appellate court held that the trial court misperceived the importance of acquiring the dryer design by "proper" means.[81] Although it found that the trial court misapplied the fourth *Spottiswoode* factor, the appellate court ultimately upheld the lower court's decision that Merrill's proprietary information did not rise to the level of a trade secret.[82]

The appellate court also affirmed the trial court's holding that the NDA of Bernier's employment contract was reasonable.[83] Rejecting Bernier's contention that Merrill could not contractually protect information outside the UTSA definition of a trade secret, the appellate court unequivocally stated that "confidential knowledge or information protected by a restrictive covenant need not be limited to information that is protected as a trade secret by the UTSA."[84] Therefore, a reasonable NDA can prevent a former employee from using confidential knowledge and infor-

75. *Id.*
76. *Id.* at 104.
77. *Id.* at 108.
78. *Id.*
79. *Id.*
80. *Id.*
81. *Id.*
82. *See id.* at 109.
83. *Id.* at 103.
84. *Id.*

mation gained in the course of employment despite the fact that the information does not qualify for trade secret protection under the UTSA.[85]

III. INFORMATION THAT DOES NOT QUALIFY FOR TRADE SECRET PROTECTION MAY BE PROTECTED CONTRACTUALLY

The supplementation of trade secret law with NDAs is appropriate for numerous reasons. First, parties use contractual NDAs to avoid the uncertainty associated with trade secret law. Second, in contrast to other areas of intellectual property law, trade secret law is amenable to broader supplementation by contract due to the scope and strength of protection that it offers. Third, contractually protecting information through NDAs does not unjustly impede the flow of information. Finally, the current development and underlying rationales of trade secret law suggest that contract law is a natural complement to the trade secret doctrine.

A. Use of Contractual Agreements to Avoid Uncertainty

The main goal of trade secret law is to encourage invention and promote the sharing of information.[86] If a company can rely on trade secret law to protect its proprietary information, it will likely share that information with its employees, thus increasing efficiency and innovation.[87] However, a company with proprietary information does not know with certainty whether its information is protectable as a trade secret until that information is litigated and judicially declared a trade secret. As seen in *Bernier*, judicial determination of this question is a highly fact-specific inquiry.[88] As a result of the uncertainty associated with trade secret litigation, companies are less likely to share their proprietary information internally if there is a significant risk that a judge may not grant the informa-

85. *Id.* (citing Ingersoll-Rand Co. v. Ciavatta, 542 A.2d 879, 894 (N.J. 1988)). *See also* Structural Dynamics Research Corp. v. Eng'g Mechs. Research Corp., 401 F. Supp. 1102 (E.D. Mich. 1975) (holding NDAs applicable not only to trade secrets but also to privileged, proprietary and confidential information). *See* Den-Tal-Ez, Inc. v. Siemens Capital Corp., 566 A.2d 1214, 1224 (Pa. Super. Ct. 1989).

86. *See supra* note 10 and accompanying text.

87. Unikel, *supra* note 1, at 871 (noting that forced reliance on "self-help" measures increases the level of investment required for profitable innovation thereby decreasing the incentive and resources available for product and process development).

88. Bernier v. Merrill Air Engineers, 770 A.2d 97, 107-08 (Me. 2001). *See* Sarkes Tarzian Inc. v. Audio Devices, Inc., 166 F. Supp 250, 257 (S.D. Cal 1958) (stating that "[w]hat is a trade secret is difficult to define.").

tion trade secret protection.[89] This failure to share information thwarts the goals of trade secret law.

Allowing parties to contractually define protected information helps alleviate the uncertainty associated with trade secret law. By creating NDAs, employers and employees are able to provide unambiguous declarations of what they view as confidential.[90] Thus, employers and employees can define what information is protected and what information is viewed as general at the outset of their relationship.[91] This certainty is likely to decrease the amount of information unfairly lost due to employee misuse or inadvertent disclosure.[92] It also helps prevent expensive and time-consuming trade secret litigation, as no such declaration is needed in the presence of an enforceable NDA. Thus, by putting employees on notice, contractual agreements allow parties to structure their relationships and reduce subsequent costs related to enforcement and litigation.[93] The certainty of protection brought about by contractual agreements also helps to achieve one of the major goals of trade secret law—the efficient sharing of information. Based on these considerations, the supplementation of trade secret law with contract law is not only appropriate, but also beneficial, efficient and desirable.

B. Broad Freedom to Contract in Trade Secret Law

Contract law may protect proprietary information that falls outside the realm of trade secret law. Inventors and authors who seek to contractually expand patent or copyright protection are generally not allowed to do so.

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89. *See* Unikel, *supra* note 1, at 847-48 ("In the absence of legal protection for valuable, independently developed information, businesses would be less likely to commit their finite resources to the creation of new technology because there is no guarantee that they will benefit from that development. Moreover, without legal protection against corporate theft, those businesses that continued to invest in innovation would be forced to expend a disproportionate amount of money on 'self-help' measures designed to protect their innovations from piracy.").

90. Collins J. Seitz, Jr., *Protection of Trade Secrets Through Employment Agreements*, 7 DEL. LAW. J. 46, 46 (1989).

91. *See* Ultra-Life Labs., Inc. v. Eames, 221 S.W.2d 224, 232 (Mo. Ct. App. 1949) (noting that the existence of contract not to divulge processes was an admission that such materials were secret). *See also* Terry Morehead Dworkin & Elletta Sangrey Callahan, *Buying Silence*, 36 AM. BUS. L.J. 151, 157 (1998).

92. *See* Dworkin & Callahan, *supra* note 91, at 157.

93. *See* Kaumagraph Co. v. Stampagraph Co., 138 N.E. 485, 486 (N.Y. 1923) (post-employment contracts "merely express the implied contract of one who enters into such an employment not to carry elsewhere into competition with his employer confidential knowledge obtained from him"). Robert Bone goes one step further to argue that when dealing with employer/employee relationships, proprietary information should be protected by contract principles only. *See* Bone, *supra* note 6, at 246-47.

This difference between trade secret law and other areas of intellectual property law is reasonable given the amount and type of protection offered by trade secret law on the one hand and patent and copyright law on the other.

Patent and copyright laws provide protection and property rights against the world—including those with no prior relationship.[94] This protection is strong and lasts for a statutorily defined period.[95] Further, especially in relation to patent law, protected information is rigidly defined with notice given to the public that such information is protected as of a given date. Reverse engineering or independent discovery by other persons does not alter the patent holder's rights to the patented invention. In contrast, trade secret law only protects information against those who acquire it through improper means (such as theft or the breach of a confidential relationship).[96] The public at large is free to reverse engineer or independently discover the information. Further, protection lasts only as long as the information remains secret, and it is the responsibility of the owner of the information to maintain its secrecy.[97] Thus, in contrast to patent holders, trade secret owners must adopt effective strategies to protect the secrecy of their information.

Courts have granted broader rights to contract in the realm of trade secret law than in other areas of intellectual property law in part because trade secret law affords information owners weak protection. The *Listerine* case[98] provides a classic example of this principle. In *Listerine*, after the formula for the mouthwash became widely known, the plaintiff sued for a judgment declaring that it was no longer required to pay royalties based on the manufacture and sale of Listerine.[99] The agreement between the parties stipulated that the plaintiff would make royalty payments for the use of the

94. Bone, *supra* note 6, at 243. *See generally* MERGES, *supra* note 10, at 137.

95. *See* 35 U.S.C. § 154(a)(2) (1994) (defining patent protection term as 20 years from the filing date of the application); 17 U.S.C. § 302-05 (1998) (defining copyright protection term as the life of the author plus 70 years, or in the case of entity authors, 95 years from first publication or, if not published, 120 years from the year of creation).

96. *See* Kewanee Oil Co. v. Bicron Corp., 416 U.S. 470, 475-76 (1974). *See also* 1 MELVIN F. JAGER, TRADE SECRETS LAW § 3.03[3][a], 3-47 (1996) ("Unlike a patent owner, a person who possesses a trade secret does not have an exclusive right to the information."); David D. Friedman et al., *Some Economics of Trade Secret Law*, 5 J. ECON. PERSP. 61, 62 (1991) (noting that most of trade secret law is based on independent common law wrongs, such as breach of contract and theft, rather than on infringement of rights in the information itself).

97. *See supra* note 32 and accompanying text.

98. Warner-Lambert Pharm. Co. v. Reynolds, 178 F. Supp. 655 (S.D.N.Y. 1959).

99. *Id.* at 657.

secret formula for Listerine as long as it continued to manufacture and sell the product.[100] The formula for Listerine was made public after the agreement was executed, and was no longer receiving trade secret protection at the time of the litigation.[101] The court nonetheless held that one cannot escape a contractual obligation to pay royalties simply because a trade secret no longer receives legal protection.[102] The court reasoned that if the plaintiff wanted to pay royalties only while the formula remained secret, it could have included this provision in the contract.[103] This holding is in stark contrast to the established patent and copyright principle that once legal protection ends, royalty payments must cease.[104] Thus, trade secret law allows more freedom to contract than other areas of intellectual property law.

Because trade secret law allows broad freedom to contract, and information owners must adopt effective "self-help" strategies to protect their information, many such information owners turn to contractual NDAs to protect their proprietary information. This use of contractual NDAs is an effective means to protect the secrecy of information and comports with the broader right to contract uniquely available in trade secret law.

C. Failure to Impede Information Flow

Some argue that allowing protection of proprietary information through NDAs leads to information being unjustly retained in the hands of a few, resulting in anti-competitive effects.[105] Others believe that this outcome is not necessarily the case.[106] Unacceptable anti-competitive effects caused by NDAs are unlikely because courts continue to subject such agreements to strict reasonableness inquiries.[107] Based on this strict court review, unreasonable NDAs that could result in anti-competitive effects are not enforced.[108] Therefore, if a court chooses to uphold an NDA, it is likely that the NDA is both reasonable in scope and does not unjustly limit

100. *Id.* at 658-59.

101. *Id.*

102. *Id.* at 660-61.

103. *Id.* at 666.

104. *Id.* at 664-65. *See supra* note 96 and accompanying text. *Compare with* Aronson v. Quick Point Pencil Co., 440 U.S. 257, 262 (1979) (noting that if parties include provisions for continuing royalty payments in the event a patent does not issue, this provision is enforceable).

105. *See, e.g.*, 1st Am. Sys., Inc. v. Rezatto, 311 N.W.2d 51, 57 (S.D. 1981) (enforcement of NDAs may vest information owners with monopoly power); Callahan, *supra* note 34, at 706.

106. *See generally* Bone, *supra* note 6.

107. *See supra* note 39 and accompanying text.

108. *Id.*

information flow or the departing employee's career opportunities.[109] Further, irrespective of whether there is a contract, other areas of law (such as agency law), protect an employer's proprietary information.[110] Because proprietary information is already protected, contractual protection does not expand protected information; it simply defines such information under already-established fiduciary duties of confidentiality.

1. Strict Reasonableness Inquiries

The presence of an NDA in an employment contract will not unduly restrict the flow of information because courts do not favor NDAs and continue to subject such agreements to strict reasonableness inquiries.[111] Courts will not enforce an NDA unless it legitimately balances the employer's interests in protecting proprietary information with the employee's interests in mobility.[112] This judicial review prevents employers from unreasonably protecting information.[113]

For example, in *American Family Life Assurance Co. v. Tazelaar*,[114] the court held an NDA that prevented employees from making "available any information or materials acquired from American Family to any competitor or potential competitor" invalid and unenforceable because it was overly broad.[115] The court in *Nasco Inc. v. Gimbert* also held an NDA invalid because it unnecessarily prohibited the disclosure of information.[116] As these cases demonstrate, unreasonable NDAs that could lead to unacceptable anti-competitive effects are not enforced. Thus, strict court review of NDAs protects the flow of information.

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109. *Id.*

110. *See* RESTATEMENT (SECOND) OF AGENCY §§ 395-96 (1957). "Unless otherwise agreed, an agent is subject to a duty to the principal not to use or to communicate information confidentially given him by the principal or acquired by him during the course of or on account of his agency or in violation of his duties as agent, in competition with or to the injury of the principal, on his account or on behalf of another, although such information does not relate to the transaction in which he is then employed, unless the information is a matter of general knowledge." RESTATEMENT (SECOND) OF AGENCY § 395 (1957). Section § 396(d) implies that the duty of nondisclosure continues after termination of the employment relationship. RESTATEMENT (SECOND) OF AGENCY § 396(d) (1957).

111. *See supra* note 38 and accompanying text.

112. *See supra* notes 39-40 and accompanying text.

113. *See generally* American Family Life Assurance Co. v. Tazelaar, 482 N.E.2d 1072 (1985).

114. 482 N.E.2d 1072 (1985).

115. *Id.* at 1071.

116. 238 S.E.2d 368, 370 (Ga. 1997).

2. *Protection of Nontrade Secret Information In Other Areas of Law*

Allowing the contractual protection of proprietary information does not expand the realm of protected information. NDAs do not expand the realm of protected information because a company's confidential information is already protected through other areas of the law regardless of its status as a trade secret.[117] For example, under the Restatement Second of Agency ("Second Restatement"), employees have a duty of confidentiality.[118] Employees are under an implied common law legal obligation not to disclose valuable business information regardless of whether the information qualifies for trade secret protection.[119] This obligation exists so long as the information is proprietary to the employer, revealed in confidence, and not of general knowledge.[120] Because Nontrade secret information is already protected by the common law, the presence of an NDA does not impermissibly expand the realm of protected information; it simply serves to provide a definition of what information the employer and employee view as confidential under the Second Restatement's duty of confidentiality.[121]

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117. *See* Nucor Corp. v. Tennessee Forging Steel Serv., Inc., 476 F.2d 386, 392 (8th Cir. 1973) ("[E]mployees have a high duty not to disclose confidential information received by them as employees to competitors regardless of the fact that the information disclosed might not technically be considered a trade secret. This view is consistent with that expressed in the Restatement (Second) of Agency, §§ 395 and 396 (1958). We think it is the correct view."); Coulter Corp. v. Leinert, 869 F. Supp. 732, 735 (E.D. Mo. 1994) ("[T]he scope of an agent's duty of confidentiality and loyalty is not limited to protecting a principal against the disclosure of trade secrets. . . [T]he state's UTSA did not bar an action for breach of confidentiality. . . ."). *See also* HENRY H. PERRITT, JR., TRADE SECRETS: A PRACTITIONER'S GUIDE 163-64 (1994) ("A confidential relationship may exist between employers and employees with respect to certain information, even in the absence of a restrictive covenant agreement, during employment as well as after termination.").

118. *See supra* note 114.

119. Structural Dynamics Research Corp. v. Eng'g Mechs. Research Corp., 401 F. Supp. 1102, 1144 (E.D. Mich. 1975) (noting that an employee has an obligation not to disclose confidential information revealed to him or her in the course of employment and it is immaterial that such information might not technically qualify as a trade secret).

120. *See* Jet Spray Cooler, Inc. v. Crampton, 282 N.E.2d 921, 926-27 (Mass. 1972) (holding that former employees breached duty of confidentiality by using confidential reports prepared for their former employer in their own competing business); By-Buk Co. v. Printed Cellophane Tape Co., 329 P.2d 147, 151 (Ca. 1958) (noting that employees are under implied obligations not to use confidential information acquired by reason of their employment).

121. *See* Neufeld, *supra* note 7.

D. Trade Secret Law Rationales Suggest Contract Supplementation is Appropriate

In analyzing whether it is appropriate to supplement trade secret law with contract law, it is useful to examine the underlying theories of trade secret law.[122] Recall that nineteenth century courts rooted the original justifications for trade secret law firmly in property law.[123] The original property justification for trade secret doctrine centered on the idea of exclusive control of secret and valuable information.[124] If the secrecy of the information was lost, there was nothing left to protect.[125] These original property justifications kept trade secret law distinct from contract law because the legal protection of information depended solely on the secret nature of the information.[126] Courts generally did not examine how the information at issue lost its secrecy.[127] Because trade secret law was so firmly rooted in property law with no contract principles evident, it might have been inappropriate to supplement trade secret law with contract law in the nineteenth century.[128]

When Justice Holmes stated, "the property may be denied," in *E. I. duPont deNemours Powder Co. v. Masland*,[129] trade secret law lost its strict grounding in property law.[130] Over time, the breach of a confidential relationship became the new justification for trade secret law.[131] Because the confidential relationship could not be denied under the new formulation of the rule, courts began to focus misappropriation analyses not only on the characteristics of the information, but also on the expectations and relationship between the parties.[132] As a result of this addition to the trade secret analysis, trade secret law became more closely aligned with contract

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122. The following analysis of modern trade secret law is based on an analysis of the UTSA.

123. *See supra* note 15 and accompanying note.

124. *Id.*

125. *See supra* note 18 and accompanying text.

126. Bone, *supra* note 6, at 259-60.

127. *Id.* at 255 ("Secrecy required constant vigilance . . . since ideas, like wild animals, had a tendency to escape. Once gone, they returned to the commons as public property.") (citing Werckmeister v. American Lithographic Co., 134 Fed. 321, 324 (2d Cir. 1904)).

128. *See id.* at 260.

129. *See supra* note 21 and accompanying text.

130. Bone, *supra* note 6, at 260.

131. *See supra* note 20 and accompanying text.

132. *Id.*

law.[133] It therefore became more appropriate to supplement trade secret law with contract law than it had been in the nineteenth century.

As stated, this analysis of the evolution of modern trade secret law is based on an analysis of the UTSA. It is noteworthy that not all states have adopted the UTSA, and some retain the property justification of the trade secrets doctrine under certain circumstances.[134] For example, although Missouri adopted the UTSA in 1995, if an instance of trade secret misappropriation began prior to the UTSA adoption, Missouri common law applies.[135] In *Group One Ltd. v. Hallmark Cards*[136] the court suggested that Missouri common law would adopt the property theory rather than the breach of a confidential relationship theory of trade secret law.[137] Further, the 1995 Restatement on Unfair Competition rejects the "bad behavior" element of the trade secret analysis and returns to the more basic property approach.[138] Therefore, in evaluating whether the supplementation of trade secret law with contract law is appropriate, it is important to consider the theories of specific jurisdictions. Nevertheless, the vast majority of states and jurisdictions have adopted the UTSA, thus rendering the strict property-based approach the exception to modern trade secret analyses.

IV. CONCLUSION

Supplementing trade secret law with NDAs is a valid mechanism for protecting information that does not qualify as a trade secret. Because the application of trade secret law is often ambiguous prior to litigation, allowing parties to contractually define protected information provides certainty. Further, the protection afforded by trade secret law (as compared to other areas of intellectual property law) suggests that supplementation of protection through contract is appropriate. It is also unlikely that NDAs will severely impede the flow of information that should not be protected. Agreements that restrict former employees are not favored in the law, and courts will not enforce any agreement that appears unreasonable based on the scope of the restraint. Importantly, proprietary information that does not qualify as a trade secret is protected independently of contract elsewhere in the law. Therefore, allowing contractual protection of such information does not expand protected information. It simply allows parties

133. Bone, *supra* note 6, at 244.
134. Group One v. Hallmark Cards, Inc., 254 F.3d 1041, 1049-50 (Fed. Cir. 2001).
135. *Id.*
136. *Id.*
137. *Id.* at 1051-52.
138. *See supra* note 33 and accompanying text.

to define protected information in an otherwise murky area of the law. Finally, the modern justifications underlying trade secret law suggest a role for contract law within the doctrine. Therefore, there is little danger in allowing parties in employment relationships to clarify and define *ex ante* protected proprietary information.

GLOBESPAN, INC. V. O'NEILL

By Danielle Pasqualone

To survive in a competitive business environment, an employer needs to retain a highly skilled workforce with the know-how to stay one step ahead of its rivals. In that same environment, however, an experienced employee stands to realize higher compensation and greater career satisfaction by frequently changing employers. The loss of an employee, especially one with trade secret information, may present a significant set-back to an employer's competitive edge. To prevent loss of trade secret information, an employer may attempt to enjoin an employee from working for a competitor by invoking the doctrine of inevitable disclosure.[1] This doctrine is based on the presumption that an employee cannot help but use or disclose her former employer's trade secrets in the performance of a new position having similar responsibilities. Because of its tension with public policy favoring employee mobility, state and federal jurisdictions have applied the doctrine sparingly and with considerable circumspection.

Following precedent from federal district courts, the Central District of California in *GlobeSpan, Inc. v. O'Neill* rejected the doctrine as counter to California's strong public policy favoring employee mobility as articulated under California Business and Professions Code Section 16600.[2] Although not subject to appellate review, *GlobeSpan* and its predecessors indicate that California federal courts have adopted a *per se* rule barring the doctrine in actions for trade secret misappropriation.

This Note argues that rejection of the doctrine as counter to public policy was improper. The doctrine does not fall within the intended scope of section 16600, which historically has been limited to the invalidation of contracts that encourage monopolistic practices. Further, a judicially created exception to section 16600 allows restraint of employee mobility where trade secrets are at stake. Therefore, the doctrine should at least survive a motion of summary judgment so that a court may properly weigh the evidence supporting the existence of trade secrets and their threatened disclosure, especially where disclosure would result in substantial, irreparable harm. To preserve the rights of employees, however, a court should

1. *See generally* JAMES POOLEY, TRADE SECRETS § 7.02[2][b][ii] (2001).
2. *See* GlobeSpan, Inc. v. O'Neill, No. CV 01-04350 LGB, 2001 WL 801609 (C.D. Cal. July 12, 2001); CAL. BUS. PROF. CODE § 16600 (West 1997).

apply the doctrine rarely and only when the evidence overwhelmingly supports an allegation of trade secret misappropriation.

I. LEGAL BACKGROUND

A. Introduction to Trade Secrets Law

Legal regimes that protect trade secrets provide businesses with an important incentive to create and develop new technologies.[3] Businesses can utilize proprietary information to their economic advantage only so long as it remains secret from competitors.[4] By punishing those who improperly disclose and use protected information, trade secrets law spurs innovation by providing an efficient means through which businesses can protect their investments in research and development.[5] Trade secrets law finds further support under theories of fairness and morality: it is simply wrong to steal the fruits of another's labor.[6] However, overbroad application of trade secrets law can interfere with competition and employee mobility.[7] Thus, trade secrets law must strike a careful balance between protecting business' proprietary information and promoting competition through employee mobility.[8]

Trade secrets doctrine, which originated as a common law tort, first emerged as a unified body of law in the Restatement (First) of Torts and later in the Uniform Trade Secrets Act ("UTSA").[9] Forty-two states, including California, and the District of Columbia have adopted the UTSA or a modified version of the UTSA.[10] The scope of subject matter protectable as a trade secret is broadly defined under the UTSA as follows:

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3. *See generally* ROBERT MERGES ET AL., INTELLECTUAL PROPERTY IN THE NEW TECHNOLOGICAL AGE 31-122 (2d ed. 2000).

4. RESTATEMENT (FIRST) OF TORTS § 757 cmt. b (1939).

5. *See* Susan Street Whaley, Comment, *The Inevitable Disaster of Inevitable Disclosure*, 67 U. CIN. L. REV. 809, 816 (1999).

6. *See* JOHN LOCKE, TWO TREATISES OF GOVERNMENT (Peter Laslett ed., Cambridge Univ. Press 1988) (1690); *see also* MERGES ET AL., *supra* note 3, at 43.

7. Whaley, *supra* note 5, at 840-41.

8. *Id.*

9. RESTATEMENT (FIRST) OF TORTS § 757 (1939); UNIF. TRADE SECRETS ACT, 14 U.L.A. 437-38 (1990 & Supp. 2001); *see* POOLEY, *supra* note 1, § 2.02[1] ("The first major effort at synthesis of the developing U.S. law of trade secrets was the *Restatement of Torts* . . . .").

10. Benjamin A. Emmert, Comment, *Keeping Confidence with Former Employees: California Courts Apply the Inevitable Disclosure Doctrine to California Trade Secret Law*, 40 SANTA CLARA L. REV. 1171, 1177 (2000).

> [I]nformation, including a formula, pattern, compilation, program, device, method, technique, or process, that: (i) derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use, and (ii) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.[11]

The UTSA further provides that "[a]ctual or threatened misappropriation [of a trade secret] may be enjoined."[12]

Trade secrets law in California generally follows the UTSA with minor modifications. California's version of the UTSA (hereinafter "CTSA") eliminates the "readily ascertainable" language in clause (i), thereby providing even broader protection.[13] Like the UTSA, section 3426.2(a) of the CTSA also provides for injunctive relief in the event of "[a]ctual or threatened misappropriation."[14] For a finding of trade secret misappropriation under the CTSA, California courts require that 1) the subject matter for which the plaintiff seeks protection is, in fact, a trade secret; 2) the defendant used, disclosed, or acquired knowledge of the trade secret, knowing the secret was acquired by improper means or in violation of a duty of confidentiality; and 3) public policy favoring protection of the trade secret outweighs the interest of the employee in using her knowledge to support herself in other employment.[15]

B. The Problem of the Departing Employee

The departing employee presents a potentially difficult problem for employers seeking to protect their trade secrets.[16] Typically, an employee acquires knowledge of her employer's trade secrets over the course of her employment, especially if she holds a position in management or technology development.[17] When the employee departs, she is allowed to take

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11. UNIF. TRADE SECRETS ACT, § 1(4).

12. *Id.* § 2(a).

13. CAL. CIV. CODE § 3426.1(d) (West 1997). Deletion of the "readily ascertainable" language essentially shifts the burden of proof from the plaintiff to the defendant. Under the UTSA, the plaintiff must show that the information was not readily ascertainable, while under the CTSA, the defendant has the burden of proving that the information was readily ascertainable to make her defense. John Allcock et al., *Overview of California Trade Secrets Law*, *in* TRADE SECRETS PRACTICE IN CALIFORNIA § 1.2 (2d ed. 1996).

14. CAL. CIV. CODE § 3426.2(a).

15. *See* CAL. CIV. CODE § 3426.1(b); GlobeSpan, Inc. v. O'Neill, No. CV 01-04350 LGB, 2001 WL 801609, at *5 (C.D. Cal. July 12, 2001); Danjaq, LLC v. Sony Corp., No. CV 97-8414-ER, 1999 WL 317629, at *1 (C.D. Cal. Mar. 11, 1999).

16. *See generally* MERGES ET AL., *supra* note 3, at 84-90.

17. *See, e.g.*, PepsiCo v. Redmond, 54 F.3d 1262, 1264-66 (7th Cir. 1995).

with her the general skills and knowledge acquired during her employment,[18] but she may not take away her employer's trade secrets.[19] To protect its trade secrets, the employer may attempt to prevent the employee from assuming a new job with a competitor either by enforcing a noncompetition agreement or by invoking the doctrine of inevitable disclosure.[20] In some cases, the employer may elect to pursue both strategies.[21]

A noncompetition agreement, also known as a "restrictive covenant" or a "covenant not to compete," bars an employee from working for a competitor, generally for a specified period of time following her departure.[22] In many cases, an employer will condition an offer of employment upon execution of a noncompetition agreement by the prospective employee.[23] Because noncompetition agreements arise during the hiring process, they are viewed as "bargained for" agreements under which the employee receives valuable consideration in exchange for her promise not to compete.[24]

Additionally, an employer may invoke the doctrine of inevitable disclosure to obtain injunctive relief when an employee leaves to work for a competitor.[25] In its application, the doctrine is an evidentiary presumption based on the premise that an employee cannot help but rely on her knowledge of a former employer's trade secrets in the performance of a new position having similar responsibilities.[26] Based on the weight of this evi-

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18. Official Aviation Guide Co. v. Am. Aviation Assocs., 150 F.2d 173, 178 (7th Cir. 1945); Morlife, Inc. v. Perry, 66 Cal. Rptr. 2d 731, 734 (Ct. App. 1997).

19. *Morlife*, 66 Cal. Rptr. 2d at 734; *see* Continental Car-Na-Var Corp. v. Moseley, 148 P.2d 9, 13 (Cal. 1944).

20. *See generally* MERGES ET AL., *supra* note 3, at 88-96.

21. *See, e.g.*, DoubleClick, Inc. v. Henderson, No. 116914/97, 1997 WL 731413 (N.Y. Sup. Ct. Nov. 7, 1997). Plaintiff employer relied on both a noncompetition agreement and the doctrine of inevitable disclosure to obtain injunctive relief.

22. Whaley, *supra* note 5, at 817.

23. *Id.*

24. *Id.* at 841. In reality, however, the relative bargaining positions of the employer and the prospective employee undermine the latter's ability to demand consideration. *See* State Farm Mut. Auto. Ins. Co. v. Dempster, 344 P.2d 821, 822 (Cal. Ct. App. 1959) (finding that insurance agents were given no opportunity to negotiate an employment contract containing a non-compete provision); *cf.* Latona v. Aetna U.S. Healthcare, Inc., 82 F. Supp. 2d 1089, 1096 (C.D. Cal. 1999) (arguing that an employee will comply with a noncompetition agreement even if she believes it to be unenforceable where the employer is large and powerful).

25. Whaley, *supra* note 5, at 819.

26. *Id.*; James Pooley, *The Sky Is Not Falling: When It Comes to Trade Secrets and Employee Mobility, a Little 'Inevitable Disclosure' Is Not Such a Bad Thing*, RECORDER, Nov. 1998, at S31; Michael Starr, *The Two Faces of Inevitable Disclosure*, MONDAQ BUS. BRIEFING, May 29, 2001, *available at* 2001 WL 8986722.

dence, a court may decide to enjoin an employee from assuming a new position with her former employer's competitor for a specified period of time, usually the time required for the secret to become "stale."[27] Alternatively, a court may issue an injunction allowing the employee to work for her former employer's competitor but limiting the scope of her duties to noncompeting products or services.[28] In principle, the former employer need not show actual misappropriation or even intent to misappropriate under the doctrine of inevitable disclosure.[29]

C. Recent Application of the Doctrine of Inevitable Disclosure

In the leading case of *PepsiCo v. Redmond*, the Seventh Circuit breathed new life into the doctrine of inevitable disclosure.[30] In this case, PepsiCo sought to enjoin defendant Redmond, a former employee, from working for its direct competitor, Quaker.[31] As a high-level executive, Redmond managed PepsiCo's entire business unit in California.[32] He acquired knowledge of PepsiCo's trade secrets, including its three-year strategic plan, pricing structure, plans for gaining further market share, and new product delivery system.[33] In 1994, Redmond left PepsiCo to accept a nearly identical position at Quaker, where he would implement marketing and distribution strategies for competing beverages nationwide.[34]

The court affirmed the lower court's order prohibiting Redmond from working for Quaker for six months and permanently enjoining him from disclosing confidential information.[35] In its opinion, the court stated that "unless Redmond possessed an uncanny ability to compartmentalize information, he would necessarily be making decisions about Gatorade and

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27. *See, e.g.*, PepsiCo v. Redmond, 54 F.3d 1262, 1272 (7th Cir. 1995) (granting injunction for six months); Lumex, Inc. v. Highsmith, 919 F. Supp. 624, 636 (granting injunction for six months).

28. *See, e.g.*, FMC Corp. v. Varco Int'l, Inc., 677 F.2d 500, 505 (5th Cir. 1982) (granting injunction that allowed defendant employee to work for new employer but prohibited new employer from placing employee in a "position that would create an inherent threat of disclosure"); Merck & Co. v. Lyon, 941 F. Supp. 1443, 1464-65 (M.D.N.C. 1996) (granting injunction that allowed defendant employee to work for new employer but prohibited him from working on specific competing products).

29. Matthew K. Miller, Note, *Inevitable Disclosure Where No Noncompetition Agreement Exists: Additional Guidance Needed*, 6 B.U. J. SCI. TECH. L. 9, ¶ 16 (2000).

30. *See* PepsiCo v. Redmond, 54 F.3d 1262 (7th Cir. 1995).

31. *Id.* at 1263.

32. *Id.* at 1264.

33. *Id.* at 1265-66.

34. *Id.* at 1266-67.

35. *Id.* at 1272.

Snapple by relying on his knowledge of [PepsiCo's] trade secrets."[36] In reaching its decision, the court also relied heavily on Redmond's lack of candor and "out and out lies" to PepsiCo regarding his negotiations with Quaker and his decision to accept their offer.[37]

Since *PepsiCo*, several state and federal district courts have applied the doctrine of inevitable disclosure in granting injunctions that restrain the mobility of departing employees.[38] However, many of these cases, like *PepsiCo*, demonstrate the courts' willingness to apply the doctrine only when the plaintiff has presented evidence that the departing employee was not forthcoming in disclosing her plans for new employment or otherwise acted in bad faith.[39] Some commentators interpret these decisions as limiting the doctrine's applicability to situations where there exists substantial evidence of "threatened" or intentional misappropriation.[40] Similarly, courts are reluctant to apply the doctrine in situations where the employer simply fears that the departing employee may inadvertently or unconsciously use or disclose her knowledge of trade secrets.[41] Therefore, the courts appear to require a substantial showing of threatened misappropriation in order to overcome the presumption of free employee mobility.

D. California Public Policy Favors Employee Mobility

California Business and Professions Code Section 16600 reflects the state's strong public policy favoring employee mobility.[42] Section 16600 provides that "every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void."[43] Under this statute, California courts have consistently rejected noncompetition agreements as counter to public policy that favors em-

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36. *Id.* at 1269.

37. *Id.* at 1267, 1270.

38. *See, e.g.*, DoubleClick, Inc v. Henderson, No. 116914/97, 1997 WL 731413 (N.Y. Sup. Ct. Nov. 7, 1997); Uncle B's Bakery, Inc. v. O'Rourke, 920 F. Supp. 1405 (N.D. Iowa 1996); Merck & Co. v. Lyon, 941 F. Supp. 1443 (M.D.N.C. 1996); Novell, Inc. v. Timpanogos Research Group, Inc., 46 U.S.P.Q.2d (BNA) 1197 (Utah D. Ct. 1998).

39. *See DoubleClick*, 1997 WL 731413, at *6; *Uncle B.'s Bakery, Inc.*, 920 F. Supp. at 1419; *Merck & Co.*, 941 F. Supp. at 1461; *Novell, Inc.*, 46 U.S.P.Q.2d (BNA) at 1204. *See infra* notes 112-124 and accompanying text. See also Miller, *supra* note 29, ¶¶ 43-49, for a general discussion of the implicit "bad faith" requirement.

40. Miller, *supra* note 29, ¶ 49; Starr, *supra* note 26.

41. *See, e.g.*, Int'l Bus. Mach. Corp. v. Seagate Tech., Inc., 941 F. Supp. 98, 101 (D. Minn. 1992) (on remand from the Eighth Circuit).

42. *See* Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 900-01 (Ct. App. 1998).

43. CAL. BUS. PROF. CODE § 16600 (West 1997).

ployee mobility.[44] Courts in most other states, on the other hand, apply a "rule of reason" in determining whether to uphold noncompetition agreements.[45]

The policy reasons supporting section 16600 are based first and foremost on the long-held proposition that "every citizen shall retain the right to pursue any lawful employment and enterprise of their choice."[46] Judicial enforcement of this right protects the fundamental interests of the individual in her own mobility and betterment.[47] Failure to defend this right could deprive an individual of her livelihood.[48] Additionally, section 16600 supports California's interest in "protecting the freedom of movement of persons whom California-based employers . . . wish to employ."[49] Under this rationale, section 16600 benefits both California employees and employers by facilitating and promoting employers' access to potential employees.[50] Finally, section 16600 supports the public's interest in efficiency and productivity by allowing the public to benefit from the exercise of an individual's specialized knowledge and expertise.[51]

Supporting this policy, several commentators have attributed the success of Silicon Valley, California's technology center, to the mobility of its employees[52] and particularly to section 16600.[53] Lacking the restraints of noncompetition agreements, the job-hopping culture of Silicon Valley has encouraged the "spill-over" of knowledge among established technology firms and start-ups.[54] Although such spill-overs may put trade secrets at risk, their overall effect is to promote innovation and invention.[55] These benefits appear to have exceeded the potential costs of trade secret disclo-

44. *See* Muggill v. Reuben H. Donnelly Corp., 398 P.2d 147, 149 (Cal. 1965); *Application Group, Inc.*, 61 Cal. App. 4th at 901.

45. *See* Scott v. Snelling & Snelling, Inc., 732 F. Supp. 1034, 1042 (N.D.Cal. 1990).

46. *Application Group, Inc.*, 61 Cal. App. 4th at 900.

47. *See id.* (citing Diodes, Inc. v. Franzen, 67 Cal. Rptr. 19, 26 (Ct. App. 1968)).

48. *See* State Farm Mut. Auto. Ins. Co. v. Dempster, 344 P.2d 821, 825 (Cal. Ct. App. 1959).

49. *Application Group, Inc.*, 61 Cal. App. 4th at 900-01.

50. *See id.*

51. *See, e.g.*, Wright v. Ryder, 36 Cal. 342, 360-62 (1868).

52. *See generally* ANNALEE SAXENIAN, REGIONAL ADVANTAGE: CULTURE AND COMPETITION IN SILICON VALLEY AND ROUTE 128 (1994).

53. *See* Ronald J. Gilson, *The Legal Infrastructure of High Technology Industrial Districts: Silicon Valley, Route 128, and Covenants Not To Compete*, 74 N.Y.U. L. REV. 575 (1999).

54. *Id.* at 579, 585-86.

55. *Id.*

sure, as demonstrated by the rapid expansion and sustained growth of Silicon Valley compared to other technology centers in the United States.[56]

E. Rejection of Inevitable Disclosure in Federal Court

Until recently, it was unclear whether the doctrine of inevitable disclosure applied to cases in both California and the Ninth Circuit.[57] Some state court decisions suggested that it could.[58] In *Advanced Micro Devices, Inc. v. Hyundai Electronics America*, plaintiff Advanced Micro Devices ("AMD") filed a complaint against defendant Hyundai alleging misappropriation of trade secrets when Hyundai created a competing "flash memory" division.[59] Hyundai staffed its new division by hiring several former AMD employees with knowledge of AMD's proprietary flash memory technology. Although AMD presented no direct evidence of misappropriation, it convinced the court that disclosure of its trade secrets by its former employees was inevitable.[60] On this basis, the court issued a preliminary injunction blocking the former AMD employees from working on certain projects for Hyundai.[61]

In *Electro Optical Industries, Inc. v. White*, the Court of Appeal for the Second Appellate District stated in dicta that "[a]lthough no California court has yet adopted it, the inevitable disclosure doctrine is rooted in common sense and calls for a fact specific inquiry. We adopt the rule here."[62] Notwithstanding its approval of the doctrine, the court did not actually apply it in its decision.[63] Instead, the court affirmed the lower court's denial of plaintiff's motion for a preliminary injunction, finding that the disputed trade secrets either were not known by the defendant or were not in fact secret.[64] Nonetheless, several commentators viewed this decision as an affirmative adoption of the doctrine of inevitable disclosure

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56. *Id.* at 609.

57. Gary E. Weiss & Sean A. Lincoln, *Accepting the Inevitable: The California Court of Appeal Has Finally Adopted the Trade Secret Doctrine of 'Inevitable Disclosure,'* RECORDER, Feb. 2000, at S6.

58. *See* cases cited *infra* notes 59 and 62.

59. First Amended Complaint, Advanced Micro Devices, Inc. v. Hyundai Elecs. Am., No. CV 752679 (Cal. Super. Ct. Oct. 24, 1995); *see also* Emmert, *supra* note 10, at 1192-96.

60. Emmert, *supra* note 10, at 1195.

61. *Id.* The case later settled.

62. Electro Optical Indus., Inc. v. White, 90 Cal. Rptr. 2d 680, 684 (Ct. App. 1999), *ordered depublished* (April 12, 2000).

63. *See id.*

64. *Id.* at 685.

by California.[65] However, the California Supreme Court later depublished this decision.[66]

In contrast to state court doctrine, recent cases from federal district courts in California have summarily rejected the doctrine. In *Danjaq, LLC v. Sony Corp.*, the court stated outright that plaintiffs could not rely on the inevitable disclosure doctrine as articulated in *PepsiCo* because "*PepsiCo* is not the law of the State of California or the Ninth Circuit."[67] In *Computer Sciences Corporation v. Computer Associates International, Inc.*, the plaintiffs did not invoke the doctrine to support a claim for injunctive relief but instead attempted to use the doctrine as evidence supporting actual misappropriation.[68] In granting summary judgment for the defendants, the court held that a plaintiff alleging actual misappropriation could not rely on the doctrine to fill in gaps in the evidentiary record.[69]

In *Bayer Corp. v. Roche Molecular Systems, Inc.*, the Northern District of California similarly held that "California trade secrets law does not recognize the theory of inevitable disclosure; indeed, such a rule would run counter to the strong public policy in California favoring employee mobility."[70] The court found that the doctrine creates an *ex post facto* covenant not to compete, and, as such, is properly rejected under section 16600.[71] The court further noted that the doctrine "does not supply the proof needed to . . . raise serious questions about actual use or threat [of misappropriation],"[72] suggesting that evidence of inevitable disclosure would never suffice to support a plaintiff's claim of misappropriation. By denying recognition of the doctrine of inevitable disclosure in California, the decisions in *Danjaq*, *Computer Sciences*, and *Bayer* established precedent in the dis-

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65. *See* Emmert, *supra* note 10, at 1200-01; Weiss & Lincoln, *supra* note 57.

66. Electro Optical Indus., Inc. v. White, 90 Cal. Rptr. 2d 680 (Ct. App. 1999), *ordered depublished* (April 12, 2000).

67. Danjaq, LLC v. Sony Corp., No. CV 97-8414-ER, 1999 WL 317629, at *1 n.1 (C.D. Cal. Mar. 11, 1999).

68. Computer Scis. Corp. v. Computer Assocs. Int'l Inc., Nos. CV 98-1374-WMB SHX, CV 98-1440-WMB SHX, 1999 WL 675446 (C.D. Cal. Aug. 12, 1999).

69. *Id* at *16.

70. Bayer Corp. v. Roche Molecular Sys., Inc., 72 F. Supp. 2d 1111, 1120 (N.D. Cal. 1999).

71. *Id.* at 1119. Application of the doctrine of inevitable disclosure necessarily results in an *ex post facto* or judicially implied covenant not to compete. If disclosure is truly inevitable, then the only effective remedy is injunctive relief prohibiting the employee from assuming a competing position. An alternative form of relief, for example, allowing the employee to assume a competing position but enjoining the use or disclosure of the trade secret, would prove ineffectual because disclosure is outside the power of the employee to consciously prevent or control.

72. *Id.* at 1112.

trict courts of the Ninth Circuit, thus laying the groundwork for the decision rendered in *GlobeSpan*.

II. CASE SUMMARY

A. Facts and Procedural Posture

Plaintiff GlobeSpan, Inc., a New Jersey corporation, employed defendant John O'Neill for nearly three years as a Market Development Manager and Product Line Manager in its "DSL" division.[73] O'Neill left GlobeSpan to work for defendant Broadcom, a California corporation and one of GlobeSpan's direct competitors.[74] Defendants O'Neill and Broadcom first filed suit in California seeking declaratory relief for non-misappropriation of trade secrets, and alleging unfair competition.[75] GlobeSpan later filed suit in New Jersey state court alleging, *inter alia*, misappropriation of trade secrets.[76] The defendants removed the action from New Jersey state court to New Jersey federal district court on the grounds of diversity of citizenship.[77] The New Jersey federal district court transferred the action to the Central District of California for consolidation with the defendants' first filed suit.[78]

GlobeSpan's complaint set forth the following counts: 1) misappropriation of trade secrets against defendants O'Neill and Broadcom; 2) unfair competition against defendants O'Neill and Broadcom; and 3) breach of the duty of loyalty against defendant O'Neill.[79] GlobeSpan further moved to enjoin O'Neill from entering into an employment contract with Broadcom for at least one year.[80] The court granted Broadcom's motions to dismiss counts one and two on the grounds that the inevitable disclosure doctrine does not provide a sufficient basis to support either of these allegations.[81]

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73. GlobeSpan, Inc. v. O'Neill, No. CV 01-04350 LGB, 2001 WL 801609, at *1 (C.D. Cal. July 12, 2001).

74. *Id.*

75. *Id.*

76. *Id.*

77. *Id.*

78. *Id.*

79. *Id.*

80. *Id.*

81. *Id.* at *7. The court did not address in its opinion count 3 of the complaint.

B. The Court's Analysis of Plaintiff's Trade Secrets Misappropriations Claim

Relying on the *Bayer*, *Computer Sciences*, and *Danjaq* decisions, the court rejected GlobeSpan's argument that the inevitable disclosure doctrine, on its own, supports a claim for actual misappropriation of trade secrets. In a brief opinion, Judge Baird stated that "[t]he Central District of California [in *Computer Sciences* and *Danjaq*] has considered and rejected the inevitable disclosure doctrine."[82] Citing *Bayer*, the court noted that California trade secrets law does not recognize the doctrine of inevitable disclosure, which runs counter to the strong public policy in California favoring employee mobility.[83] On these grounds, the court subsequently concluded that the doctrine of inevitable disclosure failed to prove that defendant Broadcom actually used or disclosed plaintiff's trade secrets.[84]

The court also rejected GlobeSpan's claim on the grounds that the "Plaintiff has not alleged that either Defendants Broadcom or O'Neill *will* use or disclose Plaintiff's trade secrets."[85] By this statement, the court apparently acknowledged that a plaintiff might bring a valid claim under section 3426.2(a), which allows injunctive relief for "threatened misappropriation." However, the court's holding, like that in *Bayer*, implied that the doctrine of inevitable disclosure could under no circumstances meet the evidentiary requirements for such a claim.[86]

III. ANALYSIS

A. Section 16600 Does Not Reach the Doctrine of Inevitable Disclosure

1. The Intended Scope of Section 16600

Section 16600 was originally adopted in 1872 as section 1673 of the California Civil Code.[87] The purpose of section 1673 was to invalidate contracts that restrained trade by restricting competition.[88] The cases cited in the comment to section 1673 generally involved contracts for the sale of

82. *Id.* at *6.
83. *Id.*
84. *Id.*
85. *Id.* (emphasis added).
86. *See id.* at *6.
87. CAL. CIV. CODE § 1673 (1872) (repealed 1941) ("Every Contract by which anyone is restrained from exercising a lawful profession, trade, or business of any kind, otherwise than is provided by the next two sections, is to that extent void.").
88. Gilson, *supra* note 53, at 618-19 & n.152 (1999).

goods used in a trade or business conditioned upon a promise by either the buyer or seller not to compete.[89] These cases did not involve the application of restrictive covenants to former employees, nor did they address issues concerning trade secrets.[90] Therefore, the adoption of section 1673 occurred outside the employment context, primarily for the purpose of promoting free trade and preventing monopolies.

The Supreme Court of California later applied section 1673 to invalidate restrictive covenants that prohibited departing employees from competing with their former employers.[91] In these cases, the employees took with them only general skills and knowledge, not their employers' trade secrets.[92] Therefore, the employers' purpose in attempting to enforce these covenants could not have been to protect specific trade secrets. More likely, the employers sought to stifle competition by limiting the availability of a generally skilled workforce.[93] Consistent with the purpose of section 1673, the California Supreme Court properly rejected these broad-reaching covenants as restraining trade and fostering monopolies.[94]

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89. *See* § 1673 cmt. (citing Wright v. Ryder, 36 Cal. 342 (1868) (voiding as counter to public policy a contract for the sale of a steam boat that precluded operation of the boat in the waters of California); More v. Bonnet, 40 Cal. 251 (1870) (voiding as counter to public policy a contract for the sale of roofing tools and materials wherein the seller promised not to engage in a competitive roofing business in the state of California)). *But see* California Steam Navigation Co. v. Wright, 6 Cal. 258 (1856). Under the disputed contract, which did not involve the sale of goods, defendant received consideration for a promise not to navigate certain waters of California for three years. The California Supreme Court reversed the lower court's dismissal of plaintiff's breach of contract suit.

90. *See* cases cited *supra* note 89.

91. Davis v. Jointless Fire Brick Co., 300 F. 1 (9th Cir. 1924) (relying on section 1673 to dissolve an injunction prohibiting a salesman from selling brick and cement products in competition with his former employer); Merchants' Ad-Sign Co. v. Sterling, 57 P. 468 (Cal. 1989) (voiding under section 1673 a covenant not to compete in a suit brought by an employer against a former manager and stockholder who established a competing advertising business). *Cf.* Chamberlain v. Augustine, 156 P. 479 (Cal. 1916) (voiding under section 1673 a contract for the sale of stock wherein the stock purchaser agreed not to engage in a competing business).

92. *See* cases cited *supra* note 91.

93. *See* Maureen B. Callahan, *Post-Employment Restraint Agreements: A Reassessment*, 52 U. CHI. L. REV. 703, 715 (1985). ("An employer with market dominance . . . may be able to use post-employment restraints to prolong that position by reducing the dissemination of knowledge that would allow others to compete effectively with the employer or by restricting the number of potential competitors . . . the employer may attempt to preserve market power simply by preventing the employee from using his skills in competition with the employer.").

94. The preponderance of cases decided by the California Supreme Court under section 1673 emphasizes the antitrust purpose of this section. *See* Vulcan Powder Co. v. Hercules Powder Co., 31 P. 581 (Cal. 1892) (rejecting under section 1673 a contract that

Currently, many employers continue to require restrictive covenants from employees at all levels, regardless of whether these employees will become aware of trade secrets.[95] Because these covenants are broadly imposed upon employees who only have general knowledge and skills, their primary purpose is probably not to protect trade secrets, but to deprive competitors of skilled employees. Because these covenants are similar in purpose and scope to those previously rejected under section 1673, California courts should reject them under section 16600 as anti-competitive and monopolistic.

In contrast, judicially created restrictive covenants compelled by the doctrine of inevitable disclosure restrain employee mobility for the purpose of protecting trade secrets. Because a legitimate and lawful motivation underlies the formation of these covenants, they are of a substantially different character than those contemplated by section 16600 and its predecessor, section 1673. Therefore, the courts should not view such judicially created restrictive covenants through the same critical lens of section 16600. To do so would impermissibly expand section 16600 beyond its intended scope, which historically has been limited in its inception and its application to the invalidation of contracts that purposefully contravene antitrust doctrine.

2. *A Judicially Created Exception to Section 16600*

Even if the doctrine of inevitable disclosure creates an *ex post facto* restrictive covenant that violates the policy goals of section 16600, the doc-

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fixed prices by a syndicate of dynamite manufacturers); Getz Bros. v. Fed. Salt Co., 81 P. 416 (Cal. 1905) (rejecting under section 1673 and the Sherman Act a contract whereby defendants agreed to purchase all their salt requirements from plaintiffs and to discourage "in any possible manner any such shipments or importations of salt [to the Pacific coast] by any other parties"); Morey v. Paladini, 203 P. 760 (Cal. 1922) (rejecting under section 1673 and the Sherman Act a contract whereby plaintiff suppliers agreed not to sell lobsters to anyone but defendants so that the latter would be guaranteed an exclusive right to the sale of lobsters in the Pacific coast states); Endicott v. Rosenthal, 16 P.2d 673 (Cal. 1932) (rejecting under section 1673 a contract that fixed prices by a syndicate of dry cleaners).

95. Leslie Miller, Associated Press, *Noncompete Clauses Hurt Job Hunters; Companies Protect Corporate Secrets from Rival Firms* (Sept. 11, 2001) ("Companies that once limited noncompete agreements to top executives . . . are now asking rank-and-file workers to sign them."), *available at* 2001 WL 3769828; *NBC News Today: The Prevalence Today of Noncompete Agreements with Employers and How They Affect Employees' Futures* (NBC television broadcast, July 24, 2001) (reporting on a noncompetition agreement enforced against a mattress salesman). "[I]t's a growing trend in American business. As corporations try to protect their competitive edge, noncompetes are no longer just for top level executives." *Id.*

trine nonetheless falls squarely within a judicially created exception to section 16600. State and federal courts in California have consistently recognized, albeit in dicta, that restrictive covenants are enforceable where necessary to protect an employer's trade secrets.[96] For example, the California Supreme Court in *Muggill v. Reuben H. Donnelly Corp.* stated that section 16600 "invalidates provisions in employment contracts prohibiting an employee from working for a competitor after completion of his employment or imposing a penalty if he does so, *unless they are necessary to protect the employer's trade secrets*."[97] Recently, the Northern District of California in *Scott v. Snelling and Snelling, Inc.*, confirmed that "California courts recognize a judicially created exception to section 16600 and will enforce a restrictive covenant" if a former employee uses a former employer's trade secrets or otherwise commits unfair competition.[98] Notwithstanding their approval of this exception to section 16600, California courts have yet to actually apply it.[99]

In view of this judicially created "trade secrets" exception to section 16600, the court in *GlobeSpan* should not have summarily rejected the doctrine of inevitable disclosure as counter to section 16600 without first determining whether the exception applied. In making this determination, the court should have examined the evidence to ascertain whether O'Neill's former employer actually possessed trade secrets. If so, the court should have determined under the *Muggill* standard whether injunctive relief was "necessary to protect the employer's trade secrets"[100] Thus,

96. *See* Muggill v. Reuben H. Donnelly Corp., 42 Cal. Rptr. 107, 109 (1965); Scott v. Snelling and Snelling, Inc., 732 F. Supp. 1034, 1043 (N.D. Cal. 1990); Roll Systems, Inc. v. Shupe, No. 97-12689-GAO, 1998 U.S. Dist. LEXIS 3142, at *6 n.1 (D. Mass. Jan. 22, 1998) (applying California law). As authority for this judicially created exception, *Muggill* cites *Gordon v. Landau*, 321 P.2d 456 (Cal. 1958). In this case, the California Supreme Court held that an employment contract prohibiting a salesman from divulging or soliciting clients from a carefully cultivated customer list for one year after termination did not violate section 16600 and was otherwise enforceable. *Id.*

97. *Muggill*, 42 Cal. Rptr. at 109 (emphasis added; internal citations omitted). This direct quotation from *Muggill* has since been cited with approval by California appellate courts. Metro Traffic Control, Inc. v. Shadow Traffic Network, 22 Cal. App. 4th 853, 859 (Ct. App. 1994); Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 900 (Ct. App. 1998).

98. *Scott*, 732 F. Supp. at 1043 (citing Hollingsworth Solderless Terminal v. Turley, 622 F.2d 1324, 1338 (9th Cir. 1980)). The court in *Scott* concluded that the judicially created exception to section 16600 "appears to remain a proper statement of the law in California." *Id.*

99. *See Scott*, 732 F. Supp. at 1044-45 (finding that plaintiff's failure to prove the existence of trade secrets precluded application of the exception to section 16600); Gilson, *supra* note 53, at 607-08.

100. *Muggill*, 42 Cal. Rptr. at 109.

summary judgment in favor of the defendant based on section 16600 was improper where there remained a question of fact as to whether the evidence met this standard.

The judicially created "trade secrets" exception to section 16600 and its application to the doctrine of inevitable disclosure strike an appropriate balance between trade secret protection and the policy interests of section 16600 in free employee mobility. The California Court of Appeal's approach in *Diodes, Inc. v. Franzen* supports such a balance.[101] In this case, the court held that "[t]he interests of the employee in his own mobility and betterment are deemed paramount to the competitive business interests of the employers, *where neither the employee nor his new employer has committed any illegal act accompanying the employment change*."[102] Therefore, restraints on employee mobility to prevent an illegal act, such as trade secret misappropriation, are reasonable and appropriate, notwithstanding section 16600.

B. Subjecting Inevitable Disclosure Claims to Strict Scrutiny

1. Availability of Inevitable Disclosure in California

Summary judgment based solely on the grounds that the doctrine of inevitable disclosure conflicts with section 16600 is a conclusory and improper outcome. However, the question remains as to whether evidence of "inevitable disclosure," absent evidence of actual misappropriation or intent to misappropriate, is *ever* sufficient to support a claim of trade secret misappropriation.

To argue that evidence of inevitable disclosure can never support a misappropriations claim is to bar application of the doctrine as a matter of law. The district courts' holdings in *Bayer* and *GlobeSpan* apparently adopt such a *per se* rule.[103] Although *Bayer* and *GlobeSpan* eliminate the current uncertainty surrounding the doctrine by providing a bright-line rule against it, barring the doctrine without exception may prove unreasonable given the irreparable consequences of trade secret misappropriation. In most cases, there exists no adequate remedy for loss of a trade secret: "[a] trade secret, once lost, is lost forever; its loss cannot be measured in money damages."[104] Consequently, "preventing the disclosure of trade secrets is far preferable to suing for misappropriation after they have

101. *See* Diodes, Inc. v. Franzen, 67 Cal. Rptr. 19 (Ct. App. 1968).

102. *Id.* at 26 (emphasis added).

103. *See supra* notes 70 and 82 and accompanying text.

104. Earthweb, Inc. v. Schlack, 71 F. Supp. 2d 299, 308 (S.D.N.Y. 1999), *aff'd*, No. 99-9302, 2000 WL 1093320 (2d Cir. May 18, 2000).

already been disclosed."[105] Therefore, the doctrine should remain available as a means for preventing the potentially irreversible damage caused by trade secret misappropriation.

2. *Bootstrapping Evidence of Inevitable Disclosure with Additional Case-Specific Factors*

Although the doctrine of inevitable disclosure serves a legitimate purpose in trade secrets law, there exists a serious potential for abuse of the doctrine if it is applied in an overly broad manner. For example, overzealous employers may use the doctrine to bring suits that lack merit in an attempt to intimidate or even cripple the competition, particularly when the competition is a resource-limited start-up.[106] Strategic use of the doctrine in this manner appears to be particularly prevalent in the high-tech industry, where employers often take a highly personal and emotional interest in protecting their trade secrets.[107] Employees in the midst of such lawsuits

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105. MERGES ET AL., *supra* note 3, at 92.

106. *See* Vikas Bajaj, *Alcatel Guards Its Trade Secrets: Lashed by Industry Critics, VP Makes No Apologies for Lawsuits*, DALLAS MORNING NEWS, Sept. 3, 2000, at 1H, *available at* 2000 WL 25850899 (reporting that general counsel's policy of "aggressively suing competitors" for alleged trade secret misappropriation has brought "hundreds of millions in settlements and judgments into Alcatel coffers," with one critic contending that "they [Alcatel] don't seem to be able to differentiate between where they have merit and don't have merit"); Renee Deger, *Clash: Trade Secrets, Workers Rights, but High-Tech Companies Aren't Rushing To Test "Inevitable Disclosure"*, THE RECORDER, June 18, 1998, at 1 (reporting that Silicon Graphics dropped its suit against former employees who started their own company, possibly because the suit lacked merit); *see also infra* note 107 and accompanying text.

107. Gilson, *supra* note 53, at 629 n.70 (describing a newspaper advertisement placed by Oracle in the San Francisco Examiner). Oracle's advertisement apparently attempted to embarrass the CEO of its archrival Informix. The advertisement describes how, after eleven key research engineers left Informix to join Oracle, the CEO of Informix confronted the CEO of Oracle at his home, demanding that he return the eleven "runaway" employees. Informix filed suit for trade secret misappropriation the next day. *Id.* Four months later, Informix dropped its suit after learning "through the legal discovery process" that neither Oracle nor the departed employees misappropriated any Informix trade secrets. No money changed hands in the settlement. *Informix Corp.: Allegations Against Oracle Erroneous, Suit Is Dropped*, WALL ST. J., June 10, 1997, at B11. In a prepared statement, Informix informed the press that it "regret[ted] any statements or allegations that the engineers misappropriated any trade secrets or disclosed them to Oracle." *Informix Drops Lawsuit Against Oracle; Firm Regrets Charge of Stealing Trade Secrets Through Hires*, S.F. EXAMINER, June 10, 1997, at C-1. *See also* Deger, *supra* note 106 ("Trade secret cases are very emotional and tough to settle, because each side believes that only its cause is just and that the other party has ulterior motives."); Joseph A. Slobodzian, *AT&T Sued over Departed VP: Is the Issue Trade Secrets, or Jealousy, in Case Involving Qwest?*, NAT'L L.J., Aug. 21, 2000, at B1.

experience feelings of persecution and oppression.[108] Thus, if not rationally applied and appropriately limited, the doctrine of inevitable disclosure could have a chilling effect on entrepreneurship, innovation, and employee productivity.[109]

Therefore, courts should view evidence presented under the rubric of the inevitable disclosure doctrine with an extremely critical eye. The District Court for the Southern District of New York presented a useful framework for applying the doctrine:

> [I]n its purest form, the inevitable disclosure doctrine treads an exceedingly narrow path through judicially disfavored territory. *Absent evidence of actual misappropriation by an employee, the doctrine should be applied in only the rarest of cases.* Factors to consider in weighing the appropriateness of granting injunctive relief are whether: (1) the employers in question are direct competitors . . . (2) the employee's new position is nearly identical to his old one, such that he could not reasonably be expected to fulfill his new job responsibilities without utilizing the trade secrets of his former employer; and (3) the trade secrets at issue are highly valuable to both employers. Other case-specific factors such as the nature of the industry and trade secrets should be considered as well.[110]

The three factors enumerated above form the core of an inevitable disclosure case. However, these factors alone should not form the basis for injunctive relief. In the discussion that follows, this Note seeks to clarify and propose additional case-specific factors that would tip the balance either in favor of or against the plaintiff employer, once she has shown that the "core" factors weigh in favor of proving inevitable disclosure. These additional factors include dishonesty or bad faith motive of the employee, the nature of the trade secret, and the nature of the industry.

a) Dishonesty/lack of candor as evidence of intent to misappropriate

In *PepsiCo*, the court held that "a plaintiff may prove a claim of trade secret misappropriation by demonstrating that defendant's new employment will inevitably lead him to rely on the plaintiff's trade secrets."[111] However, the court in *PepsiCo* also conceded that "the mere fact that a

108. *See* Bajaj, *supra* note 106.

109. *Id.*

110. Earthweb, Inc. v. Schlack, 71 F. Supp. 2d 299, 310 (S.D.N.Y. 1999) (emphasis added), *aff'd*, No. 99-9302, 2000 WL 1093320 (2d Cir. May 18, 2000).

111. PepsiCo v. Redmond, 54 F.3d 1262, 1269 (7th Cir. 1995).

person assumed a similar position at a competitor does not, *without more*, make it inevitable that he will use or disclose . . . trade secret information."[112] The court then relied heavily on the defendants' deceptive statements and lack of candor in reaching its decision to grant injunctive relief.[113] The court based its decision, therefore, as much on its intuition that Redmond lacked credibility as on the inevitability of disclosure.[114]

Courts in other jurisdictions have followed suit, generally requiring a showing of dishonesty or bad faith on the part of the departing employee or the new employer.[115] As in *PepsiCo*, a North Carolina district court found in *Merck & Co. v. Lyon* that defendant Lyon "was not entirely forthright in his representations to plaintiffs regarding his [future] employment with [defendant] Glaxo."[116] The court subsequently crafted a narrow injunction permitting Lyon to assume employment at Glaxo while preventing him from working on a particular product line.[117] Similarly, in *DoubleClick, Inc. v. Henderson*, the departing employees left evidence on their laptops suggesting that they intended to incorporate their former employer's confidential information into their own start-up's business plan.[118] The court further remarked upon the employees' "cavalier attitude toward their duties to their former employer."[119] The court subsequently issued a six month preliminary injunction blocking the employees from competing with their former employer.[120]

Dishonesty on the part of the employee or her new employer speaks to the issue of intent. It provides circumstantial evidence of the parties' willingness to misappropriate trade secrets and their efforts to conceal as much. Similarly, the degree to which the new employer pursued or heavily recruited the employee speaks to the issue of whether the new employer intentionally recruited the employee for her knowledge of trade secrets rather than for her general skills and experience.[121] The presence of either

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112. *Id.* (emphasis added; internal quotations omitted).

113. *Id.* at 1271-72.

114. *See* 1 ROGER M. MILGRIM, MILGRIM ON TRADE SECRETS § 5.02[3][d] (2001).

115. *See* sources cited *supra* note 39.

116. Merck & Co. v. Lyon, 941 F. Supp. 1443, 1461 (M.D.N.C. 1996).

117. *Id.* at 1464-65.

118. DoubleClick, Inc. v. Henderson, No. 116914/97, 1997 WL 731413, at *5 n.3 (N.Y. Sup. Ct. Nov. 7, 1997).

119. *Id.* at *6.

120. *Id.* at *8.

121. *See, e.g.*, PepsiCo v. Redmond, 54 F.3d 1262, 1271 (7th Cir. 1995) ("The [lower] court also pointed out that Quaker . . . seemed to express an unnatural interest in hiring PCNA [PepsiCo] employees: all three of the people interviewed for the position Redmond ultimately accepted worked at PCNA. [Quaker] may well have focused on re-

or both of these factors should weigh in favor of the former employer. Conversely, good faith efforts on the part of the employee and her new employer to prevent disclosure of trade secrets should weigh in favor of the employee.[122]

b) Nature of the trade secret and the industry

i) Technological information

Trade secrets, in the form of technological information, lie along a spectrum. At one end of the spectrum lies the "classic" trade secret case in which an employer, generally an industry leader, has developed a pioneering technological advance over many years and at great expense.[123] An employee then leaves to join a new employer who has previously tried and failed to develop the same technology or otherwise has no previous history of independent development of this technology.[124] In this scenario, the employer should be entitled to broad trade secret protection and, accordingly, a court should give substantial weight to evidence of inevitable disclosure.[125] This approach is modeled after the broad protection that is often accorded to "pioneer" patents.[126]

At the other end of the spectrum lie trade secrets developed in a high-tech industry where innovations occur rapidly and mainly through improvements on pre-existing technologies. In this scenario, the employer should only be entitled to narrow trade secret protection.[127] Absent evi-

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cruiting PCNA employees because . . . they were good and not because of their confidential knowledge. Nonetheless, the district court, after listening to the witnesses, determined otherwise. That conclusion was not an abuse of discretion."); FMC Corp. v. Varco Int'l, Inc., 677 F.2d 500, 501 (5th Circ. 1982) (finding that defendant employer solicited an employee from its competitor due to the employee's "precise competitive background"); Merck & Co. v. Lyon, 941 F. Supp. 1443, 1461 (M.D.N.C. 1996) (noting that there was "no evidence that Glaxo thought to recruit Lyon because of his knowledge of plaintiffs' trade secrets").

122. *See Merck & Co.*, 941 F. Supp. at 1460-61 (finding that "some type of limited injunction would be appropriate . . . because Glaxo has not shown that it has made any efforts to prevent potential disclosure of plaintiff's trade secret information").

123. *See* 1 MILGRIM, *supra* note 114, § 5.02[3][d] (discussing E.I. Du Pont de Nemours & Co. v. Am. Potash & Chem. Corp., 200 A.2d 428 (Del. Ch. 1964)).

124. *Id.*

125. *Id.*

126. MERGES ET AL, *supra* note 3, at 134.

127. *See* Intel Corp. v. Broadcom Corp., No. CV 788310, 2000 WL 33260713 (Cal. Super. Ct. June 20, 2000) (crafting narrow injunctive relief where employees left one leading chipmaker to join another); *see also* Karen Alexander, *Ruling Boosts Ability To Hire from Competitors Courts: Intel Loses Bid for Injunction, but Suit Accusing Broad-*

dence of actual misappropriation or intent to misappropriate, inevitable disclosure should not provide a basis for injunctive relief for two reasons. First, the line between general knowledge and trade secrets is blurred in "improvement-based" technologies.[128] Therefore, a court should give the employee the benefit of the doubt. Second, restraints on employee mobility could impede the progress of improvement-based technologies. Therefore, a court should adopt a legal framework that encourages the knowledge "spill-over" viewed by some commentators as key to innovation.[129] This approach is modeled after the narrow protection that is often accorded to "improvement" patents.[130]

In a rapidly evolving technology-based environment, narrow protection for trade secrets (and increased employee mobility) may appear to disadvantage those employers who lose employees with knowledge of trade secrets. However, the effect is reciprocal: an employer who is disadvantaged by the loss of an employee may just as likely gain an employee with innovative knowledge.[131] Therefore, the proper inquiry asks whether the trade secret is so pioneering and so valuable that the loss of the employee, and possibly the secret, is unlikely to be offset by the future gain of an employee with knowledge that can spur further innovation. If not, a finding of inevitable disclosure should not be dispositive. Instead, evidence of actual misappropriation or intent to misappropriate should be required.

ii) Business information

Business information, such as business plans, pricing strategies, marketing strategies, and the like, should generally receive even narrower trade secret protection compared with technology-based trade secrets.[132] This approach is recommended due to the difficulty in valuing business information and in establishing that such information is, in fact, a trade secret.[133] Although businesses generally maintain the confidentiality of

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com of Gleaning Secrets from Ex-Employees Will Proceed, L.A. TIMES, May 27, 2000, at C1.

128. Gilson, *supra* note 53, at 599.

129. *Id.* at 579.

130. MERGES ET AL, *supra* note 3, at 134.

131. *See* Gilson, *supra* note 53, at 609.

132. *See* 1 MILGRIM, *supra* note 114, § 5.02[3][d] n.38 (referring to business trade secrets as a "marginal form of protectable information" in his analysis of *PepsiCo.*)

133. *See* Merck & Co. v. Lyon, 941 F. Supp. 1443, 1461 (M.D.N.C. 1996). Although the court found that trade secrets were at stake, it also found that these secrets were not of the "type or value" that merited broad injunctive relief. The court found that the secrets comprised "general business information, the exact specifics of which might not be

their specific pricing and marketing plans, these plans are of the type that all businesses research and develop.[134] If a business independently develops and anticipates its competitor's plans using the same marketing research tools and general business acumen that its competitor uses, then such plans lose their trade secret status.[135] Furthermore, the value of pricing and marketing plans is difficult to ascertain because they are often changed and updated based on their relative market success upon implementation.[136]

In sum, a court should apply a two-part analysis in its evaluation of an inevitable disclosure claim. The first part should examine the "core" *DoubleClick* factors: the degree of competition between the former and new employers; the degree of similarity between the employee's former and new positions; and the existence and value of the former employer's trade secrets. If these factors weigh in favor of the former employer, the court should then proceed to the second step of its analysis by examining the employee's candor, the nature of the employers' industry, and the technological or business character of the former employer's trade secrets. Only when these "second-step" factors weigh in favor of the former employer should the court grant injunctive relief, and this relief should be crafted as narrowly as possible.

IV. CONCLUSION

In *GlobeSpan*, the court's rejection of the doctrine of inevitable disclosure under California Business and Professions Code Section 16600 was improper. Because the doctrine does not conflict with California law, a court should not summarily dismiss a claim of trade secret misappropria-

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known to competitors, but which in general is the type of information developed by all business organizations." Further, the court observed that "the information, while important, is not of critical value and, in any event, is time-dated." These findings supported the court's granting a "very narrow injunction."

134. *See id.*

135. *See id.* at 1457. Supply agreements and marketing plans "constitute competitively valuable information not generally known. However, this information is also subject to rapidly being outdated and is subject to some extent to independent development." *Id.*

136. *See id.* It is interesting to note that PepsiCo ultimately bought Quaker. Ameet Sachdev, *PepsiCo Agrees To Buy Quaker: Company To Be Acquired for $13.4 Billion in Stock*, CHI. TRIB., Dec. 4, 2000, at 1. Can we infer from this transaction that PepsiCo's marketing strategy failed to raise its sports beverage, "All Sport," to the level of its competitor, Gatorade, despite PepsiCo's having kept its marketing secrets (and Redmond) out of Quaker's hands? Perhaps this conclusion stretches the imagination, but nevertheless, PepsiCo may have overestimated the value of its marketing strategy.

tion based on inevitable disclosure. Instead, a court should carefully weigh the facts that a plaintiff presents under the purview of the doctrine to determine if the threat of misappropriation and its possible consequences merit injunctive relief. By subjecting inevitable disclosure claims to strict judicial scrutiny, a court will maintain a sensible balance between trade secret protection and employee mobility that, in all but the most extreme cases, favors the employee.

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ANTITRUST

UNITED STATES V. MICROSOFT CORP.

By Samuel Noah Weinstein

Microsoft's Windows operating system is the sun in the solar system of the information economy. With tens of millions of users worldwide, Windows is the most significant platform for continued software innovation. As Windows has matured, its interoperability has increased. Functions once considered distinct, such as disk de-fragmentation and memory management, have become part of the Windows system. While this interoperability offers advantages to consumers, it also raises serious antitrust concerns. The most pressing worry is that Microsoft will use its monopoly power in operating systems to quash innovation in other software markets by "integrating" formerly competitive functions into Windows. This tension, between the advantages of interoperability and the threat to competition, was at the core of the D.C. Circuit's decision in *United States v. Microsoft.*[1]

The verdict in this case was much anticipated. This anticipation grew both out of Microsoft's unique position in the American economy, and out of a desire to see a clear resolution of the complicated antitrust issues implicated in the case. As to Microsoft's fate, despite some press reports painting the decision as a victory for the software king,[2] the holding was a mixed result. Although the circuit court overturned both the breakup remedy and tying liability, remanding both for reconsideration, it firmly upheld liability for monopolization under section 2 of the Sherman Act.[3] Microsoft's real victories may have come later, when the Department of Justice announced that it would drop the tying charge and no longer pursue the breakup of the company,[4] and in the settlement agreement.[5]

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1. United States v. Microsoft Corp., 253 F.3d 34 (D.C. Cir. 2001) ("*Microsoft III*"). For the sake of convenience, this Note refers to the 1998 D.C. Circuit decision as "*Microsoft II.*" The more recent Microsoft litigation, encompassing both the 2000 district court decision and the 2001 D.C. Circuit decision, is referred to as "*Microsoft III.*" "*Microsoft I,*" the consent decree decision of 1995, plays only a minor role in this Note.

2. *See, e.g.*, *Microsoft Marches On*, S.F. CHRON., June 29, 2001, at A24; John Hendren, *Microsoft Ducks Bullet, Again Talks About Deal*, SEATTLE TIMES, June 29, 2001, at A1.

3. United States v. Microsoft Corp., 253 F.3d at 51.

4. Justice Department Informs Microsoft of Plans for Further Proceedings in the District Court, http://www.usdoj.gov/atr/public/press_releases/2001/8981.htm (Sept. 6, 2001).

With regard to antitrust law, the holding does little to resolve the tension between interoperability and protection of competition. This failure is reflected in the decision's tying analysis. This Note focuses on that analysis and concludes that while the court's economic reasoning and its rejection of the current Supreme Court tying regime were substantially correct, its proposed rule provides too little guidance to courts and technology firms, and will result in uncertainty in this critical area of antitrust law. A new tying rule is necessary to strike the proper balance between a monopolist's ability to innovate through integration and the need to maintain competitive markets. Judges and scholars have proposed a number of candidates for this role. This Note will evaluate these proposals and conclude that a structured rule of reason test is the preferred solution.

I. BACKGROUND

In order to understand this complex decision, it is useful to lay out the principal antitrust doctrines implicated by the case and to discuss some of the economics of antitrust.

A. Antitrust Doctrine

The *Microsoft* case implicates a number of areas within antitrust law, some settled and some in flux. The charges against Microsoft included monopolization and attempted monopolization under section 2 of the Sherman Act,[6] fairly settled areas of law, and tying under section 1 of the Sherman Act,[7] a topic that has been the subject of significant disagreement.

1. Monopolization

Under section 2 of the Sherman Act, liability for monopolization requires: "(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power" not based on "a superior product, business acumen, or historic accident."[8]

In applying the initial prong of the test, a court will first define the relevant antitrust market. In general, the market will encompass all prod-

5. Department of Justice and Microsoft Corporation Reach Effective Settlement on Antitrust Lawsuit, http://www.usdoj.gov/atr/public/press_releases/2001/9463.htm (Nov. 2, 2001). The terms of the settlement can be found at http://www.usdoj.gov/atr/cases/f9400/9495.htm (Nov. 6, 2001).

6. 15 U.S.C. § 2 (1994).

7. 15 U.S.C. § 1 (1994).

8. United States v. Grinnell Corp., 384 U.S. 563, 570-71 (1996).

ucts "reasonably interchangeable by consumers for the same purposes."[9] Once the market is defined, the court will decide whether the defendant has monopoly power in that market, with monopoly power defined as "the power to control prices or exclude competition."[10] Direct proof of monopoly power is rarely available, so courts typically rely on circumstantial evidence, such as market share combined with barriers to entry.[11]

If a court finds that monopoly power exists, it will determine whether the defendant has acquired or maintained that power through exclusionary conduct. A four-part test is used: (1) did the defendant's conduct have anticompetitive effect?[12] (2) did the defendant's actions in fact injure competition?[13] (3) if the plaintiff can demonstrate anticompetitive effect, does the monopolist have a "procompetitive justification" for its conduct?[14] and (4) if the plaintiff cannot rebut the procompetitive justification, can the plaintiff show that the "anticompetitive harm of the conduct outweighs the procompetitive benefit"?[15]

If the court finds both monopoly power and exclusionary conduct, the defendant will be liable under section 2.

2. *Attempted Monopolization*

In order to establish liability for attempted monopolization under section 2 of the Sherman Act, the evidence must prove that (1) the defendant engaged in "predatory or anticompetitive conduct" with (2) "a specific intent to monopolize" and (3) "a dangerous probability of achieving monopoly power."[16] Just as in a monopolization analysis, a court must define the relevant antitrust market in order to rule on the third prong.[17]

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9. United States v. E.I. DuPont de Nemours & Co., 351 U.S. 377, 395 (1956).

10. *Id.* at 391.

11. *See* Rebel Oil Co. v. Atl. Richfield Co., 51 F.3d 1421, 1434 (9th Cir. 1995). Barriers to entry are factors that prevent potential competitors not currently in the market from quickly responding to an increase in price above the competitive level by entering the market. *See* S. Pac. Communications Co. v. AT&T, 740 F.2d 980, 1001-02 (D.C. Cir. 1984).

12. A court will find anticompetitive effect when the defendant's actions "unfairly tend[ed] to destroy competition." Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 458 (1993).

13. *See generally* Brooke Group v. Brown and Williamson Tobacco Corp., 509 U.S. 209, 225-26 (1993).

14. *See* United States v. Microsoft Corp., 253 F.3d 34, 59 (D.C. Cir. 2001).

15. *Id.*

16. *Spectrum Sports*, 506 U.S. at 456.

17. *See id.* at 455-56.

3. *Tying*

Under current law a firm is liable for a tying violation if four conditions are met. First, there must be two separate products involved. Second, the defendant must not have allowed customers to purchase the tied product without the tying product. Third, the arrangement must affect a significant volume of interstate commerce. Fourth, the defendant must have market power in the tying product.[18] This is a per se test—if all four elements are satisfied, liability is automatic.[19] Most tying litigation focuses on the first and fourth elements, and in technological innovation cases the question of whether one product or two is involved has become a very difficult doctrinal issue.[20]

The Supreme Court laid out the standard test for determining whether a combination of goods or services represents one product or two in *Jefferson Parish Hospital District No. 2 v. Hyde*.[21] The Court held that the question of whether there are two products involved turns "not on the functional relation between them, but rather on the character of the demand for the two items."[22] In other words, if there is "sufficient demand" for the purchase of one product "separate from" the second product, then there are two products for the purpose of tying analysis.[23]

B. The Evolving Economics of Antitrust

The Sherman Act, the first and most significant American antitrust law, is a famously imprecise piece of legislation. It includes general prohibitions on illegal monopolization and contracts or combinations in restraint of trade, but it does little to define specific violations.[24] It has been left up to the courts to fill in the meaning of the Act and to create detailed

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18. Eastman Kodak Co. v. Image Technical Servs., Inc., 504 U.S. 451, 461-62 (1992); Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 12-18 (1984).

19. Northern Pac. Ry. Co. v. United States, 356 U.S. 1, 5 (1958).

20. *See* Michael Katz & Carl Shapiro, *Antitrust in Software Markets*, *in* COMPETITION, INNOVATION, AND THE MICROSOFT MONOPOLY: ANTITRUST IN THE DIGITAL MARKETPLACE 29, 72-73 (Jeffrey A. Eisenach and Thomas M. Lenard eds., 1999); Renato Mariotti, *Rethinking Software Tying*, 17 YALE J. ON REG. 367, 368-69 (2000); J. Gregory Sidak, *An Antitrust Rule for Software Integration*, 18 YALE J. ON REG. 1, 26 (2001).

21. 466 U.S. 2, 19 (1984).

22. *Id.*

23. *Id.* at 21.

24. Section one outlaws "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations," while section two penalizes any "person who shall monopolize or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations." 15 U.S.C. §§ 1-2 (1994).

antitrust guidelines. These guidelines have changed as courts have gained economic sophistication in the century or so since the Act's passage. Perhaps the most important overall impact of economic theory on antitrust law has been a general move away from per se rules, which declare certain arrangements to be illegal without exception, and toward the more general use of the "rule of reason," which requires courts to measure a practice's anticompetitive effect against its procompetitive benefits. This shift occurred as a result of a growing understanding among economists of the efficiency benefits of a number of activities that courts had previously deemed suspect.[25] These activities include nonstandard contracts, such as vertical exclusive distribution agreements,[26] and expansion to achieve economies of scale and scope.[27]

1. The Economics of Technologically Dynamic Markets

In recent years economists have gained a more nuanced understanding of the characteristics of high-technology markets. Many economists agree that these markets have three important defining characteristics: strong economies of scale, the presence of network effects, and the tendency toward a lock-in effect for successful technologies.[28]

Most high-technology industries involve products that are knowledge-intensive, rather than labor-intensive. Knowledge, especially the kind of knowledge needed to develop software, biotechnology, and other types of high-tech products, is generally expensive to produce. Once these products are developed, however, they are usually cheap to reproduce. This means that these industries tend to be characterized by high fixed costs and low marginal costs, and as a result average costs are reduced as output increases.[29] Thus, there are strong economies of scale on the supply side in many high-technology markets.

Strong "network" effects are a second key characteristic of high-technology markets. Network effects occur when the value of owning a good or service increases in relation to the number of consumers who al-

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25. *See* Richard Gilbert & Oliver Williamson, *Antitrust Policy*, *in* THE NEW PALGRAVE DICTIONARY OF ECONOMICS AND THE LAW 83-85 (Peter Newman ed., 1998).

26. In Continental T.V. v. GTE Sylvania 433 U.S. 36 (1977), the Supreme Court held that vertical non-price restrictions were to be judged under the rule of reason, as these arrangements had potential procompetitive benefits.

27. *See* Gilbert & Williamson, *supra* note 25.

28. Katz & Shapiro, *supra* note 20, at 32-36; Robert Litum, *Antitrust and the New Economy*, 62 U. PITT. L. REV. 429 (2001).

29. Litan, *supra* note 28, at 429.

ready own it.[30] The telephone system provides a good example. As the number of individuals who own phones rises, phone ownership becomes more valuable to potential consumers.[31] Computer operating systems are an obvious new-economy example of a product with network effects.

Third, some high-technology products are subject to a lock-in effect. This means that once consumers are familiar with a product and are trained to use it, they are reluctant to switch to a different product.[32] This is true of many software products, which can be difficult and time-consuming to master.

These characteristics—supply-side economies of scale, network effects, and lock-in—combine to create important tendencies toward monopoly in high-technology markets.

2. *The Economics of Tying in the Software Context*

The distinctive characteristics of high-technology markets, and the software market in particular, have shaped economists' view of the proper role of tying law in these markets. A number of economic concerns animate the traditional ban on tying arrangements. First, tying reduces consumers' freedom of choice.[33] Under current market conditions, for instance, tying a browser to Windows leaves consumers of Intel-based PC operating systems fewer options in browser technology. In addition, tying arrangements concern economists because they have the strong potential to reduce competition on the merits in the tied product market.[34] There are also procompetitive reasons for manufacturers to bundle products. These include transaction costs savings, which result from economies of scale or scope in production and marketing, and quality assurance.[35]

Many economists argue that the traditional economics of tying do not map well onto the conditions in software markets.[36] This is because the innovation rate in software is much higher than in the "static" industries

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30. Katz & Shapiro, *supra* note 280 at 32-34; Robert Pitofsky, *Antitrust and Intellectual Property: Unresolved Issues at the Heart of the New Economy*, 16 BERKELEY TECH. L.J. 535, 538-39 (2001).

31. *See* Daniel L. Rubinfeld, *Antirust Enforcement in Dynamic Network Industries*, 43 ANTITRUST BULL. 859, 861 (1998).

32. Litan, *supra* note 28, at 430.

33. *See* Phillip Areeda & Louis Kaplow, ANTITRUST ANALYSIS: PROBLEMS, TEXT, CASES 687-92 (5th ed. 1997).

34. *Id.* at 686; Katz & Shapiro, *supra* note 20, at 70.

35. Katz & Shapiro, *supra* note 20, at 67-68; J. Gregory Sidak, *An Antitrust Rule for Software Integration*, 18 YALE J. ON REG. 1, 9-10 (2001).

36. *See* Katz & Shapiro, *supra* note20, at 66-78; Sidak, *supra* note 35.

upon whose characteristics traditional tying law was based.[37] As a result it is often very difficult to determine whether a software bundle is one product or two, or whether it is anticompetitive.[38] This difficulty led the D.C. Circuit to craft a new tying rule for software products in *Microsoft III*.

II. THE CASE

In May 1998,[39] the Department of Justice and a group of nineteen state plaintiffs filed suit against Microsoft, alleging four types of antitrust violations: unlawful exclusive dealing arrangements and unlawful tying in violation of section 1 of the Sherman Act, and unlawful monopoly maintenance and attempted monopolization under section 2.[40]

A. Factual Background

The allegations against Microsoft emerged from what the plaintiffs characterized as the company's efforts to maintain its operating system monopoly by destroying threats posed by Netscape Navigator, a web browser, and Sun Java, a cross-platform programming language.[41] Both Navigator and Java are species of "middleware," software programs that can serve as platforms for other software applications.[42] According to the plaintiffs' theory, middleware posed two distinct threats to the Windows monopoly. First, because the middleware applications themselves could be used as software platforms, they competed directly with Windows.[43] Second, middleware designed to run on more than one operating system would allow software developers to write programs that worked on any

37. *See* Sidak, *supra* note 35, at 26-27.

38. *See* Katz & Shapiro, *supra* note 20. In addition, because marginal costs of production are so low that a manufacturer can bundle a program for an insignificant cost, there are many situations in which bundling is efficient. *Id.* at 67.

39. The roots of this case reach back at least seven years. In 1994 the DOJ filed suit against Microsoft, charging the company with illegally maintaining its monopoly in the operating system market through anticompetitive licensing and software agreements. United States v. Microsoft Corp., 56 F.3d 1448, 1451 (D.C. Cir. 1995) ("*Microsoft I*"). This issue was settled by consent decree in 1995. United States v. Microsoft Corp., 56 F.3d 1448. In 1998 the DOJ brought suit against Microsoft for allegedly violating aspects of the consent decree by bundling Internet Explorer 3.0 and 4.0 with Windows 95. The D.C. Circuit held, however, that Microsoft's actions did not violate the consent decree. United States v. Microsoft Corp., 147 F.3d 935 (D.C. Cir. 1998) ("*Microsoft II*").

40. Government's Complaint at 1, United States v. Microsoft Corp., 87 F. Supp. 2d 30 (D.D.C. 2000), *at* http://www.usdoj.gov:80/atr/cases/f1700/1763.wpd.

41. *Id.* at 1-2.

42. United States v. Microsoft Corp., 84 F. Supp. 2d 9, 22-23 (1999).

43. Government's Complaint at 1-2, United States v. Microsoft Corp., 87 F. Supp. 2d 30 (D.D.C. 2000), *at* http://www.usdoj.gov:80/atr/cases/f1700/1763.wpd.

number of these systems, potentially leading to a lowering of the "applications barrier to entry," which, plaintiffs argued, protected Microsoft's Windows monopoly.[44] The plaintiffs alleged that Microsoft engaged in a number of anticompetitive acts in its efforts to destroy the threats posed by Navigator and Java. These acts included securing exclusive dealing contracts with Original Equipment Manufacturers ("OEMs") and Internet Access Providers ("IAPs"), barring these entities from using Navigator in addition to Internet Explorer ("IE"),[45] and pressuring Apple Computer to drop its use of Navigator. In addition, the plaintiffs alleged that Microsoft had illegally tied IE to Windows in an effort to destroy competition in the browser market.[46]

1. The District Court Holding

The district court held that Microsoft had a monopoly in the market for Intel-compatible PC operating systems[47] and that the company had engaged in a variety of anticompetitive practices to maintain that monopoly power.[48] These practices were aimed at destroying the "middleware threat."[49] They included an attempt to convince Netscape not to release a version of its browser that might have served as a substantial platform for applications;[50] exclusive contracts with OEMs, IAPs, and Apple Computer that forced these parties to favor IE over Netscape;[51] bundling of IE and Windows to reduce rival browser share;[52] and Microsoft's creation of its own version of a Java Virtual Machine ("JVM") and the contracts it used to force Independent Software Vendors ("ISVs") to use this version.[53] Having found both monopoly power and anticompetitive conduct, Judge Jackson held that Microsoft violated section 2 by illegally maintaining its monopoly in the operating system market.[54]

Judge Jackson also held Microsoft liable for attempted monopolization under section 2. The judge found Microsoft's offer to Netscape to divide

44. *Id.*
45. *Id.* at 6, 8-12.
46. *Id.* at 7-8.
47. United States v. Microsoft, 87 F. Supp. 2d at 36-37.
48. *Id.* at 37-44.
49. *Id.* at 38-39.
50. *Id.* at 39.
51. *Id.* at 39-42.
52. *Id.* at 39-40.
53. *Id.* at 43-44
54. *Id.* at 44.

the browser market sufficient to constitute a "dangerous probability" that Microsoft might achieve a monopoly in the browser market.[55]

As for the section 1 violations, Judge Jackson found Microsoft liable for tying but not for exclusive dealing. In his tying analysis, Judge Jackson applied the *Jefferson Parish* "separate demand" test and found that IE and Windows were separate products.[56] By conditioning the licensing of Windows on the purchase of IE, Judge Jackson ruled that Microsoft had created an illegal tie-in.[57] Judge Jackson, however, refused to find Microsoft liable for exclusive dealing because the defendant had not foreclosed a sufficient share of the market for browser sales.[58]

B. The D.C. Circuit Holding[59]

1. Monopolization

The circuit court upheld the lower court's ruling that Microsoft possessed monopoly power in the market for Intel-compatible PC operating systems.[60] The court rejected Microsoft's argument that the district court had incorrectly defined the relevant market. The court also rejected Microsoft's assertion that, because the software industry is uniquely dynamic, direct proof of market power rather than the standard circumstantial evidence was necessary.[61]

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55. *Id.* at 45-46.

56. *Id.* at 48-51.

57. *Id.*

58. *Id.* at 51-53.

59. The following discussion addresses only the antitrust aspects of the case. The circuit court also considered Microsoft's appeal of the district court's procedural rulings with respect to both the trial and remedy phases. The circuit court brushed off Microsoft's complaint that the district court erred in ordering an expedited trial and in agreeing to use summary witnesses, noting the lower court's "broad discretion to conduct trials as it sees fit." United States v. Microsoft Corp., 253 F.3d 34, 98 (D.C. Cir. 2001). As to the remedy phase, the circuit court held that the district court judgment must be vacated on three separate grounds: first, the district court had erred in failing to hold a remedies-specific evidentiary hearing in the face of a factual dispute; second, the court had failed to provide adequate explanations for its remedy; and third, the circuit court's revisions of the scope of Microsoft's liability required a fresh look at the remedy. *Id.* at 98, 101-05. The circuit court also held that Judge Jackson's public comments on the case, his ex parte contacts, and his failure to appear impartial meant that he must be disqualified from the case retroactive to the date he entered the breakup order. *Id.* at 107-16. The court refused, however, to overturn Judge Jackson's Findings of Fact and Law, as Microsoft failed to prove that Judge Jackson's actions rose to the level of actual bias. *Id.* at 116.

60. *Id.* at 51-59.

61. *Id.* at 56. Microsoft asserted that the district court had erred by excluding non-Intel operating systems, such as Apple, non-PC systems, such as hand-held devices, and

The court also upheld the district court's finding that Microsoft had engaged in anticompetitive conduct. This conduct included the restrictions Microsoft imposed on OEMs through licenses for Windows,[62] which the court held reduced the usage of rival browsers through contractual limitations rather than on the basis of a superior Microsoft product.[63] Other anticompetitive conduct included some of the ways in which Microsoft bundled IE with Windows,[64] Microsoft's exclusive contracts with IAPs,[65] ex-

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middleware, such as Netscape and Java from the relevant market. *Id.* at 52. The court rejected Microsoft's arguments as to the first two proposed substitutes because the company failed to challenge the district court's findings that neither type of product was a realistic substitute for Intel operating systems. *Id.* Microsoft's argument regarding middleware was potentially more persuasive than its other arguments in this area. The company pointed out that because the lower court clearly held that middleware was a threat to the Windows monopoly, it must be considered part of the market for monopoly analysis. *Id.* at 53-54. The circuit court noted, however, that the district court classified middleware as a potential *future* threat. *Id.* In order to affect the market analysis, however, middleware would have to be able to act as a substitute for Windows in the near future. *Id.* This, the circuit court ruled, was not likely, and as a result middleware was not part of the proper antitrust market. *Id.*

Microsoft next argued that even if the relevant antitrust market was Intel-compatible PC operating systems, the company did not have monopoly power in this market. The crux of Microsoft's argument was that despite Windows' 95% share of this market, the possibility of competition from new entrants prevented the company from exercising monopoly power. *Id.* at 54-55. As a necessary corollary, Microsoft also challenged the existence of the "applications barrier to entry." *Id.* at 55-56. The circuit court agreed that the possibility of new entrants may affect the monopoly power analysis, but held that no such effect existed in this situation. *Id.* at 54-55. The court concurred with the lower court's conclusion that the applications barrier would keep competitors out. *Id* at 55-56.

62. *Id.* at 59-64. These licenses prohibited the OEMs from (1) removing any desktop icons, folders, or "Start" menu entries; (2) altering the initial boot sequence; or (3) otherwise altering the appearance of the Windows desktop. *Id.* at 61. The court found each of these restrictions anticompetitive. The court did hold that OEMs that had altered the operating system so that the Windows desktop never appeared had engaged in a "drastic alteration of Microsoft's copyrighted work." *Id.* at 60. The court ruled that the harm of this alteration outweighed the anticompetitive effect of preventing OEMs from inserting a different interface that would appear upon completion of the boot sequence. *Id.*

63. *Id.* at 62, 64.

64. *Id.* at 67. In particular, the court ruled that the exclusion of IE from the "Add/Remove Programs" utility and the commingling of browser code with other code so that a user trying to get rid of IE would destroy the entire system were anticompetitive. *Id.* The court held that Microsoft was not liable for a third aspect of the bundle, the fact that under certain circumstances Windows would override the user's choice of a default browser. The court noted that the plaintiffs had not rebutted Microsoft's justification for this feature. *Id.*

65. *Id.* at 67-71. Under the terms of these contracts, Microsoft furnished easy access to the IAPs from the Windows desktop in return for an agreement to promote IE to the

clusive dealing arrangements with ISVs, and Microsoft's deal with Apple in which Apple bundled IE with its operating system and made it the system's default browser.[66]

Turning to Microsoft's involvement with the Java technology, the court held that Microsoft's "First Wave Agreements" with ISVs, which offered Windows technical information in exchange for a promise to exclusively promote Microsoft's version of Java, were anticompetitive because they reduced the distribution of Navigator and foreclosed a substantial portion of the Java Virtual Machine market.[67] Microsoft had also deceived ISVs by promising them that programs created on Microsoft's JVM would run on Sun's version, when in fact they would not.[68] The court held that this deception was also anticompetitive.[69] In addition to these actions, Microsoft had threatened Intel that if it did not give up its efforts to create a cross-platform JVM, Microsoft would begin to support Intel's main competitor, Advanced Micro Devices.[70] The court found that this coercion, too, was anticompetitive.[71]

Thus, while the circuit court did overturn some of the lower court's findings of anticompetitive behavior, it ruled nonetheless that Microsoft had engaged in a long list of anticompetitive acts. These acts, combined with Microsoft's monopoly power, led the court to uphold the finding of section 2 violations for monopoly maintenance.

2. *Attempted Monopolization*

The D.C. Circuit overturned the district court's finding of liability for attempted monopolization on the grounds that the Government had not made a sufficient showing that Microsoft's conduct raised a "dangerous

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exclusion of other browsers and to limit the number of Netscape browsers they shipped to consumers. The court held that because these contracts ensured that most IAP users were offered IE either as a default browser or as the only browser, the contracts helped maintain Microsoft's monopoly. *Id.* at 71. The circuit court overturned the district court's finding of liability as to other aspects of these contracts. Specifically, the court found that offering IE at no cost to IAPs, offering IAPs a payment for each customer recruited to use IE, and creating and giving IAPs a free kit that allowed them to customize IE were not anticompetitive practices. *Id.* at 67-68.

66. *Id.* at 72-74. The court overturned the lower court's decision that Microsoft's deals with Internet Content Providers ("ICPs") were anticompetitive, as the plaintiffs had failed to show that these deals had a substantial effect on competition. *Id.* at 71.

67. *Id.* at 74-76.

68. *Id.* at 76-77.

69. *Id.*

70. *Id.* at 77-78.

71. *Id.*

probability of achieving monopoly power" in the browser market.[72] The opinion noted that generally under these conditions the court would remand the case so that the district court could properly define the market in question. The court ruled that remand was unnecessary here, however, because the plaintiffs did not provide enough information on the defining characteristics of browsers and possible substitutes for the district court to perform the analysis.[73]

3. *Tying*

The D.C. Circuit overturned the district court's holding that Microsoft's bundling of Internet Explorer and Windows was per se unlawful.[74] Ignoring Supreme Court precedent squarely on point, the court announced a new tying rule for situations "involving platform software products."[75] Rather than judging these arrangements under the per se rule, as required by *Northern Pacific* and *Jefferson Parish*, the court held that the rule of reason is the appropriate test and remanded the case to the district court for judgment under this standard.[76]

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72. *Id.* at 80-81. The court held that both the plaintiffs and the district court had committed the fundamental error of assuming that liability for attempted monopolization of the browser market was an automatic outgrowth of Microsoft's section 2 liability for monopolization of the operating system market. *Id.* at 80-81. As a result, the Government failed to demonstrate that the browser market could in fact be monopolized, a showing which in turn would have required the Government to define the market, and prove that substantial barriers to entry protect that market. *Id.* The circuit court held that the Government failed on both these fronts and that the district court ignored these failures. *Id.* at 81-82.

73. *Id.* at 81-82. The analysis might have ended there, because lack of market definition carries the day, but the circuit court went on to overturn the district court's holding on barriers to entry. Specifically, the circuit court held that pointing to the proposed deal between Microsoft and Netscape to split the browser market as a barrier to entry was "far too speculative." The circuit court admitted the possibility that a showing of network effects in the browser market might have been sufficient to demonstrate a barrier to entry, but held that the district court failed to find either that these network effects existed in the browser market or that a barrier to entry on the basis of network effects would confer monopoly power. These failings were directly related to the fact that the Government did not provide sufficient evidence on either point. *Id.* at 82-84.

74. Part III *infra* offers a detailed analysis of this part of the holding.

75. United States v. Microsoft Corp., 253 F.3d at 84.

76. *Id.* The court suggested that to prevail on remand, the plaintiffs must show that "Microsoft's conduct unreasonably restrained competition." *Id.* at 95. In other words, the plaintiffs would have to prove that the anticompetitive effects of Microsoft's bundling outweighed whatever procompetitive justifications the company offered.

III. RECONSIDERING TYING LAW

The tying allegations against Microsoft raised the most challenging and important legal issues to emerge from the case. At the heart of the tying controversy is the delicate balance between the advantages of high-technology product integration and the serious risk of anticompetitive forced buying. There is sharp disagreement among judges and scholars about the type of tying rule best able to achieve this balance.

This disagreement is reflected in the D.C. Circuit's remarkable abrogation of Supreme Court tying precedent. The circuit court carved out a special exception to the law of the land for tying as stated in *Northern Pacific* and *Jefferson Parish*[77] and held that "the rule of reason, rather than per se analysis, should govern the legality of tying arrangements involving platform software products."[78]

In order to understand what drove the D.C. Circuit to reject relevant Supreme Court precedent, the following analysis starts with a discussion of the economics of tying in high-technology markets and then examines the incongruity between current economic theory and the legal rules governing tying. The next section argues that while the D.C. Circuit was right to displace *Jefferson Parish*, its new rule is too open-ended. The *Jefferson Parish* rule and the D.C. Circuit's rule of reason are at opposite ends of a jurisprudential spectrum stretching from the overly formalistic to the dangerously formless. The final section of this Note reviews a number of proposed tying tests that occupy the middle ground along this spectrum and concludes that a structured rule of reason test is the preferred approach.

A. The Economics of Tying

For many years courts have viewed tying arrangements as necessarily anticompetitive and judged them under a per se standard.[79] This approach is based on the assumption that tie-ins never result in efficiencies. In recent years, however, economists have demonstrated that tying arrangements can be efficient and procompetitive in certain circumstances.[80] For instance, tie-ins may provide transaction cost savings resulting from economies of scope and scale in production, distribution, and marketing.[81] In addition, when two components are used together in a system, a tying arrangement can provide quality assurance. The tie-in allows the monopo-

77. *See supra* Part I.A.3.
78. United States v. Microsoft Corp., 253 F.3d at 84.
79. PHILIP AREEDA, IX ANTITRUST LAW 267 (1991).
80. Katz & Shapiro, *supra* note 280, at 67-69.
81. *Id.* at 67-68.

list in product A to ensure that lower quality versions of product B do not reduce A's performance.[82] Naturally, tying arrangements can have anticompetitive results as well. Specifically, tie-ins are anticompetitive when they are designed to foreclose competition. Foreclosure can occur in two ways. The tie-in can directly eliminate competition in the tied product market by forcing consumers to purchase the monopolist's version of the tied product.[83] The tie-in can also foreclose competition by forcing competitors to enter both the tied and tying markets simultaneously. This "two-stage entry" problem makes it difficult for competitors to emerge.[84]

Current economic analysis thus indicates that tying arrangements can be either pro- or anticompetitive, depending upon their particular characteristics and design. An effective tying rule must therefore be able to differentiate between pro- and anticompetitive tie-ins. Current tying law fails at this task.

B. The Need to Rethink *Jefferson Parish*

As noted above, the current Supreme Court test for tying requires a court to determine whether the arrangement in question involves one product or two. In *Jefferson Parish* the Supreme Court held that two products exist for the purposes of tying law if there is "sufficient demand for the purchase" of the products separately.[85] As the D.C. Circuit observed, the *Jefferson Parish* test is a "prox[y] for net efficiency."[86] In other words, it is a relatively simple way of determining whether a particular tying arrangement increases consumer welfare. The logic here is that separate demand for products will exist when the benefits of product choice outweigh the efficiencies of a particular product integration.[87] The question is whether this test is a useful proxy, and the answer is that it is in some, but not all cases. This is because, while it is true that consumers tend to understand the market they are in, they are not always able to judge the efficiencies of a particular product integration.[88] It is not difficult to imagine a

82. *Id.* at 68-69.
83. *Id.* at 70.
84. *Id.* at 70-71.
85. *Jefferson Parish*, 466 U.S. at 22.
86. United States v. Microsoft Corp., 253 F.3d 34, 87-88 (D.C. Cir. 2001).
87. *Id.*
88. One commentator has suggested that relying on consumer demand is problematic because consumer perception of products is significantly affected by marketing and packaging. In other words, there is the risk that consumers will believe that browsers and operating systems are not separate products simply because Microsoft promotes an integration of the two as a unified product. The ability of software designers to adjust code to make what might be two distinct products appear unified on the desktop heightens this

situation in which separate consumer demand continues to exist after the creation of an efficiency-enhancing integration because consumers are slow to recognize the efficiencies. If the other elements of a tying charge were met, a court relying on *Jefferson Parish* would find such an integration illegal. This type of ruling would not advance the goals of antitrust law, which exists not to quash innovation, but to prevent forced buying.

C. "Not All Ties Are Bad": The D.C. Circuit's Dilemma

In *Microsoft III*, the D.C. Circuit confronted a situation in which the logic of the relevant Supreme Court precedent was no longer supported by current economic theory. The tying portion of the opinion is propelled by this incongruity. Noting that "not all ties are bad,"[89] the court relied upon current economic theory for the idea that tying arrangements can produce transaction costs savings and economies of scale and/or scope.[90] The court also noted that the *Jefferson Parish* test cannot always differentiate good ties from bad.[91]

At this point in the opinion, the court appeared ready to reject the *Jefferson Parish* test on its own terms. Because the circuit court could not directly overturn the Supreme Court's test, however, the opinion was forced to take a circuitous route to get out from under *Jefferson Parish*. To do so, the court appealed to more general Supreme Court precedent on the applicability of per se rules. Repeating the Supreme Court's admonition that per se rules are only appropriate "after considerable experience with certain business relationships,"[92] the D.C. Circuit concluded that "technological integration of added functionality into software that serves as a platform for third-party applications" is not such a familiar business relationship.[93]

This argument collapses upon the slightest scrutiny. The Supreme Court has already held that tying arrangements *as a category* are a type of business relationship that experience has shown always hurts competition

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risk. Renato Mariotti, *Rethinking Software Tying*, 17 YALE J. ON REG. 367, 377-79 (2000).

89. *United States v. Microsoft Corp.* , 253 F.3d at 87.

90. *Id.*

91. *Id.* at 89.

92. *Id.* at 84 (quoting Broadcast Music, Inc. v. CBS, 441 U.S. 1, 9, 60 (1972)).

93. *Id.* The D.C. Circuit also held that a rule of reason analysis is necessary here because tying in software markets produces efficiencies that courts are not yet trained to recognize and that are not accounted for by the per se rule. *Id.* at 93. The court noted that the course of product development is very difficult to predict in technologically dynamic markets and that the efficiencies of new arrangements are often difficult to understand. *Id.* at 94.

and therefore are illegal per se. Reliance upon more general statements about the conditions under which per se rules should apply cannot overcome Supreme Court precedent that is directly on point.

Nonetheless, the court remanded the tying charge for consideration under the rule of reason.[94] The court provided very little guidance as to how the test should be administered, however. The opinion states only that the district court should balance the bundle's "benefits against the costs to consumers."[95]

D. The D.C. Circuit's Unstructured Rule of Reason Test

The D.C. Circuit decision yanks tying law from reliance on the overly formalistic *Jefferson Parish* rule to the opposite end of the jurisprudential spectrum, creating a rule that provides little guidance to courts about how to identify anticompetitive tying arrangements. While its requirement of thorough analysis and its open-ended character are reasons to favor the D.C. Circuit's rule of reason, the test also has significant drawbacks.

The first and most significant drawback of the unstructured rule of reason is that it provides much less predictability to innovating firms whose actions may brush up against the antitrust laws. With evaluation of net efficiency left to the courts, firms would have very little idea how a trial might turn out. This uncertainty might chill innovation or embolden monopolists.[96] Because the D.C. Circuit's rule of reason test provides no guidelines at all, it is not even clear which economic variables courts will consider. Potential litigants and their lawyers are likely to have little ability to predict how courts will view new tying arrangements.[97]

The second problem with the D.C. Circuit test is that it is questionable whether courts are equipped to make these sorts of determinations. The D.C. Circuit itself has stated that "[c]ourts are ill-equipped to evaluate the

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94. *Id.*

95. *Id.*

96. For evaluation of the difficulties created by the unstructured rule of reason test, see Philip Areeda, *Antitrust Law as Industrial Policy: Should Judges and Juries Make It?*, *in* ANTITRUST, INNOVATION, AND COMPETITIVENESS 29 (Thomas M. Jorde & David J. Teece eds., 1992); Frank H. Easterbrook, *Ignorance and Antitrust*, *in* ANTITRUST, INNOVATION, AND COMPETITIVENESS, *supra*, at 119; Gregory J. Werden, *Antitrust Analysis of Joint Ventures: An Overview*, 66 ANTITRUST L.J. 701, 734 (1998) ("Sorting out the facts of actual cases under the rule of reason is apt to be difficult and subject to significant error.").

97. Professor Areeda has warned that "[a] rule that cannot be consistently applied invites confusion and quixotic results contrary to the statutory purpose." PHILLIP AREEDA, ANTITRUST LAW 396 (1986).

benefits of high-tech product design."[98] There is merit to this criticism. What sort of evidence would courts rely upon to determine whether an integration's efficiencies outweigh the loss of consumer choice? The D.C. Circuit does not suggest any.

The drawbacks to both the *Jefferson Parish* and unstructured rule of reason tests prompt the question of whether a balanced alternative exists. Is there a test that demands a more thorough analysis than that required by *Jefferson Parish* but is not so open-ended that courts have no useful guideposts for evaluating tying arrangements in technologically dynamic markets? A number of candidates already exist.

E. Other Points on the Spectrum: Alternative Tying Tests

These candidates themselves range from the highly structured to the more open-ended. At the structured end is the D.C. Circuit's rule from *Microsoft II*. In that case the court rejected *Jefferson Parish* because it failed to distinguish "an upgrade from a separate product."[99] To overcome this problem, the D.C. Circuit held that any "genuine technological integration" should be treated as one product, "regardless of whether elements of the integrated package are marketed separately."[100] The court defined "genuine technological integration" as any "product that combines functionalities . . . in a way that offers advantages unavailable if the functionalities are bought separately and combined by the purchaser."[101] The D.C. Circuit set an extremely low bar for determining whether a product meets this test. All the defendant has to show is "a plausible claim" that the combination "brings some advantage."[102]

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98. United States v. Microsoft, 147 F.3d 935, 952 (D.C. Cir. 1998). The most recent D.C. Circuit opinion flailed in its attempt to explain away this earlier statement, asserting that "[t]o the extent that [*Microsoft II*] completely disclaimed judicial capacity to evaluate 'high-tech product design,' . . . it cannot be said to conform to prevailing antitrust doctrine (as opposed to resolution of the decree-interpretation issue then before us)." United States v. Microsoft, 253 F.3d 34 at 92.

99. *Microsoft II*, 147 F.3d at 947.

100. *Id.* at 948.

101. *Id.*

102. *Id.* at 950. It is important to note that the D.C. Circuit was careful to say that all it was doing in *Microsoft II* was interpreting the Consent Decree that governed Microsoft's behavior. *Id.* at 946. The court was also quite clear, however, that it believed its definition of integration was "consistent with the antitrust laws" and the tone of the opinion suggests the court's belief that this rule was the proper one for settling the two-product question as an antitrust matter. *Id.* at 948. In any event, the genuine technological integration rule has been treated as one potential substitute for the current tying rule and therefore should be considered in that light. *See* Sidak, *supra* note 35, at 34-37.

This test provides clear guidelines for deciding the separate-product question; any plausible claim of advantage wins the day for the defendant. As a result, the "genuine technological integration" test heavily favors potential innovation over protection of competition. The advantage of the test is that courts can avoid the mistake, possible under *Jefferson Parish,* of finding a truly procompetitive bundling arrangement illegal simply because separate demand continues to exist for the elements of the bundle. The great (and probably fatal) disadvantage of this test, however, is that it opens the door to increased anticompetitive behavior by monopolists.[103] Under the test, for instance, Microsoft may link any feature to Windows and survive antitrust scrutiny simply by making claims of some potential benefit.[104] These benefits may never accrue, or they may be so slight as to be far outweighed by the anticompetitive effect of the tie-in. In either case, the arrangement would survive under the "genuine technological integration" test.[105]

1. Market Practices Tests

While the *Microsoft II* test focused on the attributes of the product itself, "market practices" tests rely on the behavior of market participants for clues about whether a tying arrangement is anticompetitive.[106] Professor Phillip Areeda has proposed a well-known example of this type of test. His proposal concentrates on whether bundling is universal in a competi-

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103. United States v. Microsoft, 147 F.3d 935, 956-57 (D.C. Cir. 1998) (Wald, J., dissenting) (arguing that the majority rule creates "too safe a harbor with too easily navigable an entrance").

104. *Id.* at 957. *See also* Mariotti, *supra* note 88, at 386-389.

105. Professor Lawrence Lessig proposed a useful variation on this test in his amicus brief submitted in *Microsoft III.* Brief of Lawrence Lessig as Amicus Curiae, United States v. Microsoft Corp., 87 F. Supp. 2d 30 (D.D.C. 2000). Professor Lessig argued that courts should begin with the presumption that a software integration is one product rather than two and that a showing of special anticompetitive concern should be necessary to overcome this presumption. *Id.* at 40. Professor Lessig noted that anticompetitive concerns are raised by particular market conditions. For instance, if the bundled products are partial substitutes for each other, and the defendant has monopoly power in the tying product, then the bundle may be a way to ensure that the tied product does not become a competitive threat to the tying product monopoly. *Id.*

This rule is an improvement over the *Microsoft II* rule. While both rules favor potential innovation over protection against anticompetitive conduct, the Lessig rule makes it more likely that anticompetitive bundles will be rooted out. Professor Lessig's analysis openly acknowledges the risk that a low bundling bar will allow monopolists to engage in "strategic bundling" with anticompetitive effect. *Id.* The rule also provides some guidance for courts to recognize when this type of strategic bundling is taking place.

106. *See* Mariotti, *supra* note 88, at 374-77.

tive market or, if the market in question is not competitive, in analogous markets.[107] Universal bundling, according to Areeda, indicates one of three things: consumers prefer the bundle to the stand-alones, producing the bundle creates cost savings that appeal to consumers more than freedom of product choice, or the bundle provides an improvement in quality that outweighs loss of product choice.[108] If the market in question is not competitive, analogous markets can be used to perform the analysis.[109] If bundling is predominant rather than universal, the Areeda test would still find one product rather than two.[110]

The primary problem with the Areeda test is that because of network effects, economies of scale, and lock-in, software markets are often not competitive.[111] This means that "analogous markets" will need to be found in order to perform the test. It is not clear, however, which markets are analogous to those implicated in *Microsoft*. Geographical analogues are not available because the market for Windows is worldwide and there are very few consumers who are not locked-in. Thus, while the theory behind the Areeda test makes sense, it appears to be unworkable in practice.[112]

Despite the problems with the Areeda test, market practices tests are a promising avenue for reform. A well-structured test relying on both manufacturer and consumer behavior in the relevant antitrust market has the potential to provide clear rules for courts to follow while also successfully differentiating between anti- and procompetitive ties.[113]

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107. PHILLIP AREEDA ET AL., X ANTITRUST LAW 196 (1996).

108. *Id.* at 197.

109. Analogues may include similar markets in different geographic regions, historical markets, and markets for buyers who are not "locked in." *Id.* at 198-200.

110. Predominant bundling occurs when less than ten percent of the tying items are sold unbundled. *Id.* at 202.

111. *See supra* Section II.B.1.

112. For a detailed discussion of these problems with the Areeda test see Renato Mariotti, *Rethinking Software Tying*, 17 YALE J. ON REG. 367, 374-377 (2000).

113. The basis for such a test can perhaps be found in *United States v. Jerrold Elecs. Corp.* 187 F. Supp. 545 (E.D. Pa. 1960), *aff'd per curiam*, 365 U.S. 567 (1961). *Jerrold* concerned a community television antenna system that had four components. The defendant had market power in one of the components and was bundling it with the others. In order to decide the two-product question, the judge looked at a variety of factors including the behavior of other companies in the market, the fact that Jerrold charged customers per component rather than per system, and the fact that some customers wanted to purchase the entire system rather than the separate elements. *Id.* at 559. While the dispositive evidence was that the Jerrold system was initially unstable and needed to be sold as a unit, the way in which the opinion evaluated the behavior of market participants on both sides of the transaction was instructive.

2. *Economic Measurement Tests*

Another alternative is what I term "economic measurement" tests. Unlike market practices tests, which analyze the behavior of market participants for clues as to whether an arrangement is anticompetitive, economic measurement tests attempt to directly evaluate the costs and benefits of tying arrangements. Professors Janusz A. Ordover and Robert D. Willig have formulated one such test.[114] Their three-step approach applies to situations in which the defendant has "bottleneck" power in the primary market.[115] If such power exists, the first step is to determine whether the alleged exclusionary conduct creates a dangerous probability of a new monopoly in a "noncoincident" market.[116] This market must be clearly identified, and the challenged conduct must be the cause of the potential monopolization.[117] The second step is to measure profit from the challenged conduct versus profit from a hypothetical less-exclusionary alternative, with the assumption that the excluded rival continues to compete.[118] If the less-exclusionary conduct is more profitable, then the monopolist is sacrificing short-term profits in exchange for adverse effects on present and future competition.[119] The final step is to determine whether the exclusionary strategy is more profitable than the less-exclusionary strategy because it has led to the reduction of competition in the relevant market.[120] This step assumes that no rivals have survived.[121]

This test directly measures the costs and benefits of the arrangement to the monopolist. An arrangement offering higher costs than benefits, absent monopolization of a noncoincident market, will be anticompetitive.[122] While the spirit of the test is in line with current economic theory, it suf-

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114. Janusz A. Ordover & Robert Willig, *Access and Bundling in High-Technology Markets*, *in* COMPETITION, INNOVATION, AND THE MICROSOFT MONOPOLY: ANTITRUST IN THE DIGITAL MARKETPLACE, *supra* note 20, at 103.

115. Bottleneck power is defined as control over a component of a system in which the other components are independently useless. This bottleneck component is akin to an "essential facility." *Id.* at 105.

116. *Id.* at 109-11. A "non-coincident market" is a market outside the primary market. Examples include the primary market at a future date, the primary market at another geographic location, or an entirely different market. The Microsoft case concerned the first of these possibilities, an attempt to control the primary market (operating systems) at some later date (a possible future in which middleware supplanted Windows). *Id* at 110.

117. *Id.*

118. *Id.* at 110-11.

119. *Id.*

120. *Id.* at 111-13.

121. *Id.*

122. *Id.* at 109.

fers from the same implementation problems as the Areeda test. An analysis that requires courts to make suppositions about hypothetical markets and measure hypothetical costs will be difficult to put into practice.[123]

Other economic measurement tests include a number of proposed rules that would balance an arrangement's economic gains against its costs. Judge Wald's dissent in *Microsoft II* proposed one example. Judge Wald recommended a test that would balance the "synergies" generated by integrating two software products against the strength of evidence that distinct markets exist for the two products.[124] This test directly measures the benefits of the integration, but it suffers from the same implementation problems as the Ordover-Willig test. How is a court to accurately measure the pertinent synergies? Judge Wald suggested using "affidavits, consumer surveys . . . as well as testimony from experts."[125] This method provides only marginally more structure than the unstructured rule of reason test. It is hard to disagree with the majority's statement that the test "is not feasible in any predictable or useful way."[126]

Other tests require similar balancing acts.[127] One commentator has suggested a test for technologically dynamic markets that balances increased demand or reduced costs created by the integration against losses to consumer welfare resulting from reduced competition caused by the in-

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123. As one observer noted of the Ordover-Willig test:

> [M]y major question concerns the practicability of prongs 2 and 3. Though they may be sensible in principle, how much practical guidance do they provide to antitrust policy makers? How would they help . . . decide whether Microsoft should or should not be forced to allow the PC manufacturers to delete its Explorer browser from their licensed software. How would prongs 2 and 3 help . . . decide whether Microsoft should be allowed to bundle its browser with Windows 98 or instead be required to sell the browser separately. I fear that an understanding of prongs 2 and 3 will not provide much help in addressing these questions.

Lawrence J. White, *Microsoft and Browsers. Are the Antitrust Problems Really New?*, *in* COMPETITION, INNOVATION, AND THE MICROSOFT MONOPOLY: ANTITRUST IN THE DIGITAL MARKETPLACE, *supra* note 20, at 137, 150.

124. United States v. Microsoft, 147 F.3d 935, 958-59 (D.C. Cir. 1998) (Wald, J., dissenting).

125. *Id.* at 958 n.3.

126. *Microsoft II*, 147 F.3d at 952.

127. *See e.g.*, Renato Mariotti, *Rethinking Software Tying*, 17 YALE J. ON REG. 367 (2000) (balancing the gains in innovation and reduction in transaction costs for consumers who want both the tying and tied product against the costs to consumers who only want the tying product)

tegration.[128] As with Judge Wald's test, this formulation asks the right question: does the integration increase consumer welfare? But again, it is difficult to imagine the test being applied in practice. The problem with of these tests is that the variables to be balanced are very difficult to measure.

Economic measurement tests are attractive because rather than using proxies to determine whether conduct is anticompetitive, they strive to directly measure competitive effect. The problem with these tests, at least those proposed to date, is that they are difficult to put into practice. This is because they require courts either to perform complicated economic analyses of purely hypothetical markets and practices, or to make measurements that may be inexact at best.

IV. CONCLUSION: THE PRESSING NEED TO FASHION A NEW TEST

Microsoft has already raised fresh tying concerns by bundling an instant messaging program with its new operating system.[129] This type of action is facilitated by the overly vague D.C. Circuit rule of reason test for tying cases. A more structured rule is needed to make the bounds of legal integration clear. While economic measurement tests closely track current economic theory, they are difficult for courts to apply. A well-designed market practices test relying on both manufacturer and consumer behavior in the relevant antitrust market provides the best chance to generate accurate, consistent, and predictable jurisprudence in this arena.

In markets that tend toward monopoly, it is likely that this will not be the last time the tying issue is litigated. Lacking a definitive standard, courts will not be able to provide consistent outcomes in these kinds of cases. Courts should move quickly to cut through the confusion left in the wake of *Microsoft III* or face continued problems with product integration.

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128. Sidak, *supra* note 35. Sidak proposes a four-part test for determining whether an integration in a technologically dynamic market violates the antitrust laws. The first step is to determine whether the market is technologically dynamic. If it is not, *Jefferson Parish* will apply. If it is, the next step is to determine whether consumers will benefit from the integration, with benefits measured by increased consumer demand, lowered costs of production, or both. These benefits are not measured in comparison with a hypothetical world in which the products have not been integrated. The only question is whether some actual benefits have been created by the integration. The third step is to determine whether the integration will preserve a monopoly over the tying product market. If it will, the fourth step is to balance the integration's consumer benefits against the losses in consumer welfare caused by any reduction in competition. *Id.* at 28-33.

129. Einer Elhague, *A Smart Move on Microsoft*, BOSTON GLOBE, Sept. 11, 2001, at C4; Joseph Menn, *Microsoft, Officials to Seek Mediator*, L.A. Times, Oct. 12, 2001, at 152.

IN RE MICROSOFT CORP. ANTITRUST LITIGATION

By Ramona Mateiu

The Department of Justice's suit against Microsoft for antitrust violations has been headline news for the past few years. While much attention has focused on the government's case against Microsoft, an important decision regarding the private suits by consumers against the software giant also warrants discussion. In *In re Microsoft Antitrust Litigation*, the United States District Court for the District of Maryland applied the *Illinois Brick* doctrine to dismiss 38 private antitrust lawsuits filed against Microsoft. The *Illinois Brick* doctrine was established at a time when the phrase "bricks and mortar" referred only to building materials and computer software was a term only scientists and engineers used. The doctrine, which forbids private antitrust suits by indirect purchasers of a product, was structured around traditional notions of products and services. Many of the underlying principles supporting the *Illinois Brick* doctrine do not apply to our information-driven economy. In *Microsoft*, the court was faced with difficult questions regarding the application of the *Illinois Brick* doctrine to the software industry. Rather than answering these questions, the court dismissed them with little discussion.

This Note will consider two of the plaintiffs' arguments in the *Microsoft* case and conclude that *Illinois Brick* should not bar private antitrust lawsuits against Microsoft. First, this Note will explore the plaintiffs' assertion that their case falls within the control exception to the direct purchaser rule because Microsoft controls the Original Equipment Manufacturers ("OEMs"). This Note will then discuss plaintiffs' argument that *Illinois Brick* does not bar their suits because consumers are direct purchasers of Microsoft's product. While the court's refusal to apply the control exception was consistent with precedent, if not good policy, the court should have accepted the plaintiffs' second argument. The software industry generally licenses products to consumers, rather than sell them to OEMs outright. Therefore, the court should have held that Microsoft sells its product directly to the consumer, barring application of the *Illinois Brick* doctrine.

I. LEGAL BACKGROUND

Section four of the Clayton Act provides that "any person who shall be injured in his business or property by reason of anything forbidden in the

antitrust laws may sue therefore . . . and shall recover threefold the damages . . . ."[1] Congress had two broad objectives when it allowed private enforcement of the antitrust laws. First, Section 4 was enacted to compensate victims of antitrust violations for their injuries.[2] Congress's second objective was deterrence; Section 4 was meant to deter antitrust violations by imposing significant costs on violators.[3] While these goals imply broad power to sue under the antitrust laws, the Supreme Court has limited the private right of action in antitrust suits. A central limitation in many private suits, including the suits against Microsoft, is the direct purchaser rule established in *Illinois Brick Co. v. Illinois*.[4]

A. Direct Versus Indirect Purchasers

The Court first established the distinction between direct and indirect purchasers in antitrust law in *Hanover Shoe v. United Machine Corp.*[5] A direct purchaser is the initial buyer in the vertical supply chain, who therefore buys directly from the monopolizing firm.[6] An indirect, or downstream, purchaser is one who purchases a price-fixed product from a middleman, who will have passed on the anticompetitive overcharge to his customer.[7] Often, the direct purchaser of the monopoly product is not the final consumer; distributors or other manufacturers higher up on the vertical supply chain are the direct purchasers.[8] According to the pass-on theory, the direct purchaser absorbs part of the overcharge and passes the rest on to the next link in the supply chain.[9] The process is repeated as each indirect purchaser sells to the next indirect purchaser in the chain. In the end, however, the final product purchased by consumers reflects the majority of the overcharge.[10] In *Hanover Shoe*, defendants argued that plaintiff shoe manufacturers should not be allowed to sue under Section 4 because they had passed on the alleged overcharge to their customers.[11] The

1. 15 U.S.C. § 15(a) (1994).
2. Jill S. Kingsbury, *The Indirect Purchaser Doctrine: Antecedent Transaction?* 65 MO. L. REV. 473, 477 (2000).
3. *Id.*
4. 431 U.S. 720 (1977).
5. 392 U.S. 481 (1968).
6. Kingsbury, *supra* note 2, at 478.
7. *Id.*
8. *Id.*
9. *Id.*
10. *Id.*
11. 392 U.S. at 491-92.

Supreme Court rejected this argument and barred the use of the pass-on theory as a defense.[12]

B. *Illinois Brick* Doctrine

The Supreme Court's decision in *Illinois Brick* further restricted the use of the pass-on theory.[13] In that case, the Court held that indirect purchasers of goods and services from firms engaged in price fixing could not use a pass-on theory to recover for the alleged antitrust violations.[14] The plaintiffs argued that they were entitled to recover damages because the direct purchasers passed on the overcharge to them.[15] The Court explained that only direct purchasers could sue for alleged antitrust violations.[16] The plaintiffs in *Illinois Brick* were public entities that owned buildings constructed with concrete block purchased from defendants by subcontractors.[17] The plaintiffs sought to recover treble damages under Section 4 of the Clayton Act.[18] They alleged that defendants conspired to fix prices of concrete block in violation of Section 1 of the Sherman Act.[19]

The Court denied the indirect purchasers' claims on three grounds. The Court first reasoned that the rule regarding the pass-on theory must apply equally to both plaintiffs and defendants.[20] Otherwise, if indirect purchasers were free to sue for overcharges passed on, and defendants could not use the pass-on defense against direct purchasers, defendants would be subject to multiple liabilities. The *Illinois Brick* Court had either to reverse *Hanover Shoe* or to prohibit the use of the pass-on theory by the plaintiffs if it was to avoid multiple liabilities for defendants.[21] The Court opted to deny the use of pass-on theory completely.[22]

The Court also feared that suits by indirect purchasers would get out of control because each downstream purchaser would attempt to show the amount of damages it suffered as a result of some remote price-fixing

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12. *Id.* at 488.
13. *See* Roger D. Blair & Jeffrey L. Harrison, *Reexamining the Role of* Illinois Brick *in Modern Antitrust Standing Analysis,* 68 GEO. WASH. L. REV. 1 (1999) (discussing the restrictions on use of the pass-on theory).
14. 431 U.S. at 747.
15. *Id.* at 727.
16. *Id.* at 728.
17. *Id.* at 726.
18. *Id. See also* 15 U.S.C. § 15 (1994).
19. 15 U.S.C. § 1 (1994).
20. 431 U.S. at 729.
21. *Id.* at 730.
22. *Id.*

scheme.[23] Federal courts would therefore be left with the impossible task of apportioning damages among direct and indirect victims.[24] The Court explained that allowing the plaintiffs to assert pass-on theories would "greatly complicate and reduce the effectiveness of already protracted treble-damages proceedings."[25]

Finally, the Court found that the value of deterring violations of the antitrust laws and depriving violators of gains from illegal activity outweighed the need to compensate victims for antitrust violations.[26] The Court held that concentrating the full recovery in direct purchasers would provide a greater incentive for them to bring actions, thereby deterring others from committing similar violations.[27] The Court did not have a problem with direct purchasers collecting the full amount of the overcharge, even if it exceeded the actual harm they suffered.

C. Exceptions to the Direct Purchaser Rule

In two footnotes of the opinion, the *Illinois Brick* Court left open two possible ways for indirect purchasers to recover treble damages for an overcharge. An indirect purchaser can recover if either: (1) the indirect purchaser has a preexisting cost plus contract with the direct purchasers or (2) the direct purchaser is owned or controlled by its customer.[28] The second exception actually applies both when the indirect purchaser controls the direct purchaser and when the price fixing firm controls the direct purchaser.[29] Courts have interpreted these two exceptions to the direct purchaser rule narrowly, however, and the Supreme Court has eliminated the possibility of other exceptions to the rule.

At first, it appeared that courts could interpret the exceptions to the direct purchaser rule broadly, allowing indirect purchasers to sue in other situations. In *California v. ARC America Corp.*,[30] the Supreme Court stated that "indirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was

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23. *Id.* at 732.
24. *Id.*
25. *Id.*
26. *Id.* at 746.
27. *Id.*
28. *Id.* at 736, n.16.
29. *In re* Microsoft Corp. Antitrust Litig., 127 F. Supp. 2d 702, 712 (D. Md. 2001). *See also In re* Brand Name Prescription Drugs Antitrust Litig., 123 F.3d 599, 605 (7th Cir. 1997); Jewish Hospital Ass'n v. Stewart Mech. Enters., 628 F.2d 971, 975 (6th Cir. 1980); *In* re Mid-Atlantic Toyota Antitrust Litig., 516 F. Supp. 1287, 1292 (D. Md. 1981).
30. 490 U.S. 93 (1989).

passed on to them."[31] However, in *Kansas v. Utilicorp United, Inc.*,[32] the Supreme Court retreated from this broad interpretation of the *Illinois Brick* exceptions and severely narrowed application of exceptions to the direct purchaser rule.

In *Utilicorp*, the Court completely eliminated the possibility of any policy-based exceptions to *Illinois Brick*. In that case, public utilities filed suit against natural gas producers and pipeline companies for antitrust violations.[33] Kansas and Missouri also filed suits asserting similar antitrust claims in *parens patriae* capacity on behalf of residential consumers who purchased gas from the public utilities.[34] The states argued that consumers paid inflated prices because a pipeline and a group of gas production companies were fixing prices.[35] Residents of Kansas and Missouri, however, were indirect purchasers of natural gas because they purchased from utilities, not gas producers.[36] The states claimed that their suit should nonetheless move forward because utilities, which were the direct purchasers, passed on the full overcharge to consumers and thus the apportionment problem present in *Illinois Brick* did not exist.[37]

The majority rejected the plaintiffs' assertion. The Court held that "only the utility has the cause of action because it alone has suffered injury within the meaning of § 4."[38] The plaintiffs asserted that none of the rationales underlying *Hanover Shoe* and *Illinois Brick* exist in cases involving public utilities. The Court, however, stated that, while the rationales of *Hanover Shoe* and *Illinois Brick* might "not apply with equal force in all instances," it was "inconsistent with precedent and imprudent in any event to create an exception for regulated public utilities."[39]

The application of the control exception to private Microsoft lawsuits is further complicated by the Seventh Circuit's holding in *In re Brand Name Prescription Drugs Antitrust Litigation* ("*PDAL*").[40] In that case, the Seventh Circuit applied a narrow interpretation of the control exception to the direct purchaser rule. Plaintiff pharmacies sued both manufacturers and wholesalers of prescription drugs alleging a price-fixing con-

31. *Id.* at 102, n.6 (dictum).
32. 497 U.S. 199 (1990).
33. *Id.* at 203.
34. *Id.* at 204.
35. *Id.* at 204-5.
36. *Id.* at 207.
37. *Id.* at 208.
38. *Id.* at 204.
39. *Id.* at 216.
40. 123 F.3d 599 (7th Cir. 1997).

spiracy.[41] The pharmacies claimed that defendants conspired among themselves to deny them discounts from the list price of brand name drugs and maintained this differential pricing through a "chargeback" system.[42] Under the system, manufacturers signed contracts which favored some customers, including hospitals, health maintenance organizations, nursing homes, and mail order companies, setting a discounted price at which these customers were entitled to buy from wholesalers.[43] The manufacturers then reimbursed the wholesalers for the difference between the regular wholesale price and the discounted price.[44] The plaintiffs' claim was not based on the discrimination as such; it was based on the high prices that resulted as a consequence of defendants' conspiracy, prices that competition would have otherwise brought down.[45]

Manufacturers argued that pharmacies that purchased the drugs from wholesalers were indirect purchasers; therefore, the direct purchaser rule prevented them from bringing suit.[46] The district court interpreted the control exception to the direct purchaser rule broadly to allow suits by indirect purchaser pharmacies.[47] The district court asserted that the control exception should apply where "the degree of control exercised by the defendant effectively transforms the transaction—from defendant to middleman to indirect purchaser—into one sale."[48]

The Seventh Circuit rejected the district court's broad reading of the control exception. The court held that pharmacies were not allowed to bring suit for overcharges under the Sherman Act against manufacturers for purchases made through wholesalers.[49] According to the court, "[t]he manufacturers do no control the wholesalers through interlocking directorates, minority stock ownership, loan agreements that subject the wholesalers to the manufacturers' operating control, trust agreements, or other modes of control separate from ownership of a majority of the wholesalers' common stock" and thus the control exception did not apply.[50]

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41. *Id.* at 603.
42. *Id.*
43. *Id.*
44. *Id.*
45. *Id.*
46. *Id.* at 604.
47. *Id.*
48. In re Brand Name Prescription Drugs Antitrust Litig., No. 94 C 897, 1996 U.S. Dist. LEXIS 4335, at *88 (N.D. Ill. Apr. 4, 1996) (citing Jewish Hosp. Ass'n v. Stewart Mech. Enters., 628 F.2d 971 (6th Cir. 1980)).
49. *In re* Brand Name Prescription Drugs Antitrust Litig., 123 F.3d at 605-06.
50. *Id.*

D. Federal Preemption of State Indirect Purchaser Statutes

After the Supreme Court's decision in *Illinois Brick*, a number of states and the District of Columbia enacted *Illinois Brick* repealer statutes.[51] These statutes allowed indirect purchasers to sue under state antitrust laws. In one of the most significant decisions regarding private antitrust litigation, the Supreme Court held that federal antitrust law did not preempt state *Illinois Brick* repealer statutes.[52]

In *California v. ARC America Corp.*, the plaintiffs were state governments that were indirect purchasers of cement.[53] The plaintiffs filed their lawsuits under both federal antitrust law and under state antitrust laws that allowed suits by indirect purchasers. The Supreme Court was forced to decide whether *Illinois Brick* and *Hanover Shoe* preempted state laws permitting indirect purchasers to recover damages against antitrust violators.[54] The Court held that preemption did not occur in this case because Congress did not intend to occupy the field and the state statutes did not actually conflict with federal law.[55] The Court explained that suits by indirect purchasers would not necessarily complicate matters in federal courts.[56] State antitrust issues would be decided in state courts and federal courts could decline to consider state claims.[57] The Court also found that allowing indirect purchasers to sue under state antitrust laws would not decrease the incentive for direct purchasers to sue under federal antitrust laws.[58] Finally, the Court addressed the issue of multiple liabilities by stating that the Court has never identified a federal policy against states imposing liability in addition to that imposed by federal law.[59]

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51. *Illinois Brick* repealer statutes were enacted by Alabama, Arizona, California, Colorado, District of Columbia, Hawaii, Idaho, Illinois, Kansas, Maine, Maryland, Michigan, Minnesota, Mississippi, Nevada, New Mexico, New York, North Carolina, North Dakota, Rhode Island, South Dakota, Tennessee, Vermont, and Wisconsin. *See* Thomas Greene et al., *State Antitrust Law and Enforcement,* 1252 PLI/CORP 1129 (2001).

52. California v. ARC Am. Corp., 490 U.S. 93 (1989).

53. *Id.* at 97-98. For a complete discussion of *California v. ARC America Corp.*, see Ronald W. Davis, *Indirect Purchaser Litigation:* ARC America*'s Chickens Come Home to Roost on the* Illinois Brick *Wall,* 65 ANTITRUST L.J. 375 (1997).

54. 490 U.S. at 100.

55. *Id.* at 103.

56. *Id.*

57. *Id.* at 104.

58. *Id.* at 105.

59. *Id.*

E. The Relation Between Antitrust Standing Doctrine and *Illinois Brick*

While *Illinois Brick* appears to be about standing under federal antitrust law, the Supreme Court has not treated it as such. The Court developed a multipart test for determining antitrust standing in *Associated General Contractors, Inc. v. California State Council, Inc.* ("*AGC*").[60] To have standing to sue, the plaintiff must have suffered an antitrust injury.[61] Once injury is established, a court must weigh the remoteness of the injury, the existence of a potential plaintiff with greater motivation to sue, and the complexity of the ensuing litigation, before the plaintiff is permitted to bring an action.[62] It seems logical that suits by most indirect purchasers would be barred by the second part of the *AGC* test. It is likely that the injury to indirect purchasers would be too remote, that there would be other plaintiffs with greater motivation to bring an action, and that litigation by an indirect purchaser would be overly complex.[63] However, the Court has not folded *Illinois Brick* into a general standing analysis.[64] Instead, *Illinois Brick* is viewed as analytically distinct from the *AGC* test.[65] So, while some indirect purchasers might pass the *AGC* standing test, their suits are nonetheless automatically barred under *Illinois Brick.*

II. CASE SUMMARY

A. Factual Background

In May 1998, the U.S. government and nineteen states filed suit against Microsoft alleging antitrust violations under sections one and two of the Sherman Act. As the Department of Justice's highly publicized suit against Microsoft progressed, consumers in various states filed private suits for treble damages under Section 4 of the Clayton Act and under state antitrust laws. Microsoft transferred sixty-one antitrust actions to a multidistrict litigation in a Maryland federal court.[66]

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60. 459 U.S. 519 (1983).
61. *Id.* at 540.
62. *Id.* at 542-544.
63. *See* Blair & Harrison, *supra* note 13, at 16-17.
64. *Id.*
65. *Id.* at 17.
66. The suits were consolidated under 28 U.S.C. § 1407(a), entitled Multidistrict Litigation, which states that "when civil actions involving one or more common questions of fact are pending in different districts, such actions may be transferred to any district for coordinated or consolidated pretrial proceedings."

The plaintiffs in the multidistrict litigation made several allegations regarding Microsoft's exclusionary, predatory and anticompetitive acts. The plaintiffs alleged that Microsoft intentionally caused end users to suffer unique injury as a direct result of Microsoft's restrictive and exclusionary practices.[67] The plaintiffs maintained that Microsoft deprived end users of the benefits of competition including "technological innovation, market choice, product variety and substitutable supply."[68] Furthermore, Microsoft's end-user license agreement ("EULA") restrictions forced consumers to acquire a new EULA with each new PC, and thus deprived consumers of other products.[69]

According to the plaintiffs, Microsoft abused its operating system licensing monopoly power so as to anticompetitively deprive consumers of any new technology that would permit consumers to use applications without the Microsoft operating system.[70] The new technology included, among other things, the DR-DOS and OS/2 operating systems, Mirrors, Object Windows Library, Native Signal Processing, Netscape and Sun Microsystem's Java programming language.[71] With respect to Java, for example, Microsoft deceived Java developers by leading them to believe that Microsoft's Java Virtual Machine ("JVM") was compatible with Sun's JVM and vice versa.[72] Microsoft sought to quash the development of Java because it feared that it would make all operating systems compatible with one another. Furthermore, the plaintiffs claimed that once Microsoft eliminated all products that competed with its operating system, it began charging a higher price and imposed far more anticompetitive restrictions on end users.[73]

The court in *In re Microsoft Corp. Antitrust Litigation*, dismissed damages claims in many of the cases consolidated in the Maryland federal court.[74] The court granted Microsoft's motion to dismiss as to cases filed by consumers who did not purchase their products directly from Microsoft and as to foreign plaintiffs, but remanded those cases that had valid state claims back to state court.[75] The court held that suits by consumers who did not purchase Microsoft's product directly from Microsoft and who

67. *In re* Microsoft Corp. Antitrust Litig., 127 F. Supp. 2d 702, 706 (D. Md. 2001).
68. *Id.*
69. *Id.* at 707.
70. *Id.* at 705.
71. *Id.* at 706-08.
72. *Id.* at 708.
73. *Id.* at 707.
74. *Id.* at 704.
75. *Id.*

sought to recover an overcharge were barred under the direct purchaser rule of *Illinois Brick*.[76]

B. The Multi-district Litigation Analysis and Conclusion

1. Illinois Brick *Issues*

In deciding whether *Illinois Brick* barred the plaintiffs' suit, the court asked two questions. First, were the plaintiffs seeking damages for an illegal overcharge?[77] And second, were the plaintiffs indirect purchasers of Microsoft product?[78] The court answered both questions in the affirmative, and thus held that the *Illinois Brick* doctrine barred their lawsuits.

The court focused on the question of whether the plaintiffs were claiming damages for an illegal overcharge. The plaintiffs' damages claims fell into four general categories.[79] The plaintiffs first claimed damages for supracompetitive prices for Windows and three application programs: Word, Excel, and Office Suites.[80] Second, the plaintiffs sought damages for denial of the benefit of technologically superior products, including alternative operating systems and application programs.[81] The plaintiffs' third damages claim arose out of increased restriction on their EULA rights.[82] Finally, the plaintiffs claimed damages from degradation of computer performance by the tying of Internet Explorer to Windows.[83] The court denied all four types of the plaintiffs' damages claims.

The court held that the plaintiffs' claim for supracompetitive prices was clearly barred under *Illinois Brick* because the plaintiffs sought recovery for illegal overcharges.[84] The court next rejected the plaintiffs' damages claims for denial of the benefit of technologically superior products, holding that the damages amounted to a measurable overcharge. Moreover, the court held that the plaintiffs lacked standing to assert these claims because Microsoft's competitors were more direct victims of the alleged antitrust violations, and because calculating and apportioning the plaintiffs' damages would be virtually impossible.[85] The court also denied the plaintiffs' claims that they were damaged by Microsoft's increased

76. *Id.*
77. *Id.* at 709.
78. *Id.* at 708.
79. *Id.* at 709.
80. *Id.*
81. *Id.*
82. *Id.* at 710.
83. *Id.*
84. *Id.*
85. *Id.* at 711.

EULA restrictions.[86] The court held that these claims amounted to a claim for an overcharge, and were therefore barred by *Illinois Brick*.[87] Finally, the court rejected the plaintiffs' last damages claim because it did not constitute an antitrust injury. The court held that the plaintiffs' claims for degradation of the performance of their computers caused by the alleged tying of Internet Explorer to Windows was only incidentally related to the alleged anticompetitive behavior.[88]

The plaintiffs in the Microsoft multi-district litigation argued that they were direct purchasers of Microsoft's product.[89] They maintained that the product they purchased was not the software, but EULAs that ran between Microsoft and themselves.[90] The court quickly rejected the plaintiffs' claims that they were direct purchasers.[91] It held that, although the EULA may have established a direct relationship between Microsoft and the plaintiffs, it was not sufficient to make them "direct purchasers" within the meaning of *Illinois Brick*.[92]

The plaintiffs also argued that their case fell within the control exception to *Illinois Brick*. Microsoft, they argued, used its monopoly power "to capture, dominate and exclusively control the OEM distribution channel."[93] Microsoft also forced OEMs to act as its agents in offering end-user licenses for acceptance or rejection by customers under terms strictly and exclusively dominated by Microsoft.[94] The court held that the control exception should be narrowly construed to include only "relationship[s] involving such functional economic or other unity . . . that there effectively has been only one sale."[95]

The court further held that the control exception only applies where the price fixing firm controls the direct purchaser "through interlocking directorates, minority stock ownership, loan agreements that subject wholesalers to the manufactures' operating control, trust agreement, or other modes of control separate from ownership of a majority of the

86. *Id.* at 712.
87. *Id.*
88. *Id.*
89. *Id.* at 709.
90. *Id.*
91. *Id.*
92. *Id.*
93. *Id.* at 713.
94. *Id.*
95. *Id.* (quoting Jewish Hosp. Ass'n v. Stewart Mech. Enters., 628 F.2d 971, 975 (6th Cir. 1980).

wholesalers' common stock."[96] Finding that OEMs are clearly independent entities capable of making their own decisions, the court refused to apply the control exception to *Illinois Brick*.[97] The court nonetheless implied that if Microsoft controlled the OEMs' decision-making process with respect to setting prices, the control exception might apply. However, the plaintiffs did not allege, and the court did not find, that Microsoft controlled the OEMs' pricing decisions.[98]

C. Private Microsoft Suits Filed Under State Antitrust Laws

Microsoft's victory under the federal antitrust laws will not necessarily translate into victory under state antitrust laws. If consumers in the states that have enacted *Illinois Brick* repealer statutes can show Microsoft abused its monopoly power, they can sue under those states' antitrust laws. In fact, dozens of private suits are still moving forward in several states. Consumer suits in Arizona, California, Michigan, and Minnesota have already been granted class-action status.[99] Microsoft may face its toughest battles under these state laws, especially in states like California, where there are strong pro-consumer laws. The option of state law actions may make it unlikely that the plaintiffs will appeal the Maryland federal court's decision.

III. DISCUSSION

The *Microsoft* plaintiffs' arguments regarding the control exception and direct purchasing of licenses deserve more serious consideration than the court gave them. According to the plaintiffs, the control exception to *Illinois Brick* should apply in this case because Microsoft exhibits substantial control over the direct purchasers, the OEMs. Thus, the direct purchaser rule should not bar private antitrust suits against Microsoft by consumers. The court's decision not to apply the control exception may be consistent with precedent, but it is not consistent with good policy or the goals of *Illinois Brick*. Even if the court's refusal to apply the control exception was proper, the plaintiffs' suits should not have been dismissed. The plaintiffs also claimed that consumers are direct purchasers of Microsoft's product because consumers purchased the EULA, which is the actual product, directly from Microsoft. The court rejected this argument

96. *Id.* (quoting *In re* Brand Name Prescription Drugs Antitrust Litig., 123 F.3d 599, 605-06 (7th Cir. 1997)).

97. *Id.*

98. *Id.*

99. *Private Microsoft Suit Wins Class-action Status*, CNET NEWS, Apr. 5, 2001, *at* http://news.com.com/2100-1001-255410.html?legacy=cnet.

without really addressing the plaintiffs' assertions. One does not ordinarily think of a contract as the product, but given the nature of the software industry, it is surprising that the court dismissed the plaintiffs' argument so quickly. The court should have accepted the argument that consumers are direct purchasers because it is consistent with both software industry practices and the court's treatment of software licenses.

A. The Control Exception of *Illinois Brick*

The plaintiffs in the private suits against Microsoft argued that the control exception to the direct purchaser rule applied in their case because Microsoft used its monopoly power to control the OEM distribution channel.[100] The court refused to apply the control exception, holding that OEMs were still capable of making their own decisions.[101] There are, however, strong arguments that support applying the control exception to the suits against Microsoft.

Microsoft is a uniquely powerful monopoly, possessing a market share of over 95%.[102] Microsoft's monopoly is a consequence of anticompetitive practices and network effects[103] in the software industry. In the years leading up to the antitrust litigation, the combination of restrictive licenses and network effects effectively gave Microsoft control over the OEMs. Microsoft controlled OEMs using restrictive license agreements, which prohibited the OEMs from doing such things as removing any desktop icons, folders, or "Start" menu entries, altering the initial boot sequence, or otherwise altering the appearance of the Windows desktop.[104] Microsoft imposed these restrictions on OEMs in an effort to prevent them from installing Netscape or any other program that threatened Microsoft's market power.[105] Network effects in the computer industry also contributed to Microsoft's power over the OEMs. OEMs could not risk standing up to Microsoft without being driven out of business if Microsoft stopped dealing with them. The OEMs did not have other valid options for an operating system; consumers would not buy a computer that did not have an op-

100. *In re Microsoft*, 127 F. Supp. 2d at 712.

101. *Id.* at 713.

102. U.S. v. Microsoft Corp., 253 F.3d 34, 52 (D.C. Cir. 2001).

103. When network effects are present, a product becomes more attractive to buyers as more people use the product. Microsoft's operating system is an example of a virtual network, one in which consumers are not actually connected to each other. A second type of network is a real network, one where consumers are connected; for example, fax machines. *See* CARL SHAPIRO & HAL R. VARIAN, INFORMATION RULES: A STRATEGIC GUIDE TO THE NETWORK ECONOMY 3, 174-75 (1999).

104. *Microsoft Corp.*, 253 F.3d at 60.

105. *Id.* at 59.

erating system for which software was available. Microsoft therefore had substantial power over the OEMs.

The legal standard for the control exception, however, requires Microsoft to exhibit a much higher level of control over OEMs. According to the Seventh Circuit decision in *PDAL*, customers must demonstrate that Microsoft controlled the OEMs through "interlocking directorates, minority stock ownership, loan agreements that subject the wholesalers to the manufacturers' operating control, trust agreement, or other modes of control separate from ownership of a majority of the wholesalers' common stock."[106] The *PDAL* opinion also implies that "the manufacturers' ability to dictate wholesalers' pricing policies would permit the plaintiffs to avail themselves of the control exception to *Illinois Brick* only if the manufacturers had affirmatively intervened in the wholesalers' pricing decisions vis-à-vis plaintiffs."[107]

If manufacturers had used their economic power to force wholesalers to raise prices the Seventh Circuit might have applied the control exception and permitted the plaintiffs to sue. This interpretation of *PDAL* seems consistent with the *Microsoft* court's interpretation. Recall that the court stated that the plaintiffs did not allege that Microsoft controlled the intermediaries' decision-making processes with respect to setting prices.[108] According to the court, the setting of prices is a critical issue in applying the control exception.[109] While Microsoft exerted substantial control over the OEMs, it does not appear that Microsoft controlled the OEMs' price setting practices. Thus, under the Seventh Circuit's standard, it is clear that the court's holding that the control exception did not apply to the *Microsoft* case was correct.

The court's decision not to create another exception to the direct purchaser rule based on Microsoft's unique position in the market was also consistent with precedent. After the Supreme Court's holding in *Utilicorp*, it is apparent that courts should not create any further exceptions to the *Illinois Brick* doctrine based on policy considerations, even in cases where the monopolizing firm has such a high market share. While Microsoft's control over the market for Intel-compatible PCs is substantial, the *Utilicorp* Court held that there are ample justifications for not carving out ex-

106. *In re* Brand Name Prescription Drugs Antitrust Litig., 123 F.3d 599, 605-06 (7th Cir. 1997).

107. Michael S. Jacobs, *Lesson From the Pharmaceutical Antitrust Litigation: Indirect Purchasers, Antitrust Standing, and Antitrust Federalism,* 42 ST. LOUIS U. L.J. 59, 77 (1998).

108. *In re* Microsoft Corp. Antitrust Litig., 127 F. Supp. 2d at 713.

109. *Id.*

ceptions to the direct purchaser rule for particular types of markets. According to the majority, "the possibility of allowing an exception, even in rather meritorious circumstances, would undermine the rule."[110]

Recent precedent therefore supports the court's holding that consumers in the *Microsoft* case did not meet the technical requirements for the control exception. The court's finding, however, implies a problem with interpretation of the control exception, not a lack of control. The *Illinois Brick* court explained that the exceptions to the direct purchaser rule were designed to cover situations in which market forces have been superseded.[111] The court's language suggests that the exceptions to the direct purchaser rule should be interpreted broadly. There is no doubt that market forces have been superseded in the *Microsoft* case. Furthermore, the *Illinois Brick* Court's language does not suggest that the two exceptions were meant to be exclusive.[112] The exceptions only provide concrete examples of which exceptions to the direct purchaser rule will best serve the policies underlying the Court's opinion.[113] The exceptions suggest that indirect purchasers may sue when the direct purchaser has little motivation to sue.[114] Consumers should therefore be able to sue Microsoft for antitrust violations because the OEMs have not, and likely will not, sue Microsoft.[115]

A fundamental goal of the Supreme Court in *Illinois Brick* was to ensure that the party with the most motivation to sue could sue.[116] The Court stressed that the goal of deterrence was more important than the need to compensate victims of antitrust violations.[117] In the *Microsoft* case, the consumer is the party with the most motivation to sue; in fact the consumer is the only party with motivation to sue. OEMs with no viable alternative to Microsoft's products cannot risk suing their only supplier.

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110. Kansas v. Utilicorp United, Inc., 497 U.S. 199, 216 (1990).

111. Illinois Brick v. Illinois, 431 U.S. 720, 736 n.16 (1977).

112. Jerome Musheno, *Antitrust Law—Should Standing Be an Issue for the Indirect Purchaser in a Vertical Conspiracy?*, 72 TEMP. L. REV. 251, 277 (1999).

113. *Id.*

114. Blair & Harrison, *supra* note 13, at 2.

115. As discussed *supra* text accompanying notes 104-105, OEMs could not afford to risk their relationships with Microsoft, so much so that OEMs did not support the government's case against Microsoft. In Texas, Dell Computer Corporation persuaded the state not to join the federal government's case. ROBERT W. HAHN, THE COSTS OF REGULATING MICROSOFT, SD72 ALI-ABA 93, 100 (1999).

116. 431 U.S. at 746.

117. *Id.*

B. Consumers Are Direct Purchasers

Precedent supports the district court's holding that the control exception to the direct purchaser rule does not apply to the relationship between Microsoft and OEMs. However, the plaintiffs also argued that consumers are direct purchasers because the EULA is the product. The court should have accepted this argument, particularly because it does not require any further exceptions to the direct purchaser rule, and there is no need to broaden the two exceptions created by the *Illinois Brick* Court. The argument that consumers are direct purchasers fairly characterizes software industry practices while removing the case from the purview of the *Illinois Brick* doctrine.

1. The Nature of the Software Industry

Transactions involving computer software differ from those involving ordinary goods because software transactions focus on the transfer of intangibles.[118] Most software transactions do not result in the transfer of title to the underlying software; rather, software manufacturers typically confer use rights to the software via license agreements.[119] The two most common types of license agreements are those between the software producer and the OEM, and those between the software producer and the end user.[120] The rights conferred by these two types of licenses are fundamentally different.

Microsoft distributes its software primarily through OEM licenses.[121] These OEM licenses run directly between Microsoft and the OEMs, and allow the OEMs to pre-install Microsoft software on PCs sold to end users.[122] The OEMs then sell the computer hardware containing the Microsoft software. Consumers receive computers with software preinstalled. Purchasing the computer does not automatically confer any rights to the software. Consumers cannot access the software until they enter into a license agreement with Microsoft. The fact that the software is pre-installed on the computer does not imply that consumers receive Microsoft's software as a free "bonus" when purchasing the computer. If the consumer

118. Raymond T. Nimmer, *License Contracts Under Article 2 of the Uniform Commercial Code: A Proposal.* 19 RUTGERS COMPUTER & TECH. L.J. 281, 283 (1993).

119. *Id. See also* IAN BALLON, E-COMMERCE AND INTERNET LAW § 21 (2001).

120. Nimmer, *supra* note 118.

121. Michael P. Akemann, *Microsoft's Licensing Agreements: Theory & Evidence on the Sale of MS-DOS & Windows*, 24 J. CORP. L. 553, 562 (1999).

122. *In re* Microsoft Corp. Antitrust Litig., 127 F. Supp. 2d 702, 706 (D. Md. 2001).

does not agree to the terms of the EULA, Microsoft will refund the money the consumer "paid" for the product.[123]

The EULA allows consumers to install and use the software on a single computer or multiple computers, depending on the terms of the license.[124] Microsoft grants the right to use the software on the PCs only to a specified number of end users.[125] The price of the EULA varies based on the number of operating systems that consumers may run concurrently.[126] Microsoft's EULA cannot be negotiated; consumers take it or leave it by clicking "I agree" on the computer or taking other actions to indicate acceptance of Microsoft's offer of license rights.[127]

Although both are license agreements, the OEM license and the EULA contain different terms and therefore have different values. The value of the software stems from the right to use the software; this value is transferred via the license agreement and will vary widely depending on the terms of the license. For example, the value of a license that allows 10 people to use the software will be considerably less than the value of a license that allows 10,000 people to use the software.[128] The tremendous difference in the value exists even though the "intrinsic value of the underlying software itself is unchanged."[129] In the most fundamental sense, the product is the thing that contains value. Therefore, in the software industry the license is the product. Robert Gomulkiewicz[130] argues that "[f]or most software products, the license is the product; the computer program provides functionality to the user, but the license delivers the use rights."[131] In fact, without software licenses "some [software] companies would have had no valid products at all."[132]

In the context of ordinary goods, it may seem strange to think of a contract or agreement as the product. However, transactions that involve the

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123. *Id.*

124. Robert W. Gomulkiewicz, *The License is the Product: Comments on the Promise of Article 2B for Software & Information Licensing*, 13 BERKELEY TECH. L.J. 891, 921-922 (1998).

125. *In re Microsoft*, 127 F. Supp. 2d at 706.

126. *Id.*

127. *Id.*

128. *Controversial New Rules for Computer Contracts*, TECH. COMMENTARIES, (Jones, Day, Reavis & Pogue), May 2000, at 1.

129. *Id.*

130. Mr. Gomulkiewicz is a senior corporate attorney for Microsoft Corporation. We cannot doubt his disclaimer that the views expressed in his article are his own and not those of Microsoft.

131. Gomulkiewicz, *supra* note 124, at 896.

132. *Id.* at 897.

transfer of rights in software technology implicate issues that are fundamentally different from those in the sale of goods. In a case involving the sale of an ordinary good, such as a pencil, the value is in the good itself. It is difficult, if not impossible, to separate the good and the right to use the good. Pencil manufacturers do not sell the right to use their pencils; they sell the pencils. Software manufacturers, on the other hand, sell only the right to use their software.

Microsoft's own business practices indicate that the company treats the EULA as the product. The terms of the OEM license specifically state that the OEMs do not purchase or receive title to the end user rights to the software or to the EULA.[133] OEMs are simply allowed to install the Microsoft programs.[134] The terms of the EULA expressly state that it is between Microsoft and the end users, not between the end user and the OEM.[135] Finally, the EULA provides that Microsoft, not the OEM, will issue refunds to prospective end users who do not agree to the "take-it-or-leave-it" terms of Microsoft's EULA.[136]

Some commentators refer to these software licenses as a "legal fiction."[137] The software industry created the software license as a response to the lack of intellectual property protection for software.[138] In the late 1970s and early 1980s it was not clear that copyright or patent law would protect computer software.[139] As a result, computer programmers sought trade secret protection for their programs.[140] The software industry created the "legal fiction that they were licensing rather than selling their software" because they needed proof that they were not disclosing trade secrets by selling the software. The license required customers to keep the software confidential, thus the software became protectable.[141]

Although computer programs are now protectable by copyright and patents, the software industry continues to use the software license. The industry benefits from this "legal fiction" because licensing software, rather than selling it, gives software manufacturers more control over what consumers do with the software. For example, license agreements often

133. *In re Microsoft*, 127 F. Supp. 2d at 706.
134. *Id.*
135. *Id.*
136. *Id.*
137. Mark A. Lemley, *Intellectual Property & Shrinkwrap Licenses*, 68 S. CAL. L. REV. 1239, 1244 (1995).
138. *Id.*
139. *Id.* at 1243.
140. *Id.* at 1244.
141. *Id.* at 1245.

prohibit licensees from reselling, transferring, or assigning their particular copy of the software.[142] These provisions clearly "conflict with the 'first sale' doctrine in copyright law, which gives the owner of a particular copy of a copyrighted work the right to dispose of that copy without the permission of the copyright owner."[143] However, software manufacturers avoid the first sale doctrine by licensing their software rather than selling it.[144] The software industry therefore diligently promotes the idea that software is licensed, not sold. The software industry should be subject to all of the consequences of this arrangement, rather than just reaping the benefits. Along those lines, the court should have recognized that the EULA is the product and treated the end users as direct purchasers.

Support for the proposition that software is not sold extends beyond Microsoft and the software industry. While there is more debate outside the software industry, both courts and academics have accepted the argument that software is licensed, not sold. Microsoft has successfully argued in court that its software is licensed rather than sold, in order to preclude an infringer from relying on the first sale doctrine.[145] The strongest support, outside the software industry, comes from the drafters of the Uniform Computer Information Transactions Act ("UCITA").[146] The National Conference of Commissioners of Uniform State Laws ("NCCUSL") drafted UCITA because there was no uniform body of contract law that governed information industries.[147] Article 2 of the Uniform Commercial Code ("UCC") does not cover computer information because "[c]omputer information is not a good and is usually licensed, not sold."[148] That software is licensed, not sold, is a fundamental tenet of UCITA.

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142. *Id.* at 1267.

143. *Id.*

144. *See id.* at 1273 (explaining that the House Committee Notes accompanying section 109(a) make it clear that parties can contract around the first sale doctrine and citing Notes of Comm. on the Judiciary, H.R. Rep. No. 94-1476, *reprinted in* 1976 U.S.C.C.A.N. 5659).

145. Microsoft Corp. v. Harmony Computers & Elecs., Inc., 846 F. Supp. 208, 212-13 (E.D.N.Y. 1994). *But see* Microsoft Corp. v. DAK Indus., 66 F3d 1091 (9th Cir. 1995) (holding that the economic realities of the agreement indicated a sale, not a license to use); Softman Products Co. v. Adobe Systems, Inc. 2001 WL 1343955 (C.D. Cal. Oct. 19, 2001) (concluding that software is sold, licensed).

146. *See* Raymond T. Nimmer, *Materials on UCITA: What Is It and Why Is So Much Misrepresented About the Statute?*, 670 PLI/PAT 591, 594 (2001).

147. *Id.*

148. *Id.*

2. *Application of the* Illinois Brick *Doctrine to the Software Industry*

The most important step in applying the *Illinois Brick* doctrine is correctly identifying the alleged monopoly product.[149] Identifying the product is critical because it is impossible to pinpoint the direct purchaser if one cannot identify the monopolized product.[150] There is a distinction between "goods" and "services" that cannot be ignored when attempting to identify the monopolized product. Goods are capable of being purchased and resold; however, in most cases services provide value only to the direct purchaser.[151] Once the service is provided it is consumed and cannot be transferred.[152] Therefore, there are very few scenarios in which it is possible to have an indirect purchaser of a service.[153]

Transactions involving software blend traditional elements of goods transactions with components involving intangible rights and services.[154] Software resembles traditional goods in that it is reusable; it is not "used up." Unlike goods, however, software is not purchased or sold—it is licensed. Software also has the characteristics of a service because it is intangible. While software often comes on a diskette or a compact disc, tangible media are often not necessary. Software can be transferred in intangible form, via the Internet, for example. In fact, once the software is installed, the diskette or compact disc is no longer necessary. The value conveyed in a software transaction is therefore independent of the tangible item involved.

The court in *Microsoft* mistakenly applied the *Illinois Brick* doctrine because it did not identify the product correctly. The court failed to recognize that computer software lies on the line between goods and services. Consumers do not purchase Microsoft's software, they purchase the right to the software. The value lies in the right to the software, and that value is transferred via the license agreements. The private suits against Microsoft involved two distinct products, the OEM license and the EULA. Each of these products had its own direct purchaser: the OEMs purchased the OEM license, and the end users purchased the EULA. Therefore, both OEMs and end users are direct purchasers of Microsoft's product.

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149. Kingsbury, *supra* note 2, at 488.
150. *Id.*
151. *Id.* at 489.
152. *Id.*
153. *Id.*
154. Nimmer, *supra* note 118, at 293.

IV. CONCLUSION

The court's application of the *Illinois Brick* doctrine to bar consumer suits against Microsoft is inconsistent with both policies underlying *Illinois Brick* and with software industry practices. One of the central goals of *Illinois Brick* was deterrence. The Court wanted to give the party with the most motivation to sue the right to sue. In the *Microsoft* case, the parties with the most motivation to sue are consumers, not OEMs. Unfortunately, courts have interpreted the control exception to the direct purchaser rule very narrowly, and so the *Microsoft* court held that the control exception did not apply in this case. While the court's decision undermines the goals of *Illinois Brick*, it is consistent with recent precedent. However, the court should have recognized the distinctive nature of the software industry and held that consumers are direct purchasers of Microsoft's product. Software licenses differ from the sale of traditional goods in two major ways. First, software licenses focus on intangibles and the right to use these intangibles. Second, software is licensed, not sold. The true value of the software is contained in the software license. Consumers are purchasing the right to use Microsoft's software. The EULA is therefore the product Microsoft is selling and consumers are direct purchasers of that product.

HATCH-WAXMAN USE OR ABUSE? COLLUSIVE SETTLEMENTS BETWEEN BRAND-NAME AND GENERIC DRUG MANUFACTURERS

By Julia Rosenthal

In 1984, Congress passed the Hatch-Waxman Act,[1] amending the Federal Food, Drug and Cosmetic Act.[2] Also known as The Drug Price Competition and Patent Term Restoration Act of 1984, the Act was a far-reaching attempt to meet two mutually exclusive goals: to reward innovative new drug research, while simultaneously speeding the entry of inexpensive generic versions of drugs into the market.[3]

These apparently incompatible goals were achieved by rewarding research-based drug development with extra patent protection and modifying parts of the regulatory approval process for generic drugs.[4] Although the Hatch-Waxman Act has largely met the goal of stimulating new drug development and increasing the availability of generics,[5] provisions of the Act may have unwittingly created perverse incentives for anticompetitive activity. Several recent agreements between brand-name and generic pharmaceutical companies have attracted significant attention for their antitrust ramification. These arrangements between supposed competitors have acted to stall the introduction of lower-priced generic drugs, rather than speeding their entry as intended. This Note begins with a description of the Act's main provisions and goals, followed by summaries of the cases and a discussion of proposed legislative reforms. This Note concludes that proposed legislation modifying two provisions of the Act, rather than increased antitrust surveillance, should be adopted in order to fulfill the Act's goals.

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1. Pub. L. No. 98-417, 98 Stat. 1585 (codified as amended in scattered sections of 15, 21, 28, and 35 U.S.C.).

2. 21 U.S.C. § 355 (1994).

3. Alfred B. Engelberg, *Special Patent Provisions for Pharmaceuticals: Have They Outlived Their Usefulness?*, 39 IDEA 389 (1999).

4. *Id.* at 390-91.

5. *See* CONGRESSIONAL BUDGET OFFICE, HOW INCREASED COMPETITION FROM GENERIC DRUGS HAS AFFECTED PRICES AND RETURNS IN THE PHARMACEUTICAL INDUSTRY 1 (1998) [hereinafter CONGRESSIONAL BUDGET OFFICE STUDY].

I. STATUTORY BACKGROUND

The Hatch-Waxman Act ("HWA") contained two separate titles, the first of which is the subject of this Note.[6] Both titles are currently the subject of considerable debate.[7]

A. The Reduced Filing Requirements for Generic Drugs

The first provision of Title I concerns regulatory changes for federal Food and Drug Administration ("FDA") approval of generic drugs. The HWA established reduced approval requirements for generic drugs.[8] While new ("pioneer") drug approval requires the submission of extensive and lengthy documents in a New Drug Application ("NDA") to the FDA,[9] generic versions of these drugs can bypass part of this process, by filing an Abbreviated New Drug Application ("ANDA") for the generic versions of previously approved drugs. An ANDA incorporates data that the brand-name or pioneer manufacturer had already submitted to the FDA regarding the pioneer drug's safety and efficacy. The generic manufacturer must simply include data demonstrating that its generic version is "bioequivalent"[10] to the pioneer drug.[11]

To protect the patent rights of the pioneer drug maker, the applicant generic manufacturer must also certify that the generic drug will not infringe any patent that claims the pioneer drug.[12] One type of certification,

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6. Title II contained additional provisions for pharmaceutical development, including patent term restoration for term lost to FDA regulatory approval delay and freedom from patent infringement liability for testing during regulatory approval periods.

7. For example, Title II reform is urged by the biotechnology industry to give greater patent term restoration for biotechnology pharmaceuticals in recognition of the extended time required for their testing and approval. *See, e.g.*, William Holtz, *Reassessing Hatch-Waxman Incentives*, FOOD & DRUG L. INST. UPDATE, Issue 2, at 47 (2001), *available at* http://www.fdli.org/pubs/Update/2001/Issue2/Holtz/article.html; David Schmickel, *The Biotechnology Industry Organization's View on Hatch-Waxman Reform*, 54 FOOD & DRUG L. J. 241, 242 (1999).

8. 21 U.S.C. § 355(j) (1994).

9. *Id.* § 355(a) (1994).

10. A "bioequivalent" drug has an equivalent rate and extent of absorption in the body
as the original listed (pioneer) drug. Bioavailability and Bioequivalence Requirements, 21 C.F.R. § 320.1(e) (1982).

11. 21 U.S.C. § 355(j)(2)(A)(iv) (1994).

12. Manufacturers of the previously approved pioneer drug must list all patents related to their products in the FDA's "Orange Book" (officially known as the "Approved Drug Products with Therapeutic Equivalence Evaluations") as part of their initial NDA process. 21 U.S.C. § 355(b)(1) (1994). Generic manufacturers must then cite all Orange Book patents related to their ANDA drug.

a Paragraph IV certification, allows the generic manufacturer to allege that the pioneer drug patent is either invalid or would not be infringed by the marketing of the generic drug.[13]

As an incentive to file Paragraph IV certifications, the first generic manufacturer to file an ANDA containing a Paragraph IV certification regarding a particular patent receives a one hundred and eighty day period of exclusivity in which to market the generic drug, thereby preventing any other generic versions of the product from receiving ANDA approval during that time.[14] This period of exclusivity is one of the subjects of this Note. Although designed to encourage generic manufacturers to pursue the market, it has in fact been an inducement for generic and pioneer drug producers of a given drug to collaborate, rather than compete, with each other by stalling the entry of the less expensive generic into the marketplace.

B. The Thirty Month Stay of ANDA Approval

Paragraph IV filing also requires that the generic manufacturer give notice to the pioneer drug manufacturer. On receipt of notice of a Paragraph IV filing, the patentee (usually, but not always, the pioneer drug manufacturer)[15] has forty-five days in which to file suit against the generic manufacturer for patent infringement.[16] The FDA cannot approve the generic ANDA for thirty months if such an action is brought. If the court hearing the infringement suit rules the patent at issue is either invalid or not infringed before the thirty months period expires, the generic is granted approval on the date of the court's decision.[17] This automatic thirty month stay is the other problematic aspect of the Act currently under discussion.

C. Impact of the HWA on the Drug Marketplace

There is little disagreement that the HWA has profoundly increased consumer access to lower priced generic drugs. According to a 1998 Congressional Budget Office Study,[18] the generic drug share of United States prescription drug volume has increased from 19% in 1984 (the year before

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13. *Id.* § 355(j)(2)(A)(vii)(IV).

14. *Id.*

15. This Note will treat the terms patentee and brand-name manufacturer interchangeably; in some cases, of course, they will be separate companies.

16. *Id.* § 355(b)(1).

17. If there is no decision before the thirty month expiration, the generic is granted ANDA approval at the end of the thirty month period.

18. CONGRESSIONAL BUDGET OFFICE STUDY, *supra* note 5, at 1.

HWA enactment) to over 40% in 1996.[19] The percent of top-selling branded drugs that have a generic competitor on the market has increased from 36% in 1983 to nearly 100% in 1998 for brand-name drugs with expired patents.[20] The generic share of prescription drug volume has increased nearly 150% overall since HWA enactment.[21] In 1994 alone, consumers saved between $8 and $10 billion through the purchase of generic drugs.[22]

Additionally, there is evidence that the HWA expanded the number of generic manufacturers producing the same drug, which further lowers costs.[23] For example, the entry of a second generic version usually doubles the price decrease initiated by the first generic; three or more companies offering a generic version can lower the price by at least fifty percent or more from the branded price.[24]

These results indicate that the sooner more companies offer the same generic product, the greater the price competition, and the lower the price consumers pay for a generic version of a drug.[25] This demonstrates both that the rationale underlying the HWA was correct and that maneuvers that undercut these goals keep lower priced drugs away from the consumer.[26]

II. CASES

Three recent cases illustrate the potential for anti-competitive agreements between generic and brand-name manufacturers. The first two—*Abbott-Geneva*[27] and *HMRI-Andrx*[28]—have settled by consent agreement,

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19. *Id.* at 27.
20. *Id.* at xii.
21. *Id.* at 27.
22. *Id.* at xiii.
23. *Id.* at 32.
24. David A. Balto, *Pharmaceutical Patent Settlements: The Antitrust Risks*, 55 FOOD & DRUG L.J. 321, 326 (2001).
25. CONGRESSIONAL BUDGET OFFICE STUDY, *supra* note 5, at 27.
26. FEDERAL TRADE COMMISSION, THE PHARMACEUTICAL INDUSTRY: A DISCUSSION OF COMPETITIVE AND ANTITRUST ISSUES IN AN ENVIRONMENT OF CHANGE 206 (1999), *available at* http://www.ftc.gov/reports/pharmaceutical/drugrep.pdf.
27. Complaint, *Abbott Labs. and Geneva Pharm.*, FTC Dkt. No. C-3945 (May 22, 2000) [hereinafter *Abbott-Geneva* Complaint].
28. Complaint, *Hoechst Marion Roussel, Inc., Carderm Capital L.P. and Andrx Corp.*, FTC Dkt. No. 9293 (Mar. 16, 2000).

while the third, *Schering Plough-ESI/Upsher-Smith,* is currently under Federal Trade Commission ("FTC") investigation.[29]

A. *In re Abbott Laboratories and Geneva Pharmaceuticals*

The first case the FTC addressed regarding potential HWA abuses concerned Hytrin,[30] a brand-name for terazosin HCL. Terazosin HCL is a drug used to treat hypertension and enlarged prostate, and is produced by Abbott Laboratories.[31] In January 1993, Geneva filed an ANDA for FDA approval of its generic version of terazosin, in both capsule and tablet form. In April 1996, Geneva filed Paragraph IV certification, representing that its drug would not infringe the Abbott patent because the patent was invalid.[32]

Abbott sued Geneva within the stipulated forty-five day period, triggering the thirty month stay on FDA approval for Geneva's generic drug.[33] Abbott failed, however, to file infringement action against the capsule version of Geneva's product, although both capsule and tablet forms were involved.[34] Thus, the FDA approval process for the capsule form continued.

As first filer for the generic form, Geneva would have exclusivity for the first one hundred and eighty days after FDA approval, which it obtained in March 1998.[35] Geneva informed Abbott that it would launch its product unless Abbott paid it not to enter the market.[36] Abbott agreed to make payments of $4.5 million per month into an escrow account in exchange for Geneva's promise not to release the generic product (in either capsule or tablet form) until the resolution of their litigation or the entry of another generic into the market, whichever came first.[37] These payments to Geneva continued until July 1999, even after Geneva won the patent suit in September 1998,[38] as Geneva calculated that it was more profitable to have Abbott pay into the escrow account and stay out of the market than

29. Complaint, *Schering-Plough Corp.*, FTC Dkt. No. 9297 (Mar. 30, 2001) [hereinafter *Schering-Plough* Complaint].

30. *Abbott-Geneva* Complaint, *supra* note 27, at ¶ 11.

31. *Id.*

32. *Id.* ¶ 17.

33. *Id.* ¶ 18.

34. *Id.*

35. *Id.* ¶ 22.

36. *Id.* ¶ 36.

37. *Id.* ¶ 26.

38. *Id.* ¶ 31.

to enter with the generic.[39] Geneva cancelled the agreement in August 1999, pending an FTC investigation into the arrangement.[40]

The antitrust case was settled by FTC consent decree prior to litigation.[41] The agreement sharply limited similar arrangements between the competitors in the future. First, it established that future agreements between the brand-name and generic drug companies which cause relinquishment of the one hundred and eighty day exclusivity period to the brand-name company are prohibited.[42] Second, agreements in which the generic manufacturer is paid to stay off the market are barred in the context of ongoing patent litigation, unless approved by a court after the FTC is given time to present its views to the court.[43] Third, respondents are required to give the FTC thirty days notice before entering into such agreements in other contexts.[44]

The absence of financial penalties is noteworthy. However, the FTC implied that future instances of similar conduct would lead it to seek monetary recovery from the defendants, including disgorgement of illegal profits.[45]

B. *In re Cardizem Litigation*

In contrast to the *Abbott-Geneva* case, the second publicized case of potential HWA collusion involved a generic manufacturer actively trying to avoid infringing the brand-name company's patents.[46]

1. *Contractual and Patent Relationships Between Defendants Andrx, Carderm, and Hoechst Marion Roussel*[47]

United States Patent No. 5,470,584 ("the '584 patent") issued to defendant Carderm on November 28, 1995. The '584 patent claims a delayed-release diltiazem hydrochloride formulation with a specific in-vitro dissolution profile.[48] This heart medication formulation is manufactured

39. *Id.* ¶ 29.
40. *Id.* ¶ 33.
41. Consent Order, *Abbott Labs. and Geneva Pharm.*, FTC Dkt. No. C-3945 (May 22, 2000).
42. *Id.* at II.
43. *Id.* at III.
44. *Id.* at IV.
45. Statement of FTC Chairman Robert Pitofsky & Commissioners Sheila Anthony, Mozelle Thompson, Orson Swindle, and Thomas Leary, *Abbott Labs. and Geneva Pharm.*, FTC Dkt. No. C-3945-46 (May 22, 2000).
46. *In re* Cardizem CD Antitrust Litig., 105 F. Supp. 2d 682, 695 (E.D. Mich. 2000).
47. Hoechst Marion Roussel is now Aventis Corp.
48. *Cardizem,* 105 F. Supp. 2d at 686.

and sold under the name Cardizem CD by defendant Hoechst Marion Roussel ("HMRI") through a license from Carderm.[49]

Two months prior to the issuance of the '584 patent, defendant Andrx filed an ANDA for its controlled-release generic version of Cardizem.[50] On December 31, 1995, Andrx filed for Paragraph IV certification for all unexpired patents claiming Cardizem CD, and certified to HMRI that its generic formulation did not infringe patents belonging to HMRI, including the '584 patent.[51] HMRI and Carderm filed a patent infringement suit against Andrx in the United States District Court for the Southern District of Florida on January 31, 1996, thereby triggering the thirty month HWA waiting period.[52] Andrx could neither gain final approval for its ANDA, nor commercially market its generic version of Cardizem, until either the thirty months expired or the court found the patent invalid or not infringed.[53]

On September 24, 1997, less than ten days after receiving tentative FDA approval for its ANDA, Andrx entered into an agreement with HMRI in which it promised not sell its generic version of Cardizem.[54] This agreement acknowledged that Andrx had created a bioequivalent version of Cardizem CD, had filed an ANDA on this product with the right to amend it, and that this generic product was the subject of infringement litigation between Andrx and HMRI.[55] The agreement also stated that HMRI intended to prevent the marketing or distribution of Andrx's product prior to a final judgment in the patent infringement case. To reduce the costs of litigation, Andrx agreed it would not commence the commercial sale of its generic version until: (1) a final judgment in the infringement litigation, (2) the licensing of Cardizem CD to Andrx by HMRI under this agreement, or (3) notice from HMRI that it was authorizing for itself or a third party the right to begin commercial sale of a generic version.[56] Andrx's ANDA received final FDA approval when the thirty month Hatch-Waxman period expired on July 8, 1998. HMRI began payments to Andrx for its nonmarketing of the generic July 9, 1998.[57] Andrx mean-

49. *Id.*
50. *Id.*
51. *Id.*
52. *Id.* at 687.
53. *Id.*
54. *Id.*
55. *Id.* at 696.
56. *Id.*
57. *Id.* at 687.

while altered its formula in order to get around the '584 patent and submitted the changes to the FDA for supplemental approval.[58]

The FDA gave final approval to Andrx's supplemental ANDA on June 9, 1999, and on that same day, Andrx and HMRI agreed to settle their litigation and terminate their agreement.[59] This agreement contained several provisions, one of which was the continued assertion by HMRI that Ardrx's product infringed the '584 patent, while Andrx asserted that it did not. Second, Andrx stated its intent to market its reformulated product following FDA approval, but agreed not to market it in the U.S. without a license from HMRI.[60]

Andrx began commercial marketing of its Cartia XT generic on June 23, 1999, triggering the one hundred and eighty day period of Hatch-Waxman exclusivity and blocking the entry of generic versions from any other manufacturer into the market.[61] By this point, HMRI had paid Andrx almost $90 million under the terms of the agreement.[62]

2. *Private Litigation*

In addition to federal antitrust enforcement, private and state plaintiffs also sought to enforce Section 1 of the Sherman Act against HMRI, Carderm, and Andrx.[63] Class action and individual suits commenced in the United States District Court for the Eastern District of Michigan under the Sherman Act and corresponding state law provisions, alleging that the agreement between Andrx and HMRI/Carderm was illegal as a horizontal market allocation.[64] These suits were consolidated by plaintiffs into a single motion for partial summary judgment on the issue of whether the agreement between manufacturers was a per se violation of antitrust regulations.[65]

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58. *Id.* In fact, in an effort to avoid infringement action from HMRI, Andrx twice filed prior approval supplements to its ANDA. The second supplement was filed on September 11, 1998, adding a small amount of a new ingredient to its generic formula and further modifying the dissolution profile for its generic version away from that of the '584 patent. In a Second Supplemental Certification (a Paragraph IV Certification), Andrx argued that its generic product, Cartia XT, did not infringe the '584 patent due to these differences. In spite of these efforts, HMRI pursued its attempts to keep Andrx's product off the market. *Id.* at 687-89.

59. *Id* at 689.

60. *Id.*

61. *Id.* at 690.

62. *Id.* at 689.

63. *Id.* at 682.

64. *Id.*

65. *Id.*

Judge Edmunds found that the agreement was unlawful on its face and constituted a per se violation of Section 1 of the Sherman Antitrust Act.[66] The Court determined that the HMRI/Andrx agreement was an agreement between horizontal competitors which allocated the entire U.S. market for the drug at issue and its bioequivalents. The court also found that the agreement was not ancillary to any pro-competitive purpose.[67] Partial summary judgment was granted for claimants.[68]

3. *Antitrust Analysis in Private Litigation*

The essential elements of a Sherman Act Section 1 violation are: (1) a contract, combination, or conspiracy; (2) affecting interstate commerce; (3) which imposes an unreasonable restraint on trade.[69] Horizontal agreements, that is, agreements between competitors, "pose the most significant dangers of competitive harm,"[70] and are antitrust's most "suspect classification,"[71] as they preclude competition between firms that would be competitors but for the accused arrangement.[72] Two modes of analysis are used by the court, the per se analysis and the rule of reason. A per se analysis implies that certain market actions, such as horizontal price fixing and market allocation, are so inherently anticompetitive that each is illegal per se without inquiry into the actual harm done. Such violations are usually only found when prior cases have established the anticompetitive effects of a sufficiently similar business practice.[73]

HMRI and Andrx argued that the per se rule was inapplicable to their agreement because they were never actual horizontal competitors; Andrx had not yet entered the market with its generic version of Cardizem when the agreement was formed.[74] The Court dismissed the defendants' argu-

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66. *Id.* at 706.
67. *Id.*
68. *Id.*
69. 15 U.S.C. § 1 (1994).
70. 11 HERBERT HOVENKAMP, ANTITRUST LAW ¶ 1902(a) (1998).
71. *Id.*
72. *Id.*
73. N. Pac. Ry. Co. v. United States, 356 U.S. 1, 5 (1958).
74. Rule of reason analysis is used for less presumptively illegal actions, requiring the factfinder to find that under all circumstances of the case, the practice in question imposes an unreasonable restraint on trade. Which of these analyses to use on the restraint of trade at issue is a question of law for the court. *In re Cardizem CD Antitrust Litig.*, 105 F. Supp. 2d 682, 691 (E.D. Mich. 2001). The District court's finding of a per se agreement was dramatic, as it can be argued that no "sufficiently similar" business practice had ever occurred before with which to compare the manufacturers' alleged behavior. Patent settlements, in general, are analyzed under the rule of reason. HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY § 5.5(c) (2d ed. 1999).

ment, noting that "an arrangement is said to be 'horizontal' when (1) its participants are either (a) actual rivals at the time the agreement is made or (b) potential rivals at the time the agreement is made, and (2) the agreement eliminates some avenue of rivalry among participants."[75]

4. *Federal Trade Commission Action*

The Federal Trade Commission also instigated its own investigation in 1999. This action culminated in a consent decree in April 2001,[76] with limitations on future agreements similar to those placed on Abbott and Geneva.[77]

C. Schering Plough Agreements with ESI and Upsher-Smith Concerning the Drug K-Dur 20

The third instance of an alleged anticompetitive agreement under the HWA is currently under investigation.[78] Both the government and private plaintiffs have filed actions against Schering Plough for separate agreements with Upsher-Smith[79] and ESI.[80] These firms manufacture generic versions of Schering's K-Dur 20, an extended-release potassium chloride formulation used for the treatment of depleted potassium levels.[81]

Upsher-Smith filed a Paragraph IV certification for generic K-Dur 20 and notified Schering Plough on November 3, 1993.[82] Schering promptly sued Upsher-Smith for patent infringement.[83] On the eve of their patent trial, Schering and Upsher-Smith agreed to settle their litigation. Under the agreement, Schering paid $60 million to Upsher-Smith to keep Upsher from entering the market with any version of K-Dur 20, whether it infringed Schering's patent or not.[84] Ostensibly, the payment was in exchange for licenses to market five Upsher-Smith products, but these li-

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75. *Cardizem,* 105 F. Supp. 2d at 700 (citing 11 HOVENKAMP, supra note 70, ¶ 1901b).

76. Consent Order, *Hoechst Marion Roussel, Inc., Carderm Capital L.P. & Andrx Corp.,* FTC Dkt. No. 9293 (Nov. 27, 2000).

77. *Id.* at II.

78. This case is currently in administrative trial.

79. *Schering-Plough* Complaint, *supra* note 29.

80. ESI Lederle, Inc. is a division of American Home Products Corporation, primarily engaged in generic drug research and manufacture. *Schering-Plough* Complaint, *supra* note 29, ¶ 6.

81. *Schering-Plough* Complaint, *supra* note 29, ¶ 31.

82. *Id.* ¶ 38.

83. *Id.* ¶ 39.

84. *Id.* ¶ 44.

censes had minimal value to Schering Plough, which has made little or no use of them.[85]

In November 1998, Upsher-Smith received FDA approval to market Klor Con M20, its generic version of K-Dur 20.[86] In accordance with its agreement with Schering however, Upsher withheld the generic from the market.[87]

Similarly, Schering paid $20 million to ESI, a generic manufacturer that planned to launch its generic K-Dur 20 formulation after Upsher-Smith's one hundred and eighty days of exclusivity had run.[88] Once again, the payments were in exchange for licenses for two ESI products that Schering has not marketed to date.[89]

Although ESI received tentative approval of its ANDA from the FDA on May 11, 1999, it will not be able to obtain final approval until Upsher-Smith's one hundred and eighty day period of exclusivity has run.[90] But because Upsher has never introduced its generic into the market, this one hundred and eighty days has never begun, and thus cannot expire.[91]

III. FEDERAL RESPONSES

The HWA has unwittingly created opportunities for the formation of horizontal agreements between competitors in the pharmaceutical industry. By providing pioneer drug manufacturers with the thirty month stay of ANDA approval for generic competitors, the HWA provides an opportunity for "sham" or delaying litigation, because approval for the generic ANDA cannot proceed while the patent litigation takes place. This litigation may have little to do with the underlying value of the patent(s) at issue, and amounts, in some cases, to a stipulated preliminary injunction without judicial review.[92]

Second, the reward of one hundred eighty days of exclusivity for the first generic challenger has essentially functioned as a plum to reward the

85. *Id.* ¶ 45-46.
86. *Id.* ¶ 48.
87. *Id.* ¶ 49.
88. *Id.* ¶ 59.
89. *Id.* ¶ 56.
90. *Id.* ¶ 60.
91. *Id.*
92. *See* Sheila Anthony, Riddles and Lessons from the Prescription Drug Wars: Antitrust Implication of Certain Types of Agreements Involving Intellectual Property, Prepared Remarks Before the Am. Bar Assoc. Antitrust and Intellectual Property: The Crossroads Program (June 1, 2000), *available at www.ftc.gov/speeches/anthony/sfip000601.htm.*

formation of a collusive agreement or settlement. As written, the HWA contains no requirement that the one hundred and eighty days actually ever be triggered in order to act as blockade against subsequent generic challengers who might have competing products.[93] As long as the patent infringement litigation between the pioneer manufacturer and the first generic challenger is ongoing, or even if it has settled and the generic challenger has not yet launched its product, the generic market is essentially held closed. The drug is kept at the original on-patent price until the patent expires, regardless of the validity of the patent itself.[94] This issue will only intensify in importance, as it is estimated that in the next five years, some two hundred drugs, with combined sales of $30 billion, will go off-patent.[95]

Responses to these loopholes in the HWA fall into two main categories: calls for structural modification of the HWA itself, or increases in antitrust surveillance of agreements between brand-name and generic drug companies. There are currently a number of issues related to pharmaceuticals under Congressional review, and this will likely increase as pressure from industry groups like Pharmaceutical Research and Manufacturer of America ("PhRMA")[96] and the numbers of drugs going off-patent increase over the next several years.[97]

A. Structural Reform

The McCain-Schumer "Greater Access to Affordable Pharmaceuticals Act" undertakes broad structural reform of the HWA itself.[98] This bill has four major modifications, two of which are discussed below.[99]

First, the McCain-Schumer bill would alter the automatic thirty month stay provision for challenged generic ANDAs. Instead, the pioneer manufacturer could seek a preliminary injunction in the courts to stop the first generic challenge to its patent(s), eliminating, in theory, the possibility of "sham" or delaying litigation by the pioneer company. Since the stay would not be triggered without judicial review of the validity of the under-

93. *Id.*

94. *Id.*

95. Peter Stone, *PhRMA Fights Back*, NAT'L J., July 21, 2001.

96. For further information on PhRMA, see http://www.phrma.org.

97. *See* William Waller, *Pharmaceutical Legislative Update*, 5 FOOD & DRUG L. INST. UPDATE 4, *available at* http://www.fdli.org/Update/2001/Issue5/waller/html; Stone, supra note 95.

98. S. 812, 107th Cong. (2001).

99. The bill would also increase federal investigation of the citizen petition process, and relax the bioequivalence standards used to compare original and generic drugs. S. 812, 107th Cong. § 2 (2001).

lying patents, the main goal of Paragraph IV filing—to encourage generic challenge of weak or invalid patents—would be met. Critics have argued that this solution would not be successful in the pharmaceutical industry, where courts are reluctant to grant preliminary injunctions in cases where technical expertise requirements are high and monetary compensation would seem suitable.[100]

Second, the McCain-Schumer bill would establish a "use it or lose it" trigger for the one hundred and eighty day first-to-file generic exclusivity. If a successful generic challenger failed to launch its product within a specified number of days[101] after winning the infringement suit, the one hundrer and eighty day exclusivity would roll over to a second generic manufacturer.[102] This would eliminate the incentive for the pioneer manufacturer to pay the first generic challenger to simply stay out of the market indefinitely.

This bill also included a budget for a FTC study within five years of enactment to assess effectiveness of the changes.[103] Senate Bill 812, the McCain-Schumer bill, was introduced in May 2001 and was referred to the Committee on Health, Education, Labor, and Pensions.[104]

B. Antitrust Surveillance

Increased antitrust surveillance procedures have also been advocated to forestall anticompetitive collusion between drug manufacturers.

1. The Leahy Notification Bill

Rather than changing the HWA itself, Senator Leahy's "Drug Competition Act of 2001"[105] would increase FTC scrutiny of patent infringement settlements between innovator and generic drug companies. Any agreement between brand-name and generic manufacturers that could have the effect of limiting the appearance of a generic version of the brand-name company's product on the market would require notice to the FTC within ten days of the agreement's execution,[106] subject to a $20,000 per day

100. *See e.g.*, Anthony, *supra* note 92, at 2.

101. The McCain-Schumer bill provides for a ninety day limit. S. 812, 107th Cong. § 3(a)(3) (2001). A previous attempt at reforming HWA suggested a one hundred and eighty day limit. 64 Fed. Reg. at 42,873.

102. S. 812, 107th Cong. § 3(a)(3) (2001).

103. *Id.* § 8.

104. At the time of publication, the McCain-Schumer bill was still in Committee. *See* http://thomas.loc.gov/cgi-bin/bdquery/z?d107:SN00812:.

105. S. 754, 107th Cong. (2001)

106. *Id.* § 6.

penalty for each day of violation.[107] This bill left the Judiciary Committee in October with a favorable recommendation.[108]

2. *The Response of the FTC: Assessing the Scope of the Problem*

In response to the rising tide of concern, Representative Waxman, one of the original co-sponsors of the HWA, asked that the FTC "investigate and produce a study on the use of agreements between and among pharmaceutical companies and potential generic competitors and any other strategies that might delay generic drug competition throughout the U.S."[109] In October 2000, the FTC announced that it would undertake such a study and initiated a period of public comment. The study was aimed at examining the extent to which agreements between brand-name pharmaceuticals and generic drug firms may have delayed generic competition and the operation of the one hundred and eighty day exclusivity provision. In addition, the study would look at the impact of provisions in the Act on listing of patents by brand-name pharmaceutical companies in the FDA "Orange Book" and of provisions that trigger a stay on FDA approval of a proposed generic drug.[110]

According to the testimony of Molly Boast, then Director of the FTC Bureau of Competition, to Congress in May 2001, the Commission hoped that the study "would provide valuable information to Congress as it considers possible reform of the Hatch-Waxman Act."[111]

Responses to the FTC's requests for information were collected from brand-name and generic manufacturers in June 2001, and the Commission hopes to have the study completed by the end of 2001.[112] Upon completion of this study, the FTC will issue its recommendations for federal responses to the current HWA dilemma.[113] An accurate assessment of the number of companies involved in potentially anticompetitive abuses of the Act will provide guidance in the push for reform.

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107. *Id.* § 7.

108. *Bill Summary & Status for the 107th Congress*, *at* http://thomas.loc.gov/cgi bin/bdquery/z?d107:SN00754:(last visited Feb. 19, 2002).

109. Press release, Federal Trade Comm'n, FTC Testifies on Competition in the U.S. Pharmaceutical Industry (May 24, 2001), *available at* http://www.ftc.gov/opa/2001/05/drugtest.htm [hereinafter FTC Press Release].

110. *Id.*

111. Molly Boast, Competition in the Pharmaceutical Marketplace: Antitrust Implications of Patent Settlements, Prepared Statement of the Federal Trade Commission Before the Senate Judiciary Committee (May 24, 2001), *available at* http://www.ftc.gov/os/2001/05/pharmtstmy.htm.

112. *Id.*

113. *Id.*

IV. DISCUSSION

Revisions to the HWA have been proposed repeatedly through the years.[114] However, modification of a highly complicated piece of legislation like the Act is fraught with both difficulties and pitfalls. Unquestionably, the Act has been successful at achieving its stated goals. Tinkering with the "balancing act"[115] and demonstrated value of HWA raises concerns.[116]

The alternative, simply increasing enforcement of the antitrust laws and surveillance of potential anticompetitive agreements, raises its own set of problems. The Department of Justice and the FTC have finite resources. If they are called upon to study every proposed agreement or patent settlement in the pharmaceutical field, delays in approval time would undoubtedly increase even with substantial investment in personnel and resources to support this increased scrutiny.[117]

Several commentators have suggested ways to look at the relationship between the legislation itself and intellectual property in general. A discussion of these is helpful in analyzing the value of proposed solutions.

A. Basic Conflict between Intellectual Property and Antitrust

Patents provide one of the few exceptions to the general rule against monopolies. As incentives for innovation, they drive the market for new inventions and goods forward.[118] The HWA was enacted with the intent to maintain and increase the drive for new pharmaceutical development.[119]

Additionally, public policy favors the efficient resolution of disputes, including patent litigation,[120] to conserve judicial resources and lower

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114. David A. Balto, *Pharmaceutical Patent Settlements: The Antitrust Risks,* 55 FOOD & DRUG L.J. 321 (2001). *See, e.g.,* Drug Patent Term Restoration Review Procedure Act of 1999, S. 1172, 106th Cong. (1999).

115. *See, e.g., Pharmaceutical Intellectual Property Issues: Hearing Before the Senate Comm. on the Judiciary,* 107th Cong. (2001) (statement of Alan F. Holmer, President of the Pharmaceutical Research and Manufacturers of America).

116. *See, e.g., Recent Developments Which May Impact Consumer Access to, and Demand for, Pharmaceuticals: Hearing Before the Health Subcomm. of the House Energy and Commerce Comm.,* 107th Cong. (2001) (written testimony of Greg Glover, of Ropes and Gray).

117. Balto, *supra* note 114.

118. *Id.*

119. Pub. L. No. 98-417, 98 Stat. 1585 (codified as 15 U.S.C. §§ 68(b)-68(c), 70(b) (1994)).

120. U.S. Dep't of Justice & FTC, Antitrust Guidelines for the Licensing of Intellectual Property § 5.5 (1995), *available at* http://www.usdoj.gov/atr/public/guidelines/ipguide.htm (Apr. 1995).

transaction costs.[121] Settlements between litigants in patent cases can facilitate cooperation and further innovation. The Intellectual Property Guidelines jointly issued by the Department of Justice and the FTC adopt this view, stating that "settlements involving the cross-licensing of intellectual property rights can be an efficient means to avoid litigation and, in general, courts favor such settlements."[122] Settlements between horizontal competitors, however, raise special concerns. Where settlements could involve such agreements, the Guidelines advise that the government should "consider whether the effect of the settlement is to diminish competition among entities that would have been actual or likely competitors."[123]

1. *Azcuenaga's Test*

Former FTC Commissioner Mary Azcuenaga has proposed a simple test for evaluating the relationship between antitrust law and intellectual property.[124] First, one determines whether the intellectual property right was obtained in a proper manner. If there was no fraud or inequitable conduct in acquiring the patent, then antitrust laws may apply. Next, one considers whether the holder of the patent right improperly expanded the scope of the right. If the intellectual property right was properly obtained, and the patentee has not improperly extended it, there is no need to apply antitrust law.[125]

The *Cardizem*, *Abbott/Geneva*, and *Schering-Plough* cases would all appear to involve the second instance. There is no evidence of the patents being improperly obtained, but there is evidence that the HWA loopholes were used to improperly expand the scope (in this case, duration) of the brand-name drug's patent monopoly. Applying this test would weigh in favor of adopting the McCain-Schumer revisions—closing the loopholes in the Amendment itself, rather than intensifying antitrust law.

2. *Leary's Test for Reverse Payments*

FTC Commissioner Thomas Leary has recently suggested that the most straightforward test of the legitimacy of patent settlements between potential competitors is the presence of payments from the patent holder to

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121. *Id.*

122. *Id.*

123. *Id.*

124. Mary Azcuenaga, Recent Issues in Antitrust and Intellectual Property, Address at the Boston University School of Law (Oct. 23, 2000), *in* B.U. J. SCI. & TECH. L. (2001).

125. *Id.* at Part V.

the potential challenger.[126] Since these payments flow in the opposite direction of an expected license agreement for the intellectual property right in question,[127] they can be considered evidence of a presumptively anticompetitive agreement.[128] All three of the above HWA cases meet this simple test. In each situation the holder of the patent was paying the competitor, rather than the competitor paying the patent owner, for the right to use the intellectual property at issue.

Efficiency would weigh in favor of modifying HWA provisions themselves rather than simply increasing antitrust scrutiny. Judge Edmund's finding of a per se Section 1 violation in the Cardizem litigation demonstrates that these collusive agreements would be quickly invalidated as facially anticompetitive in court. However, the HWA, as currently written, provides an arguably legitimate way to use the thirty month stay and the one hundred and eighty day exclusivity period to forestall generic entry. Thus brand-name and generic companies can have their cake and eat it too—brand-name manufacturers get longer market exclusivity, and their generic partners make greater profit by not entering the market at all. Preventing these collusive agreements from occurring in the first place by closing the HWA loopholes prevents the consumer from losing early access to generics, rather than waiting for antitrust enforcement to catch up.[129]

B. Industry and Consumer Group Responses

Not surprisingly, PhRMA, the largest lobbying group for research-based pharmaceutical companies, is vigorously opposed to modification of the HWA.[130] Fearing strengthened generic access to the drug market, PhRMA has intensified public comment against McCain-Schumer passage and is donating significant sums of money to Congressional members with influence on its passage.[131]

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126. Thomas Leary, Antitrust Issues in the Settlement of Pharmaceutical Patent Disputes, Part II, Speech Before the American Bar Association's Antitrust Healthcare Program (May 17, 2001), *available at* http://www.ftc.gov/speeches/leary/learypharmaceuticalsettlement.htm.

127. *Id.* at Part IV.

128. *Id.*

129. Balto, *supra* note 114, at 340 ("[C]onsumers will have paid millions of dollars in unlawfully high prices before such a determination (of an antitrust violation) is made, and the Commission will be put in the position of seeking disgorgement and restitution, which, while serving the ends of justice, are imperfect tools for making consumers whole.")

130. Stone, *supra* note 95.

131. *Id.*

Generic manufacturers' groups are strongly in favor of adoption of the McCain-Schumer bill. In spite of smaller budgets, efforts by the Generic Pharmaceutical Association include hiring successful outside lobbyists as part of their plan to "correct the imbalance in the marketplace that favors brand-name companies."[132]

Consumer and managed healthcare groups such as Public Citizen,[133] Consumer's Union,[134] the U.S. Public Interest Research Groups,[135] and the Academy of Managed Care Pharmacy[136] all support the bill's passage. The Consumer's Union asserts that it "eliminates some of the delay tactics that have allowed the brand-name companies to hold up the process [of generic entry] and deny consumers the chance to buy generic alternatives."[137]

V. CONCLUSION

Agreements that make anticompetitive use of the automatic thirty month stay of approval for generic challengers and the one hundred and eighty day generic exclusivity period are unintended side effects of the Hatch-Waxman Act. While the HWA has clearly improved access to lower-priced generic alternatives for the consumer,[138] three recent cases illustrate the ease with which manufacturers can use the Act's provisions to illegitimately extend their patent rights, to the consumer's cost rather than benefit.[139] The financial incentives to exploit these provisions will only increase over the next several years, as a large number of high-selling pharmaceuticals go off-patent and motivation increases for their manufacturers to extend the period of monopoly pricing.[140]

The results of the FTC's current study of the pervasiveness of anticompetitive agreements in the pharmaceutical field will generate further

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132. *Id.*

133. Press Release, Public Citizen, Public Citizen Applauds Introduction of Schumer-McCain Bill to Make Less Costly Generic Drugs More Widely Available (May 1, 2001) (on file with author).

134. Press Release, Consumers Union, CU Praises McCain-Schumer Drug Bill, (May 1, 2001) (on file with author) [hereinafter CU Press Release].

135. Press Release, Academy of Managed Care Pharmacy, AMCP Endorses the 'Greater Access to Affordable Pharmaceuticals Act' (Jun. 7, 2001) (on file with author).

136. Stone, *supra* note 95.

137. CU Press Release, *supra* note 134.

138. CONGRESSIONAL BUDGET OFFICE STUDY, *supra* note 5, at 1.

139. *Id.*

140. For example, heart-burn drug Prilosec, the top-selling prescription drug, earned $4.62 billion in U.S. sales in 2000. Its patent expired April 1, 2001. Dana S Elfin, *As Patent Controversies Engulf Prilosec, Generics Call for Hatch-Waxman Reform*, 9 HEALTHCARE POLICY REP. (BNA) 12 (Mar. 26, 2001).

grounds for reform when complete.[141] Even in the absence of this data, the magnitude of the Abbott-Geneva, HMRI-Andrx and Schering-Plough agreements, and the numbers of pharmaceuticals soon to go off-patent,[142] demonstrate the need for closing the loopholes in the HWA. By eliminating the automatic thirty month stay following Paragraph IV filing, the Schumer-McCain bill will eliminate the ability of a brand-name manufacturer to stall generic approval and marketing based on a possibly valueless patent. It will also remove the one hundred and eighty day exclusivity period as an incentive to hold off the entry of generic drugs into the market. In the interest of fulfilling the Act's original goals of increasing consumer access to both new drugs and lower priced generics, the Bill should be adopted.

141. FTC Press Release, *supra* note 109.
142. Elfin, *supra* note 140, at 475.

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CYBERLAW

PAVLOVICH V. SUPERIOR COURT OF SANTA CLARA COUNTY

By Sonal N. Mehta[†]

Over the last several years, courts and commentators alike have attempted to establish when the exercise of personal jurisdiction over the Internet is appropriate. In conducting their analyses, they have sought to balance competing interests—limiting jurisdiction over the Internet while ensuring plaintiffs adequate fora to protect and enforce their rights. In trying to formulate a test that properly balances these objectives, and provides consistent and predictable outcomes, courts and commentators have proposed various standards.

This Note analyzes the state of Internet jurisdiction one year into the new millennium. Using the case of Matthew Pavlovich as its vehicle, this Note surveys recent case law on the exercise of personal jurisdiction over the Internet and demonstrates the inconsistency that currently exists. Underlying this inconsistency, however, is a common thread whereby courts implicitly consider the "bad faith" of defendants when deciding whether to exercise jurisdiction. In proposing a return to the reasonableness prong of the jurisdictional analysis, this Note attempts to formulate a test for Internet jurisdiction that considers this common thread in a concrete manner.

I. CASE SUMMARY

A. Facts

Jon Johansen, a Norwegian teenager, purchased a DVD player while on vacation elsewhere in Europe.[1] Upon returning home to Norway, he discovered that it would not play Norwegian DVDs due to Region Code Restrictions.[2] Using their expertise with Linux, he and a couple of others were able to decrypt the software safeguards employed by the consortium

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1. DVD Update: Movie Studios Admit DeCSS Not Related to Piracy, available at http://www.eff.org/IP/Video/DVD_Updates/20000718_dvd_update.html (Jul. 18, 2000).

2. *Id.*

of DVD manufacturers.[3] They posted the solution, DeCSS, to a Linux Video ("LiVid") list on the Internet.[4]

Matthew Pavlovich was and continues to be a leader in the open source movement, the purpose of which is to make as much information available over the Internet as possible.[5] Pavlovich founded and operated the LiVid project, aimed at aiding the development of an unlicensed system for DVD playback and copying.[6] Pavlovich owned and operated a website called "livid.on.openprojects.net" where he posted the DeCSS program. DeCSS was the solution to the CSS, the DVD Copy Control Association's copy protection system, or "Content Scramble System." The DeCSS program consisted of misappropriated trade secrets derived through unauthorized reverse engineering.[7] Despite his knowledge of how the DeCSS program incorporated the trade secrets of the DVD Copy Control Association ("DVD CCA"), Pavlovich sought to and actually disseminated those trade secrets.[8]

B. Procedural History

In December 1999, real party in interest DVD CCA filed a complaint in Santa Clara County Superior Court against Pavlovich and other defendants for misappropriation of trade secrets.[9] On June 6, 2000, Pavlovich filed a motion to quash service of summons on the ground that the superior court lacked personal jurisdiction.[10] A student in Indiana and resident of Texas, Pavlovich claimed to have insufficient contacts with the State of California to warrant the exercise of jurisdiction by the state.[11] On August 30, 2000, the superior court denied petitioner's motion to quash.[12]

In mid-September 2000, Pavlovich filed a petition for writ of mandate with the Court of Appeal of California for the Sixth Appellate District ("Court of Appeal") to compel the trial court to quash the service of process.[13] The Court of Appeal summarily denied Pavlovich's writ petition on

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3. *Id.*
4. *Id.*
5. Pavlovich v. Super. Ct. of Santa Clara County, 109 Cal. Rptr. 2d 909, 911 (Ct. App. 2001), *hearing granted*, No. S100809 (Cal. Dec. 12, 2001).
6. *Id.* at 911-12.
7. *Id.* at 912.
8. *Id.*
9. *Id.* at 911.
10. *Id.*
11. *Id.*
12. *Id.*
13. *Id.*

October 11, 2000.[14] Twelve days later, Pavlovich filed a petition for review with the California Supreme Court.[15] On December 19, 2000, the California Supreme Court granted review and transferred the case back to the Court of Appeal "with directions to vacate its order denying mandate and to issue an order directing respondent superior court to show cause why the relief sought in the petition should not be granted."[16] The Court of Appeal vacated its order denying mandate, and ordered the superior court to show cause why the relief sought in the petition should not be granted.[17] On August 7, 2001, the Court of Appeal again denied Pavlovich's petition for writ of mandate, holding that California's long-arm statute allows for jurisdiction in this case.[18]

C. The Court's Analysis and Conclusion

In finding personal jurisdiction proper, the court relied primarily on several cases outlining personal jurisdiction and the "effects test." The court cited *Calder v. Jones*,[19] in which the United States Supreme Court held that the assertion of jurisdiction was proper if a defendant's conduct caused certain "effects" in the forum state.[20] In *Calder*, the court concluded that California courts had personal jurisdiction over the defendant in Florida because the defendant's conduct was "calculated to cause injury to [the] respondent in California."[21]

The court also relied upon the California Supreme Court's decision in *Vons Companies, Inc. v. Seabest Foods, Inc.*[22] In *Vons*, the California Supreme Court stated that the assertion of personal jurisdiction in California state courts over a nonresident defendant who had not been served with process comported with due process if the defendant had such minimum contacts with the state that assertion of jurisdiction did not violate "traditional notions of fair play and substantial justice."[23] The court held that the

14. *Id.*
15. *Id.*
16. *Id.*
17. *Id.*
18. *Id.* at 912. On December 12, 2001, the California Supreme Court again granted review of the Court of Appeal's decision. *See* Supreme Court Minutes, *available at* http://www.courtinfo.ca.gov/courts/minutes/ documents/SDEC12A.PDF (Dec. 28, 2001); *see also* Michael Bartlett, California Supreme Court Will Hear DVD-Copying Appeal, NEWSBYTES, Dec. 13, 2001, *at* http://www.newsbytes.com/news/01/172967.html.
19. 465 U.S. 783 (1984).
20. *Id.* at 789.
21. *Id.* at 791.
22. 14 Cal. 4th 434 (1996).
23. *Id.* at 444 (citing Int'l Shoe Co. v. Wash., 326 U.S. 310, 319 (1945); Burnham v. Super. Ct., 495 U.S. 604 (1990)).

minimum contacts requirement is satisfied "if the defendant has purposefully availed himself or herself of forum benefits, and the 'controversy is related to or "arises out of" a defendant's contacts with the forum.'"[24] The *Vons* court went on to hold that "as long as the claim bears a substantial connection to the nonresident's forum contacts, the exercise of specific jurisdiction is appropriate."[25]

In applying personal jurisdiction jurisprudence to the case at bar, the Court of Appeal found that Pavlovich "knew that California is commonly known as the center of the motion picture industry, and that the computer industry holds a commanding presence in the state."[26] The court held that Pavlovich "knew or should have known, that the DVD republishing and distribution activities he was illegally doing and allowing to be done through the use of his Web site, while benefiting him, were injuriously affecting the motion picture and computer industries in California."[27] Because California's long-arm statute looks at "the effects, not at the system that delivered and produced those effects," the court concluded that the exercise of jurisdiction was proper.[28]

The court additionally found there to be a sufficient showing of "purposeful availment" within the meaning of *Vons* and cited the general rule that the "purposeful availment" requirement is "satisfied where a defendant's intentional conduct causes harmful effects within the state."[29] The court reasoned that the Internet was the "functional equivalent" of physical presence of the person posting the material on the Internet, and that "[i]t is as if the poster is instantaneously present in different places at the same time, and simultaneously delivering his material at those different places."[30]

Having established that the exercise of jurisdiction was proper, the *Pavlovich* court went on to address the issue of unreasonableness, ultimately concluding that the exercise of personal jurisdiction by the California court was reasonable.[31] As the court noted, "seven factors may be considered in determining whether jurisdiction over a nonresident defendant comports with notions of fair play and substantial justice under the due

24. *Id.* at 446 (internal citations omitted).
25. *Id.* at 452.
26. Pavlovich v. Super. Ct. of Santa Clara County, 109 Cal. Rptr. 2d 909, 915 (Ct. App. 2001), *hearing granted*, No. S100809 (Cal. Dec. 12, 2001).
27. *Id.* at 916.
28. *Id.*
29. *Id.*
30. *Id.*
31. *Id.* at 917-18.

process clause."[32] These factors include: (1) the extent of a defendant's purposeful interjection; (2) the burden on the defendant in defending in the forum; (3) the extent of conflict with the sovereignty of the defendant's state; (4) the forum state's interest in adjudicating the dispute; (5) the most efficient judicial resolution of the controversy; (6) the importance of the forum to the plaintiff's interest in convenient and effective relief; and (7) the existence of an alternative forum.[33] Under factor 1, the court found that Pavlovich knew that his actions would affect the DVD and motion picture industries, each with a significant presence in California, and that Pavlovich knew that his website "allowed the illegal publishing and distribution of DVDs."[34] As to factor 2, the court recognized that defending a lawsuit in California would be burdensome to Pavlovich, but nevertheless held that the "inconvenience was not so great as to deprive him of due process."[35] The court briefly noted that factors four through seven also favored California.[36]

II. LEGAL BACKGROUND

A. Personal Jurisdiction—the General Standard

Under the Due Process Clause, a court may not have personal jurisdiction over a defendant who has "no meaningful 'contacts, ties, or relations'"[37] with the forum state. Furthermore, while a defendant need not have been physically present in the forum state for a court to have jurisdiction,[38] there must be certain "minimum contacts" between the defendant and the forum "such that maintenance of the suit does not offend 'traditional notions of fair play and substantial justice.'"[39]

"Minimum contacts" has been defined as "conduct and connection with the forum . . . such that [the defendant] should reasonably anticipate being haled into court there."[40] A court may determine that the defendant's contacts are sufficient for "general jurisdiction" when the defendant's contacts with the forum are "substantial" or "continuous and systematic," in-

32. *Id.* at 917.
33. *Id.* (citing Panavision Int'l, L.P. v. Toeppen, 141 F.3d 1316, 1323 (9th Cir. 1998)).
34. *Id.* at 917.
35. *Id.*
36. *Id.* at 918.
37. Burger King v. Rudzewicz, 471 U.S. 462, 471-72 (1985) (citing Int'l Shoe Co. v. Wash., 326 U.S. 310, 319 (1945)).
38. *See id.* at 476.
39. *Int'l Shoe*, 326 U.S. at 316 (citation omitted).
40. World-Wide Volkswagen Corp. v. Woodson, 444 U.S. 286, 297 (1980).

dicating that the defendant "purposefully avail[ed] itself of the privilege of conducting activities within the forum State, thus invoking the benefits and protections of its laws."[41] While the defendant's contacts may be less than continuous when the plaintiff seeks to establish "specific jurisdiction," the plaintiff has the burden of showing that the defendant took action "purposefully directed" at the forum, and that the cause of action arises from this action.[42] The Supreme Court has held that "purposeful availment," or "purposeful direction," occurs when "the contacts proximately result from actions by the defendant *himself* that create a 'substantial connection' with the forum State."[43]

Beyond the basic minimum contacts standard, the court must consider several "reasonableness" factors in its personal jurisdiction analysis.[44] Thus, although a court may determine that the defendant's contacts with the forum meet the minimum contacts threshold, it may nevertheless find personal jurisdiction improper.

B. Personal Jurisdiction on the Internet—a Special Case

1. Inset—the Old Standard

Inset Systems, Inc. v. Instruction Set, Inc.[45] was one of the first cases to address personal jurisdiction over the Internet. In *Inset*, the court held that the defendant's website, which contained advertising and a toll-free number, constituted sufficient minimum contacts for the state to exercise personal jurisdiction.[46]

In *Inset*, the defendant, Instruction Set, Inc. ("ISI"), was a Massachusetts corporation with its principal place of business in Massachusetts.[47] ISI had no employees or offices in Connecticut and did not conduct business on a regular basis in the state.[48] Nevertheless, the district court found specific jurisdiction in Connecticut proper because ISI's website directed its advertising activities towards *all* states.[49] In its holding, the court found that Internet advertisements were even more continuous and persistent

41. Hanson v. Denckla, 357 U.S. 235, 253 (1958).

42. *See* Calder v. Jones, 465 U.S. 783, 789 (1984) (upholding jurisdiction where conduct was allegedly calculated to cause injuries in the forum state and the cause of action arose from this conduct).

43. *Burger King*, 471 U.S. at 475.

44. *See supra* note 33 and accompanying text; *Burger King*, 471 U.S. at 476-77.

45. 937 F. Supp. 161 (D. Conn. 1996).

46. *Id.* at 162-65.

47. *Id.* at 162-63.

48. *Id.*

49. *Id.* at 165.

than television or radio advertisements since the Internet is accessible twenty-four hours a day.[50] The district court therefore concluded that personal jurisdiction over ISI was proper because it had purposefully availed itself of the privilege of doing business within Connecticut.[51]

2. Zippo—*the Sliding Scale*

Less than one year after *Inset*, *Zippo Manufacturing Company v. Zippo Dot Com, Inc.*[52] described *Inset* as "the outer limits of the exercise of personal jurisdiction based on the Internet."[53] The *Zippo* court attempted to limit the *Inset* approach, instead proposing a sliding scale to govern the jurisdictional inquiry. At one end of the spectrum were defendants who "clearly [did] business over the Internet"[54] with persons in the forum state. Here, exercise of personal jurisdiction was appropriate.[55] At the other end of the spectrum were defendants with "passive Web site[s]"[56] that merely made information available to interested users in foreign jurisdictions. Exercise of jurisdiction over these defendants was not appropriate.[57] In the middle of the spectrum were "interactive Web sites where a user can exchange information with the host computer."[58] The court concluded that "[i]n these cases, the exercise of jurisdiction is determined by examining the level of interactivity and commercial nature of the exchange of information that occurs on the Web site."[59]

Several circuit courts and numerous district courts have cited *Zippo* as the proper standard in Internet jurisdiction cases.[60] In practice, however, *Zippo* seems to have added little to these courts' personal jurisdiction

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50. *Id.*
51. *Id.*
52. 952 F. Supp. 1119 (W.D. Pa. 1997).
53. *Id.* at 1125.
54. *Id.* at 1124.
55. *Id.*
56. *Id.*
57. *Id.*
58. *Id.*
59. *Id.*
60. *See, e.g.*, Intercon, Inc. v. Bell Atl. Internet Solutions, Inc., 205 F.3d 1244, 1248 (10th Cir. 2000); Soma Med. Int'l v. Standard Chartered Bank, 196 F.3d 1292, 1296 (10th Cir. 1999); Mink v. AAAA Dev't LLC, 190 F.3d 333, 336 (5th Cir. 1999); Panavision Int'l, L.P. v. Toeppen, 141 F.3d 1316, 1320 (9th Cir. 1998); Cybersell v. Cybersell, 130 F.3d 414, 418 (9th Cir. 1997); Blumenthal v. Drudge, 992 F. Supp. 44, 55-56 (D.D.C. 1998); SF Hotel Co. v. Energy Invs., Inc., 985 F. Supp. 1032, 1034 (D. Kan. 1997); Smith v. Hobby Lobby Stores, Inc., 968 F. Supp. 1356, 1365 (W.D. Ark. 1997).

analyses, which instead seem to rely exclusively on traditional personal jurisdiction principles.[61]

The first example of this is the Ninth Circuit's decision in *Panavision International, L.P. v. Toeppen*.[62] Here, the defendant was a cybersquatter[63] who had deliberately registered plaintiff Panavision's trademarks as his own domain name for the purpose of extorting money from Panavision.[64] The defendant's websites were completely passive, exhibiting photographs or the word "Hello."[65] The Ninth Circuit did not base its finding of purposeful direction upon the fact that the defendant clearly did business over the Internet, or upon the level of interactivity or the commercial nature of the defendant's websites, as required by *Zippo*. Rather, the court relied on the "intended effects doctrine" set forth by the U.S. Supreme Court in *Calder v. Jones*.[66] By aiming his extortion scheme at Panavision, the defendant intended to cause harm in California where most of the motion picture industry and Panavision's activities were located.[67] The *Panavision* court, in direct opposition to *Zippo*, held that the defendant's use of passive and noncommercial websites supported a finding of personal jurisdiction.

The Tenth Circuit in *Intercon, Inc. v. Bell Atlantic Internet Solutions, Inc.*[68] similarly cited *Zippo*, but based its finding of specific jurisdiction on the theory of intentional effects established in *Calder*.[69] In *Intercon*, the court held that the defendant knowingly and intentionally directed unauthorized e-mail traffic through the plaintiff's server in the forum state.[70] While the court acknowledged that the defendant may have had legitimate business reasons for not terminating its unauthorized use of the plaintiff's

61. Michael Traynor & Laura Pirri, *Personal Jurisdiction and the Internet: A Return to Basic Principles* (Working Paper, 2002) (on file with author).

62. 141 F.3d 1316 (9th Cir. 1998).

63. A "cybersquatter" can be defined as someone who registers an Internet domain name that is "the same as or related to the name of a trademark of another entity, usually a company or organization." Susan Thomas Johnson, Note, *Internet Domain Name and Trademark Disputes: Shifting Paradigms in Intellectual Property*, 43 ARIZ. L. REV. 465, 476 (2001) (citing G. Peter Albert, *Right on the Mark: Defining the Nexus Between Trademarks and Internet Domain Names*, 15 J. MARSHALL J. COMPUTER INFO. L. 277, 304 (1997)).

64. *Panavision*, 141 F.3d at 1319.

65. *Id.*

66. *Id.* at 1321-22 (citing Calder v. Jones, 465 U.S. 783 (1984)).

67. *See Panavision*, 141 F.3d at 1322.

68. 205 F.3d 1244 (10th Cir. 2000).

69. *Id.* at 1248.

70. *Id.* at 1247-48.

server, it found that the use still constituted purposeful direction.[71] The Tenth Circuit subsequently held that the defendant's activities in the forum state satisfied the minimum contacts required by due process and allowed for the exercise of personal jurisdiction.[72]

Finally, in *Cybersell, Inc. v. Cybersell, Inc.*,[73] another trademark infringement case, the Ninth Circuit indicated its approval of the *Zippo* spectrum,[74] but also affirmed *Asashi Metals*' "something more" requirement for purposeful direction.[75] Finding that a nonresident defendant's advertisements on its corporate website were insufficient by themselves to justify personal jurisdiction, the Ninth Circuit required "'something more' to indicate that the defendant purposefully (albeit electronically) directed his activity in a substantial way to the forum state."[76] The *Cybersell* court held that there was no jurisdiction because the defendant did not: (1) encourage forum residents to access its site; (2) otherwise solicit or transact business in the forum state; and (3) intentionally aim its website at the forum, knowing that the plaintiff's trademark rights were likely to be harmed there.[77]

3. *A Move Away from* Zippo

In the last couple of years, courts have begun moving away from the *Zippo* approach—or more accurately, lip service to the *Zippo* approach—and have returned to general personal jurisdiction analyses rooted in Supreme Court precedent.[78] For example, the D.C. Circuit in *GTE New Media Services Inc. v. BellSouth Corporation*[79] rejected the district court's application of the *Zippo* framework.[80] GTE sued five regional Bell operating companies, alleging that they had violated antitrust laws by providing Internet Yellow Pages services.[81] Three of the five defendants moved to

71. *Id.* at 1248.
72. *Id.*
73. 130 F.3d 414 (9th Cir. 1997).
74. *Id.* at 419 ("In sum, the common thread, well stated by the district court in *Zippo*, is that 'the likelihood that personal jurisdiction can be constitutionally exercised is directly proportionate to the nature and quality of commercial activity that an entity conducts over the Internet.'").
75. *Id.* at 418 (citing Asahi Metal Indus. Co. v. Super. Ct. of Cal., 480 U.S. 102 (1987)).
76. *Cybersell*, 130 F.3d at 418.
77. *Id.* at 419.
78. Traynor & Pirri, *supra* note 61.
79. 199 F.3d 1343 (D.C. Cir. 2000).
80. *Id.* at 1349-50.
81. *Id.* at 1346.

dismiss for lack of personal jurisdiction.[82] Placing the defendants' Yellow Pages websites in the middle of *Zippo*'s spectrum, the district court upheld specific jurisdiction, finding that the sites were "highly interactive" and provided the defendants with significant economic benefit.[83]

The D.C. Circuit reversed, rejecting the *Zippo* court's assumption that if a defendant's website is active and commercial, as opposed to passive and noncommerical, the defendant has purposefully availed itself of the benefits of doing business in the forum state.[84] The court instead found that the interactive use of the Yellow Pages sites reflected little more than unilateral acts by the D.C. residents themselves; they did not constitute persistent conduct by the defendants.[85] The D.C. Circuit also rejected the premise that the commercial nature of the defendants' websites meant that the defendants were "transacting business" within the forum when residents used the sites.[86] Because users had free access to the sites, and the user and advertiser conducted business transactions directly, the court concluded that the defendants had not actually engaged in any business in the forum.[87] In its holding, the court expressed its concern that broadly applying *Zippo* would establish jurisdiction in almost all Internet jurisdiction cases, undermining the relevance of Due Process.[88] The D.C. Circuit specifically noted that it "d[id] not believe that the advent of advanced technology, say, as with the Internet, should vitiate long-held and inviolate principles of federal court jurisdiction."[89]

Similarly, a few district courts have moved away from *Zippo*, returning to non-Internet specific personal jurisdiction analyses. In *Winfield Collection, LTD v. McCauley*,[90] for example, the court found that a "special Internet-focused test" of personal jurisdiction was unnecessary because the minimum contacts analysis was sufficient.[91] Further, in *Millennium Enterprises, Inc. v. Millennium Music, LP*,[92] the court found that:

82. *Id.*
83. GTE New Media Servs., Inc. v. Ameritech Corp., 21 F. Supp. 2d 27, 38-39 (D.D.C. 1998).
84. *See GTE New Media*, 199 F.3d at 1349-50.
85. *Id.*
86. *Id.* at 1350.
87. *Id.*
88. *Id.*
89. *Id.*
90. 105 F. Supp. 2d 746 (E.D. Mich. 2000).
91. *Id.* at 750.
92. 33 F. Supp. 2d 907 (D. Or. 1999)

> the middle interactive category of Internet contacts as described in *Zippo* needs further refinement to include the fundamental requirement of personal jurisdiction: "deliberate action" within the forum state in the form of transactions between the defendant and residents of the forum or conduct of the defendant purposefully directed at residents of the forum state.[93]

In other words, the court held the *Zippo* framework inadequate in Internet jurisdiction cases because it failed to include the fundamental concept of "deliberate action."

Most recently, in *Digital Control Inc. v. Boretronics Inc.*,[94] a district court in Washington found the *Inset-Zippo* framework for personal jurisdiction over the Internet unsatisfactory in determining whether the forum state had personal jurisdiction over an alleged patent infringer who offered the accused product for sale on a website.[95] The *Digital Control* court held:

> until the advertiser is actually faced with and makes the choice to dive into a particular forum, the mere existence of a worldwide web site, regardless of whether the site is active or passive, is an insufficient basis on which to find that the advertiser has purposely directed its activities at residents of the forum state.[96]

Thus, the court in *Digital Control* rejected the *Inset-Zippo* test because it may grant personal jurisdiction too broadly, e.g., where the defendant has not chosen to interact with a particular forum.

These opinions indicate dissatisfaction with the *Zippo* framework and a return to traditional standards for personal jurisdiction which can be applied both in and out of the Internet context.[97] Notably, although these courts have returned to standard minimum contacts and effects analyses when discussing Internet-based jurisdiction, they have given short shrift to the reasonableness inquiry required by *Burger King*.

C. Personal Jurisdiction on the Internet—Inconsistency in Outcome

Reviewing the multitude of district court and appellate decisions on personal jurisdiction on the Internet, one is struck by their seeming incon-

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93. *Id.* at 921.
94. 161 F. Supp. 2d 1183 (W.D. Wash 2001).
95. *Id.* at 1186-87.
96. *Id.*
97. *See also* Michael Geist, *Is There a There There? Toward Greater Certainty for Internet Jurisdiction*, 16 BERKELEY TECH. L.J. 1345 (2001).

sistencies and apparently random outcomes.[98] These inconsistent outcomes have not gone unnoticed.[99]

1. *Commerce on the Internet*

The question of personal jurisdiction on the Internet is perhaps most relevant in the context of Internet commerce. As *Zippo* illustrates, courts assert personal jurisdiction most readily in cases where the defendant's website is both commercial and active—where the defendant offers products for sale. Nevertheless, courts do not assert jurisdiction in all such cases. The court in *Digital Control*, for example, held that personal jurisdiction was improper, even though the defendant had offered the allegedly infringing product for sale on his website.[100]

On rare occasions, courts have found online advertising sufficient for the court to assert personal jurisdiction over the defendant. The *Inset* court made such a determination because the defendant had continuously advertised on the Internet.[101] The court noted that the defendant's online advertisement constituted purposeful direction of its activity toward the forum state and indicated that the defendant should have reasonably anticipated being haled into court there.[102] Similarly, in *TELCO Communications v. An Apple a Day*,[103] the court found online advertising to be a "persistent course of conduct" under Virginia's long-arm statute.[104] The court subsequently held that Apple's activities were "sufficient to serve as an analogue for physical presence."[105]

More commonly, courts are unwilling to assert personal jurisdiction based upon online advertising. In *Grutkowski v. Steamboat Lake Guides &*

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98. One commentator aptly notes that "[t]he current hodgepodge of case law is inconsistent, irrational, and irreconcilable." Howard B. Stravitz, *Personal Jurisdiction in Cyberspace: Something More is Required on the Electronic Stream of Commerce*, 49 S.C. L. REV. 925, 939 (1998).

99. *See, e.g.*, Susan Nauss Exon, *A New Shoe is Needed to Walk Through Cyberspace Jurisdiction*, 11 ALB. L.J. SCI. & TECH. 1 (2000); Kevin R. Lyn, *Personal Jurisdiction And The Internet: Is A Home Page Enough To Satisfy Minimum Contacts?*, 22 CAMPBELL L. REV. 341 (2000); Sarah K. Jezairian, Note, *Lost in the Virtual Mall: Is Traditional Personal Jurisdiction Analysis Applicable to E-Commerce Cases?*, 42 ARIZ. L. REV. 965 (2000).

100. Digital Control Inc. v. Boretronics Inc., 161 F. Supp. 2d 1183 (W.D. Wash. 2001).

101. Inset Sys., Inc. v. Instruction Set, Inc., 937 F. Supp. 161, 165 (D. Conn. 1996).

102. *Id.*

103. 977 F. Supp. 404 (E.D. Va. 1997).

104. *Id.* at 406.

105. *Id.* at 406-08.

Outfitters, Inc.,[106] for example, a case arising out of a wrongful death action, the court found defendant's commercial, but passive, website insufficient to warrant an assertion of personal jurisdiction.[107] Similarly, in *McDonough v. Fallon McElligott*,[108] the court found the defendant's advertising in California insufficient to find personal jurisdiction because he had not actually placed any products into the stream of commerce.[109] Other courts have adopted similar approaches.[110]

2. *Trademark Infringement and Dilution*

In the context of trademark infringement and dilution on the Internet, the case law on personal jurisdiction is similarly inconsistent. As discussed above, the court in *Panavision* exercised personal jurisdiction over an alleged cybersquatter who registered domain names using over one hundred trademarks and then attempted to sell the trademark owners the domain names for a large profit.[111] Similarly, in *PurCo Fleet Services, Inc. v. Towers*,[112] the court found personal jurisdiction proper. Here, the defendant registered the plaintiff trademark holder's domain name and then set up a website under the name.[113] The defendant then attempted to extort money by selling rights in the domain name for a cash payment and solicited business from a forum resident through this website.[114]

Other courts, however, have come to different results in trademark infringement and dilution cases. In *Bensusan Restaurant Corporation v. King*,[115] a Missouri night club called The Blue Note posted monthly calendars of future events and the Missouri telephone number for its box of-

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106. No. Civ. A. 98-1453, 1998 WL 962042 (E.D. Pa. Dec. 28, 1998).

107. *Id.* at *2-6.

108. 40 U.S.P.Q.2d (BNA) 1826 (S.D. Cal. 1996).

109. The court noted:

> While Fallon places advertisements and associates with businesses who sell products to Californians, Fallon itself has no significant California clients, and has not placed any products into the stream of commerce that have been purchased by Californians. As such, jurisdiction upon the basis of the California contacts of Fallon's business associates would be one-step removed. Personal jurisdiction cannot be so attenuated.

Id. at 1828-29.

110. *See, e.g.*, IDS Life Ins. Co. v. SunAmerica, Inc., 958 F. Supp. 1258 (N.D. Ill. 1997), *rev'd on other grounds*, 266 F.3d 645 (7th Cir. 2001).

111. Panavision Int'l, L.P. v. Toeppen, 141 F.3d 1316, 1320 (9th Cir. 1998).

112. 38 F. Supp. 2d 1320 (D. Utah 1999).

113. *Id.* at 1323-24.

114. *Id.* at 1324.

115. 126 F.3d 25 (2d Cir. 1997)

fice on its website. It also posted a hypertext link to the plaintiff's website, www.bluenote.com, which contained information about the Blue Note jazz club in New York.[116] The court held that defendant's website did not have sufficient contacts with the forum state, New York, to warrant the exercise of personal jurisdiction.[117] In determining that jurisdiction was improper, the court looked to the New York long-arm statute, which required a defendant to either commit a tort while physically present in New York, or commit a tort outside the state, resulting in injury to person or property within the state.[118] The defendant did not satisfy the first provision because he was not physically present in New York.[119] The court found that the defendant did not fall under the second provision either, as the defendant did not reasonably expect the tortious act to have consequences within New York or derive substantial revenue from interstate commerce.[120] Similarly, the *Cybersell* court held that a Florida company's passive website, which included the service mark of an Arizona company, did not justify the exercise of jurisdiction by Arizona.[121] The defendant did not purposefully avail itself of the benefits and protections of Arizona law.[122]

3. *Defamation and Libel*

Yet another area in which Internet jurisdiction jurisprudence has developed with great inconsistency is that of online defamation and libel. The court in *U-Haul International, Inc. v. Osborne*,[123] for example, held that the forum state did not have personal jurisdiction over the defendant in a libel action. U-Haul sued for libel and other causes of action in response to defendants' "U-Hell" website which posted their bad experience with U-Haul, and provided e-mail links that directed visitors to U-Haul's website.[124] The court characterized the website as passive and held that the defendants' Internet activities did not establish purposeful availment.[125]

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116. *Id.* at 27.
117. *Id.* at 29.
118. *Id.* at 27-29.
119. *Id.*
120. *Id.*
121. Cybersell, Inc. v. Cybersell, Inc., 130 F.3d 414, 418-19 (9th Cir. 1997).
122. *Id.*
123. No. CIV 98-0366-PHX-RGS, 1999 U.S. Dist. LEXIS 14466 (D. Ariz. Feb. 17, 1999).
124. *Id.* at *3.
125. *Id.* at *10-13.

Amway Corporation v. Procter & Gamble Company,[126] however, stands in opposition to *U-Haul*. In *Amway*, a disgruntled Amway employee residing in Oregon created an Internet website entitled "Amway: the Untold Story."[127] The website included allegedly defamatory statements about Amway and allowed viewers of the website to post responses.[128] The court held that the forum state had jurisdiction over the defendant, whom the court determined had committed an intentional tort, because he knew that the brunt of the harm would be felt in the forum state, Amway's principal place of business.[129] Similarly, the court in *Blumenthal v. Drudge*[130] held that the exercise of personal jurisdiction over defendant was appropriate. Matt Drudge allegedly posted libelous statements about a new White House aide on his website.[131] The court found that Drudge's maintenance of an interactive website, to which visitors could e-mail Drudge directly with gossip and request subscriptions to the "Drudge Report," in addition to his non-Internet contacts with the forum, were sufficient for a finding of personal jurisdiction.[132]

The inconsistent nature of decisions in Internet jurisdiction cases has led commentators to devote great amounts of ink and paper in analyzing the issue. Commentators have offered various explanations for the inconsistent case law[133] and have proposed their own solutions to this problem.[134] Arguably, these works have only added to the morass. While this

126. No. 1:98-CV-726, 2000 U.S. Dist. LEXIS 372 (W.D. Mich. Jan. 6, 2000).

127. *Id.* at *6-7.

128. *Id.*

129. *Id.* at *13-16.

130. 992 F. Supp. 44 (D. D.C. 1998).

131. *Id.* at 47-48.

132. *Id.* at 56-57.

133. *See, e.g.*, Jezairian, *supra* note 99 (finding that "[s]everal similar cases have produced utterly different results in terms of whether or not the court chose to assert personal jurisdiction"); Todd D. Leitstein, Comment, *A Solution for Personal Jurisdiction on the Internet*, 59 LA. L. REV. 565 (1999) (noting that "[p]redictable internet jurisdiction is becoming an oxymoron. In this quagmire of decisions, a few give the illusion of stability but rely on spurious differentiations for guidance" and attempting to explain inconsistencies by discussing three nominal categories of conduct on the Internet).

134. *See, e.g.*, Stephen Patrick Beatty, *Litigation in Cyberspace: The Current and Future State of Internet Jurisdiction*, 7 U. BALT. INTELL. PROP. J. 127, 136-39 (1999) (discussing alternate dispute resolution and cyberspace sovereignty as alternative schemes for internet jurisdiction); Mark C. Dearing, *Personal Jurisdiction and the Internet: Can the Traditional Principles and Landmark Cases Guide the Legal System into the 21st Century?*, 4 J. TECH. L. & POL'Y 4 (1999) (arguing that the *Zippo* and effects tests are best-suited to address Internet jurisdiction issues); Exon, *supra* note 99 (proposing two alternative solutions: system of registration and cybercourts); Stravitz, *supra* note 98 (suggesting an analysis that would emphasize the "fair play and substantial jus-

Note may suffer the same fate, it does so with the aim of simultaneously explaining and resolving the inconsistency in Internet jurisdiction jurisprudence.

III. DISCUSSION

This Note attempts to explain the underlying considerations that may lend some consistency to Internet jurisdiction jurisprudence. In doing so, it proposes a *complete* return to general jurisdictional standards with a particular emphasis on the oft-forgotten reasonableness analysis. Part III.A discusses the hidden 'bad faith' analysis which brings some coherence to the Internet jurisdiction jurisprudence. Part III.B proposes a formalization of this 'bad faith' analysis through a return to the long-standing reasonableness inquiry. Finally, Part III.C applies this new standard—or more accurately, old standard applied in a new way—to the case of Matthew Pavlovich.

A. Explaining the Inconsistency—The Hidden 'Bad Faith' Analysis

How does one explain the inconsistency in Internet jurisdiction cases? One explanation—which finds support in the case law surrounding Internet jurisdiction—is that the application of traditional personal jurisdiction analysis to specific situations leads to differing outcomes.[135]

While courts have consistently applied the traditional personal jurisdiction standards to Internet jurisdiction cases, some courts have given increasingly short shrift to the reasonableness analysis. Though the court in *GTE New Media* expressed its concern that the overly broad Internet-specific *Zippo* sliding scale may undermine the due process elements of personal jurisdiction, for example, it did not even address the reasonable-

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tice" requirement and a focus on due process); Note, Bensusan Restaurant Corp. v. King, *An Erroneous Application of Personal Jurisdiction Law to Internet-based Contacts (Using the Reasonableness Test to Ensure Fair Assertions of Personal Jurisdiction Based on Cyberspace Contacts)* [hereinafter *Bensusan* Note], 19 Pace L. Rev. 149 (1998) (arguing for greater emphasis on the reasonableness analysis in Internet jurisdiction cases); J. Christopher Gooch, Note, *The Internet, Personal Jurisdiction, and the Federal Long-Arm Statute*, 15 ARIZ. J. INT'L & COMP. LAW 635 (1998) (proposing a test that focuses on "fair play and substantial justice" instead of minimum contacts); Jezairian, *supra* note 99 (addressing several possible internet jurisdiction analyses, including federal regulation, state regulation, self-regulation and judicial intervention); Leitsen, *supra* note 133 (proposing a three-prong test for personal jurisdiction on the internet, the factors of which are: (1) volition; (2) harm caused in the forum state; and (3) foreseeability of harm caused).

135. Exon, *supra* note 99, at 7-8.

ness inquiry or the general standard that the exercise of personal jurisdiction comport with traditional notions of fair play and substantial justice.[136] Similarly, in *Pavlovich*, the court mentioned a few of the reasonableness factors, but devoted very little of its substantive discussion to this inquiry.[137]

As noted above, various courts applying minimum contacts and effects analyses have come to inconsistent outcomes though faced with similar factual circumstances.[138] In attempting to explain these inconsistent outcomes, there appears to be a common thread: the nonresident defendant's bad faith.

In the context of online trademark disputes, for example, the presence of "bad faith" may distinguish the decisions in *Panavision* and *PurCo Fleet* from that in *Bensusan*. If one were only to look at the defendants' minimum contacts with and effects in the forum states, the distinction would not be completely clear. In each case, the defendant's URL was identical to the plaintiff's trademark.[139] What might distinguish *Bensusan* from the cybersquatting cases, therefore, is the lack of "bad faith" on the defendant's part. In fact, the defendant in *Bensusan* encouraged visitors to his site to visit the plaintiff's establishment when they found themselves in New York.[140]

The importance of bad faith becomes even more relevant in the context of online libel and defamation. In *Amway* and *Blumenthal*, the defendants' actions were indicative of "bad faith." There, the defendants' allegedly defamatory statements were aimed at interfering with the plaintiffs' business or destroying the plaintiffs' personal reputation, respectively.[141] On the contrary, the defendants in *U-Haul*—though they posted defamatory material on the Internet—did not seem to possess the same level of "bad faith" as those in *Amway* or *Blumenthal*. While the *U-Haul* defendants' website *U-Hell* did post negative information about the plaintiff, the defendants used the website to relay their own negative experiences with

136. GTE New Media Servs. Inc. v. BellSouth Corp, 199 F.3d 1343, 1350 (D.C. Cir. 2000).

137. Pavlovich v. Super. Ct. of Santa Clara County, 109 Cal. Rptr. 2d 909, 917-18 (Ct. App. 2001), *hearing granted*, No. S100809 (Cal. Dec. 12, 2001).

138. *See supra* Part II.C.

139. Panavision Int'l, L.P. v. Toeppen, 141 F.3d 1316, 1319 (9th Cir. 1998); PurCo Fleet Servs., Inc. v. Towers, 38 F. Supp. 2d 1320, 1321-22 (D. Utah 1999); Bensusan Restaurant Corp. v. King, 126 F.3d 25, 27 (2d Cir. 1997).

140. *Bensusan*, 126 F.3d at 27.

141. Amway Corp v. Procter & Gamble Co., No. 1:98-CV-726, 2000 U.S. Dist. LEXIS 372 (W.D. Mich. Jan. 6, 2000); Blumenthal v. Drudge, 992 F. Supp. 44 (D. D.C. 1998).

the plaintiff and allow others to contact the plaintiff with their own concerns.[142] Though the distinction between good and bad faith is finer in the context of defamation and libel than in trademark disputes, there seems to be a qualitative difference in the actions of the *U-Haul* and *Amway/Blumenthal* defendants.

While the defendants' "bad faith" seems to play some role in Internet jurisdiction cases, it does so in a subtle way. If defendants' bad faith influences the eventual outcome of Internet jurisdiction cases, it is important that the role of this factor be brought to light.

B. Return to Reasonableness—Bringing Bad Faith out of the Shadows

In bringing the bad faith inquiry out of the shadows, courts may also find occasion to resolve another issue inherent in recent Internet jurisdiction jurisprudence: the short shrift given to the reasonableness inquiry. This cursory analysis of reasonableness is questionable because courts seem to have given undue weight to the first part of the general jurisdictional analysis. If a court is going to apply minimum contacts and effects-based analyses to Internet jurisdiction cases, it must also apply the corresponding reasonableness inquiry.

In order to formalize their bad faith analyses, courts should give greater weight to the reasonableness factors, particularly factors one and four. Factor one allows the court to consider the extent of the defendant's purposeful interjection into the forum.[143] Factor four allows the court to consider the forum state's interest in adjudicating the dispute.[144] In cases where there is bad faith on the part of the defendant, both of these factors would weigh in favor of personal jurisdiction. A defendant who acts with bad faith has likely purposefully interjected himself into a forum.[145] Similarly, the forum state will have a substantial interest in adjudicating the dispute in order to address the defendant's actions.

Giving greater weight to the reasonableness inquiry will also serve other purposes. In minimizing the import of due process and reasonableness considerations, the courts currently discount one of the major dangers

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142. U-Haul Int'l, Inc. v. Osborne, No. CIV 98-0366-PHX-RGS, 1999 U.S. Dist. LEXIS 14466 (D. Ariz. Feb. 17, 1999).

143. *See supra* note 33 and accompanying text; *Burger King*, 471 U.S. at 476-77.

144. *Id.*

145. *See, e.g.*, Pavlovich v. Super. Ct. of Santa Clara County, 109 Cal. Rptr. 2d 909, 916 (Cal. Ct. App. 2001), *hearing granted*, No. S100809 (Cal. Dec. 12, 2001).

of the Internet—the potential for overbroad personal jurisdiction.[146] As the court in *GTE New Media* noted, however, the advent of the Internet is no reason to abandon long-held principles of federal court jurisdiction or notions of due process.[147] The potential for overbroad personal jurisdiction standards on the Internet is significant. As courts continue to apply increasingly expansive definitions of "minimum contacts," "purposeful direction," and "direct effects," and continue to apply increasingly cursory due process and reasonableness analyses, the dangers of overbroad jurisdiction grow. Overbroad personal jurisdiction will have a chilling effect on both commerce and speech on the Internet. If one fears being haled into court all over the United States, and potentially all over the world, one is less likely to engage in otherwise lawful activities.

Courts can try to counteract the dangers of overbreadth by giving due process and reasonableness considerations greater weight when addressing personal jurisdiction. By considering whether the exercise of jurisdiction comports with notions of fair play and substantial justice, courts can limit the fora in which a defendant might have to defend himself. The seven reasonableness factors may aid in this analysis. For instance, if a court were to consider the burden on the defendant in defending in the forum, it may well consider the possibility that defendant will be defending himself in several fora. Additionally, the most efficient judicial resolution of the controversy and existence of alternative fora factors may also work to limit the breadth of personal jurisdiction on the Internet.

Therefore, courts should give greater weight to the reasonableness analysis. In doing so, courts will bring more formality to the hidden bad faith analysis which seems to underlie Internet jurisdiction jurisprudence. Additionally, courts will begin to define limitations of Internet jurisdiction.

C. Reasonableness in *Pavlovich*

Though a return to general reasonableness analyses will serve the development of a consistent Internet jurisdiction jurisprudence, it likely would not change the outcome in the *Pavlovich* case.

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146. *See Bensusan* Note, *supra* note 116 ("Greater focus on the reasonableness test and acceptance of an Internet contact as constitutionally valid, will satisfy several issues. First, it will allay fears that world-wide jurisdiction will necessarily result.").

147. *See supra* note 89 and accompanying text.

The reasonableness inquiry in *Pavlovich* was cursory at best.[148] With regard to factor one, the court noted that "Pavlovich knew that his Web site allowed the illegal publishing and distribution of DVDs."[149] The defendant also knew that the motion picture, computer and telecommunications industries all had substantial presence in California.[150] With regard to factor four, the court merely noted that "[f]actors 4 through 6 clearly favor California."[151]

In applying a more rigorous reasonableness analysis, the court would likely have come to the same result because defendant Pavlovich acted with bad faith. In considering factor one, the court should give great weight to the fact that Pavlovich knowingly posted misappropriated trade secrets on his website. In doing so, Pavlovich affected several industries with a substantial presence in California. As the court noted in its purposeful availment analysis, Pavlovich "knew that California is commonly known as the center of the motion picture industry and that the computer industry holds a commanding presence in the state."[152] Furthermore, the court found that Pavolovich "knew, or should have known, that the DVD republishing and distribution activities he was illegally doing and allowing to be done through the use of his Web site, while benefiting him, were injuriously affecting the motion picture and computer industries in Cali-

148. Pavlovich v. Super. Ct. of Santa Clara County, 109 Cal. Rptr. 2d 909, 917-18 (Ct. App. 2001), *hearing granted*, No. S100809 (Cal. Dec. 12, 2001).

149. *Id.*

150. *Id.*

151. *Id.*

152. *Id.* at 915. The court also quoted a portion of Pavlovich's deposition testimony related to his understanding of the motion picture industry's presence in California. When asked if he had any understanding of where the major motion picture studios are located, Pavlovich responded, "[y]eah, they make a lot of movies in California, Hollywood, yeah." *Id.* With regard to California's dominance in the computer industry, Pavlovich testified:

> Q: Do you have any understanding of whether or not a significant number of hardware manufacturers are located in California?
>
> A: I believe . . . there is a lot of technology companies out in California . . .
>
> Q: And as far as—for lack of a better term, hot spot of technology, is Silicon Valley—its your understanding that Silicon Valley is such a hot spot for technology with respect to hardware or software and programmers? . . . [I]s that correct?
>
> A. Yeah.

Id. at 915-16.

fornia."[153] These acts indicate bad faith on the part of Pavlovich; in fact, the court explicitly noted that "Pavlovich cannot claim innocent intent."[154] Instead of restricting application of Pavlovich's bad faith to the purposeful availment analysis, therefore, the court should consider intent or bad faith in its reasonableness analysis, as well.

Factor four also weighs in favor of a finding of personal jurisdiction in this reasonableness analysis. The fact that Pavlovich directly affected California industry creates a significant interest in adjudication of the dispute in California. When a defendant acts with bad faith, the forum state has a strong interest in adjudicating the dispute in order to address the injury.

IV. CONCLUSION

By giving more attention to the reasonableness prong of the personal jurisdiction analysis, courts can formalize the underlying bad faith analysis which appears to explain, at least to a certain degree, the inconsistent outcomes in Internet jurisdiction case law. When the California Supreme Court decides the fate of Matthew Pavlovich this year, its decision will likely consider (whether explicitly or implicitly) his "bad faith" in posting the DeCSS on the Internet. In doing so, the California Supreme Court should strongly consider the reasonableness prong of the personal jurisdiction analysis.

153. *Id.* at 916.
154. *Id.*

YAHOO! INC. V. LICRA

By Christine Duh

Yahoo! v. LICRA[1] is a harbinger of the problems that Internet companies will face in a borderless world. Because the United States is unusual in its broad freedom of speech guarantees, a person's speech may be legal in the United States but illegal in another country. In physical space, a person's communications can be directed to an audience that is defined and somewhat limited. Physical borders are tangible with traditional entry and exit points.[2] The Internet, however, presents a new challenge because there are no clear borders.[3] Generally, a speaker on the Internet cannot geographically limit where he is heard.[4] Thus, the speaker is susceptible to being charged with violating another country's speech regulations.

The *Yahoo!* decision offers some solace for U.S.-based websites by holding that a U.S. court will not enforce a foreign order which violates a U.S. citizen's right to free speech.[5] In doing so, the court applies fundamental law on the enforcement of foreign judgments to the context of the Internet.[6] Notwithstanding the protection offered to websites in this country, U.S.-based websites continue to be viewed in other countries. Therefore, they may still be subject to the laws of foreign countries. Consequently, Internet companies that wish to do business or maintain a physical presence in a foreign country should become familiar with and attempt to conform to the laws of that country.

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1. 169 F. Supp. 2d 1181 (N.D. Cal. 2001).
2. David R. Johnson & David Post, *Law and Borders—The Rise of Law in Cyberspace*, 48 STAN. L. REV. 1367, 1368 (1996) ("Territorial borders . . . delineate areas within which different sets of legal rules apply. There has until now been a general correspondence between borders drawn in physical space (between nation states or other political entities) and borders in 'law space.'").
3. *Id.* at 1375 ("[I]n Cyberspace, physical borders no longer function as signposts informing individuals of the obligations assumed by entering into a new, legally significant, place.").
4. Dan L. Burk, *Jurisdiction in a World Without Borders*, 1 VA. J.L. & TECH. 3, 50 (1997) ("The structure of the network is such that there is no meaningful opportunity to avoid contact with a given jurisdiction—except perhaps to stay off the Internet altogether.").
5. *Yahoo!*, 169 F. Supp. 2d at 1194.
6. *See infra* Part III.B.

I. THE CASE

A. Facts and Background

Yahoo!, an Internet service provider, is a Delaware corporation with its principal place of business in Santa Clara, California.[7] Yahoo! operates various Internet websites and services, including a search engine, an automated auction site, personal web page hosting services, and chat rooms.[8] Yahoo!'s auction site offers for sale many different types of items, including Nazi-related propaganda and memorabilia, the display and sale of which are illegal in France.[9] Historically, Yahoo! has not removed such items from its auction site because they may be protected by the First Amendment of the U.S. Constitution.[10]

On April 5, 2000, La Ligue Contre Le Racisme Et L'Antisemitisme (LICRA)[11] sent a cease and desist letter to Yahoo!'s headquarters in Santa Clara, California, threatening to take legal action if Yahoo! did not stop displaying Nazi objects for sale on its auction site.[12] Shortly thereafter, LICRA, along with L'Union Des Etudiants Juifs De France (UEJF),[13] used the U.S. Marshal's Office to serve process on Yahoo! in California. LICRA and UEJF then separately filed civil complaints against Yahoo! in the Tribunal de Grande Instance de Paris ("French Court"), alleging a violation of a French criminal statute which bars the public display of Nazi-related "uniforms, insignia or emblems" in France.[14]

On May 22, 2000, the French Court, in an opinion written by Judge Gomez, held Yahoo! liable under French law for allowing French citizens to access auction sites presenting Nazi memorabilia.[15] The court issued an order ("French Order") directing Yahoo! to:

> take all necessary measures to dissuade and render impossible any access via Yahoo.com to the Nazi artifact auction service

7. *Yahoo!*, 169 F. Supp. 2d at 1183.
8. *Id.* at 1184.
9. *Id.*
10. Complaint for Declaratory Relief at 4, Yahoo! Inc. v. LICRA, 169 F. Supp. 2d 1181 (N.D. Cal. 2001) (No. C00-21275).
11. The League Against Racism and Anti-Semitism.
12. Yahoo! Inc. v. LICRA, 145 F. Supp. 2d 1168, 1172 (N.D. Cal. 2001) (order denying motion to dismiss).
13. The Union of French Jewish Students.
14. LE NOUVEAU C. PÉN. art. R.645-2.
15. *Yahoo!*, 145 F. Supp. 2d at 1172.

> and to any other site or service that may be construed as constituting an apology for Nazism or a contesting of Nazi crimes.[16]

On November 20, 2000, after seeking expert opinion on the matter,[17] the French Court reaffirmed the order and commanded Yahoo! to (1) re-engineer its content servers in the United States and elsewhere to allow them to recognize French Internet Protocol (IP) addresses and block access to Nazi artifacts by users associated with such addresses; (2) require users with ambiguous IP addresses to make a declaration of nationality upon arriving at Yahoo!'s home page or upon initiating any search using the word "Nazi"; and (3) comply with the order within three months or face a penalty of 100,000 Francs (approximately $13,300) per day of delay.[18] Although Yahoo! subsequently amended its auction policy to prohibit individuals from auctioning certain Nazi materials, the auction site still offers items, such as stamps and coins from the Third Reich and a copy of Adolf Hitler's *Mein Kampf*, which appear to violate the French Order.[19] Further, Yahoo! does not prevent access to numerous other sites with materials prohibited by France.[20]

B. Procedural History—Determining Jurisdiction

On December 21, 2000, Yahoo! filed a Complaint for Declaratory Relief with the U.S. District Court for the Northern District of California.[21] It sought a declaration that the French Order was neither recognizable nor enforceable in the United States because it violated the Constitution and laws of the United States.[22] Defendants LICRA and UEJF moved to dismiss for lack of personal jurisdiction.[23]

The District Court, in an opinion written by Judge Fogel, held that it had personal jurisdiction over the defendants.[24] It used the Ninth Circuit's three-part test for determining whether a court may exercise specific juris-

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16. LICRA et UEJF v. Yahoo! Inc. et Yahoo Fr., T.G.I. Paris, May 22, 2000, *available at* http://www.juriscom.net/txt/jurisfr/cti/tgiparis20000522.htm. *See also Yahoo!*, 145 F. Supp. 2d at 1185 (translation of French Order attested to be accurate by Isabelle Camus, February 16, 2001).
17. *See infra* Part I.D.
18. *Yahoo!*, 145 F. Supp. 2d at 1172.
19. Yahoo!, Inc. v. LICRA, 169 F. Supp. 2d 1181, 1185 (N.D. Cal. 2001).
20. *Id.*
21. *Id.* at 1186.
22. *Yahoo!*, 145 F. Supp. 2d at 1171.
23. *Id. See* FED. R. CIV. P. 12(b)(2).
24. *Yahoo!*, 145 F. Supp. 2d at 1180.

diction.[25] First, the District Court found that the defendants knowingly engaged in actions intentionally targeted at Yahoo!'s Santa Clara headquarters "for the express purpose of causing the consequences of such actions to be felt in California."[26] In doing so, the court used the Ninth Circuit's "effects test."[27] Second, the District Court found that the claim arose out of or resulted from the defendants' forum-related activities and therefore satisfied the Ninth Circuit's "but for" test.[28] Third, the District Court found that it had jurisdiction.[29] Accordingly, the court denied the defendants' motion to dismiss the case.[30]

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25. *Id.* at 1173. *See also* Cybersell, Inc. v. Cybersell, Inc., 130 F.3d 414, 416 (9th Cir. 1997). Specific jurisdiction exists if (1) the defendant has performed some act or consummated some transaction within the forum or otherwise purposefully availed himself of the privileges of conducting activities in the forum, (2) the claim arises out of or results from the defendant's forum-related activities, and (3) the exercise of jurisdiction is reasonable. *Id.*

26. *Yahoo!*, 145 F. Supp. 2d at 1174.

27. *See* Bancroft & Masters, Inc. v. Augusta Nat'l, Inc., 223 F.3d 1082, 1087 (9th Cir. 2000) ("To meet the effects test, the defendant must have (1) committed an intentional act, which was (2) expressly aimed at the forum state, and (3) caused harm, the brunt of which is suffered and which the defendant knows is likely to be suffered in the forum state."). Previously, every Ninth Circuit decision applying the "effects test" had done so only with respect to wrongful or tortious conduct on the part of the defendant. *Yahoo!*, 145 F. Supp. 2d at 1174. "[F]iling a lawsuit in a foreign jurisdiction might be entirely proper under the laws of that jurisdiction." However, the District Court here found that "such an act nonetheless may be 'wrongful' from the standpoint of a court in the United States if its primary purpose or intended effect is to deprive a [U.S.] resident of its constitutional rights." *Id.* at 1175.

28. *Yahoo!*, 145 F. Supp. 2d at 1176. *See also* Ballard v. Savage, 65 F.3d 1495, 1500 (9th Cir. 1995) (plaintiff must demonstrate that it would have no need for a judicial declaration but for the defendant's forum-related activities). The *Yahoo!* court determined that but for the defendants' forum-related activities (i.e., filing and prosecuting the French lawsuit), Yahoo! would have no need for a declaration that the orders of the French Court were unenforceable in the United States. *Yahoo!*, 145 F. Supp. 2d at 1176.

29. *Yahoo*!, 145 F. Supp. 2d at 1177. The court balanced seven factors:

> (1) the extent of the defendant's purposeful interjection into the forum state; (2) the burden on the defendant in defending in the forum; (3) the extent of the conflict with the sovereignty of the defendant's state; (4) the forum state's interest in adjudicating the dispute; (5) the most efficient judicial resolution of the controversy; (6) the importance of the forum to the plaintiff's interest in convenient and effective relief; and (7) the existence of an alternative forum.

Id. at 1177 (quoting Bancroft & Masters, Inc. v. Augusta Nat'l, Inc., 223 F.3d 1082, 1088 (9th Cir. 2000)). The court emphasized that this case involved "only the limited question of whether [a U.S. court] should recognize and enforce [the] French Order [requiring] Yahoo! to censor its U.S.-based services to conform to French penal law." *Yahoo!*, 145 F.

C. The District Court's Analysis

On November 7, 2001, the District Court for the Northern District of California granted summary judgment on behalf of Yahoo!.[31] The court held that Yahoo! had shown that the French Order was valid under the laws of France, the French Order could be enforced with retroactive penalties, and the ongoing possibility of its enforcement in the United States chilled Yahoo!'s First Amendment rights.[32]

In reaching this decision, the District Court analyzed the requirements of the Declaratory Judgment Act,[33] which allows potential defendants to avoid multiple actions by providing a means by which a court may declare the rights and obligations of the litigants in one action.[34] The key question was whether "there [was] substantial controversy, between parties having adverse legal interests, of sufficient immediacy and reality to warrant the issuance of a declaratory judgment."[35]

The District Court found that an actual controversy existed.[36] Because the French Order subjected Yahoo! to a fine of $13,300 for each day of noncompliance, Yahoo! faced a present and ongoing threat.[37] Even though any penalty would be provisional and require further legal proceedings in France prior to any enforcement action in the United States, the French Court could assess penalties retroactively for the entire period of Yahoo!'s noncompliance.[38] The court believed that Yahoo! could not rely upon assessments in the defendants' declarations that Yahoo! was in "substantial compliance" with the French Order because the defendants had not requested, and the French Court had not made, such a finding.[39]

Supp. 2d at 1178. Taking all of these factors into consideration, the court found that its exercise of personal jurisdiction over the defendants was reasonable. *Id.* at 1180.

30. The District Court further denied without prejudice the defendants' request to certify its jurisdictional determination for interlocutory appeal pending the outcome of Yahoo!'s motion for summary judgment. Yahoo!, Inc. v. LICRA, 169 F. Supp. 2d 1181, 1186 (N.D. Cal. 2001).

31. *Id.* at 1183.

32. *Id.* at 1188-90.

33. 28 U.S.C. § 2201 (1994).

34. *See infra* Part II.A.

35. *Yahoo!*, 169 F. Supp. 2d at 1187-88 (quoting Md. Cas. Co. v. Pac. Coal & Oil Co., 312 U.S. 270, 273 (1941)).

36. *Yahoo!*, 169 F. Supp. 2d at 1187-88.

37. *Id.* at 1191. Yahoo! did not appeal the French Order. *Id.* at 1188.

38. *Id.* at 1188.

39. *Id.* at 1189.

Next, the District Court found that the French Order presented a real and immediate threat to Yahoo!'s First Amendment rights.[40] Because of this, a U.S. court could not constitutionally enforce the French Order. The court reasoned that "[t]he First Amendment does not permit the government to engage in viewpoint-based regulation of speech absent a compelling governmental interest, such as averting a clear and present danger of imminent violence."[41] Further, the court found the French Order's requirement that Yahoo!

> take all necessary measures to dissuade and render impossible any access via Yahoo.com to the Nazi artifact auction service and to any other site or service that may be construed as constituting an apology for Nazism or a contesting of Nazi crimes

to be "too general and imprecise to survive the strict scrutiny [test] required by the First Amendment."[42]

Having found that grounds for declaratory relief existed, the District Court then relied on principles of comity to refuse to enforce the French Order because it was inconsistent with the First Amendment.[43] Although France could regulate what speech was permissible within its own borders, the District Court could not enforce a foreign order that violated the U.S. Constitution by chilling protected speech that occurred simultaneously within U.S. borders.[44] The District Court concluded that because there was no body of law which established international standards with respect to speech on the Internet, nor an appropriate treaty or piece of legislation addressing enforcement of such standards to speech originating within the United States, the principle of comity was outweighed by the court's obligation to uphold the First Amendment.[45]

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40. *Id.* at 1191.

41. *Id.* at 1189.

42. *Id.* Although the defendants argued that the court should abstain from deciding the instant case, the court found no basis for abstention. Abstention is an appropriate remedy where a plaintiff is forum shopping. *Id.* at 1191. The court determined that Yahoo! sought declaratory relief not to avoid an unfavorable result in the French courts (i.e., to forum shop), but rather to determine whether a U.S. court could enforce the French Order without running afoul of the First Amendment. *Id.* at 1191-92.

43. *Id.* at 1192.

44. *Id.*

45. *Id.* The court expressed no opinion as to whether such a treaty would be constitutional. *Id.* at 1193 n.12. However, the First Amendment would probably trump any attempts to enter into a treaty not harmonious with the outcome of this case.

Finally, the Court denied the defendants' motion for a continuance for further discovery pursuant to Rule 56(f).[46] The defendants asserted that further discovery could "lead to the development of triable issues of fact concerning the extent to which Yahoo!'s modifications to its auction site [had] affected its potential liability under the French Order and as to Yahoo!'s technological ability to comply with the order."[47] The District Court reasoned that because enforcement of the French Order by a U.S. court would be inconsistent with the First Amendment, the factual question of whether Yahoo! possessed the technology to comply with the order was immaterial.[48] Even if Yahoo! did possess such technology, compliance would still involve an impermissible restriction on speech.[49] The defendants have appealed to the Ninth Circuit.[50]

D. The Expert Panel's Findings

On August 11, 2000, the French Court appointed a panel of experts ("Expert Panel") to report on whether compliance with the French Order was technically feasible.[51] The Expert Panel consisted of François Wallon of France, Ben Laurie of the United Kingdom, and Vinton Cerf of the United States.[52] The French Court asked the Expert Panel to consider whether it was technically possible for Yahoo! to comply with the judgment against it, and, if not, to what extent compliance could be achieved.[53] Specifically, the Expert Panel investigated whether Yahoo! could determine the geographical origin and nationality of users wishing to access its auction site and prevent French users from perusing the description of Nazi objects posted for auction.[54] The Expert Panel submitted its findings on November 6, 2000.

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46. *Id.* at 1194.

47. *Id.* at 1193.

48. *Id.* at 1194.

49. *Id.*

50. Yahoo! v. LICRA, 169 F. Supp. 2d 1181 (N.D. Cal. 2001), *appeal docketed*, No. 01-17424 (9th Cir. Dec. 7, 2001).

51. LICRA et UEJF v. Yahoo! Inc. et Yahoo Fr., T.G.I. Paris, Nov. 20, 2000, at 5, *available at* http://www.cdt.org/speech/international/001120yahoofrance.pdf. The French Court ordered the formation of the panel to investigate Yahoo!'s assertion that no technical solution existed that would enable Yahoo! to comply fully with the terms of the French Order. *Id.*

52. *Id.* at 15.

53. Ben Laurie, *An Expert's Apology*, *at* http://www.apache-ssl.org/apology.html (Nov. 21, 2000).

54. LICRA et UEJF v. Yahoo! Inc. et Yahoo Fr., T.G.I. Paris, Nov. 20, 2000, at 7-10, *available at* http://www.cdt.org/speech/international/001120yahoofrance.pdf.

The Expert Panel determined that full compliance was impossible; however, it suggested ways in which a reasonable level of compliance could be achieved.[55] The Expert Panel found that seventy percent of the IP addresses assigned to French users could be matched with certainty to a service provider located in France.[56] This moderate level of accuracy was attributed to the fact that Internet protocols were not designed to facilitate geographic documentation. Although Internet machines have "addresses," these locate the machine on a logical network, not in physical space.[57] The Expert Panel further suggested that Yahoo! ask users with ambiguous IP addresses to make a declaration of nationality.[58] The combination of the two procedures, namely geographical identification of the IP address and declaration of nationality, would achieve a filtering success rate approaching ninety percent.[59] After identifying a surfer's origin as France, Yahoo! could then block access to items that had been described by their owner as being of Nazi origin, or simply require the search engine to not execute requests including the word "Nazi."[60]

II. LEGAL BACKGROUND

A. Declaratory Relief

The Declaratory Judgment Act protects potential defendants from multiple actions by allowing a court to declare, in one action, the rights and obligations of the litigants.[61] Congress designed the Act "to relieve potential defendants from the Damoclean threat of impending litigation which a harassing adversary might brandish, while initiating his suit at his leisure—or never."[62] The Act permits parties to prevent the "accrual of potential damages by suing for a declaratory judgment, once the adverse po-

55. Ben Laurie, *An Expert's Apology*, *at* http://www.apache-ssl.org/apology.html (Nov. 21, 2000).

56. LICRA et UEJF v. Yahoo! Inc. et Yahoo Fr., T.G.I. Paris, Nov. 20, 2000, at 11, *available at* http://www.cdt.org/speech/international/001120yahoofrance.pdf. This same fact enables Yahoo! to display French advertising banners on its auction site. *Id.*

57. Burk, *supra* note 4, at 15.

58. LICRA et UEJF v. Yahoo! Inc. et Yahoo Fr., T.G.I. Paris, Nov. 20, 2000, at 10, *available at* http://www.cdt.org/speech/international/001120yahoofrance.pdf. One of the three experts, Vinton Cerf, found this approach problematic. *Id.* at 15.

59. *Id.* at 14.

60. *Id.* at 10-11.

61. 28 U.S.C. § 2201 (1994).

62. Japan Gas Lighter Ass'n v. Ronson Corp., 257 F. Supp. 219, 237 (D.N.J. 1966).

sitions have crystallized and the conflict of interests is real and immediate."[63]

A federal District Court may issue a declaratory judgment in a given matter only if an actual controversy exists.[64] The threshold question is whether "there is a substantial controversy, between parties having adverse legal interests, of sufficient immediacy and reality to warrant the issuance of a declaratory judgment."[65] The "[m]ere possibility, even probability, that a person may in the future be adversely affected by official acts not yet threatened does not create an actual controversy"[66] necessary for declaratory relief. The party invoking the federal jurisdiction bears the burden of showing that it faces an immediate or actual injury.[67]

B. Enforcement of Foreign Judgments

1. Comity

In determining whether to recognize and enforce foreign court judgments, U.S. courts follow the principle of international comity.[68] Comity refers to "the degree of deference that a domestic forum must pay to the act of a foreign government not otherwise binding on the forum."[69] Comity helps to ensure that litigation ends after the parties have had an opportunity to present their cases fully and fairly to a court of competent jurisdiction.[70] In deciding whether to grant comity, U.S. courts balance two interests—international duty and convenience versus the rights of U.S. citizens or other persons under the protection of U.S. laws.[71] In general, U.S. courts respect and enforce foreign judgments and decrees unless enforcement would be prejudicial or contrary to the United States's interests.[72]

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63. *Id.*

64. 28 U.S.C. § 2201 (1994).

65. Md. Cas. Co. v. Pac. Coal & Oil Co., 312 U.S. 270, 273 (1941).

66. Garcia v. Brownwell, 236 F.2d 356, 358 (9th Cir. 1956).

67. Rincon Band of Mission Indians v. County of San Diego, 495 F.2d 1, 5 (9th Cir. 1974).

68. DAVID EPSTEIN ET AL., INTERNATIONAL LITIGATION: A GUIDE TO JURISDICTION, PRACTICE, AND STRATEGY § 11.02 (3d ed. 1998).

69. Laker Airways Ltd. v. Sabena, Belgian World Airlines, 731 F.2d 909, 937 (D.C. Cir. 1984).

70. Cunard S.S. Co. Ltd. v. Salen Reefer Servs. AB, 773 F.2d 452, 457 (2d Cir. 1985).

71. *See* Hilton v. Guyot, 159 U.S. 113, 164 (1895).

72. Somportex Ltd. v. Phila. Chewing Gum Corp., 453 F.2d 435, 440-41 (3d Cir. 1971).

2. *The Public Policy Exception*

U.S. courts deny enforcement of foreign judgments which violate U.S. public policy.[73] The judgment must be "repugnant to fundamental notions of what is decent and just in the [country] where enforcement is sought."[74] For example, U.S. courts will not recognize or enforce a foreign judgment based on laws which do not comport with fundamental First Amendment principles.[75]

Both state and federal courts have denied enforcement of foreign judgments which offend free speech values protected by the First Amendment. In the seminal case of *Bachchan v. India Abroad Publications, Inc.*,[76] the Supreme Court of New York held that the enforcement of an English libel judgment against the operator of a New York news service violated the First Amendment of the U.S. Constitution.[77] Here, the defendant distributed a defamatory report on the plaintiff's alleged crimes in the United Kingdom.[78] The plaintiff brought an action against the defendant in London, England, and was awarded £40,000 in damages in addition to attorney's fees.[79] The plaintiff then sought to enforce the U.K. libel judgment in the United States. However, because the U.K. court had applied libel standards deemed appropriate in the United Kingdom but considered antithetical to the protections afforded the press by the U.S. Constitution,[80] the U.S. court found that enforcement of the U.K. judgment would have a chilling effect on speech and seriously jeopardize the First Amendment's protection of free speech and the press.[81]

Similarly, in *Matusevitch v. Telnikoff*,[82] a U.S. District court denied enforcement of a U.K. libel judgment because U.K. libel standards "deprive[d] the plaintiff of his [U.S.] [C]onstitutional rights."[83] In this case, the defendant Matusevitch, a Russian émigré living in the United King-

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73. EPSTEIN, *supra* note 68, § 11.07.

74. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 117 cmt. C (1971).

75. *See, e.g.*, Matusevitch v. Telnikoff, 877 F. Supp. 1 (D.D.C. 1995), *aff'd on other grounds*, 159 F.3d 636 (D.C. Cir. 1998); Bachchan v. India Abroad Publ'ns Inc., 585 N.Y.S.2d 661 (N.Y. Sup. Ct. 1992).

76. 585 N.Y.S.2d 661 (N.Y. Sup. Ct. 1992).

77. *Id.* at 665.

78. *Id.* at 661.

79. *Id.* at 662.

80. *Id.* at 665. English libel law does not distinguish between private persons and public figures involved in matters of public concern. Moreover, plaintiffs need not prove falsity of the libel or fault on the part of the defendant. *Id.* at 663.

81. *Id.* at 664-65.

82. 877 F. Supp. 1 (D.D.C. 1995).

83. *Id.* at 4.

dom, made statements in the London Telegraph that the plaintiff was racist and anti-Semitic.[84] The plaintiff filed a libel action in London, England, and was awarded £240,000.[85] Matusevitch sought a declaration in a U.S. district court that the English judgment was repugnant to the First and Fourteenth Amendments of the U.S. Constitution.[86] In refusing to enforce the English libel judgment, the U.S. court found that the plaintiff's offending statement was considered protected speech under the First Amendment.[87]

III. DISCUSSION

The District Court's application of traditional law on the enforcement of foreign judgments to the Internet context in *Yahoo!* is relatively straightforward. The holding is fairly narrow, limited to the proposition that the United States will not enforce another country's unconstitutional orders.[88] Clearly, France and other foreign countries can still regulate speech within their own borders. However, the case does demonstrate that a U.S. court may grant declaratory relief on a thin showing of imminent harm, particularly where a First Amendment violation is concerned.

The United States is unusual in its broad freedom of speech guarantees.[89] At least fifty-nine countries currently impose limitations on the freedom of speech online.[90] For example, the People's Republic of China "severely restricts communication via the Internet, including all forms of dissent and the free reporting of news."[91] Thus, while a person's speech may be legal in the United States, it may not be legal in another country. This notion is nothing new. However, in today's world of widely divergent value systems, the Internet's far-reaching capabilities and lack of clear borders may cause countless online speakers to be subject to the laws of other countries.

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84. Telnikoff v. Matusevitch, 702 A.2d 230, 256 (Md. 1997).

85. *Id.* at 235.

86. *Id.*

87. Matusevitch v. Telnikoff, 877 F. Supp. 1, 2 (D.D.C. 1995).

88. Yahoo!, Inc. v. LICRA, 169 F. Supp. 2d 1181, 1185, 1192 (N.D. Cal. 2001).

89. Joel R. Reidenberg, *The Yahoo! Case and the International Democratization of the Internet*, Fordham University School of Law, Research Paper 11, April 2001, at 12 ("[O]ther democracies do not have as an expansive view of free speech as the United States.").

90. Brief of Amici Curiae Center for Democracy & Technology (CDT) et al. at 6, Yahoo!, Inc. v. LICRA, 169 F. Supp. 2d 1181 (N.D. Cal 2001) (No. C00-21275 JF), *available at* http://www.cdt.org/jurisdiction/010406yahoo.pdf.

91. *Id.*

In physical space, a person's communications can be directed to an audience that is defined and somewhat limited.[92] The Internet renders the physical distance between speaker and audience virtually meaningless, allowing ideas and information to easily transcend borders.[93] Thus, the Internet speaker is more susceptible to being charged with violating another country's speech regulations. Internet users in the United States routinely engage in speech that violates, for instance, China's laws against religious expression, the laws of various nations against advocacy of gender equality or homosexuality, and even the United Kingdom's restrictions on freedom of the press.[94] More lawsuits in the vein of the French action will surely follow.[95]

The *Yahoo!* decision offers some solace to website owners who may be worried about the possibility of getting dragged into court in foreign jurisdictions. However, as a practical matter, as long as companies like Yahoo! want to do business or maintain a physical presence in other countries,[96] they should become familiar with and attempt to conform to the laws of those countries.[97] In that sense, *Yahoo!* serves as a harbinger of the problems that Internet websites will face in a borderless world.[98]

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92. *See, e.g.*, Burk, *supra* note 4, at 14 ("In real space, a business can usually locate the person or entity with whom it is interacting; this tends to facilitate identification of partners and validation of transactions.").

93. *Yahoo!*, 169 F. Supp. 2d at 1186. *See also* Johnson & Post, *supra* note 2, at 1370-71 ("Cyberspace has no territorially based boundaries, because the cost and speed of message transmission on the Net is almost entirely independent of physical location. Messages can be transmitted from one physical location to any other location without degradation, decay, or substantial delay, and without any physical cues or barriers that might otherwise keep certain geographically remote places and people separate from one another.").

94. *Yahoo!*, 169 F. Supp. 2d at 1186-87.

95. *See, e.g.*, Center for Democracy & Technology, *International Jurisdiction*, *at* http://www.cdt.org/jurisdiction (Dec. 27, 2000) ("An Italian court . . . recently issued a similar ruling [to the French Order] regarding a case of libel carried out online.").

96. *See* Reidenberg, *supra* note 89, at 15 ("Yahoo! . . . actively sought global business from its web sites in the United States and had significant activity in France through ownership and control of its French subsidiary.").

97. *See* Jack L. Goldsmith, *Against Cyberanarchy*, 65 U. CHI. L. REV. 1199, 1217 (1998) ("A [company's] physical presence or assets within the territory remains the primary basis for a nation or state to enforce its laws.").

98. The United States has itself exercised jurisdiction over Internet sites based in other nations for conduct that is purportedly legal in those nations but illegal in the United States. *See, e.g.*, People v. World Interactive Gaming Corp., 714 N.Y.S.2d 844 (1999) (ordering an Antigua-based casino to stop offering gambling over the Internet to New Yorkers); Twentieth Century Fox v. iCraveTV.com, 2000 U.S. Dist. LEXIS 11670 (W.D. Pa. 2000) (prohibiting a Canadian web site from transmitting U.S. copyrighted

A. The Granting of Declaratory Relief for First Amendment Violations

Yahoo! v. LICRA suggests that, particularly where a First Amendment violation is concerned, U.S. courts may grant declaratory relief on a thin showing of imminent harm. In this case, it was not clear that the defendants would seek to enforce the French Order in the United States. In fact, the defendants disclaimed any intent to seek enforcement in the United States or France, since Yahoo! had already removed certain Nazi-related materials from its auction and other sites.[99] Further, even if the defendants wanted to seek enforcement in the United States, they would first have to bring an action in France to liquidate the penalty.[100] The French Court would then have to assess Yahoo!'s compliance with the French Order and determine whether or not to impose penalties.[101] Only after the French Court assessed penalties against Yahoo! could the defendants seek enforcement of the French Order in the United States.[102] Thus, it seemed that Yahoo! was multiple steps away from facing an imminent threat of harm.[103]

Nevertheless, the District Court found that a real and immediate threat to Yahoo! existed.[104] The court relied on the possibility that the defendants might actually attempt to enforce the French Order, stressing that the provisions of the French Order requiring Yahoo! to regulate the content on its websites remained in full force and effect.[105] Moreover, because the French Order could assess the penalties retroactively,[106] the court found that the ongoing possibility of its enforcement had the immediate effect of inducing Yahoo! to implement new restrictive policies on its auction site, thus chilling Yahoo!'s First Amendment rights.[107] Although Yahoo! had

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programming into the United States); Playboy Enters., Inc. v. Chuckleberry Publ'g Inc., 939 F. Supp. 1032 (S.D.N.Y. 1996) (prohibiting the use of an American trademark, PLAYMEN, by an Italian web server that offered a magazine available in the United States through the Internet). In the third case, the U.S. court required that the defendant block website access to U.S. users. *Id.*

99. Opposition to Motion for Summary Judgment at 7-8, Yahoo! Inc. v. LICRA et al. (N.D. Cal. 2001) (No. C00-21275).

100. *Id.* at 8. There was no final order imposing a penalty in any amount. *Id.*

101. *Id.* at 7-8.

102. *Id.* at 8.

103. *Id.*

104. Yahoo!, Inc. v. LICRA, 169 F. Supp. 2d 1181, 1189-90 (N.D. Cal. 2001).

105. *Id.* at 1191 ("[T]he provisions of the French [O]rder [have not] been waived, suspended or stayed . . . .").

106. *Id.* at 1190.

107. *Id.* at 1189-91.

removed a number of Nazi materials from its websites, Yahoo! continued to offer at least some Third Reich memorabilia as well as *Mein Kampf* on its auction site and permitted access to numerous web pages with Nazi-related content.[108] The fact that Yahoo! did not know whether its efforts to date had met the French Court's mandate was the precise harm against which the Declaratory Judgment Act was designed to protect.[109]

In sum, *Yahoo! v. LICRA* demonstrates that as long as a foreign judgment against a U.S. company exists, with retroactive penalties attached, a U.S. court may find the existence of an actual controversy and grant declaratory relief. In this case, the court determined that Yahoo! faced immediate harm even though the defendants had not sought, and might possibly never seek, enforcement of the judgment in the United States.

B. The Application of Fundamental Law to Foreign Internet Judgments

After deciding that grounds for declaratory relief existed, the District Court went on to extend basic laws on the enforcement of foreign judgments to the Internet context.[110] U.S. courts will refuse to enforce foreign judgments that violate the First Amendment.[111] The French Order's content and viewpoint-based regulation of Yahoo!'s web pages and auction site impinged on Yahoo!'s First Amendment right.[112] Therefore, the U.S. court correctly denied enforcement of the French Order. Although France may regulate speech within its own borders,[113] the United States cannot enforce France's speech-restrictive judgments for France if they violate the First Amendment.[114] The District Court's application of this fundamental principle to the Internet context is relatively straightforward.

Because the Internet allows the same speech to be communicated in two places at once (e.g., in the United States and abroad),[115] a case could be made that an order requiring a website to make certain items inaccessible in a foreign nation may not necessarily contravene the First Amend-

108. *See supra* note 19 and accompanying text.

109. *Yahoo!*, 169 F. Supp. 2d at 1189.

110. *Id.* at 1192-93.

111. *See supra* Part II.B.2.

112. *Yahoo!*, 169 F. Supp. 2d at 1192. *See also* R.A.V. v. City of St. Paul, 505 U.S. 377 (1992) (holding that the First Amendment does not permit the government to impose special prohibitions on speakers who express views on disfavored subjects).

113. *Yahoo!*, 169 F. Supp. 2d at 1192.

114. *See supra* Part II.B.2.

115. *Yahoo!*, 169 F. Supp. 2d at 1192. The unique challenge of the Internet stems in part from its ability to allow a person to speak in more than one place simultaneously. *Id.*

ment.[116] If Yahoo! could employ substantially successful measures to discriminate between French and other users and effectively filter out Nazi-related materials for just the French users, then arguably only speech occurring *in France* would be affected. However, the District Court stated that whether Yahoo! possessed the technology to comply with the French Order was immaterial.[117]

The District Court correctly noted that even if Yahoo! possessed the technical means to comply with the French Order, compliance would still involve an impermissible restriction on speech.[118] There is no way to enforce an order such as this in a manner which does not violate the First Amendment. In *Matusevitch*, the statements at issue were made entirely outside the U.S., yet the U.S. court still refused to uphold the foreign judgment.[119] Thus, it seems to make no difference that a plaintiff's speech took place entirely *outside* the United States. If enforcement of a foreign judgment would violate the First Amendment, a U.S. court will not likely enforce it.

The French Order states that requiring Yahoo! to ban symbols of Nazism is mandated by "simple public morality" and has "the merit of satisfying an ethical and moral imperative shared by all democratic societies."[120] While the fight to continue displaying Nazi artifacts may not seem particularly appealing, it is only the beginning of a string of speech-related fights. A U.S. court's endorsement of a seemingly harmless speech restriction is the first step on a dangerous slippery slope of prohibiting broad categories of protected speech. If U.S. courts enforced foreign speech standards such as the French law that gave rise to the French Order, other countries would be likely to pursue similar penalties in the hopes of silencing other disfavored categories of speech online.[121] "Freedom of expression would be crippled were online speakers in the United States required to conform their speech to the restrictions of foreign nations."[122] In the end, absent an effective means of technological compliance, all websites

116. *But see id.* at 1190 (Defendants did not "argue directly that the French [O]rder somehow could be enforced in the United States in a manner consistent with the First Amendment.").

117. *Id.* at 1194.

118. *Id.*

119. *See supra* notes 82-87 and accompanying text.

120. LICRA et UEJF v. Yahoo! Inc. et Yahoo Fr., T.G.I. Paris, Nov. 20, 2000, at 18, *available at* http://www.cdt.org/speech/international/001120yahoofrance.pdf.

121. Brief of Amici Curiae Center for Democracy & Technology (CDT) et al. at 7, Yahoo!, Inc. v. LICRA, 169 F. Supp. 2d 1181 (N.D. Cal. 2001) (No. C00-21275 JF), *available at* http://www.cdt.org/jurisdiction/010406yahoo.pdf.

122. *Id.* at 10.

would be forced to comply with the rules of the most restrictive nation. Thus, the District Court rightly extended the U.S.'s general refusal to enforce foreign judgments contrary to the First Amendment to a violation of this type on the Internet.

C. The Need for U.S.-Based Websites Doing International Business to Comply With Foreign Laws

The *Yahoo!* ruling is actually a very narrow one, limited to the proposition that under normal principles of comity, a U.S. court will not enforce a foreign order that violates the public policy of this country. This ruling does not mean that U.S.-based websites no longer need to comply with foreign speech restrictions. As the District Court stressed, this case is not about "the right of France or any other nation to determine its own laws and social policies."[123] "France clearly has the right to enact and enforce laws such as those relied upon by the French Court" in issuing its order.[124] Therefore, an Internet company like Yahoo! would still need to comply with French speech regulations if it wished to do business or maintain a physical presence in France. Because that seems to be the case here,[125] it is important to consider ways in which Yahoo! could comply with the French Order.[126]

1. Removal of Prohibited Content to Achieve Compliance

In order to comply with the French Order, Yahoo! could alter its business model and not permit the posting of any materials that violate the French Order. Prior to the French action, Yahoo! already regulated its auction site by banning particular items from being sold (e.g., stolen goods, body parts, prescription and illegal drugs, weapons, and goods violating U.S. copyright laws or the Iranian and Cuban embargos).[127] The French Court suggested in its Order that Yahoo! could easily (and at a low cost) extend this ban to symbols of Nazism.[128]

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123. Yahoo!, Inc. v. LICRA, 169 F. Supp. 2d 1181, 1186 (N.D. Cal. 2001).

124. *Id.*

125. Ben Laurie, *An Expert's Apology*, *at* http://www.apache-ssl.org/apology.html (Nov. 21, 2000) ("If Yahoo! wants to be beyond France's reach, they can surely achieve that, by withdrawing their operations from France. The fact that they don't means that, presumably, they see an economic advantage in continuing to maintain a presence there, despite this problem.").

126. Technical compliance may also be important in future opinions involving a foreign order that the United States might have no problems enforcing.

127. *Yahoo!*, 169 F. Supp. 2d at 1184.

128. LICRA et UEJF v. Yahoo! Inc. et Yahoo Fr., T.G.I. Paris, Nov. 20, 2000, at 18, *available at* http://www.cdt.org/speech/international/001120yahoofrance.pdf.

In an attempt to comply with the French Order, Yahoo! amended its policy to also prohibit individuals from auctioning "[a]ny item that promotes, glorifies, or is directly associated with groups or individuals known principally for hateful or violent positions or acts, such as Nazis or the Ku Klux Klan."[129] Examples of prohibited "hate materials" include Hitler mousepads, swastika flags, patches, and posters, and KKK patches, belt buckles, and hats.[130] Yahoo! still offers certain items for sale that appear to violate the French Order.[131] The defendants apparently found this to be a reasonable level of compliance, stating that they no longer intended to seek enforcement of the French Order "in light of Yahoo!'s removal of offending matter from its Auction and other sites."[132]

2. *Employing Technical Measures to Achieve Compliance*

In order to comply with the French Order, Yahoo! could employ technical measures to identify French users and then filter out Nazi-related propaganda for them.[133] According to the Expert Panel, full compliance with the French Order was not possible.[134] However, the Expert Panel believed that Yahoo! could achieve a reasonable level of compliance by implementing specified technical measures.[135] While Yahoo! could possibly achieve a reasonable level of compliance with the French Order, it seems clear that the technical measures suggested by the Expert Panel may not be scalable.

The Expert Panel determined that Yahoo! could achieve a filtering success rate approaching ninety percent by first using IP addresses to match users to French service providers and then asking users with ambiguous IP addresses to make a declaration of nationality.[136] Even so, there are many means by which IP address technology may be circumvented.[137] A French web surfer may simply use an anonymizer to conceal

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129. *Yahoo!*, 169 F. Supp. 2d at 1185. *See also* Yahoo! Auctions, *Yahoo! Auctions Guidelines*, *at* http://user.auctions.shopping.yahoo.com/html/guidelines.html (last visited Feb. 8, 2002).

130. Yahoo! Auctions, *What Am I Not Allowed to Sell?*, *at* http://help.yahoo.com/help/us/auct/asell/asell-21.html (last visited Feb. 8. 2002).

131. *See supra* note 19 and accompanying text.

132. Opposition to Motion for Summary Judgment at 8, Yahoo! Inc. v. LICRA et al. (N.D. Cal. 2001) (No. C00-21275).

133. *See supra* Part I.D.

134. *See supra* note 55 and accompanying text.

135. *Id.*

136. *See supra* note 59 and accompanying text.

137. LICRA et UEJF v. Yahoo! Inc. et Yahoo Fr., T.G.I. Paris, Nov. 20, 2000, at 10-11, 14, *available at* http://www.cdt.org/speech/international/001120yahoofrance.pdf.

his IP address.[138] He may also lie when asked to declare his nationality.[139] The technical remedies have therefore been called "inaccurate, ineffective and trivially avoided."[140] However, imperfect regulation does not equal ineffective regulation.[141] The French Court would not likely have held Yahoo! responsible for users who sought to affirmatively circumvent responsible measures that Yahoo! put in place. Democracies do not normally hold citizens liable for the illegal acts of third parties.[142] Thus, Yahoo!'s less-than-perfect identification of French users would probably have satisfied the French Court.

Even if Yahoo! could determine geographic location at an acceptable level, blocking access by French users to Nazi artifacts might be more difficult. The French Court reasoned that since Yahoo! could use French banner ads in targeting France, it probably possessed the technological capability to comply with the French Order.[143] However, filtering out offending material is much more difficult than triggering particular banner ads.[144] The Expert Panel noted that "there [was] no automatic or infallible approach for identifying images or items that 'constitute an apology for Nazism or a contesting of Nazi crimes.'"[145] It suggested that Yahoo! could block access to items that had been described by their owner as being of Nazi origin. Still, blocking automatically by keywords, like "Nazi" or "Hitler," would surely block permitted content as well (e.g., historical discussions of WWII, anti-Nazi materials, or literary works like *The Diary of Anne Frank*).[146] Further, numerous offending materials would not be blocked out by a simple keyword search.[147] The Expert Panel recom-

138. Ben Laurie, *An Expert's Apology*, *at* http://www.apache-ssl.org/apology.html (Nov. 21, 2000).

139. *Id.*

140. *Id.*

141. Goldsmith, *supra* note 97, at 1229.

142. No legal system in a democracy can assure full compliance with all laws without resorting to police state tactics. Reidenberg, *supra* note 89, at 16.

143. LICRA et UEJF v. Yahoo! Inc. et Yahoo Fr., T.G.I. Paris, Nov. 20, 2000, at 13, *available at* http://www.cdt.org/speech/international/001120yahoofrance.pdf.

144. *See* Troy Wolverton & Erich Luening, *Will Yahoo's ban on auctioned Nazi items work?*, CNET News.com, Jan. 3, 2001, *at* http://news.com.com/2100-1017-250484.html?legacy=cnet&tag=rltdnws.

145. Complaint for Declaratory Relief at 7, Yahoo! Inc. v. LICRA, 169 F. Supp. 2d 1181 (N.D. Cal. 2001) (No. C00-21275).

146. Motion for Summary Judgment at 10, Yahoo! Inc. v. LICRA et al. (N.D. Cal. 2001) (No. C00-21275).

147. For example, not all Nazi-related materials will contain the word "Nazi" in their product names or descriptions. Moreover, it is not feasible to have a human being manually examine every web page for offending materials.

mended that, as an alternative, Yahoo! could require the search engine to not execute requests including the word "Nazi."[148]

Although the French Court found that this level of compliance would be reasonable,[149] it seems clear that technical compliance with even one speech restriction of one foreign country presents many difficulties. As increasingly more lawsuits like the French action arise, compliance with speech-restrictive judgments will grow even more burdensome and difficult.

IV. CONCLUSION

Yahoo! v. LICRA offers some protection for U.S.-based websites which find themselves unexpectedly in a foreign court. As long as U.S.-based websites keep all their assets in the United States, they will be protected against foreign judgments which impose unconstitutional speech restrictions upon them. As a result of this ruling, U.S.-based websites may move all their assets to the United States, so that foreign courts will not be able to collect on any money judgments. At least one commentator believes that "[t]he United States [may] turn into a haven for extremists and racists using the Internet to spread their beliefs."[150] However, the *Yahoo!* court's extension of fundamental laws on enforcement of foreign judgments to the Internet was both necessary and relatively straightforward. A U.S. court's endorsement of a seemingly harmless speech restriction could have been the first step on a dangerous slippery slope. The decision might have encouraged "international forum shopping by people looking for the best country in which to sue."[151] In the end, countries would have been able to use their laws to force Internet companies to answer to the lowest common denominator.[152]

As a practical matter, if a U.S.-based website wants to do business or maintain a physical presence in another country, it needs to become familiar with and attempt to conform to that country's laws. Moreover, even if a U.S.-based website kept all its assets in the United States, other considerations might cause the site to attempt to comply with foreign judgments

148. *See supra* note 60 and accompanying text.

149. LICRA et UEJF v. Yahoo! Inc. et Yahoo Fr., T.G.I. Paris, Nov. 20, 2000, at 21, *available at* http://www.cdt.org/speech/international/001120yahoofrance.pdf.

150. Nikla Gibson, *French Say U.S. Yahoo Ruling Poses Extremism Risk*, Tech News from Reuters, Nov. 9, 2001, *available at* http://news.excite.com/news/r/011109/10/net-tech-yahoo-ruling-dc.

151. Tamara Loomis, *Internet Companies Sighing With Relief, For Now*, New York Law Journal, Nov. 15, 2001, *at* http://www.law.com.

152. *Id.*

against it.[153] In order to achieve a reasonable level of compliance, a website would have to remove content altogether or employ technical filtering measures.[154] This leads to problems of scalability. Conducting business in a country-by-country basis is impractical.[155] Even if a website achieves a reasonable level of compliance with the laws of one country, in the end, scalability issues might require most sites to tailor all their content to fit the laws of the most restrictive country.

New legal rules may affect technological evolution.[156] In June 2001, Yahoo! signed a deal to use geographic targeting technology from Akamai Technologies to deliver online ads to consumers based on their physical location.[157] Akamai geo-targeting technology can pinpoint a person's location by city, state, and country with, on average, a ninety-eight percent accuracy.[158] Another technology company, Digital Envoy, recently received $10.5 million in funding for its work in developing an Internet-mapping technology, which can pinpoint the geographic location of computer users by country, state, city and demographic marketing area. Digital Envoy states that its geo-mapping technology is roughly ninety-nine percent accurate at determining the consumer's country of origin.[159] This would take care of the first step involved in complying with the French Order. However, Yahoo! would still need to find a way to identify banned material or stop French users from viewing it. Perhaps the threat of enforcement of foreign judgments will spur the development of technologies that allow a level of compliance that today seems impossible. For now, most companies may have to follow Yahoo!'s lead by removing the offending items from the site altogether.

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153. *See, e.g.*, Center for Democracy & Technology, *International Jurisdiction*, *at* http://www.cdt.org/jurisdiction (Dec. 27, 2000) ("[A] German court ruled that an Australian web site owner—whose web site questioning the Holocaust is illegal in Germany but not in Australia—could be jailed for violating German speech laws.").

154. *See supra* Part III.C.

155. Tamara Loomis, *Internet Companies Sighing With Relief, For Now*, New York Law Journal, Nov. 15, 2001, *available at* http://www.law.com.

156. Goldsmith, *supra* note 97, at 1229.

157. Stefanie Olsen, *Yahoo ads close in on visitors' locale*, CNET News.com, Jun. 27, 2001, *at* http://news.cnet.com/news/0-1005-202-6397360.html.

158. *Id.*

159. *See* Stefanie Olsen, *Investors follow trail of geo-tracking firm*, CNET News.com, Aug. 13, 2001, *at* http://news.cnet.com/news/0-1005-202-6860853.html?tag=prntfr (last visited Feb. 2, 2002).

STATE INTERNET REGULATION AND THE DORMANT COMMERCE CLAUSE

By Michelle Armond

In *American Libraries Association v. Pataki*,[1] a U.S. District Court struck down a state statute prohibiting the Internet dissemination of obscene materials to minors on dormant Commerce Clause grounds. Over the next few years, courts followed the reasoning of *Pataki* and invalidated a wide range of state Internet regulations. Although some commentators argued otherwise,[2] it seemed that state Internet regulations were categorically invalid under the dormant Commerce Clause. However, the Washington Supreme Court recently issued the first major decision upholding a state Internet regulation on dormant Commerce Clause grounds: *State v. Heckel*[3] upheld a Washington regulation that prohibited the Internet transmission of fraudulent e-mail.[4]

This Note will consider the intersections of *Pataki* and *Heckel* and propose that some narrow classes of state Internet regulations are compatible with the demands of the dormant Commerce Clause. Part I will examine dormant Commerce Clause jurisprudence, notably the *Pike* balancing test, and the Supreme Court's transportation and extraterritoriality cases. Part II will analyze categories of state Internet regulation, especially obscenity and spam, and present *Pataki* and *Heckel* in greater detail. Part III will consider the dormant Commerce Clause as applied in these decisions, addressing underlying statutory and geographic concerns and discussing how they affect the dormant Commerce Clause analysis of state Internet regulations.

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1. 969 F. Supp. 160 (S.D.N.Y. 1997).

2. *See, e.g.*, Daniel A. Farber, *Expressive Commerce in Cyberspace: Public Goods, Network Effects, and Free Speech*, 16 GA. ST. U. L. REV. 789, 818 (2000) (arguing for a more restrained application of the dormant Commerce Clause in striking down state Internet regulations).

3. 24 P.3d 404 (Wash. 2001).

4. Recently, a California appellate court followed suit and reversed a trial court's sustainer of a demurrer on the ground that California Business & Professions Code § 17538.4, prohibiting the transmission of unsolicited electronic mail, violated the dormant Commerce Clause. Ferguson v. Friendfinders, Inc., 115 Cal. Rptr. 2d 258 (Cal. Ct. App. 2002). The court distinguished the dispute from *Pataki* and looked favorably on the reasoning in *Heckel*, which the court characterized as "a case upholding a statute analogous to section 17538.4 against a dormant Commerce Clause challenge." *Id.* at 266.

I. THE DORMANT COMMERCE CLAUSE

The Commerce Clause expressly grants Congress the power "[t]o regulate Commerce . . . among the several states."[5] Beginning with *Gibbons v. Ogden*,[6] courts have found an implied power in the Commerce Clause and struck down state regulations that interfere with interstate commerce by effecting policies of economic discrimination.[7] This implied power, known as the dormant Commerce Clause, has been used to enjoin states from impeding the flow of interstate commerce, practicing "economic protectionism," and discriminating against outsiders.[8] The dormant Commerce Clause has had significant impact on state regulation of Internet communications.

When evaluating a state statute under the dormant Commerce Clause, a court must determine whether the statute facially discriminates against interstate commerce.[9] If the statute facially discriminates, the statute is deemed "virtually *per se* invalid."[10] If it does not, the court must apply the balancing test from *Pike v. Bruce Church*[11] to determine whether the local benefits outweigh the burdens on interstate commerce.[12] Under the *Pike* test, the court must determine whether "the burden imposed . . . is clearly excessive in relation to the putative local benefits."[13] Another factor in the balancing test is whether the local interest can be promoted by other regulations that have a lesser impact on interstate activities.[14]

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5. U.S. CONST. art. I, § 8, cl. 3.

6. 22 U.S. (9 Wheat.) 1 (1824).

7. Michael A. Lawrence, *Toward a More Coherent Dormant Commerce Clause: A Proposed Unitary Framework*, 21 HARV. J.L. & PUB. POL'Y 395, 403 (1998); James E. Gaylord, Note, *State Regulatory Jurisdiction and the Internet: Letting the Dormant Commerce Clause Lie*, 52 VAND. L. REV. 1095, 1106 (1999). The Supreme Court's dormant Commerce Clause jurisprudence has been criticized as "erratic," with "complex exceptions" and "dubious consistency." Lawrence, *supra*, at 397-98.

8. Dan L. Burk, *Federalism in Cyberspace*, 28 CONN. L. REV. 1095, 1123-24 (1996).

9. Oregon Waste Sys., Inc. v. Dep't of Envtl. Quality, 511 U.S. 93, 99 (1994).

10. *Id.*

11. 397 U.S. 137 (1970).

12. *Id.* at 142 ("Where the statute regulates even-handedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits."). *See also* William Lee Biddle, Comment, *State Regulation of the Internet: Where Does the Balance of Federalist Power Lie?*, 37 CAL. W. L. REV. 161, 165 (2000); Gaylord, *supra* note 7, at 1108-09.

13. *Pike*, 397 U.S. at 142.

14. *Id.*

Two lines of cases have emerged where courts have struck down state statutes under the dormant Commerce Clause: the transportation cases and the extraterritoriality cases. Some scholars view these two lines of cases as specialized applications of the *Pike* test.[15] *Cooley v. Board of Wardens*[16] introduced the concept that some aspects of commerce require uniform national regulation.[17] The transportation cases are the progeny of *Cooley*.[18] In a leading decision, *Kassel v. Consolidated Freightways*, the Supreme Court invalidated a state law that limited truck lengths on state highways based on safety rationales.[19] The Court acknowledged that states may regulate matters of local concern that affect interstate commerce to some extent and was extremely reluctant to invalidate "regulations that touch upon safety."[20] Nonetheless, the Court found no compelling safety evidence[21] and pointed to exceptions given to trucks traveling wholly intrastate as raising the specter of interstate discrimination.[22] Thus, a statute

15. *See* Donald H. Regan, *The Supreme Court and State Protectionism: Making Sense of the Dormant Commerce Clause*, 84 MICH. L. REV. 1091, 1184 (1986) (noting that the transportation cases involve limited application of *Pike* benefit/balancing in consideration of the significant interest in a national transportation system); Kenneth D. Bassinger, Note, *Dormant Commerce Clause Limits On State Regulation of the Internet: The Transportation Analogy*, 32 GA. L. REV. 889, 897 (1998) (noting that *Pike* balancing principles appear in transportation cases).

16. 53 U.S. 299 (1851). The Court found that a requirement that all boats traveling through the Philadelphia harbor hire a local pilot or pay a fine did not violate the dormant Commerce Clause. *Id.* at 312. For an overview of the transportation cases in the state Internet regulation context, see Bassinger, *supra* note 15, at 898-904; Biddle, *supra* note 12, at 170-77.

17. *Cooley*, 53 U.S. at 316-17 ("[T]his subject of the regulation of pilots and pilotage has an intimate connection with, and an important relation to, the general subject of commerce with foreign nations and among the several states, over which it was *one main object of the Constitution to create a national control.*") (emphasis added).

18. *See, e.g.*, Bibb v. Navajo Freight Lines, 359 U.S. 520 (1959) (invalidating an Illinois law that required trucks to be equipped with a specific, curved type of tire mud guard); S. Pac. Co. v. Arizona, 325 U.S. 761 (1945) (invalidating an Arizona law that limited the length of trains within the state); S.C. State Highway Dep't v. Barnwell Bros., 303 U.S. 177 (1938) (upholding a South Carolina law that admittedly burdened interstate commerce by placing width and weight restrictions that 85% to 95% of trucks currently in use would exceed); Wabash Ry. Co. v. Illinois, 118 U.S. 557 (1886) (invalidating an Illinois law that prohibited price discrimination by railroad companies in setting their shipping rates).

19. 450 U.S. 662, 678-79 (1980).

20. *Id.* at 670.

21. *Id.* at 671 ("[T]he State failed to present any persuasive evidence that 65-foot doubles are less safe than 55-foot singles.").

22. *Id.* at 677 ("The origin of the 'border cities exemption' also suggests that Iowa's statute may not have been designed to ban dangerous trucks, but rather to discourage interstate truck traffic.").

that imposed a burden on interstate commerce and was not justified by a strong state interest violated the dormant Commerce Clause.[23]

In another line of cases beginning with *Edgar v. MITE Corp.*,[24] the Court proposed that the "Commerce Clause . . . precludes the application of a state statute to commerce that takes place wholly outside the state's borders, whether or not the commerce has effects within the State."[25] These extraterritoriality cases[26] held that a statute that directly controls commerce occurring outside a state's boundaries exceeds the enacting state's authority and is invalid regardless of whether the legislature intended the extraterritorial reach.[27] *Edgar* concerned an Illinois statute that required tender offers of Illinois "target" companies subject to corporate takeovers to be registered with the Illinois Secretary of State.[28] The Court acknowledged that states traditionally regulated companies incorporated under their laws, including intrastate securities regulations.[29] It nonetheless struck down the law because it could potentially regulate transactions occurring wholly outside the state. It had "sweeping extraterritorial effects," and tender offers would be stifled if all states enacted such regulations.[30]

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23. *Id.* at 678-79.

24. 457 U.S. 624 (1982).

25. *Id.* at 642-43.

26. *See, e.g.*, Healy v. Beer Inst., 491 U.S. 324 (1989) (invalidating a Connecticut liquor price affirmation statute on grounds that the statute controlled commerce occurring outside Connecticut and conflicted with other states' regulatory programs); CTS Corp. v. Dynamics Corp., 481 U.S. 69 (1987) (holding that Indiana corporate takeover law did not violate the dormant Commerce Clause by creating inconsistent regulations); Brown-Forman Distillers Corp. v. New York State Liquor Auth., 476 U.S. 573 (1986) (holding that a New York price affirmation law was invalid under the dormant Commerce Clause because it had the practical effect of regulating prices in other states, since sellers could not lower their prices in other states during the relevant time period).

27. Gaylord, *supra* note 7, at 1112.

28. *Edgar*, 457 U.S. at 626-27. The Illinois statute defined a target company as any corporation where shareholders located in Illinois owned at least 10% of the equity securities subject to the tender offer, or met two of the following conditions: had a principal executive office in Illinois, was incorporated in Illinois, or had at least 10% of its capital located in the state. *Id.* at 627. A tender offer was "registered" twenty days after a registration statement was filed with the Secretary of State. The Secretary was empowered to call a hearing any time during the twenty-day period to "adjudicate the substantive fairness of the offer" if it believed it necessary to protect the target company shareholders. *Id.*

29. *Id.* at 641.

30. *Id.* at 642.

In *Healy v. Beer Institute*,[31] a widely-followed decision, the Court invalidated a Connecticut law requiring liquor distributors to affirm that prices charged in Connecticut were no higher than those charged in bordering states.[32] Summarizing its extraterritoriality jurisprudence, the Court found that the dormant Commerce Clause precluded application of a state statute to commerce occurring wholly outside the state's borders, regardless of the statute's effects within the state.[33] Second, state statutes regulating extraterritorial commerce exceeded state authority and were invalid even if the extraterritorial effects were not intended by the legislature.[34] Finally, courts should consider not just the practical effects of the statute itself but also how a challenged statute could interact with regimes of other states, both existing regimes and theoretical regimes adopting conflicting legislation.[35] Finding that the statute controlled commerce outside Connecticut and had troublesome interactions with comparable New York regulations, the Court invalidated it.[36]

II. INTERNET REGULATORY CASES DECIDED UNDER THE DORMANT COMMERCE CLAUSE

Obscenity and spam regulations are the two types of state Internet regulations that have primarily been subject to dormant Commerce Clause analyses. The following section will examine *Pataki* and *Heckel*, two leading decisions in these areas involving significant dormant Commerce Clause concerns. In addition to spam and obscenity, states have regulated other types of conduct that occur over, or are facilitated by, the Internet. Some examples include Internet gambling, attorney advertising, online pharmacies, alcohol and cigarette sales, and state sales taxes.[37] Before the

31. 491 U.S. 324 (1989).

32. *Id.* at 326. As amended in 1984, the Connecticut statute required out-of-state beer shippers to affirm that their posted prices were no higher than prices in bordering states at the time of posting. Another provision explicitly stated that while nothing prohibited shippers from changing their out-of-state prices after the affirmed price was posted, a different statute continued to make it unlawful for out of state shippers to sell beer in Connecticut at a higher price than charged in bordering states during the month covered by the posting. *Id.* at 328-29.

33. *Id.* at 336.

34. *Id.*

35. *Id.*

36. *Id.* at 337-39.

37. *See, e.g.*, Ari Lanin, Note, *Who Controls the Internet? States' Rights and the Reawakening of the Dormant Commerce Clause*, 73 S. CAL. L. REV. 1423, 1443-46 (2000) (providing a good overview of Internet gambling issues and the dormant Commerce Clause). *See generally* Ron N. Dreben & Johanna L. Werbach, *Senators Versus*

Internet, many of these areas were traditionally regulated by states.[38] These topics will not be discussed in more detail because there are no major decisions containing appreciable dormant Commerce Clause analysis.

A. Obscenity Regulations: American Libraries Association v. Pataki

1. *Background: State Regulation of Decency*

The Internet is a collection of local computer systems connected to high-capacity national and international networks.[39] Data is transmitted via packets that are routed according to available bandwidth.[40] As some commentators have pointed out, the Internet's structure "confounds geography."[41] Internet host computers are identified by logical Internet Protocol (IP) addresses,[42] not geographic location. Even knowing locations of sender and recipient computers gives no insight into the digital routes packets will follow as they are relayed among intermediate hosts.[43]

Federal and state governments have made numerous attempts to regulate obscenity and child pornography on the Internet. General federal laws regulating these two areas ostensibly apply to the Internet.[44] Congress explicitly tried to regulate Internet content via the Communications Decency Act of 1996 (CDA),[45] parts of which were subsequently struck down by

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Governors: State and Federal Regulation of E-Commerce, 17 No. 6 COMPUTER LAW. 3 (2000).

38. *See, e.g.*, Dreben & Werbach, *supra* note 37, at 5 ("States traditionally have regulated pharmacies and doctors doing business within their borders via licensing requirements."); *id.* ("With the exception of Prohibition, states traditionally have regulated alcohol sales within their borders, and state laws can affect direct shipping, licensing, advertising, and taxes."); Lanin, *supra* note 37, at 1443 ("states have traditionally been left to decide the extent to which gambling will be permitted within their borders").

39. *See* Reno v. ACLU, 521 U.S. 844, 849-853 (1997) (describing the structure of the Internet); Burk, *supra* note 8, at 1097-1100 (discussing the origins and evolution of the Internet).

40. Burk, *supra* note 8, at 1097.

41. *See, e.g.*, Gaylord, *supra* note 7, at 1100.

42. Gaylord, *supra* note 7, at 1100 (defining IP addresses as unique 32-bit numbers identifying individual host computers).

43. Gaylord, *supra* note 7, at 1101; Bassinger, *supra* note 15, at 894 (noting that because of packet switching, "it is impossible to limit Internet communications to a particular geographic area or state").

44. *See* Dreben & Werbach, *supra* note 37, at 8.

45. Communications Decency Act of 1996, S. 652, 104th Cong. Title V (1996).

Reno v. ACLU.[46] In an attempt to remedy earlier infirmities in the CDA, Congress passed the Child Online Protection Act (COPA) in 1998, making it a federal crime for commercial websites to communicate "harmful" material to minors.[47] Last year, the United States Court of Appeal for the Third Circuit upheld an injunction against the enforcement of COPA on grounds it violated the First Amendment. The Supreme Court later granted certiorari.[48]

Since *Reno*, several states, including New York, have passed statutes in an attempt to fill the void of Internet content regulation.[49] Virginia's law, for example, prohibits the Internet dissemination of commercial material considered harmful to minors.[50] The statute prohibits the knowing sale, rental, or loan to a juvenile of electronic files depicting sexual images and the commercial display of such material in ways that juveniles can access.[51] Several state regulations have been struck down on First Amendment and dormant Commerce Clause grounds.[52] Nonetheless, similar laws continue to be enacted.[53]

2. *The Case*

In 1996, the New York legislature amended its penal law, which prohibited the dissemination of obscene or indecent materials to minors, to include general Internet communications.[54] Under the New York law, it was a felony for an individual, "[k]nowing the character and content of the communication which [depicts sexual subject matter and] is harmful to minors, [to] intentionally use[] any computer communication system . . .

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46. Reno v. ACLU, 521 U.S. 844, 874 (1997) ("We are persuaded that the CDA lacks the precision that the First Amendment requires when a statute regulates the content of speech.").

47. Child Online Protection Act, Pub. L. No. 105-277, 112 Stat. 2681 (1998) (codified at 47 U.S.C. § 231).

48. ACLU v. Reno, 217 F.3d 162 (3d Cir. 2000), *cert. granted sub nom.* Ashcroft v. ACLU, 121 S. Ct. 1997 (2001).

49. *See, e.g.*, N.M. STAT. ANN. § 30-37-3.2 (Michie Supp. 2001); MICH. COMP LAWS ANN. § 722.671a (West Supp. 2001); N.Y. PENAL LAW § 235.22 (McKinney 1999). *See also* Dreben & Werbach, *supra* note 37, at 9 (noting New Mexico, Michigan, Virginia, and New York have enacted their own "little CDAs").

50. VA. CODE ANN. § 18.2-391 (Michie Supp. 2001).

51. *Id.*

52. *See, e.g.*, ACLU v. Miller, 977 F. Supp. 1228 (N.D. Ga. 1997) (First Amendment); Am. Libraries Ass'n v. Pataki, 969 F. Supp. 160 (S.D.N.Y. 1997) (dormant Commerce Clause).

53. *See* Dreben & Werbach, *supra* note 37, at 9.

54. N.Y. PENAL LAW § 235.21 (McKinney 1999).

to initiate or engage in [sexual] communication with a . . . minor."[55] The New York law provided numerous defenses to liability,[56] and violations were class E felonies punishable by one to four years of incarceration.[57] Fearing liability under the amended statute, a broad spectrum of individuals and organizations using the Internet for communications sought declaratory and injunctive relief.[58]

3. *District Court Decision*

In a widely followed opinion,[59] the U.S. District Court for the Southern District of New York struck down the Act on dormant Commerce Clause grounds.[60] The court discussed the Internet[61] and noted that "Internet users have no way to determine the characteristics of their audience that are salient under the New York Act—age and geographic location."[62] The court discussed various states' Internet legislation and prosecution

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55. *Id.* The Act defined "harmful to minors" as "that quality of any [sexual] description or representation" which appealed to minors' prurient interests, is patently offensive to community standards, and lacks serious literary, artistic, political, and scientific value for minors. N.Y. PENAL LAW § 235.20(6) (McKinney 1999).

56. An affirmative defense is established if the obscene or indecent material contained "scientific, educational, governmental or other similar justification" for distributing the material. N.Y. PENAL LAW § 235.15(1) (McKinney 1999). A regular defense is established if the defendant made reasonable efforts to ascertain the true age of a minor, restrict access, label, or segregate material to facilitate blocking. N.Y. PENAL LAW § 235.23(3) (McKinney 1999). An exemption was made for "providing [Internet] access or connection." N.Y. PENAL LAW § 235.24 (McKinney 1999). *See also Pataki*, 969 F. Supp. at 163-64.

57. N.Y. PENAL LAW § 235.21 (McKinney 1999); *Pataki*, 969 F. Supp. at 163.

58. *Pataki*, 969 F. Supp. at 161-63 (naming plaintiffs, including book sellers and publishers, software trade associations, Internet service providers, and civil rights organizations).

59. Following *Pataki*, two appellate decisions used the dormant Commerce Clause to strike down Internet decency regulations. *ACLU v. Johnson* relied heavily on *Pataki* to strike down a New Mexico statute criminalizing the dissemination of sexual material harmful to minors. 194 F.3d 1149, 1160-62 (10th Cir. 1999). The New Mexico statute had very similar structure, language, and purpose as the New York regulation in *Pataki*. *Id.* at 1152 (quoting N.M. STAT. ANN. § 30-37-3.2 (Michie 1999)). Likewise in *Cyberspace Communications, Inc. v. Engler*, the Sixth Circuit invalidated an amendment to a Michigan statute that added computers and the Internet as prohibited means of distributing obscene and sexually explicit material to children. 238 F.3d 420 (6th Cir. 2000) (unpublished).

60. *Pataki*, 969 F. Supp. at 183-84.

61. In analyzing the Internet's structure, the Court discussed different means of Internet communication, including e-mail, listservs, newsgroups, chat rooms, and the World Wide Web. *Pataki*, 969 F. Supp. at 165-66.

62. *Id.* at 167.

attempts, pointing out that inconsistent state standards and overreaching state regulations invited dormant Commerce Clause analysis.[63]

The Court invalidated the statute on four dormant Commerce Clause grounds. First, the Act represented "an unconstitutional projection of New York law into conduct occur[ing] wholly outside New York."[64] The Court considered the legislative history and concluded that legislators intended the Act to apply to communications between New York residents and individuals outside the state.[65] Additionally, it found that the Internet's "insensitiv[ity] to geographic distinctions" would make it difficult for Internet regulations to apply to wholly intrastate activities.[66]

Second, the *Pataki* court relied on Supreme Court extraterritoriality jurisprudence that prohibited states from projecting their legislation into other states.[67] The court concluded that website owners were unable to close their sites to New York users;[68] as a result, residents of other states could be prosecuted for conduct perfectly legal in their home states.[69] It found the dormant Commerce Clause precluded a state from expanding its regulatory powers to encroach on other states.[70] The court noted that "[t]he nature of the Internet makes it impossible to restrict the effects of the New York Act to conduct occurring within New York."[71] It proposed a hypothetical scenario where conduct legal in an individual's home state could potentially subject him to prosecution in New York—thus subordinating his home state's policy to New York's local concerns.[72] Thus, the New York statute overreached and impermissibly undermined other states' regulatory authority.[73]

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63. *Id.* at 168-69. The court noted: "The unique nature of the Internet highlights the likelihood that a single actor might be subject to haphazard, uncoordinated, and even outright inconsistent regulation by states that the actor never intended to reach and possibly was unaware were being accessed." *Id.* at 168.

64. *Id.* at 169.

65. *Id.* at 170.

66. *Id.*

67. *Id.* at 173-74 (discussing *Edgar v. MITE Corp.*, 457 U.S. 624 (1982), and *Healy v. Beer Institute*, 491 U.S. 324 (1989)).

68. *Id.* at 174.

69. *Id.* at 177.

70. *Id.* at 175-76 (summarizing the *Edgar/Healy* extraterritoriality analysis into two prongs, vertical and horizontal: (1) the Commerce Clause subordinates each state's authority over interstate commerce to federal regulatory power; and (2) the Commerce Clause embodies a principle of comity that mandates one state shall not expand its regulatory power to encroach upon the sovereignty of other states).

71. *Id.* at 177.

72. *Id.*

73. *Id.* at 176.

Third, the New York law was impermissible under the *Pike* balancing test because the burdens imposed on interstate commerce outweighed the local benefits.[74] *Pataki* recognized the "quintessentially legitimate state objective" of protecting children from pedophilia.[75] Nonetheless, the court doubted that the statute would realize actual local benefits. According to the court, other New York laws and the unchallenged parts of the statute[76] left only a small category of cases uncovered, and the court predicted that jurisdictional limitations would constrain the state's ability to prosecute offenders in that category.[77] Balanced against these "limited local benefits" was "an extreme burden on interstate commerce."[78] The court concluded that the "New York Act casts its net worldwide" and produced a "chilling effect" broader than New York's ability to prosecute.[79] The court was also concerned that the costs associated with website owners' attempts to comply with the Act's enumerated defenses were excessive.[80]

Finally, the court held that the Act subjected the Internet to inconsistent regulations.[81] It analogized the Internet to other types of commerce that demanded consistent treatment and were only "susceptible to regulation on a national level."[82] The court considered Internet regulatory efforts emerging in Oklahoma and Georgia and predicted that local regulations "will leave users lost in a welter of inconsistent laws, imposed by different states with different priorities."[83]

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74. *Id.* at 177.

75. *Id.*

76. The unchallenged parts of the statute criminalize the sale of obscene materials to children (including over the Internet) and prohibit adults from luring children into sexual contact via Internet communication. *Pataki*, 969 F. Supp. at 179.

77. *Pataki*, 969 F. Supp. at 179. The court noted the practical difficulties of obtaining criminal jurisdiction over out-of-state defendants whose only contact with New York was over the Internet. *Id.* at 178.

78. *Id.* at 179.

79. *Id.*

80. *Id.* at 180.

81. *Id.*

82. *Id.* This is a similar argument to that used in the transportation cases. *See supra* notes 15-23 and accompanying text.

83. *Pataki*, 969 F. Supp. at 182.

B. Spam Regulations: State v. Heckel

1. *Background: Spam and the Internet*

"Spam" is an unsolicited e-mail message,[84] most commonly defined as unsolicited commercial e-mail (UCE) or unsolicited bulk e-mail (UBE).[85] Spam distribution is widely condemned as a practice to be regulated or eradicated.[86] Both Internet Service Providers (ISPs)[87] and recipients[88] bear spam's high and "widespread" cost.[89] Various measures have been advocated and/or implemented to counteract spam, including self-regulation,[90] technical approaches,[91] litigation,[92] and state or federal legislation.[93] As of

84. Credence E. Fogo, *The Postman Always Rings 4,000 Times: New Approaches to Curb Spam*, 18 J. MARSHALL J. COMPUTER & INFO. L. 915, 915 (2000). The term "spam" was originally derived from a Monty Python skit. *Id.* at 918 n.13.

85. These terms highlight important aspects of spam. For an e-mail to be "unsolicited," no prior relationship can exist between the sender and recipient, and the recipient cannot have explicitly consented to the communication. David E. Sorkin, *Technical and Legal Approaches to Unsolicited Electronic Mail*, 35 U.S.F. L. REV. 325, 329 (2001). "Commercial" refers to the content of the e-mail, which usually promotes the sale of goods or services, rather than the actual or presumed motivation of the sender. *Id.* at 329-30. "Bulk" e-mail is a single message sent to a large number of recipients. *Id.* at 330-31 (finding no distinction between one message addressed to a large number of recipients and separate but identical copies of a message sent to a large number of recipients). *See also id.* at 327, 333 (noting difficulties in defining spam due to differing perspectives among Internet users and discussing arguments for defining spam as UCE versus UBE).

86. It is estimated that three to thirty percent of e-mail messages are spam. Sorkin, *supra* note 85, at 336 n.48. Spam has been criticized as a burden on Internet resources, a security threat, and an interference with legitimate business. *Id.* at 336-40. Also, spam may contain sexually explicit content or solicitations for "questionable ventures" that many users find objectionable. *Id.* at 336.

87. ISPs bear a large proportion of costs, as spam consumes large amounts of "network bandwidth, memory, [and] storage space," requiring ISPs to have greater hardware capabilities than otherwise necessary. Sorkin, *supra* note 85, at 336. ISP employees spend large amounts of time filtering and blocking spam, fixing server crashes and service outages, and resolving spam-related consumer complaints; consequently consumers pay more for Internet access. Fogo, *supra* note 84, at 919; Sorkin, *supra* note 85, at 336-37.

88. Fogo, *supra* note 84, at 919 (noting decreased productivity as recipients are forced to skim and delete spam).

89. *Id.*

90. Sorkin, *supra* note 85, at 342-43, 350-56 (describing imposition of social norms and community self-regulation on the Internet, including hiding and retaliation); Sabra-Anne Kelin, Note, *State Regulation of Unsolicited Commercial E-mail*, 16 BERKELEY TECH. L.J. 435, 438 (2001).

91. Technical approaches have largely proved ineffective, as spammers have succeeded in adapting their techniques to evade anti-spam technology. Sorkin, *supra* note 85, at 356; Scot M. Graydon, *Much Ado About Spam: Unsolicited Advertising, The Internet, and You*, 32 ST. MARY'S L.J. 77, 87 (2000) (describing spammers using "guer-

February 2002, nineteen states had enacted anti-spam laws.[94] Some of these laws include opt-out systems, content regulation, and civil and/or criminal penalties.[95]

2. *The Case*

When its Commercial Electronic Mail Act (CEMA)[96] went into effect in 1998, Washington became the first state to regulate spam.[97] CEMA applies to e-mail transmissions initiated from computers located in Washington or sent to an e-mail address that the sender knew was held by a Washington resident.[98] CEMA prohibits using a third-party domain name without permission, falsifying the transmission path, or using a false or misleading subject line.[99] Sending e-mail in violation of CEMA also violates

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rilla tactics" to evade responses). *See also* Sorkin, *supra* note 85, at 346-48 (describing ISP and third-party filtering, blocking, and blacklisting); Graydon, *supra*, at 86-87 (describing filtering programs and canceling accounts).

92. Expensive individualized litigation has been effective for only relatively large entities eradicating "relatively large, highly visible, and persistent spammers." Sorkin, *supra* note 85, at 367. *See* Fogo, *supra* note 84, at 922 (noting that "scattershot private suits by ISPs" using "novel legal theories" have not worked against spammers). *See also* Sorkin, *supra* note 85, at 357-67 (describing private lawsuits by ISPs, destination operators, relay operations, and forgery victims using theories such as trespass to chattels and standard contract/tort); Fogo, *supra* note 84, at 920-22 (discussing private ISP suits); Joseph D'Ambrosio, *Should "Junk" E-mail be Legally Protected?*, 17 SANTA CLARA COMPUTER & HIGH TECH. L.J. 231, 235-37 (2001) (describing ISP lawsuits where ISPs used state common law and novel legal theories to combat spammers).

93. Sorkin, *supra* note 85, at 368-83. Numerous bills have been proposed in Congress, but none have become law. For a good treatment of current federal regulation, see Fogo, *supra* note 84, at 934-40.

94. *See* Spam Laws, *at* http://www.spamlaws.com/state/summary.html (last visited Feb. 6, 2002).

95. Sorkin, *supra* note 85, at 368-379. *See* Max P. Ochoa, Note, *Recent State Laws Regulating Unsolicited Electronic Mail*, 16 SANTA CLARA COMPUTER & HIGH TECH L.J. 459, 464-67 (2000) (discussing examples of state regulations including legitimate e-mail header information, subject line labeling, and opt-out systems allowing users to remove themselves from mailing lists).

96. WASH. REV. CODE ANN. § 19.190 (West 1999 & Supp. 2000).

97. Kelin, *supra* note 90, at 446.

98. WASH. REV. CODE ANN. § 19.190.020(1) (West Supp. 2000). Under CEMA, the sender "knows" that the intended recipient is a Washington resident if the information is available upon request from the registrant of the Internet domain name. WASH. REV. CODE ANN. § 19.190.020(2) (West Supp. 2000).

99. WASH. REV. CODE ANN. §§ 19.190.020(1)(a)-(b) (West Supp. 2000).

Washington's Consumer Protection Act.[100] CEMA provides statutory or actual damages to e-mail recipients or ISPs[101] and immunity to ISPs that block commercial e-mail that they reasonably believe was or will be sent in violation of CEMA.[102]

In 1997, Jason Heckel, an Oregon resident doing business as Natural Instincts, developed a forty-six page online booklet entitled "How to Profit from the Internet."[103] In it, he described how to set up an online promotional business, acquire free e-mail accounts, and obtain software for sending bulk e-mail.[104] Beginning in June 1998, Heckel used the methods described in his own pamphlet and began marketing the booklet by sending between 100,000 and 1,000,000 unsolicited e-mail messages per week.[105] Heckel used the Extractor Pro software program to "harvest" e-mail addresses from various online message boards and send bulk mail messages using only simple commands.[106] Heckel's e-mail text was a long sales pitch including testimonials from satisfied purchasers and an order form that the user could download, print, and mail (along with $39.95) to Heckel's Salem, Oregon mailing address.[107] Heckel sold thirty to fifty pamphlets per month using these marketing methods.[108]

In June 1998, the Washington State Attorney General's Office, Consumer Protection Division began receiving complaints from Washington residents who had received Heckel's e-mail.[109] The complaints alleged that his "messages contained misleading subject lines and falsified transmission paths."[110] The Division sent Heckel a letter advising him of CEMA.[111] In response, Heckel called the Division and discussed procedures that bulk e-mailers could follow to avoid e-mailing Washington

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100. WASH. REV. CODE ANN. § 19.190.030 (West Supp. 2000); State v. Heckel, 24 P.3d 404, 407 (Wash. 2001) ("RCW 19.190.030 makes a violation of [CEMA] a per se violation of the Consumer Protection Act, chapter 19.86 RCW").

101. WASH. REV. CODE ANN. § 19.190.040 (West 1999).

102. WASH. REV. CODE ANN. § 19.190.050 (West 1999).

103. *Heckel*, 24 P.3d at 406.

104. *Id.*

105. *Id.*

106. *Id.* The Extractor Pro software required the user to enter only a return e-mail address, subject line, and message text. *Id.*

107. *Id.*

108. *Id.*

109. *Id.*

110. *Id.*

111. *Id.* at 407.

residents.[112] Nonetheless, the Division continued to receive complaints that Heckel was violating CEMA.[113]

The State of Washington filed suit against Heckel, alleging that his transmission of e-mail to Washington residents violated CEMA.[114] In particular, the State alleged three causes of action: (1) violation of CEMA by using false or misleading subject lines;[115] (2) violation of CEMA by misrepresenting e-mail transmission paths;[116] and (3) commission of a deceptive trade practice by failing to provide a valid e-mail address to which recipients could respond.[117] The State sought a permanent injunction, civil penalties, costs, and attorney's fees.[118]

On cross-motions for summary judgment, the lower court dismissed the suit against Heckel, concluding in a brief opinion "that the statute in question here violates the Federal Interstate Commerce clause" and that it "is unduly restrictive and burdensome."[119] Challenging the trial court's finding, the State sought direct appeal and Heckel cross-appealed seeking reversal of the trial court's denial of his motion for attorney fees.[120] The Washington Supreme Court granted direct review. It held that CEMA did not "unduly burden interstate commerce" and reversed and remanded the matter for trial.[121]

3. *Washington Supreme Court Decision*

The single issue confronting the Washington Supreme Court was whether CEMA's limitations on bulk e-mailing activities violated the dormant Commerce Clause and unconstitutionally burdened interstate

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112. *Id.*

113. *Id.* In total, the Division documented twenty complaints from seventeen recipients. *Id.*

114. *Id.* at 405.

115. *Id.* at 407; WASH. REV. CODE ANN. § 19.190.020(1)(b) (West Supp. 2000). The two misleading subject lines used were, "Did I get the right e-mail address?" and "For your review—HANDS OFF!" *Heckel*, 24 P.3d at 407.

116. *Heckel*, 24 P.3d at 407; WASH. REV. CODE ANN. § 19.190.020(1)(a) (West Supp. 2000). Nine of the messages generating complaints used the domain name "13.com" as the originating ISP. However, 13.com had been registered to another user since November 1995 and was inactive at the time of Heckel's bulk e-mail advertising campaign. Thus, no messages could have been sent through 13.com. *Heckel*, 24 P.3d at 407.

117. *Heckel*, 24 P.3d at 407; WASH. REV. CODE ANN. § 19.86.020 (West 1999).

118. *Heckel*, 24 P.3d at 408.

119. State v. Heckel, 2000 WL 979720, at *1 (Wash. Super. Ct. 2000).

120. *Heckel*, 24 P.3d at 408.

121. *Id.* at 406.

commerce.[122] The court began by noting that when states enact laws that unduly burden interstate commerce, they "impermissibly intrude" on the federal government's regulatory powers.[123] The court then used a two-step test to analyze CEMA under the dormant Commerce Clause.[124] First, they determined whether CEMA "openly discriminate[d] against interstate commerce in favor of intrastate economic interests."[125] Based on CEMA's statutory language,[126] the court concluded that CEMA applied evenhandedly to in-state and out-of-state spammers and thus was not facially discriminatory.[127]

Second, the court applied the *Pike* balancing test.[128] The court was concerned about the costs of spam and who bore them[129] and looked favorably on measures that would reduce the volume of deceptive spam while making it easier to identify and delete.[130] It first noted that CEMA protected the interests of ISPs, owners of forged domain names, and e-mail users.[131] The court then discussed the actual costs spam imposed on these parties, including increased hardware and consumer service costs to ISPs.[132] When "e-mail recipients cannot promptly and effectively respond to the message (and thereby opt out of future mailings)," their efforts "cost time" and hamper their ability to use computer time most efficiently.[133] The court analogized distributing spam to sending junk mail with postage due or making telemarketing calls to a pay-per-minute cellular phone.[134]

The court found that the only burden placed on spammers was a requirement of truthfulness and that this requirement did not burden commerce but actually facilitated it "by eliminating fraud and deception."[135] The court disagreed with the trial court's emphasis on the burden of noncompliance with the Washington Act, finding that it was contrary to the

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122. *Id.* at 408. The court reviewed the trial court's summary judgment de novo, viewing all facts in the light most favorable to the State. *Id.*

123. *Id.* at 409.

124. *Id. See supra* Part I.

125. *Heckel*, 24 P.3d at 409.

126. WASH. REV. CODE § 19.190.020 (West Supp. 2000).

127. *Heckel*, 24 P.3d at 409.

128. *Id. See supra* note 12 and accompanying text.

129. *Heckel*, 24 P.3d at 410.

130. *Id.* at 411.

131. *Id.* at 409.

132. *Id.* at 409-10. Additionally, it cited instances where owners whose domain names had been forged in spam headers had had their computers shut down by large numbers of e-mail responses. *Id.* at 410.

133. *Id.*

134. *Id.*

135. *Id.* at 411 (internal quotes omitted).

Pike test's focus on compliance.[136] Thus, that a deceptive spammer is required to filter out Washington recipients to evade CEMA is not a burden to be considered.[137]

The court also dismissed Heckel's extraterritoriality arguments that CEMA could create inconsistency among states or regulate commerce occurring wholly outside of Washington.[138] It stated that the imposition of "additional, but not irreconcilable obligations" did not violate the dormant Commerce Clause.[139] The court reasoned that since CEMA requires that illegal bulk messages be read by a Washington resident or initiated from a Washington computer,[140] the statute did not extend to e-mail merely routed through Washington computers that did not otherwise meet these conditions.[141]

The court then declared that CEMA survived the *Pike* balancing test because its "local benefits surpass[ed] any alleged burden on interstate commerce."[142] On these grounds, the court reversed the trial court, vacated the order relating to attorney fees, and remanded the matter for trial.[143] On appeal, the United States Supreme Court denied certiorari without comment.[144]

III. DORMANT COMMERCE CLAUSE ANALYSIS

Following *Pataki*, the extent to which the dormant Commerce Clause preempted state-level Internet regulations was unclear. Some commentators noted the danger of courts blindly relying on *Pataki*—they will perceive every Internet regulation as extraterritorial and aggressively strike down worthwhile state regulations that place only minor burdens on outsiders.[145] The *Heckel* decision demonstrated that states can use their police powers in limited circumstances to regulate the Internet without violating

136. *Id.*
137. *Id.*
138. *Id.* at 412.
139. *Id.*
140. *Id.* at 413.
141. *Id.* at 412-13.
142. *Id.* at 409.
143. *Id.* at 413.
144. Heckel v. Washington, 122 S. Ct. 467 (2001) (mem.). For news coverage of the Supreme Court decision, *see* Carl S. Kaplan, *Ruling Sets Stage for E-mail Trial*, NEW YORK TIMES ON THE WEB, Nov. 2, 2001, *at* http://www.nytimes.com/2001/11/02/technology/02CYBERLAW.html; Katherine Pfleger, *High Court Won't Hear Espam Case*, LA TIMES, Oct. 29, 2001, *at* http://www.latimes.com/technology/wire/sns-ap-scotus-spam1029oct29.story.
145. *See, e.g.*, Farber, *supra* note 2, at 818.

the dormant Commerce Clause. On closer inspection *Pataki* and *Heckel* were both appropriately decided, their different holdings a result of different underlying statutory and geographic concerns. This section analyzes the tensions and synergies between the two cases and finds that the broad reasoning of *Pataki*, although purporting to cover a wide range of state Internet regulations, is not appropriate for narrowly-tailored regulations such as that at issue in *Heckel*. At the same time, these decisions demonstrate that the dormant Commerce Clause likely prohibits extraterritorial state Internet regulations that impose affirmative requirements on Internet communications.

A. The Impact of Different Statutes

The first part of the dormant Commerce Clause analysis asks whether the statute facially discriminates against interstate commerce.[146] The *Heckel* and *Pataki* courts decided that the statutes at issue did not facially discriminate against nonresidents. *Heckel* concluded that CEMA was not facially discriminatory because it applied evenhandedly to spammers inside and outside the state.[147] Although *Pataki* did not explicitly address this issue, in proceeding directly to the *Pike* balancing test[148] it presumably did not find facial invalidity.

If the statutes are not facially invalid, courts next apply the *Pike* balancing test.[149] Here, the *Heckel* and *Pataki* courts reached different outcomes; this was due to the characteristics of the different statutes at issue rather than inconsistent reasoning between the courts. On the local benefits side, both state regulations attempted to further important state interests, namely protecting children from pedophilia in *Pataki*[150] and reducing the high costs of fraudulent e-mail in *Heckel*.[151] The child-protection statute struck down in *Pataki* furthered a state interest at least as important as that in *Heckel*. Thus, *Pataki* illustrated that the existence of a strong state interest is not determinative. *Pataki* was consistent with previous cases in

146. *See supra* note 9 and accompanying text.

147. *Heckel*, 24 P.3d at 409 ("'*No person*' may transmit the proscribed commercial e-mail messages 'from a computer located in Washington or to an electronic mail address that the sender knows, or has reason to know, is held by a Washington resident.'") (quoting WASH. REV. CODE ANN. § 19.190.020(1) (West Supp. 2000)).

148. *See* Am. Libraries Ass'n v. Pataki, 969 F. Supp. 160, 177 (S.D.N.Y. 1997).

149. *See supra* notes 11-14 and accompanying text.

150. *See supra* note 75 and accompanying text.

151. *See supra* notes 129-134 and accompanying text.

holding that an important state interest will not ultimately prevail if the regulation severely burdens interstate commerce.[152]

Two other factors influenced the *Pike* test burdens: the types of communications regulated by the statute and the ease of compliance. *Heckel* regulated a smaller set of Internet communications than *Pataki*, and thus imposed a lesser burden on interstate commerce. CEMA was limited to regulating "commercial electronic mail messages," while the New York statute regulated communications transmitted over "any computer communication system."[153] The *Pataki* court was explicitly concerned that the New York statute could stifle a broad range of Internet communications.[154] By contrast, CEMA regulated only a subset of one type of Internet communications: fraudulent commercial e-mail.[155] Thus, the burden on interstate communications imposed by CEMA was less than that imposed by the New York law and was thus more likely to pass the *Pike* test.

A second difference is that it is likely easier for parties to comply with CEMA than the New York statute. A commercial e-mail will comply with CEMA if it does not use a third-party domain name without permission, misrepresent the transmission path, or contain misleading information in the subject line.[156] With the possible exception of the domain name requirement,[157] it is more difficult for parties to defy CEMA's requirements than to obey them: some level of deceptive intent is implicated in such efforts. For example, special software or technical sophistication is needed to falsify e-mail transmission paths. By contrast, parties wishing to shield themselves from liability under the New York statute must affirmatively conform to one of the enumerated defenses.[158] Such adherence could require substantial financial and technological investments to verify ages, restrict access, or segregate material to facilitate content filtering.[159]

152. *See supra* notes 11-14 and accompanying text.

153. *Compare* WASH. REV. CODE ANN. § 19.190.020(1)(a) (West Supp. 2000) *with* N.Y. PENAL LAW § 235.21(3) (McKinney 1999).

154. *See supra* Part II.A.3.

155. *See supra* notes 98-99 and accompanying text.

156. *See supra* note 99 and accompanying text.

157. For example, accidental violation of CEMA may occur if a sender unwittingly includes a legitimate return e-mail address including a third-party ISP domain name (e.g., sender@aol.com) without the ISP's permission or in violation of a user agreement.

158. *See supra* note 56 and accompanying text.

159. *Id.*

B. Geographic Concerns

As specialized applications of the *Pike* balancing test, the transportation and extraterritoriality cases are particularly concerned with the geographic impact of state regulations. In particular, the transportation cases prohibit state regulations that could collectively result in the imposition of inconsistent standards.[160] Extraterritoriality jurisprudence prohibits states from overreaching their geographic boundaries and regulating transactions occurring wholly outside their borders and directs courts to consider the practical effects of other states adopting conflicting regulations.[161] Geographic concerns were key elements in the *Heckel* and *Pataki* balancing analyses. In both cases, but particularly *Pataki*, the geographic scope was correlated with the size of the burden on interstate commerce. This section will focus on the imposition of potentially inconsistent regulations and affirmative requirements and discuss the impact of geographic concerns on the burdens imposed by state statutes.

1. Regulating Commerce Outside State Borders

Many commentators have agreed with the *Pataki* court that local Internet regulations are bound to produce extraterritorial effects.[162] Based on the opposite outcomes in *Heckel* and *Pataki*, this presumption should be reevaluated in light of particular statutory characteristics. Statutes with meaningful geographic restrictions are less likely to implicate extraterritorial concerns. The New York statute had no explicit geographic restrictions on what types of Internet communications were subject to regulation.[163] Other states, like California, regulate communications delivered to state residents via equipment physically located in that state.[164] By contrast, CEMA expressly limited its applicability to commercial e-mail sent "from a computer located in Washington or to an electronic mail address that the sender knows, or has reason to know, is held by a Washington

160. *See supra* notes 16-23 and accompanying text.

161. *See supra* notes 24-25 and accompanying text.

162. *See, e.g.*, Christopher S.W. Blake, Note, *Destination Unknown: Does the Internet's Lack of Physical Situs Preclude State and Federal Attempts to Regulate It?*, 46 CLEV. ST. L. REV. 129, 141-42 (1998) ("Because Internet users generally cannot prevent their communications or content from being accessed by a geographical section of the country, any state law that regulates Internet content or communications within a state runs the risk of having an extraterritorial effect on Internet sites outside that area."); Gaylord, *supra* note 7, at 1096 (noting that, because "cyberspace is a profoundly integrative . . . force," local legislation "is likely to produce effects beyond local borders").

163. *See* N.Y. PENAL LAW § 235.21(3) (McKinney 1999).

164. CAL. BUS. & PROF. CODE § 17538.4(d) (West Supp. 2001).

resident."[165] The *Heckel* court's interpretation of CEMA reinforced the statute's narrow geographic reach.[166] The Court concluded that there was no liability for data merely routed through Washington servers.[167] Likewise, it disregarded extraterritoriality arguments that liability could be imposed on out-of-state residents for sending spam ultimately read by Washington residents outside state borders.[168]

Statutes with meaningful geographic limitations, such as CEMA, are less susceptible to arguments that they could regulate Internet communications occurring wholly outside their respective borders. CEMA's explicit requirements that the communication originate or be received in Washington forecloses most extraterritorial arguments. The New York and California laws have not effectively addressed extraterritorial concerns. For example, data packets routed through or stored in equipment physically located in a state could potentially expose the sender to liability under a geographically unrestricted statute. If the equipment is merely a conduit for communications between a sender and recipient located in third-party states, such a statute raises troubling extraterritorial issues and may violate the dormant Commerce Clause.

2. *Inconsistent Regulations and Affirmative Requirements*

Another geographical concern is the danger of competing state Internet regulatory regimes imposing inconsistent standards and conflicting affirmative requirements on Internet communications. Addressing these requirements is key to evaluating the burdens on interstate commerce. In *Pataki*, the court confronted a broad statute regulating the dissemination of obscene materials via the Internet. As the only geographic limitation was its implicit jurisdictional reach, the New York law could potentially conflict with other states' regulatory regimes. Currently, it is technically difficult to exclude website visitors based on real world geography.[169] Thus, a website operator could be subject to overlapping and potentially conflicting content regulations in all the states from which the website is accessi-

165. WASH. REV. CODE ANN. § 19.190.020(1) (West Supp. 2000).

166. *See supra* notes 140-141 and accompanying text.

167. *Id.*

168. *See supra* notes 138-141 and accompanying text.

169. However, the technology to geographically identify IP addresses is now being developed. Jack L. Goldsmith & Alan O. Sykes, *The Internet and the Dormant Commerce Clause*, 110 YALE L.J. 785, 810-11 (2001). Many websites currently condition entry on payment information (e.g., credit card numbers) that could easily be correlated with geographic data. *Id.* at 809. However, this new technology is expensive and not completely effective, boasting only 80-95% accuracy in identifying IP addresses with states. *Id.* at 811.

ble. In order to insulate themselves against liability under the New York statute, defendants would need to comply with one of the statutory affirmative defenses,[170] which are likewise not guaranteed to be consistent with the defenses of other states. *Pataki* noted the danger of such inconsistent standards and weighed it heavily in the burden on interstate commerce.[171]

CEMA was well-crafted to avoid concerns of inconsistent standards and conflicting requirements. The statute imposed no affirmative requirements, such as subject line labeling.[172] Under the guise of consumer protection, the regulations only prohibited falsified transmission paths and misleading subject lines,[173] requirements that are unlikely to conflict with other states' Internet regulatory programs. Thus, the simultaneous transmission of nonfraudulent e-mail to Washington and other states would not likely cause conflicts between CEMA and other state consumer protection statutes.

As discussed in *Pataki*, numerous states regulating obscene Internet communications could make compliance with all regulations very burdensome or even impossible, thus chilling out-of-state behavior.[174] Due to current technological limitations which make it difficult and expensive to identify website visitors' geographic location, it would be burdensome to exclude residents of particular states in order to avoid those states' content regulations.[175] If states imposed affirmative requirements on all Internet communications accessible within their state borders, to avoid potential liability Internet content providers would be forced to comply with a superset of all state regulations or withdraw the regulated communications.

A similar conflict of affirmative requirements has arisen in state regulation of unsolicited commercial e-mail. Some state regulations now require subject line prefixes labeling e-mail advertisements as such[176] or demand certain content in the body of an e-mail message, such as opt-out instructions.[177] It is just as difficult to correlate geography with e-mail ad-

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170. *See supra* note 56 and accompanying text.

171. *See supra* notes 81-83 and accompanying text.

172. *See infra* notes 176-177.

173. *See supra* note 99 and accompanying text.

174. *See supra* notes 81-83 and accompanying text.

175. *See supra* note 169 and accompanying text.

176. *See, e.g.*, CAL. BUS. & PROF. CODE § 17538.4(g) (West Supp. 2001) (requiring advertising material to have the subject line prefix "ADV: " and advertising material for goods and services suitable for those over age 18 to be labeled with the subject line prefix "ADV: ADLT").

177. *See, e.g.*, CAL. BUS. & PROF. CODE § 17538.4(b) (West Supp. 2001) (requiring an unsolicited e-mail to include a statement providing a toll-free telephone number or

dresses and thus screen potential recipients of unsolicited commercial e-mail as it is to exclude website visitors based on residency. When states impose affirmative requirements on commercial e-mail, senders are in the same difficult position as website operators, forced to comply with a superset of all state regulations or not send e-mail altogether. CEMA's proposed methods of compliance, checking mailing lists against a limited access Washington e-mail registry[178] or requesting assistance from individual ISPs, would be heavy burdens under the *Pike* test. Thus, measures that go beyond Washington's limited regulation of falsified e-mail to impose affirmative requirements are in serious danger of conflicting with other states' regulatory programs. This would impose substantial burdens on Internet communications and would likely render the law unconstitutional under the dormant Commerce Clause. Due to this danger of conflict, affirmative requirements are perhaps better handled via federal regulation imposing uniform national standards.

IV. CONCLUSION

Heckel demonstrates that *Pataki*'s broad reasoning that state Internet regulations are preempted by the dormant Commerce Clause is not applicable to all types of regulation. Together, *Heckel* and *Pataki* show that state statutes based on important state interests, limited in geographic coverage, and not imposing inconsistent affirmative requirements have a good chance of surviving a dormant Commerce Clause analysis. However, the dormant Commerce Clause's geographic sensitivity imposes a significant limitation on the reach of state Internet regulations. Statutes that impose affirmative requirements on Internet communications raise significant extraterritorial concerns and should be promulgated by Congress to assure consistent standards.

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valid return address notifying the sender not to e-mail any further unsolicited documents); IOWA CODE ANN. § 714E.1(2)(d) (West Supp. 2001) (requiring an unsolicited e-mail advertisement to provide, "at a minimum," a readily-identifiable e-mail address where the recipient may send a message declining such e-mail).

178. Washington Association of Internet Service Providers, WAISP Registry Page, *at* http://registry.waisp.org (last visited Feb. 6, 2002).

COMMUNICATIONS DECENCY ACT § 230

By Paul Ehrlich

The Internet presents a unique set of problems for regulating harmful speech. Unlike traditional media, the typical arrangement of content distribution involves multiple users "logged in" to one of many servers run by an Internet Service Provider ("ISP"), or a website run by a similar entity. These users interact with one another with little or no supervision by the ISP itself. Interactions can take the form of bulletin board postings, e-mails, business transactions, and chat room discussions, to name a few.

While one would not expect harmful speech to confine itself to traditional media, certain characteristics of the Internet guarantee the prevalence of such speech in cyberspace. These features include ease of access, ability of any individual to publish, and relative anonymity. Whenever harmful speech does occur, it necessarily involves use of an ISP's servers and possibly another's website. Thus, a central question in regulating content on the Internet is the extent to which ISPs and other interactive computer services should be held liable for the torts and crimes of the individuals who use their servers.

Congress passed the Communications Decency Act ("CDA")[1] in 1996 to address the myriad problems surrounding the regulation of obscene, illegal, or otherwise tortious content found on the Internet. Many of the CDA's provisions regulating decency have been struck down by the courts as violations of the First Amendment.[2] One of the surviving elements is a congressional grant of immunity from suit to ISPs and other interactive computer services for content originating with third parties.[3]

The text of the statute relies on terms of art from the law of defamation, formally protecting interactive computer services from treatment as "publisher[s] or speaker[s]."[4] However, while defamation law recognizes a distinction between liability as a publisher and liability as a distributor,[5]

1. 47 U.S.C. § 223 (Supp. 2001).
2. *See* Reno v. ACLU, 521 U.S. 844 (1996) (holding portions of the CDA unconstitutional for its overbroad limitations on protected speech).
3. 47 U.S.C. § 230 (Supp. 2001).
4. *Id.* § 230(c)(1).
5. Publishers are presumed to have more control over material disseminated and are therefore subject to strict liability. Distributors are subject to liability under a knowl-

courts have unanimously read Section 230(c)'s grant of ISP immunity as covering both publishing and distribution liabilities.[6] In doing so, courts took Congress' desired balance between the competing interests of decency and efficiency and tipped the scales decisively towards efficiency.

The effect of these rulings has been the emergence of a comprehensive immunity from suit for ISPs so long as the suits are based on content not authored by the ISP. Whether or not Congress intended this result, ISPs and other interactive computer services have used Section 230 as a complete defense against recent suits brought by parents upset by child pornography marketed in ISP chat rooms,[7] copyright owners against eBay for facilitating sales of infringing recordings,[8] and taxpayers protesting the accessibility of pornography on public library computer terminals.[9]

After surveying the most recent of these Section 230 decisions, this Note will argue that the blanket immunity created by the courts is better than a regime of distributor liability for obscene speech, but may not be enough to combat defamatory speech. Combining immunity with a remedy that allows plaintiffs to reach the actual publisher of the defamation will best restore the balance Congress attempted to create.

I. THE PRE-CDA LANDSCAPE

Historically, the problem of harmful speech on the Internet inspired ISPs and others to limit its ill effects. For example, when a user signs a contract for Internet service, a "Terms of Service" agreement is typically included, reserving to the ISP the right to edit or remove postings that violate certain speech codes.[10] When users participate in fora like bulletin boards or chat rooms, an ISP-employed monitor can review user posts before or after they are made public. Also, the ISP can typically install a general filtering program that screens web pages for obscene words and

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edge or negligence standard. A brief discussion of the defamation categories appears in Part I.

6. *See, e.g.,* Zeran v. Am. Online, Inc., 129 F.3d 327 (4th Cir. 1997).

7. *See* Doe v. Am. Online, Inc., 783 So. 2d 1010 (Fla. S. Ct. 2001).

8. *See* Stoner v. Ebay, No. 305666, 2000 Extra LEXIS 156 (Cal. Super. Ct. Nov. 7, 2000).

9. *See* Kathleen R. v. City of Livermore, 87 Cal. App. 4th 684 (Cal. Ct. App. 2001).

10. The AOL Terms of Service Agreement in force circa *Zeran* gave AOL the right to remove posts and had a hold-harmless clause for their good faith efforts at editing. *See* David R. Sheridan, *Zeran v. AOL and the Effect of Section 230 of the Communications Decency Act Upon Liability for Defamation on the Internet*, 61 ALB. L. REV. 147, 176 (1997).

phrases to keep them from the eyes of its users. In addition to centralized censoring, users have the option of installing screening programs on their own consoles.[11] Such filtering software is relatively effective, if not overzealous, at keeping obscenity from children.[12] It is not effective, however, at distinguishing defamatory speech from nondefamatory speech, or copyright-infringing content from its genuine counterpart. That responsibility inevitably falls to the bulletin board and chat room operators. The central question is whether this sometimes-nominal amount of control over content exposes the ISP to liability if some defamatory or obscene speech slips through the filter.

Prior to passage of the CDA, courts addressed this problem in the defamation context by placing the ISP in one of the traditional First Amendment categories of publisher, distributor, or common carrier. The law applies very different legal standards to these entities based on their control over the content they disseminate. Publishers, such as newspapers or book publishers, have the opportunity to exercise a great deal of control over the final content, and are therefore subject to a strict liability standard.[13] Distributors, such as booksellers, newsvendors, and libraries, merely distribute content and hence bear liability only upon a showing of knowledge or negligence.[14] Common carriers, such as the telephone companies, transmit information mechanically with no opportunity to review its content. Therefore, common carriers are not liable for the transfer of harmful data.[15]

ISPs do not fit cleanly into any single category, and courts attempting to characterize them have reached very different results. In 1991, a federal district court held in *Cubby v. CompuServe*[16] that an ISP which maintained a database containing an allegedly defamatory document would not be treated as a publisher for liability purposes.[17] Defendant CompuServe archived publications as part of its "Journalism Forum." The plaintiff claimed CompuServe ought to be held liable for republishing a libel con-

11. For a discussion of filtering technologies, see Whitney A. Kaiser, *The Use of Internet Filters in Public Schools: Double Click on the Constitution*, 34 COLUM. J.L. & SOC. PROBS. 49, 53-56 (2000) (discussing filters used by schools, though the same principles would apply to domestic uses).

12. *See id.*

13. *See, e.g.*, Cianci v. New Times Publ'g Co., 639 F.2d 54 (2d Cir. 1980).

14. *See, e.g.*, Lerman v. Flynt Distrib. Co., 745 F.2d 123 (2d Cir. 1984).

15. For a brief discussion of common carrier immunity, see Henry H. Perritt, Jr., *Tort Liability, the First Amendment, and Equal Access to Electronic Networks*, 5 HARV. J.L. & TECH. 65, 92-95 (1992).

16. 776 F. Supp. 135 (S.D.N.Y. 1991).

17. *See id.*

tained in one of the publications archived in CompuServe's database.[18] The court refused to find CompuServe a publisher, and instead likened its database service to an online library, with corresponding status as a distributor.[19] The court held CompuServe could only be liable if it knew, or had reason to know, of the defamatory statements.[20] Since the undisputed evidence demonstrated CompuServe had no such knowledge, the case was resolved via summary judgment.[21]

In 1995, however, the New York Supreme Court reached the opposite result in *Stratton Oakmont v. Prodigy Services Co.*[22] In *Stratton*, the plaintiff alleged that a popular Prodigy message board contained libelous statements. In finding Prodigy to be a publisher, the court noted Prodigy's policy of filtering offensive content from its service. The court distinguished the case from *Cubby*, finding that Prodigy held itself out as a family-friendly ISP with policies of monitoring and editing content. Therefore, the court found Prodigy to be a publisher for purposes of defamation.[23] The court reached this conclusion despite evidence that Prodigy had some two million subscribers and could not possibly screen each message manually.[24] Thus, even without knowledge of the defamatory statements, Prodigy would be strictly liable as a publisher.

These cases set up a paradoxical no-win situation: the more an ISP tried to keep obscene or harmful material away from its users, the more it would be liable for that material.[25] In order to avoid *Stratton* publisher liability, ISPs had to take a hands-off approach so they would appear to be mere distributors.[26] If, on the other hand, an ISP chose to create a family-friendly service, thereby opening itself up to publisher liability, it had a strong incentive to overfilter in an attempt to avoid litigation.[27] The post-*Stratton* regime offered ISPs and consumers the unappetizing choice between a lack of decency and a lack of free speech.

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18. *Id.* at 139.
19. *Id.* at 140.
20. *Id.*
21. *See id.*
22. No. 31063194, 1995 N.Y. Misc. LEXIS 229 (N.Y. Sup. Ct. May 24, 1995).
23. *Id.* at *13.
24. *Id.* at *8.
25. *See* Sheridan, *supra* note 10, at 158.
26. *Id.*
27. *Id.*

II. CONGRESS OVERTURNS STRATTON OAKMONT

In 1996, Congress stepped in by passing Section 230 of the CDA. It states, in relevant part:

(c) Protection for "good samaritan" blocking and screening of offensive material.

> (1) Treatment of publisher or speaker: No provider or user of an interactive computer service shall be treated as the publisher or speaker of any information provided by another information content provider.
>
> (2) Civil liability: No provider or user of an interactive computer service shall be held liable on account of—
>
> (A) Any action voluntarily taken in good faith to restrict access to or availability of material that the provider or user considers to be obscene, lewd, lascivious, filthy, excessively violent, harassing, or otherwise objectionable, whether or not such material is constitutionally protected; or
>
> (B) Any action taken to enable or make available to information content providers or others the technical means to restrict access to material described in paragraph (1).[28]

Section (c)(1) is clearly an attempt to settle the confusion about assigning defamation liability to ISPs, specifically overturning the result in *Stratton*.[29] Section (c)(2) seems directed only at promoting the use of filtering technology and editing. It was this type of "Good Samaritan" editing that opened Prodigy up to liability in 1995. Congress may also have been concerned about lawsuits from those who had their posts edited in good faith.[30]

On a broader scale, Congress acted with the twin goals of "remov[ing] disincentives for the development and utilization of blocking and filtering

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28. 47 U.S.C. § 230(c) (Supp. 2001). "Information content provider" is defined as "any person or entity that is responsible, in whole or in part, for the creation or development of information provided through the Internet or any other interactive computer service." 47 U.S.C. § 230(f)(3) (Supp. 2001).

29. *See* S. CONF. REP. NO. 104-230, at 435 (1996) ("One of the specific purposes of this section is to overrule *Stratton Oakmont v. Prodigy* and any other similar decisions which have treated such providers and users as publishers or speakers of content that is not their own . . . .").

30. *See* Zeran v. Am. Online, Inc., 129 F.3d 327, 337 n.22 (4th Cir. 1997).

technologies,"[31] and "preserv[ing] the vibrant and competitive free market that presently exists for the Internet."[32]

III. THE COURTS INTERPRET THE CDA

While Congress tried to strike a balance between promoting decency and promoting free speech, recent court decisions interpreting Section 230 have emphatically tilted the scales in favor of free speech by removing distributor liability from ISPs entirely.

A. *Zeran* Creates Full Immunity for Interactive Computer Services

Shortly after passage of the CDA, the Court of Appeals for the Fourth Circuit handed down what has become the most influential interpretation of Section 230(c). In *Zeran v. America Online, Inc.*,[33] the court held that Section 230 constituted a complete bar to plaintiff's claims that AOL should be held liable as a distributor of defamatory statements made against the plaintiff on AOL's bulletin boards.[34]

Plaintiff Kenneth Zeran had been the target of a malicious campaign that had advertised his home phone number in connection with advertisement of tasteless t-shirts making light of the Oklahoma City bombing.[35] Zeran suffered days of threatening phone calls as a result.[36] He contacted AOL, and the message was eventually removed.[37] However, similar messages continued to reappear.[38] He again contacted AOL, and they assured him they were working to remove the posts and prevent further posts.[39] The messages continued for a week.[40] When an Oklahoma radio station picked up the story, Zeran's situation only got worse.[41] He eventually sued AOL alleging negligence in their inadequate response to his requests.[42]

Unlike the plaintiffs in *Cubby* and *Stratton*, Zeran was able to plead knowledge on the part of AOL. He argued that Section 230 only prohib-

31. 47 U.S.C. § 230(b)(4) (Supp. 2001).
32. *Id.* § 230(b)(2).
33. 129 F.3d 327 (4th Cir. 1997).
34. *Id.*
35. *Id.* at 329.
36. *Id.*
37. *Id.*
38. *Id.*
39. *Id.*
40. *Id.*
41. *Id.*
42. *Id.*

ited treatment as a publisher, and that he could therefore proceed against AOL under a distributor liability theory. The district court and Fourth Circuit Court of Appeals both ruled that distributor liability is a subset of publisher liability. As a result, Congress' prohibition on treating ISPs as publishers likewise foreclosed a finding of distributor liability.[43] In so holding, the courts concluded that even if AOL were to have notice of the defamatory activity, it would have no duty to remove the content.[44]

B. Recent Cases Follow the *Zeran* Analysis

Courts in recent cases have adopted the reasoning behind *Zeran* in contexts other than defamation. The Florida State Supreme Court held in *Doe v. America Online, Inc.*[45] that a mother's claims related to the advertising of child pornography videos involving her minor son were barred by Section 230(c).[46] While the defendant pornographer was convicted for his role in advertising the illegal videos in AOL chat rooms,[47] the court, following *Zeran*, ruled that AOL was immune from even distributor liability under the CDA.[48] All state criminal and civil law claims under such a distributor negligence theory are explicitly preempted by the CDA.[49]

In an unpublished opinion, the California Superior Court applied *Zeran* to the selling of copyright infringing sound recordings on eBay, a popular auction website. In *Stoner v. Ebay*,[50] plaintiff copyright owners brought claims against eBay for criminal sale of infringing sound recordings.[51] In addition, plaintiffs noted that eBay had knowledge that illegal sales occur, had the means to stop them, did not stop them, and in fact took a commission on these sales.[52]

Under the *Stoner* test, immunity would attach where: (1) the defendant is an interactive computer service; (2) the defendant is not an information content provider with respect to the disputed materials; and (3) the plaintiff must be trying to hold defendant liable for material originating with third parties.[53] The court found that eBay met these three criteria.[54]

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43. *Id.*
44. *Id.*
45. 783 So. 2d 1010 (Fla. S. Ct. 2001).
46. *Id.*
47. *Id.* at 1012 n.3.
48. *Id.* at 1017.
49. *See id.*
50. No. 305666, 2000 Extra LEXIS 156 (Cal. Super. Ct. Nov. 7, 2000).
51. *Id.* at *2.
52. *Id.*
53. *Id.* at *3-4.
54. *Id.*

Specifically, the court held that charging a fee for its service, combined with the knowledge of infringing sales, did not pull eBay out from under the aegis of federal immunity.[55]

CDA immunity has also been extended to protect a public library from a taxpayer suit brought to enjoin unfiltered Internet access for children at library terminals. In *Kathleen R. v. City of Livermore*,[56] the California Appellate Court found the library — specifically contemplated by Congress as an interactive computer service[57] — immune from all claims relating to obscene material originating on the Internet, including those of taxpayers.[58] While the court found that the library could not direct children to offensive material, it had no duty to filter offensive content.[59] In fact, where libraries have used filtering technology, they have been sued for violating the First Amendment.[60]

These recent cases demonstrate that courts interpreting § 230(c) of the CDA have erred on the side of broader immunity for providers of computer services as they grapple with the competing goals of Congress: promoting decency and the "vibrant and competitive free market"[61] of the Internet.

IV. DISCUSSION

The recent court decisions stripping liability from the CDA probably run counter to the intent of Congress. However, in evaluating whether the congressional method of liability or the court-enforced regime of immunity is better suited to deal with harmful speech on the Internet, this Note will argue that harmful speech can be separated into distinct categories that require different treatment. While immunity is a good solution to the problem of obscenity generally, the problem of defamation can only be solved either through a return to distributor liability (costly to free speech) or, more preferably, the weakening of anonymity for defamatory posters.

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55. *Id.* at *5-6.
56. 87 Cal. App. 4th 684 (Cal. Ct. App. 2001).
57. *Id.* at 692 (citing 47 U.S.C. § 230(f)(2)).
58. *Id.*
59. *Id.*
60. *See* Mainstream Loudoun v. Bd. of Trustees of Loudoun County Library, 24 F. Supp. 2d 552 (E.D. Va. 1998).
61. 47 U.S.C. § 230(b)(2) (Supp. 2001).

A. Full Immunity Is Not the Solution Congress Intended

Based on the legislative record, it appears that Congress never contemplated completely shielding ISPs from liability.[62] First, the plain text of the immunity provision does not expressly preclude distributor liability. Second, the legislative history of the CDA and the law's responsiveness to the split between *Cubby* and *Stratton* suggest that Congress intended ISPs to bear some liability for the acts of their users.

1. The Text Supports the Survival of Distributor Liability

The plain text of Section 230(c)(1) forbids treatment of interactive computer services as the "publisher or speaker" of content posted by third parties.[63] While Congress could have explicitly barred all claims against interactive computer services for all information originating with third parties, it did not do so. By taking care to specify the terms of art "publisher" and "speaker," the statute can easily be read as respecting the pre-existing defamation categories of publisher and distributor liability.

The court in *Zeran*, however, chose to interpret the term "publisher" as *encompassing* distributor liability.[64] The court cited Section 577 of the Second Restatement of Torts for the proposition that distributor liability is merely a subset of publisher liability.[65] As many have pointed out, however, including the dissent in *Doe v. America Online, Inc.*, the *Zeran* court ignored Section 581(1) of the Restatement, which better addresses the problem at hand.[66] That section states: "One who only delivers or transmits defamatory matter published by a third person is subject to liability if, but only if, he knows or has reason to know of its defamatory character."[67] Clearly the Restatement recognizes a category of distributor liability separate from publisher liability. The *Zeran* court's interpretation, however, ignored this distinction.

The presence of Section 230(c)(2) further lends support to this hypothesis. Section 230(c)(2) fits within the larger goal of the CDA of pro-

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62. Commentators, judicial and otherwise, have argued that Congress never contemplated full immunity. *See, e.g.*, Doe v. Am. Online, Inc., 783 So. 2d 1010, 1028 (Fla. S. Ct. 2001) ("[I]t is inconceivable that Congress intended the CDA to shield from potential liability an ISP alleged to have taken absolutely no actions to curtail illicit activities in furtherance of conduct defined as criminal, despite actual knowledge. . . .") (Lewis, J., dissenting).

63. 47 U.S.C. § 230(c)(1) (Supp. 2001).

64. Zeran v. Am. Online, Inc., 129 F.3d 327, 332-34 (4th Cir. 1997).

65. *Id.* at 332.

66. *See, e.g.*, Doe v. America Online, Inc., 783 So. 2d 1010, 1021-23 (Fla. S. Ct. 2001) (Lewis, J., dissenting) (discussing applicability of Restatement § 581).

67. RESTATEMENT (SECOND) OF TORTS § 581(1) (1977).

moting decency by encouraging action on the part of ISPs. Section 230(c)(2) removes all disincentives for using filtering software, directly immunizing interactive computer services for voluntary acts of filtering or making such technology available.[68] Some, including the *Zeran* court, speculate that this protection is aimed primarily at barring suits from those whose content was filtered.[69] It seems, however, to answer the Catch-22 presented by *Stratton* — penalizing for indecency only those who tried to maintain decency. Therefore, it would seem an incongruent result for Section 230(c)(1) to make 230(c)(2) irrelevant by removing all penalties regardless of filtering attempts or the lack thereof.

2. *An Examination of the Legislative Backdrop Militates Against Full Immunity*

The legislative history behind passage of the CDA also demonstrates that Congress did not want to give full immunity to ISPs. The CDA clearly intended to overturn the result in *Stratton*.[70] That desire, however, did not necessarily extend to overturning the court's separation of distributor and publisher liability, particularly because distributor liability was not even at issue in *Stratton*.[71] In fact, the language of the statute appears to mirror *Stratton*'s exclusive focus on publisher liability.

The two important cases that preceded passage of the CDA both recognized the distributor/publisher distinction. *Cubby* and *Stratton* both distinguished between distributor and publisher liability.[72] The former required knowledge on the part of the defendant while the latter did not. Since neither court was presented with a situation where the defendant had actual knowledge, neither actually found an ISP liable as a distributor. The

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68. 47 U.S.C. § 230(c)(2) (Supp. 2001)

No provider or user of an interactive computer service shall be held liable on account of any action voluntarily taken in good faith to restrict access to or availability of material that the provider or user considers to be obscene, lewd, lascivious, filthy, excessively violent, harassing, or otherwise objectionable, whether or not such material is constitutionally protected, or any action taken to enable or make available to information content providers or others the technical means to restrict access to material described [above].

69. *See* Zeran v. Am. Online, Inc., 129 F.3d 327 (4th Cir. 1997).

70. *See supra* note 29 and accompanying text.

71. *Stratton* had little trouble finding Prodigy to be a publisher, so presumably "overturning" *Stratton* could only mean reversing the result of finding publisher liability, not the question of whether Prodigy could also have been found liable under a distributor theory. Stratton Oakmont v. Prodigy Servs. Co., No. 31063194, 1995 N.Y. Misc. LEXIS 229 (N.Y. Sup. Ct. May 24, 1995).

72. *See* Cubby v. Compuserve, Inc., 776 F.Supp. 135, 139-40 (S.D.N.Y. 1991) (discussing different standards of liability for publishers and distributors); *Stratton*, 1995 N.Y. Misc. LEXIS at *6-7 (discussing difference between publishers and distributors).

court in *Cubby* ruled simply that CompuServe was akin to a library, and thus was not a publisher.[73] Without an allegation of knowledge, CompuServe was not liable. The court in *Stratton* went the other way, ruling Prodigy to be a publisher.[74] Prodigy was thus liable without a showing of knowledge, due to its attempts at editing.[75]

The timing of the CDA is also instructive. *Stratton* was decided a year before the CDA. *Cubby*, however, was decided in 1991, five years prior to the CDA. The acquiescence by Congress to the result in *Cubby* could demonstrate a lack of concern to imposition of distributor liability. Combined with the directed language of Section 230, this legislative silence, broken only by the result in *Stratton*, provides good evidence of the desire to overrule only the imposition of publisher liability on ISPs.

This legislative history implies that Congress tried to take the middle road between full liability, a disincentive to filter, and zero liability, a lack of incentive to filter. Courts, on the other hand, have dismissed this balance and clearly favor the latter. The remainder of this Section will argue that this choice, while contrary to Congress' intent, is actually in the best interest of the public.

B. Full Immunity Better Serves the Public and the Objectives of Congress

Even though Congress was reluctant to choose the extreme result of zero liability, the courts may have come closer to the correct solution. Assessing the correctness of this approach, however, requires an examination of two very different categories of indecent speech. On one side is the diffuse problem of obscene speech, targeted by much of the rest of the CDA. On the other side is the problem of defamation and similar offenses. The two are analytically distinct because with obscenity the harm is spread over a wide range of victims, whereas with defamation the harm is concentrated in one individual. Part III.B.1 will argue that the blanket immunity created by *Zeran* seems a good fit for obscenity because market forces in response to the use of filtering technologies are sufficient to handle the spectrum of personal tastes implicated by obscene speech. Part III.B.2 will argue these market forces are not sufficient to handle the problem of defamation. Instead, it will propose two possible solutions to the defamation question: (1) a return to distributor liability; or (2) retention of *Zeran*

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73. *See Cubby*, 776 F. Supp. at 140 ("CompuServe's CIS product is in essence an electronic, for-profit library . . . .").

74. *See Stratton*, 1995 N.Y. Misc. LEXIS at *13.

75. *See id.* ("It is PRODIGY's own policies . . . which have altered the scenario and mandated the finding that it is a publisher.").

immunity plus a reduction of anonymity for the actual posters of defamatory material. This Note will conclude by arguing that this proposition of "immunity plus" could be a robust solution to Internet defamation while avoiding the significant costs to free speech inherent in distributor liability.

1. *Regulation of Obscenity is Best Left to the Market*

It should first be noted that obscenity in general triggers fewer lawsuits than defamation. This is because the harm from obscene speech is spread over many individuals, and collective action problems prevent much litigation. Nevertheless, cases like *Kathleen R.* would force a response on the part of ISPs in the absence of full immunity. This response would most likely come in the form of filtering software designed to reduce the amount of obscenity placed on the ISP's server. Many believe the removal of liability killed all ISP incentives to filter, thwarting Congress' goal of reducing indecency.[76] Contrary to this belief, full immunity unleashes a powerful motive to reduce indecency — the market itself.

Section 230 should merely be seen as trading a stick for a carrot. Although free from potential suits for indecency, the market will still encourage internet service providers to filter where appropriate. There are several reasons to believe this to be true. First, the bright-line rule of immunity will remove uncertainty and thereby stimulate innovation. Second, the unique characteristics of Internet speech and mobility will quickly guide the market toward equilibrium. The net result will be a general level of filtering consistent with Internet community norms.

First, the elimination of distributor liability removes the last source of uncertainty for ISPs in their attempts to self-regulate. This uncertainty was costly for several reasons. Since litigation is a fickle game, ISPs could not be sure what content would lead to successful claims. Great costs must be incurred up front to prevent litigation. This cost could be borne by the ISPs in the form of costly screening, or by the Internet in the form of suppressed speech. Furthermore, leaving liability to turn on a reasonableness test in the courts imposes a costly uncertainty. As litigation drags on for months, court definitions of reasonable conduct will become stale at Internet speed. Add to this the fact that ISPs will be defending against suits in

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76. *See, e.g.*, Annemarie Pantazis, *Zeran v. America Online, Inc.: Insulating Internet Service Providers from Defamation Liability*, 34 WAKE FOREST L. REV. 531 (1999) (advocating a return to distributor liability); Andrew J. Slitt, *The Anonymous Publisher: Defamation on the Internet After Reno v. American Civil Liberties Union and Zeran v. America Online*, 31 CONN. L. REV. 389, 420 (1998) ("[A] total isolation of ISPs from the realm of defamation law, as Section 230 of the CDA does, is poor policy.").

dozens of different jurisdictions, each with its own common law definitions of distributor liability, and the result is a morass of confusing or even conflicting regulation.[77] ISPs will have no incentive to experiment with their filtering technology. They will merely gravitate toward the lowest common denominator of speech in order to achieve certainty.

A bright-line rule saves ISPs from this downward spiral. Immunity significantly reduces the disincentives of trying newer, possibly cheaper, filtering technologies. A vibrant market in such technologies would spur ISPs to keep pace with innovation without forcing them to look over their shoulders for the courts.

The second reason why obscenity is best regulated by the market is that low costs of information and movement allow the market to reach equilibrium quickly. The low costs of communication on the Internet ensure that consumer voices will be heard. If an ISP institutes a new filtering policy that angers its users, it can expect a flood of e-mails. Furthermore, users can easily switch services, choosing ISPs with filtering policies to suit their tastes. If large, national providers are not sensitive to community tastes, small providers with more or less permissive policies can fill the void. This is even truer of interactive computer services that are websites. The barriers to movement between websites are virtually nonexistent. Section 230 also encourages the development of technologies that allow individual users to filter locally. To the extent there is market demand for a decent Internet, interactive computer services will provide it, or allow users to customize it.

The net result of these market forces will be the demise of overfiltering. No interactive computer service will remove too much speech because it will never face liability for leaving such speech alone. It may have strong *disincentives* to remove too much, however, because there are significant business reasons to avoid a reputation for censorship.[78] At equilibrium, there will be a very low amount of top-level filtering by the large services, with local filters allowing for personalized access. This may be exactly what Congress intended.

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77. *See* N.Y. Times Co. v. Sullivan, 376 U.S. 254, 280 (1964) (pointing out that states have different standards for defamation actions since defamation is an amorphous common law tort).

78. *See* Sheridan, *supra* note 10, at 176-77 ("[A] service that removes members' postings without any investigation is likely to get a bad reputation in a community whose first value is the free flow of information.").

2. *Defamation Presents Unique Problems Not Solved by Immunity Alone*

Unfortunately, the problem of defamation is wholly unlike the problem of obscenity. Obscenity is diffuse and easily addressed with personalized software. However, in cases of defamation or copyright infringement, the harm is felt most acutely by a single individual and cannot be avoided with local filtering.[79] Even if one takes precautions to choose the right ISP and filtering tools, defamation can occur on a more permissive ISP and still harm the individual. Under a distributor liability regime, if the individual notified the other ISP of the defamation, the ISP would have a duty to take reasonable steps to remove it.[80] Because the ISP would be required to internalize the individual's cost, the ISP may take steps to prevent the harm in the first place, or at least mitigate the harm. Under a regime of full immunity, the ISP has no duty to internalize these costs. The ISP will thus filter at too low a level to prevent or mitigate acute individual harm.

As a result, applying full immunity to defamatory speech seems to leave victims both without a way to reduce the amount of defamation on the Internet and without recourse against the perpetrators.[81] As such, full immunity cannot resolve problems associated with defamatory speech. However, there are two alternatives that may bridge the gap between defamation and indecency. Congress could either reinstate distributor liability for ISPs or accept full immunity but give victims better access to the sources of defamation by creating a qualified removal of anonymity for defamatory posters.

a) Distributor Liability

One way to address the problem of defamation would be a return to distributor liability for the specific problem of defamation. Congress has

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79. Presumably Zeran could have had a filter on his computer to screen all obscenity or even references to Oklahoma City but it would not have prevented him from receiving threatening phone calls.

80. *See* Sheridan, *supra* note 10, at 172-74 (stating plaintiff must show notice and failure to remove defamation).

81. There may be reasons to think the current regime of full immunity would still provide some relief to victims. Defamation may create market forces friendlier to victims. Acquiescence to acts of defamation by an ISP will probably receive a negative public response. Since the Internet allows anyone to publish, an individual who is defamed can notify the public of the ISP's bad behavior in not removing posts. This could either shame the ISP into acting in other cases or drive business to other services. If such complaints become widespread, the level of ISP action will slowly rise. While this is not a complete answer to the victims of defamation, at a minimum the market will not ignore their plight.

already employed this solution in the copyright context. The Digital Millennium Copyright Act of 1998 ("DMCA")[82] imposes distributor liability for services that fail to take steps to remove infringing material from their sites.[83] Copyright infringement and defamation are alike in that a single individual suffers the harm resulting from the activity. However, even apart from the significant differences between copyright infringement and defamation,[84] the propriety of applying distributor liability to defamation is completely dependent on its cost-effectiveness. That is, regulations must still allow businesses to turn a profit. The following four scenarios illustrate this point:

In scenario 1, interactive computer services choose not to filter much defamatory content, even with notice. This leaves them open to distributor liability, but the cost of paying tort damages to the victims is lower than net revenues. Result: the Internet remains indecent, but some of the harmed parties are compensated.

In scenario 2, interactive computer services choose not to filter, but the cost of damages exceeds revenue. Result: this situation is clearly not sustainable as the services go out of business as a result of liability.

In scenario 3, interactive computer services filter to the extent they have knowledge, but even this amount of filtering costs more than the services earn in revenue. Result: this situation is also not sustainable as the services go out of business.

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82. 17 U.S.C. § 512(c) (Supp. 2001).

83. The DMCA uses distributor liability to place the burden on the interactive computer service to remove infringing material. Services that comply with requests to remove are protected from liability in a "safe harbor" arrangement. *Id.*

84. While defamation may seem enough like copyright infringement to merit similar treatment in terms of liability, substantial differences exist. First, the market is truly incompetent in reducing the amount of infringing material online. Since it is possible to post and download perfect digital copies of copyright-protected works for free, there is a strong market incentive to evade copyright protection. High-profile examples, such as Napster, highlight the danger of removing liability from the interactive computer services. Defamation may create market forces friendlier to victims. Acquiescence to acts of defamation by an ISP will probably receive a far more negative public response than similar conduct toward copyright infringement.

Second, there is a far greater risk that attempts to squelch defamation will have a chilling effect on speech. Defamatory speech is hard to separate from non-defamatory speech. This will make it more costly to identify the statements for which suppression is appropriate. High costs in screening make it more likely that ISPs will err on the side of suppressing speech. However, speech that is close to being defamatory but turns out to be innocent is part of a valuable discourse that Congress was trying to protect. Content that exists at the boundaries of copyright is less valuable "speech" in this regard.

In scenario 4, interactive computer services filter, and the cost of filtering plus whatever damage awards they lose is less than revenue. Result: the Internet is a more decent place.

It should be clear that only scenario 4 promotes both goals of decency and the free market in a sustainable way. Scenario 1 allows the survival of ISPs but at the cost of decency. Scenario 3 allows for a decent Internet but with the loss of the services themselves. Only scenario 4 allows the survival of both the Internet and the goal of decency.

Commentators that support retention of distributor liability suggest that scenario 4 would be the natural result of such a policy.[85] However, there is little reason to expect this to be the case. While noting the incredible and constantly expanding volume of communications on the Internet, such commentators disregard the cost to ISPs of removing harmful posts.[86] Merely noting that such removal would only occur after notice is given is no answer. ISPs would be required to investigate the truth of allegedly harmful posts before removal.[87] This would be done to avoid removing protected speech. The sheer volume of posts on a service like AOL makes this a daunting task, costing untold man-hours of labor.[88]

Making the job more difficult would be the explosion in recall requests once the threat of liability became public.[89] With the knowledge that ISPs will be on the hook for any harmful content that remains on their servers after notice is given, mischievous users need only give notice to harass an ISP into retracting marginally- or nonoffensive materials. The removal of some posts will trigger demands for the removal of others.[90] An ISP could thoroughly investigate all of these requests for bad faith in order to deter users from making the requests, but this raises costs even further. The easiest way for ISPs to keep costs down, and thus stay within scenario 4, is to investigate at a low level and filter at a high level, under a "better safe than sorry" theory.[91] This overfiltering approach will inevitably place a

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85. *See, e.g.,* Pantazis, *supra* note 76, at 555 ("[I]t is not altogether infeasible to require an ISP that profits from the dissemination of communication to respond to reasonable requests for deleting content and terminating accounts.").

86. *See id.* at 552 (discussing why AOL should not be held a publisher since "[i]t would be impossible for AOL to verify and review messages posted by its over nine million subscribers," but advocating that AOL should still be held liable as a distributor.)

87. Sheridan, *supra* note 10, at 176.

88. *See* Zeran v. Am. Online, Inc., 129 F.3d 327, 331 (4th Cir. 1997) (finding that the screening of millions of postings for defamation was impossible and would produce a chilling effect on speech).

89. Sheridan, *supra* note 10, at 176.

90. *Id.*

91. *Id.* at 175.

heavy burden on free speech[92] since the ISPs will suppress much decent speech in an act of overzealous self-preservation. Such a result completely defeats the balance struck in scenario 4 by ensuring the decline of the "vibrant free market" of the Internet.

b) Eliminating Anonymity for Defamatory Posters

Since a major goal of Section 230 was preserving the free market of speech on the Internet, eliminating the incentive to overfilter seems a better solution. The market alone, however, is not a complete answer since it lacks incentives to reduce the amount of defamation and mechanisms to compensate victims. This is because the Internet makes it possible for many perpetrators to remain anonymous.[93] In cases like *Zeran*, the plaintiff has no recourse against the actual offender because ISP policies may prevent disclosure of identity or allow access to those who do not provide any identifying information.[94] The offending user may also operate outside the easy reach of the law, from a foreign country, for example. Even in cases where the perpetrator is identifiable, the plaintiff may still not be compensated if the offender is insolvent.

The real obstacle for victims is not the absence of distributor liability for ISPs. Rather, it is the cloak of anonymity available to bad actors.[95] Therefore, a more direct solution might be regulation that allows a victim to lift the veil and reach a culprit's identifying information. Current law rarely permits a plaintiff to reach an anonymous poster.[96] Victims of defamation should be able to obtain a declaratory judgment that the disputed content is defamatory. This judgment would then be enforced against the ISP to compel production of the poster's identity.[97] The victim could then proceed against the actual perpetrator for damages and other relief.

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92. *Id.* at 178 ("[A]nything but absolute immunity inevitably results in the chilling of some speech.").

93. *See generally* Slitt, *supra* note 76.

94. *See* Slitt, *supra* note 76, at 419 (describing AOL's negligence primarily in terms of allowing 30-day trial access to anonymous users).

95. *See id.* ("[T]he real problems are the anonymously communicated messages whose authors are not discernable.").

96. *See id.* at 416-17 (citing *McIntyre v. Ohio Elections Commission*, 514 U.S. 334 (1995), which held that Ohio's attempt to prevent anonymous web posting was unconstitutional).

97. As one commentator has pointed out, legislating mandatory disclosure would be hard to reconcile with *McIntyre*. *See id.* at 420. Perhaps since the user lists in my example would only be available after a showing of defamation (i.e., speech not protected by the First Amendment), the Court may be willing to allow disclosure of identity.

Combined with the general immunity for ISPs, weakening the shield of anonymity will have four positive effects: 1) it will compensate many victims by holding accountable the party actually responsible for the defamation; 2) it will produce a deterrent effect on defamatory speech that distributor liability lacks; 3) it will encourage victims of defamation to mitigate damages; and 4) it will avoid the chilling effects on innocent speech that plague ISP liability.

First, allowing anonymity to be pierced in limited circumstances permits victims to recover from the "publisher or speaker" of the harmful material. Whether or not it would result in more compensation than under a distributor liability regime depends on several complex factors, including how many anonymous posters are still unreachable or are insolvent, and whether negligent ISP inaction causes a relatively large or small amount of damage.[98] In either case, holding the source of the defamation liable for all damages produces a fairer result than holding the medium of communication liable for all damages.[99]

Second, holding the source liable also produces a targeted deterrent effect.[100] Knowing they can be identified by the ISP if proven responsible, posters of defamatory material will be discouraged from publishing in the first place.[101] Anonymous posters in a distributor liability system have no such disincentive because victims will go after the deep pockets of the ISP. Even in cases where the poster is insolvent or outside the court's jurisdiction, courts could craft remedies that will deter defamatory speech.

Third, removing the ability of victims to sue ISPs also creates an incentive for them to mitigate damages. Internet users have the capability to respond quickly to negative posts. If the ISP causes additional damages by letting negative posts remain online, users can mitigate these damages by responding vigorously. The Supreme Court recognizes a higher standard of fault required for proving defamation to public figures based on superior access to response channels.[102] To the extent that Internet access is becoming pervasive, all individuals may have this heightened level of ac-

98. *See* Sheridan, *supra* note 10, at 173 (noting most defamation damages would occur before the ISP becomes responsible for removing the posting).

99. Even Congress recognized that responsibility attached primarily to the actual publisher or speaker: immunity vanishes if the ISP is in fact the information content provider. 47 U.S.C. § 230(c)(1) (Supp. 2001).

100. *See* Sheridan, *supra* note 10, at 173 (noting Zeran had no way to identify the poster and thus no way to pass along the cost).

101. *See* Slitt, *supra* note 76, at 420 ("Moreover, knowing that their identities were already retrieved and on file would discourage potential tortfeasors from acting under the cloak of anonymity.").

102. *See* N.Y. Times Co. v. Sullivan, 376 U.S. 254 (1964).

cess when defamed on the Internet. Users would have little incentive to mitigate the damages if they could sue the ISP for those additional damages.

Finally, and perhaps most importantly, removing both liability and anonymity would have a much smaller chilling effect on free speech. One could argue that anonymity is vital to a vibrant discourse on the Internet.[103] Even so, anonymity would only be removed if statements were proven to be defamatory or otherwise unlawful. Since that type of speech is not protected by the First Amendment outside of the Internet, discouraging its existence on the Internet is not problematic. At the very least, a specific disincentive is preferable to the broad filtering distributor liability would promote.

V. CONCLUSION

In passing Section 230 of the Communications Decency Act, Congress tried to achieve the disparate goals of combating indecency and maintaining the free marketplace of ideas. However, the distributor liability regime suggested by Section 230(c) disproportionately burdens the free market. Courts responded by removing liability, but a regime of full immunity seems a poor way of promoting decency. Only by granting immunity and simultaneously allowing injured parties to reach anonymous posters can both goals be effectively realized.

103. Andrew Slitt makes such an argument, noting the elimination of anonymity on the Internet is not an option in practical or legal terms. He goes on to say that "[t]ime and again citizens choose to cloak their voices in the protection of anonymity, or elect not to speak at all." Slitt, *supra* note 76, at 416.

THE CONTINUING EXPANSION OF CYBERSPACE TRESPASS TO CHATTELS

By Laura Quilter

The revival of the trespass to chattels doctrine in the context of cyberspace has had unexpected and far-reaching consequences. Trespass to chattels, a doctrine developed to protect physical property, was first applied in cyberspace cases to combat spam, unwanted commercial bulk e-mail. However, recently courts have expanded the doctrine to reach activities that lie at the heart of the Internet—noncommercial e-mail and spiders, automatic programs that search the Internet. This expansion threatens basic Internet functions and exposes the flaws inherent in applying doctrines based in real and tangible property to cyberspace. This Note charts the continuing expansion of the trespass to chattels doctrine. In *eBay, Inc. v. Bidder's Edge, Inc.*[1] and two other cases,[2] spiders searching Internet-accessible databases were held to be trespassing the database servers. In *Intel Corp. v. Hamidi*,[3] the court enjoined sending noncommercial e-mail because it was a trespass to Intel's e-mail servers. This rapid expansion of the trespass to chattels doctrine demonstrates the malleability of the doctrine as applied to cyberspace. This expansion has stretched the definition of "trespass" and "chattel" and has eliminated the traditional requirement of harm. The outcomes and reasoning in the most recent cases also illustrate the impropriety of a property doctrine that analogizes telecommunications devices to land and construes electronic contact as trespass to physical property.

1. 100 F. Supp. 2d 1058 (N.D. Cal. 2000).
2. Register.com, Inc. v. Verio, Inc., 126 F. Supp. 2d 238 (S.D.N.Y. 2000); TicketMaster Corp. v. Tickets.com, Inc., No. 99-07654, 2000 WL 1887522 (C.D. Cal. Aug. 10, 2000), *aff'd* 2 Fed. Appx. 741 (9th Cir. 2001).
3. 114 Cal. Rptr. 2d 244 (Ct. App. 2001).

I. BACKGROUND

A. Technical Background

1. The Internet and Spam

The Internet is an interconnected network of computer networks.[4] The networks (domains) are connected to each other via routers and domain servers that store location information about particular networks.[5] Each computer on the Internet has a unique numeric Internet Protocol (IP) address and usually a corresponding alphanumeric domain name.[6] As information, such as e-mail or web pages, is routed across the Internet to its destination, the files are transmitted as small packets of data and reassembled at their destination.[7] Files are stored and transmitted in standardized ways, based on open, technical standards, voluntarily applied.[8]

People access information on the Internet by sending requests from their computers to servers, which are computers that accept computer requests and "serve" information.[9] People can make any kind of information available to the rest of the world by storing computer files on Internet-accessible servers. This information may be in the form of text, graphics and other media, interactive programs, databases, or combinations of all of these.

People who wish to gain access to the Internet have a variety of options, including purchasing an account from an Internet Service Provider (ISP).[10] ISP accounts typically include an e-mail address, a way to connect to the Internet,[11] and a variety of services, such as web-hosting, access to news feeds, or special proprietary interfaces.[12] To set up websites with their own domain names, individuals and organizations may purchase domain names and then either rent storage space on web host servers or set

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4. ACLU v. Reno, 929 F. Supp. 824, 830-32 (E.D. Pa. 1996).

5. Alan Silverstein, *Under the Hood of the World Wide Web*, *available at* http://www.learnthenet.com/english/html/70alan.htm (last visited Feb. 8, 2002).

6. For example, 128.12.1.1 is a fictional IP address; www.whitehouse.gov is a real domain name. LearntheNet.com, *Domain Names* (Jan. 23, 2002), *available at* http://www.learnthenet.com/english/html/84domain.htm. Numerous online tutorials are available to explain in detail how the Internet works.

7. *Reno*, 929 F. Supp. at 830-32.

8. *Id.* at 830-32, 837-38.

9. *Id.* at 829.

10. *Id.* at 832-34.

11. For instance, Integrated Services Digital Network (ISDN), Digital Subscriber Lines (DSL), or dial-up access using telephone lines.

12. *Reno*, 929 F. Supp. at 841.

up their own servers.[13] Currently, domain names are assigned by a variety of authorized commercial domain name registrars.[14]

The explosion of access to the Internet has created new ways of communicating, and accordingly, new problems. Unsolicited e-mail, characterized as "unsolicited bulk e-mail" (UBE), "unsolicited commercial e-mail" (UCE), or, more derogatorily, "junk e-mail" or "spam," has caused both technical and legal resistance on the part of the Internet community.[15] Technical resistance has most often taken the form of filters that block the particular IP addresses of spammers.[16] Congress has considered numerous anti-spam bills over the past several years, but has failed to pass any of them.[17] Litigation has filled the void, featuring a variety of theories, including trespass to chattels, computer fraud and abuse, and trademark law.[18]

2. *Spiders*

"Spiders" are programs that search engines use to create catalogs of information about the web.[19] Like spam, spiders affect sites indiscriminately. But unlike spam, most Internet users, including consumers and businesses, find spiders to be useful.[20] Most search engine databases are compiled by spiders that search web-servers and index their contents.[21]

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13. Register.com, Inc. v. Verio, Inc., 126 F. Supp. 2d 238, 241-42 (S.D.N.Y. 2000).

14. *Id.*

15. *See generally* Scot M. Graydon, *Much Ado About Spam: Unsolicited Advertising, the Internet, and You*, 32 ST. MARY'S L.J. 77 (2000); Sabra-Anne Kelin, *State Regulation of Unsolicited Commercial E-Mail*, 16 BERKELEY TECH. L.J. 435 (2001); David E. Sorkin, *Technical and Legal Approaches to Unsolicited Electronic Mail*, 35 U.S.F. L. REV. 325 (2001).

16. Graydon, *supra* note 15, at 86-87; Kelin, *supra* note 15, at 439.

17. Sorkin, *supra* note 15, at 368-70.

18. *See, e.g.*, CompuServe, Inc. v. Cyber Promotions, Inc., 962 F. Supp. 1015 (S.D. Ohio 1997); Cyber Promotions, Inc. v. Am. Online, Inc., 948 F. Supp. 436 (E.D. Pa. 1996).

19. Spiders are also known as "robots" and "crawlers." *See generally* Niva Elkin-Koren, *Let the Crawlers Crawl: On Virtual Gatekeepers and the Right to Exclude Indexing*, 26 U. DAYTON L. REV. 179, 187 (2001) (discussing the benefits of spiders for indexing and the potential harm from trespass to chattels). *See also* Stephen T. Middlebrook & John Muller, *Thoughts on Bots: The Emerging Law of Electronic Agents*, 56 BUS. LAW. 341 (2000) (discussing the technical background of spiders and a variety of laws that currently affect or might affect spiders and Internet indexing).

20. *See* Elkin-Koren, *supra* note 19; *see also* J. Bradford DeLong & A. Michael Froomkin, Speculative Microeconomics for Tomorrow's Economy (November 22, 1999) (draft), *available at* http://www.law.miami.edu/~froomkin/articles/spec.htm.

21. Maureen A. O'Rourke, *Property Rights and Competition on the Internet: In Search of an Appropriate Analogy*, 16 BERKELEY TECH. L.J. 561, 570-74 (2001).

Although only a small amount of the material on the Internet has been indexed, locating any information on the Internet would be an almost impossible task without search engines such as Google,[22] Yahoo,[23] or FindLaw.[24] The operators of web search engines thus provide an essential service, allowing individuals to find otherwise obscure information and allowing creators of information resources to rise from obscurity.[25] Consumers also appreciate the value-added services that may be included, such as reviews and rankings of websites,[26] organized hierarchical indexes,[27] caching (back-up copies stored on the search engine's website in the event that the original server is not functioning),[28] and comparison-shopping.[29] Businesses indexed by spiders typically appreciate inclusion in the databases; after all, bad publicity is better than no publicity at all, and even if a site is ranked poorly, its presence in an index means that it is at least accessible to web searchers.[30] Website operators who do not wish to avail themselves of the publicity that spiders provide may invoke the Robot Exclusion technical standard,[31] which, like most of the standards on which the Internet is based, is open and voluntary.

B. Legal Background

1. The Classic Trespass to Chattels Action

Trespass to chattels, an old and rarely used common law tort, provides redress for unauthorized use of or intermeddling with another's personal property.[32] Chattel, or personal property, is defined as physical, tangible

22. http://www.google.com/.

23. http://www.yahoo.com/.

24. http://www.findlaw.com/.

25. Elkin-Koren, *supra* note 19, at 184-86.

26. *See, e.g.*, Yahoo, *available at* http://www.yahoo.com/; Excite, *available at* http://www.excite.com/.

27. *See, e.g.*, Yahoo, *available at* http://www.yahoo.com/.

28. *See, e.g.*, Google, *available at* http://www.google.com/.

29. *See, e.g.*, CNet, *available at* http://www.cnet.com/ (online computer hardware vendors).

30. *See* Elkin-Koren, *supra* note 19, at 183-86.

31. The Robot Exclusion technical protocol allows a website operator to control whether or how her website is indexed by placing a file named "robots.txt" on the server. The file contains instructions for robots. Many search engines obey the robots.txt standard, but it is not required.

32. *See generally* RESTATEMENT (SECOND) OF TORTS §§ 217-218 (1965); W. PAGE KEETON, PROSSER AND KEETON ON TORTS § 14 (Trespass to Chattels) (5th ed. 1984). Trespass to chattels had fallen into disuse until its recent revival in the cyberspace context. Compare this to the doctrine of trespass to land, which has played an ongoing and significant role in the law. Although trespass to chattels derives from the same historical

property and is distinguished from both real property and intellectual property.[33] "Trespass" has likewise been defined as a tangible interference with property, requiring physical contact with the property as a threshold matter.[34] To be considered trespass, a use must be intentional,[35] unauthorized,[36] and substantial.[37] A "substantial" use involves actual harm or a serious infringement of rights—an interference with the chattel which dispossesses the owner, harms the chattel, interferes with the owner's use of the chattel in a substantial way or for a substantial period of time, or causes bodily harm.[38]

Trespassers may assert several defenses, including a privilege to use public utilities.[39] Consent of the owner is also a defense to trespass to chattels,[40] although the owner can revoke consent or limit it as to time, place, or other conditions.[41] Even if the owner has consented (granted a license), licensees acting outside the scope of limited consent may bear liability for trespass to chattels.[42]

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roots as trespass to land, the two actions have diverged significantly in modern law. KEETON, *supra*, at 85-86.

33. KEETON, *supra* note 32, at 85-86; Dan L. Burk, *The Trouble With Trespass*, 4 J. SMALL & EMERGING BUS. L. 27 (2000).

34. "'Intermeddling' means intentionally bringing about a physical contact with the chattel." RESTATEMENT (SECOND) OF TORTS § 217 cmt. e. Although dispossession is listed in § 217 as one of the two ways of committing trespass ("A trespass to a chattel may be committed by intentionally (a) dispossessing another of the chattel, or (b) using or intermeddling with a chattel in the possession of another[]"), dispossessions have typically been handled under the tort action of conversion. *See infra* Part I.B.2.

35. RESTATEMENT (SECOND) OF TORTS § 217. *See also id.* § 217 cmt. b (discussing the level of intentionality required).

36. *Id.* §§ 218, 252 (Consent of Person Seeking Recovery).

37. *Id.* § 218.

38. *Id.* § 218; KEETON, *supra* note 32.

39. RESTATEMENT (SECOND) OF TORTS § 259 (Privilege to Use Facilities of Public Utility).

40. *Id.* §§ 218 cmt. b, 252, 892A (Effect of Consent).

41. *Id.* §§ 252 cmt. c, 254 cmt. a.

42. *Id.* §§ 256 (Use Exceeding Consent), 252 cmt. c. Note that in the Internet context, "permission" and "consent" are generally granted through a "clickwrap" mechanism, which is itself controversial. In "clickwrap" agreements, users are presented with a screen of conditions and a clickable "I agree" button. Users may or may not actually read the agreements and have no opportunity to modify terms or participate in any of the traditional negotiations that form the background of contract law. These contracts of adhesion have nonetheless been held enforceable in many cases. *See generally* Pamela Samuelson & Kurt Opsahl, *How Tensions between Intellectual Property Policy and UCITA are Likely to be Resolved*, 570 PLI/PAT 741 (1999); Pamela Samuelson, *Intellectual Property and Contract Law for the Information Age: Foreword to a Symposium*, 87 CALIF. L.

The remedies awarded for trespass to chattels have included both damages and injunctive relief. Typically, injunctive relief is available for ongoing trespasses.[43] Recovery for intermeddling has been limited to the actual harm or damage suffered.[44] Nominal damages are available for actual dispossession,[45] but not for de minimis harms caused by intermeddling.[46] Trespass to chattels does not protect the inviolability of the chattel—it only protects against actual harm to the chattel.[47] This rationale makes it

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REV. 1 (1999); and Ryan J. Casamiquela, Note, *Contractual Assent and Enforceability in Cyberspace*, 17 BERKELEY TECH. L.J. 475 (2002).

43. RESTATEMENT (SECOND) OF TORTS §§ 219-220 (discussing a trespasser's liability to those who are entitled to immediate possession and those who are entitled to future possession)

44. *Id.* § 218 cmt. e.

45. *Id.* § 218 cmt. d; KEETON, *supra* note 32, at 87.

> By analogy to trespass to land there might be a technical tort [where the defendant merely interferes without doing any harm]; and it has been contended that there is a real necessity for nominal damages to protect property from intermeddlers. Such scanty authority as there is, however, has considered that the dignitary interest in the inviolability of chattels, unlike that as to land, is not sufficiently important to require any greater defense than the privilege of using reasonable force when necessary to protect them. Accordingly it has been held that nominal damages will not be awarded, and that in the absence of any actual damage the action will not lie.

Id. (footnotes omitted). Although dispossessions *can* generate liability for trespass to chattels, they have typically been treated under the tort of conversion. *See infra* Part I.B.2.

46. By contrast, trespasses to *land* that cause no harm may be remedied by nominal damages. KEETON, supra note 32, § 13 (Trespass to Land).

47.

> Where someone is committing a trespass to another's chattel, while it may not be actionable because it does no harm to the chattel or to any other legally protected interest of the possessor, [it] affords the possessor a privilege to use force to defend his interest in its exclusive possession.

RESTATEMENT (SECOND) OF TORTS § 217 cmt. a.

> The interest of a possessor of a chattel in its inviolability, unlike the similar interest of a possessor of land, is not given legal protection by an action for nominal damages for harmless intermeddlings with the chattel. In order that an actor who interferes with another's chattel may be liable, his conduct must affect *some other and more important interest of the possessor.* Therefore, one who intentionally intermeddles with another's chattel is subject to liability only if his intermeddling is harmful to the possessor's materially valuable interest in the physical condition, quality, or value of the chattel, or if the possessor is deprived of the use of the chattel for a substantial time, or some other legally protected interest of the possessor is affected as stated in Clause (c). Sufficient legal protection of the possessor's interest in the mere invio-

clear that trespass to chattels does not apply to all situations in which there is use of another's chattel. Where there is no legal remedy, the owner of a chattel has a privilege to use reasonable force to protect her chattel.[48]

2. *Trespass to Chattels Distinguished from Related Common Law Theories*

Trespass to chattels is frequently confused with related common law theories, such as trespass to land, conversion, and nuisance. Recent applications of the trespass to chattels doctrine in cyberspace have liberally borrowed from the related theory of trespass to land, adding to the confusion.[49] Trespass to land, a common law tort, provides redress for any unauthorized interference with "real property" or land.[50] As with trespass to chattels, the interference must be unauthorized and involve physical contact with the property.[51] However, in contrast with trespass to chattels, trespass to land can be committed unintentionally and can involve little or no harm to the land.[52] The rationale for providing more protection for owners of land is that ownership of land creates an interest in inviolability of the land. The owner's best interests are served by inviolability—preventing any incursions, no matter how harmless, because in the real property context any minor contact could ultimately result in a grant of a license or easement.[53] Traditionally, trespass to land required physical contact, but some cases have allowed recovery for intangibles, such as sound waves, microscopic particles, dust, and smoke.[54] Most courts, however, have traditionally treated those kinds of intangible interference under nuisance law, since nuisance law allows a balancing of interests.[55]

The common law tort of private nuisance provides redress for nontrespassory interferences with land.[56] Intangible interferences with property rights, such as gasses, noxious fumes, electromagnetic interference, and blocking of light and air, have generally been handled under nuisance doc-

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> lability of his chattel is afforded by his privilege to use reasonable force to protect his possession against even harmless interference.

Id. § 218 cmt. e (emphasis added).

48. *Id.* §§ 218 cmt. e, 77 (describing the defense of possession by force).

49. *See* Burk, *supra* note 33.

50. KEETON, *supra* note 32, § 13.

51. *Id.*

52. Actions for harmless trespasses to land are awarded nominal damages. *See generally* KEETON, *supra* note 32, §§ 13, 14, at 87.

53. *See* Susan M. Ballantine, *Computer Network Trespasses: Solving New Problems With Old Solutions*, 57 WASH. & LEE L. REV. 209, 234-35 (2000).

54. *See* Burk, *supra* note 33, at 33-34.

55. *Id.* at 33.

56. *See* RESTATEMENT (SECOND) OF TORTS §§ 821D, 822.

trine.[57] Nuisance doctrine employs a balancing test—weighing the harms and benefits to the owner, the tortfeasor, and the public interest. Typically the liability is assigned on the basis of both efficiency and fairness, and the parties are able to bargain around injunctions and damages awards.[58]

A third relevant tort, conversion, involves a major interference with chattel or the owner's rights in it.[59] Conversion usually involves an actual dispossession—physically taking a tangible item of property from the owner.[60] In conversion, the dispossession is so serious that it results in a "forced judicial sale"—the defendant must pay the owner for the value of the chattel.[61] Conversion, therefore, is a more serious infringement than trespass to chattels, which has been frequently identified as "the little brother of conversion."[62] Actual dispossession of the chattel would give rise to actions for both conversion and trespass to chattels, although conversion has been by far the more commonly applied legal theory under those circumstances.[63]

3. *The Emergence of Cyberspace Trespass to Chattels*

In 1996, a California appellate court established in *Thrifty-Tel, Inc. v. Bezenek*[64] that electrons and electronic signals are sufficiently physical and tangible to constitute trespass to chattels.[65] In *Thrifty-Tel*, a telephone operator sued the families of two minors who used a computer to hack into

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57. *See id.*; Burk, *supra* note 33.

58. *See* Carol Rose, *Crystals and Mud in Property Law*, 40 STAN. L.REV. 577, 594 (1988). For instance, in a typical nuisance case a new factory producing noxious fumes might pay damages to a nearby long-time landowner. Conversely, a new housing development might pay for the factory to relocate. Both outcomes depend on the allocation of property rights and the liability. *Id.*

59. RESTATEMENT (SECOND) OF TORTS §§ 223-241.

60. Mark D. Robins, *Electronic Trespass: An Old Theory in a New Context*, 15 No. 7 COMPUTER LAW. 1, 1-2 (1998). Historically, conversion involved an owner misplacing her property and the defendant "converting" it to his own use. KEETON, *supra* note 32.

61. KEETON, *supra* note 32, § 15 (Conversion). This serious interference with the owner's rights and the subsequent forced judicial sale are the hallmarks of conversion. *Id.*

62. *Id.*

63. *See* RESTATEMENT (SECOND) OF TORTS §§ 217-218, and KEETON, *supra* note 32.

64. 54 Cal. Rptr. 2d 468 (Ct. App. 1996) The court found that computer-generated signals used to access a telephone system were sufficiently tangible. *See* Burk, *supra* note 33, for an analysis of this case, which discusses the court's flawed analysis and reliance on inappropriate precedents. *See infra* (discussing the current uses of this doctrine in cyberspace cases).

65. *See also Hacking is Trespass, Not Conversion, California Court Rules*, 13 No. 8 COMPUTER LAW. 31 (1996).

the telephone system.[66] The court in *Thrifty-Tel* found that the presence of electronic signals constituted trespass to chattels.[67] The court relied principally on unusual cases that treated intangible interferences in real property (land) as trespasses. Intangible interferences are more commonly treated under the nuisance doctrine, not trespass to land. *Thrifty-Tel*'s treatment of intangible interferences as trespass to chattels pushed the boundary of nuisance-like behavior, from trespass to land to trespass to chattels.

The reconfigured trespass to chattels doctrine was first applied to the Internet in a spam case, *CompuServe, Inc. v. Cyber Promotions, Inc.*,[68] in which CompuServe, an ISP, sued Cyber Promotions for spamming CompuServe account-holders.[69] *CompuServe* followed *Thrifty-Tel* in finding that electronic "touches" constituted a sufficient trespass to meet the requirements for trespass to chattels.[70] This was despite the fact that the very same electronic "touches" were not only permitted by CompuServe, but they were the exact kind of uses that comprised any ISP's principal service—receipt and delivery of e-mail to account-holders who paid for that service. *CompuServe* transformed these electronic touches, which form the basis of all communications on the Internet, into trespasses any time the owner of a server withdraws her permission from a particular sender. The defenses that Cyber Promotions raised—a First Amendment right to communicate to users[71] and access to CompuServe as a public utility[72]—were dismissed by the court with slim analysis.[73]

The court in *CompuServe* also loosened the requirement of harm in the trespass to chattels doctrine, granting an injunction without requiring CompuServe to show actual harm to the chattel.[74] Instead, the court broke

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66. The minors used computers to connect to Thrifty-Tel's telephone system. They then ran programs to try to determine codes to make long-distance calls. *Thrifty-Tel*, 54 Cal. Rptr. 2d at 470-71.

67. *Id.* at 468.

68. 962 F. Supp. 1015 (S.D. Ohio 1997).

69. *Id.*

70. *Id.* at 1021.

71. *Id.* at 1025-28.

72. *Id.* at 1025. The test for the public utility defense is that the service is essential to society, and that the provider occupies a monopolistic or oligopolistic position in the marketplace. *Id.* The court did not accept Cyber Promotion's defense that CompuServe was a public utility. Instead the court found that e-mail is not essential to society and that CompuServe did not occupy a monopolistic or oligopolistic position in the marketplace. *Id.*

73. *See id.* at 1025-28. The court's reasoning was based almost entirely on a previous spam case, *Cyber Promotions, Inc. v. Am. Online, Inc.* 948 F. Supp. 436 (E.D. Pa. 1996).

74. *See supra* Part I.B.1 (discussing the elements of trespass to chattels).

the chain between the trespass and the harm, allowing indirect harms to CompuServe's business interests—reputation, customer goodwill, and employee time—to count as harms to the chattel (the server).[75]

Several similar spam cases have followed suit.[76] These cases have largely adopted the reasoning in *CompuServe*, with very little additional analysis. Spam cases have until recently comprised the majority of the cyberspace trespass cases, and trespass to chattels has provided litigants with a way of dealing with the problem of unsolicited commercial bulk e-mail. There are still unanswered questions about the implications of cyberspace trespass to chattels and the elimination of the public utility and First Amendment defenses to trespass to chattels.[77]

II. CASE SUMMARIES: TRESPASS TO CHATTELS IN CYBERSPACE

The following cases chart the evolution of the cyber-trespass doctrine, stretching the traditional requirements of harm, trespass, and even the definition of a chattel. The most recent cases have stretched the trespass to chattels doctrine beyond spam to include spidering, the core computer operation that underlies web search engines. In 2000, three district court cases considered the extension of the trespass to chattels doctrine to protect against alleged interference by spiders, computer programs that search servers.[78] A fourth case used trespass to chattels to enjoin an individual from sending e-mail to Intel employees' work e-mail accounts.[79]

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75. *CompuServe*, 962 F. Supp. at 1027. The court did not address the indirect nature of these harms, glossing over the facts that (a) the servers themselves never experienced any loss of functionality, downtime, or any other harm; and (b) it was questionable whether users had any reasonable expectation that CompuServe would prevent third-party spam.

76. *See, e.g.*, Hotmail v. Van$ MoneyPie, No. 98-20064, 1998 WL 388389 (N.D. Cal. Apr. 16, 1998); Am. Online, Inc. v. IMS, 24 F. Supp. 2d 548 (E.D. Va. 1998). For a complete table, see http://walnut.he.net/~lquilter/law/trespass/ (Jan. 28, 2002).

77. For a discussion of state legislative approaches to the problem, *see* Kelin, *supra* note 15, at Part II.B.

78. TicketMaster Corp. v. Tickets.com, Inc., No. 99-07654, 2000 WL 1887522 (C.D. Cal. Aug. 10, 2000), *aff'd* 2 Fed. Appx. 741 (9th Cir. 2001); eBay v. Bidder's Edge, 100 F. Supp. 2d 1058 (N.D. Cal. 2000); Register.com, Inc. v. Verio, Inc., 126 F. Supp. 2d 238 (S.D.N.Y. 2000).

79. Intel Corp. v. Hamidi, 114 Cal. Rptr. 2d 244 (Ct. App. 2001).

A. eBay, Inc. v. Bidder's Edge, Inc.[80]

The most famous of these cases, *eBay v. Bidder's Edge*, out of the Northern District of California, featured a lengthy and thoughtful analysis of the harms requirement of the trespass to chattels action.[81] *eBay* was a dispute between two auction companies: eBay, the largest and most successful Internet auction website,[82] and Bidder's Edge, an auction aggregator that gathered data from the various auction websites, compiled it in its own database, and then provided the data on demand as a personalized consumer guide to auctions for a particular item.[83] The dispute was about access to and use of data stored and organized by eBay.[84] eBay sought to control the method of searching that the spiders used, arguing that some methods should not be used because they are more computation-intensive than others.[85] eBay successfully negotiated around spidering methods with several auction aggregators but was not able to come to an agreement with Bidder's Edge.[86] eBay then sued Bidder's Edge in the Northern District of California, and on the basis of trespass to chattels, obtained a permanent

80. 100 F. Supp. 2d 1058 (N.D. Cal. 2000).

81. *Id.*

82. *See* Elkin-Koren, *supra* note 19, at 181-182. As in many industries, this one successful business created both many competitors and many spin-off industries. In the online auction industry, one spin-off industry was "aggregators"—businesses that aggregate selected data from a variety of online auction websites and present it to the aggregator's customer in some convenient, value-added format. *See Id.* for a discussion of the economics of spidering.

83. *eBay*, 100 F. Supp. 2d 1058. After losing, Bidder's Edge appealed, then settled, then finally went out of business. Clare Saliba, *Target of eBay Lawsuit Shutting Down*, E-COMMERCE TIMES, Feb. 16, 2001, *available at* http://www.newsfactor.com/perl/story/7585.html. Bidder's Edge was not alone in providing this value-added service; other companies such as AuctionWatch performed similar services. Elizabeth Clampet, *eBay vs. Auction Aggregators: A Freedom Fight?* E-COMMERCE NEWS, Feb. 11, 2000, *available at* http://www.internetnews.com/ec-news/article/0,,4_302591,00.html.

84. *eBay*, 100 F. Supp. 2d at 1060-62.

85. *Id.* at 1062. For example, eBay wanted spiders to query the eBay database on-the-fly when a user requested information. Aggregators, such as Bidder's Edge, often prefer to search *in advance* of any particular user queries and to compile the data on their own servers. From the web-surfer's perspective, the on-the-fly method provides the most current information, while the in-advance method provides a fast retrieval of data and perhaps some value-added information sorting services that are not possible with on-the-fly calculations. The original vendor profits from any sale that transpires, regardless of the search method; however, the consumer may determine from the aggregator's comparative information that particular vendors' sales are not in their best interest.

86. *Id.* at 1067.

injunction against Bidder's Edge's spider activity.[87] Although eBay alleged several specific instances of harm, the evidence undercut those harms and the court did not allow them.[88] Instead, the *eBay* court held that a *potential* harm was sufficiently substantial to meet the requirements for trespass to chattels.[89]

B. TicketMaster Corp. v. Tickets.com, Inc.[90]

At roughly the same time as the *eBay* suit was in litigation, TicketMaster, a large retailer of events tickets, sued Tickets.com in the Central District of California.[91] Tickets.com used a spider to gather event locations and times from TicketMaster and other ticket vendors.[92] Tickets.com then reformatted the data and stored it in its own database along with links to all available vendors, including both TicketMaster and Tickets.com.[93] TicketMaster took issue with both the spidering and the linking, and

87. *Id.* Although it was appealed, the case was ultimately settled—so there was no appellate review of *eBay*, or, indeed, of any of the three spidering cases.

88. *Id.* at 1068.

89. *Id.* The potential harm was found in the (unproven) possibility that other data aggregators would also search eBay's website, and that taken as a group they would burden eBay's servers. For more detail on *eBay*, see generally Aaron Xavier Fellmeth, *Cyber Trespass Comes of Age: eBay, Inc. v. Bidder's Edge, Inc.*, 19 No. 2 INTELL. PROP. L. NEWSL. 8; Lisa M. Ferri & Robert G. Gibbons, *Forgive Us Our Virtual Trespasses: The 'eBay' Ruling*, June 27, 2000, N.Y.L.J. 1 col. 1.

90. No. 99-07654, 2000 WL 525390 (C.D. Cal., Mar. 27, 2000); No. 99-07654, 2000 WL 1887522 (C.D. Cal. Aug. 10, 2000), *aff'd* 2 Fed. Appx. 741 (9th Cir. 2001). There were two opinions issued on the motion for preliminary injunction. The first opinion, in March, denied the preliminary injunction, granting a motion to dismiss as to the trespass to chattels claim. The court primarily analyzed the copyright claim, and found a triable issue although it did find evidence of harm sufficient to grant an injunction. In its August 2000 opinion, the court reconsidered the issue in light of *eBay* but affirmed its March decision. Although both opinions were published, the court noted in its August 10, 2000, decision, that

> [t]he facts governing this preliminary injunction motion have partly been stated in the minute order of March 27 and will not all be repeated here. (In this respect, the court does not intend this to be a published opinion, but rather a minute order announcing a result, and as a result has not written for publication with the usual citation of excess authorities and other attention to grammatical or literary detail. In addition, no pronouncements of legal significance are intended; those come from the Court of Appeals. While the court cannot prevent publication, such is not done with the permission or desire of the court—and also with the hope that any typos are corrected.)

TicketMaster, 2000 WL 1887522 at 1.

91. *TicketMaster*, 2000 WL 1887522 at 1.

92. *Id.*

93. *Id.*

sought an injunction based on trespass to chattels and copyright infringement.[94]

The court issued two decisions contrary to *eBay*, finding that Tickets.com's spidering did not constitute trespass to chattels. In the first decision, the court held that "the taking of factual information from a public source was not a trespass," and even if it were, the Copyright Act preempted that claim.[95] The court noted that it was difficult to see how "entering a publicly available website could be called a trespass, since all are invited to enter."[96]

The court reconsidered the matter in a second decision issued shortly after *eBay*.[97] In the second decision, the court reiterated its reasoning from the first decision, finding no irreparable injury for either the copyright or the trespass to chattels claims. The court attempted to distinguish *TicketMaster* from *eBay* on the facts of the cases, noting that TicketMaster had shown no physical harm to the computer, insufficient evidence of obstruction of the computer's basic function, and no foreseeable harm.[98] Although the *TicketMaster* court was careful not to directly contradict *eBay*, the reasoning in *TicketMaster* is nonetheless perfectly applicable to *eBay*. *TicketMaster* is, to date, the only cyberspace trespass to chattels case in which a property owner has been unsuccessful on the merits of the claim, albeit only on a preliminary injunction motion as of yet.[99]

C. Register.com, Inc. v. Verio, Inc.[100]

Also in 2000, Register.com sued Verio in the Southern District of New York for spidering its Internet-accessible database.[101] Register.com, an ISP, maintained a database of domain name registrants.[102] The database is

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94. *Id.* In *TicketMaster*, as in many of these cases, the plaintiffs allege many causes of action to see which will stick; only those relevant to the present discussion are listed.

95. *Id.* at 4 (restating the holding from the March decision). The court effectively analyzed the trespass to chattels claim as essentially an attempt to protect TicketMaster's factual data. *TicketMaster*, 2000 WL 525390 at 4. Factual data is generally unprotectable. *Feist Publ'ns, Inc. v. Rural Tel. Serv. Co.*, 499 U.S. 340 (1991) (holding that collections of fact cannot be protected by copyright).

96. *TicketMaster*, 2000 WL 525390 at 4.

97. *TicketMaster*, 2000 WL 1887522.

98. *Id.* at 4.

99. All other spam cases that have been decided against property owners involved third-party contractors or other technicalities. *See, e.g.*, Seidl v. Greentree Mortgage, 30 F. Supp. 2d 1292 (D. Colo. 1998).

100. 126 F. Supp. 2d 238 (S.D.N.Y. 2000).

101. *Id.*

102. *Id.* at 242-43.

accessible to the general public on the Internet.[103] Verio used a spider to scan the database for recent registrants and their contact information.[104] Verio then used that information to send targeted sales pitches for its own ISP and web-hosting services, which were in direct competition with some of the same services offered by Register.com.[105] The court found that Register.com's terms of service did not forbid spiders, but that the lawsuit had put Verio on notice that its spiders were unwanted.[106] As in *eBay*, the plaintiff alleged several specific harms that were "thoroughly undercut" by the evidence.[107] Nonetheless the court, relying largely on *eBay* and *CompuServe*, found that "evidence of a mere possessory interference is sufficient to demonstrate the quantum of harm necessary to establish a claim for trespass to chattels."[108]

D. Intel Corp. v. Hamidi[109]

Intel Corp. v. Hamidi differs from the other cyberspace trespass to chattels cases in that the defendant, Hamidi, had no commercial interest at stake; Intel alleged no harm to the actual server that Hamidi allegedly trespassed; and the actual trespass was minor in comparison to the spam or spider cases. In 1999, Intel sued to enjoin Hamidi, a former employee, from sending unsolicited e-mail to current Intel employees at their work e-mail accounts. A California superior court judge found that Hamidi trespassed Intel's server by sending up to six e-mails to thirty thousand Intel employees over a three-year period of time, and permanently enjoined Hamidi from sending e-mail to employees' Intel e-mail accounts.[110]

Hamidi appealed, supported by several public interest group amici,[111] but in December 2001, a California court of appeal affirmed the lower

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103. *Id.* at 242.

104. *Id.* at 243.

105. *Id.*

106. *Id.* at 249.

107. *Id. See also* Mike Tonsing, A Tale of Two Cyberian Robots, 48-Apr. FED. LAW. 12 (2001) (comparing *eBay* with *Register.com*).

108. *Register.com*, 126 F. Supp. 2d at 250.

109. 114 Cal. Rptr. 2d 244 (Ct. App. 2001).

110. Intel Corp. v. Hamidi, 1999 WL 450944, at 1, 3 (Cal. Super., Apr. 28, 1999) (depublished).

111. The Electronic Frontier Foundation (EFF) and the American Civil Liberties Union (ACLU), Northern California, each filed an amicus brief. In the interim, Hamidi delivered his messages directly to Intel headquarters, using a horse and buggy to make the point that the Superior Court's view of modern communications technologies made no sense in the modern age. *See* http://www.intelhamidi.com/seconddelivery.htm (last visited, Feb. 8, 2002); E. Gaura, *E-Mail Delivered by Horse Mail*, S.F. CHRON. (Sep. 29, 1999), B-2.

court decision.[112] The appellate court acknowledged that there was insufficient harm to award even nominal damages,[113] but determined that since Intel was seeking an injunction and not damages, Intel did not need to demonstrate any harm to the chattel[114]—the mere fact that "the intrusion occur[red] supports a claim for trespass to chattels."[115] Although the court held that no showing of harm was necessary to award an injunction, the court nevertheless repeatedly cited the alleged harm to Intel's business interests caused by employees reading Hamidi's e-mails.[116] The court also based the injunction on the ongoing nature of the "trespass." The court cited several cyberspace trespass to chattels cases to support its point that negligible harms and indirect harms could support an injunction.[117]

III. DISCUSSION

A. Filling Regulatory and Doctrinal Gaps

Courts revived trespass to chattels to craft quick and expeditious remedies for irritations like spam.[118] The negative consequences of the new form of the doctrine were at first overshadowed by its apparently positive impact—dealing with spammers was no small accomplishment. Congress has failed to pass spam legislation for several years running,[119] but the courts successfully used trespass to chattels to step in and fill this regulatory gap.[120] While Internet users and courts alike approve of results that curtail spam, the use of trespass to chattels is not a substitute for a

112. *Intel Corp. v. Hamidi*, 114 Cal. Rptr. 2d 244 (Ct. App. 2001).

113. *Id.* at 249.

114. *Id.* at 249-50.

115. *Id.* at 249. The court cited *Register.com* as support for this proposition. *Id.*

116. *Id.*

117. *Id.* (relying on, among others, *Register.com*, *Hotmail*, and *CompuServe*).

118. In addition to the cases we have already seen, one can imagine other situations in which trespass to chattels might lie for computer damage. *See, e.g.*, Burk, *supra* note 33, at 34, 35-36. For instance, A uses B's computer without permission and actually damages it; or A hacks into B's system in some way that is not covered by the Computer Fraud & Abuse Act. *Id.*

119. *See supra* note 17 and accompanying text.

120. On the other hand, it is not at all clear that this gap *needed* to be filled. Although the court in *CompuServe* noted that spam, if unchecked, could destroy the Internet, spam has remained largely unchecked, and the Internet arguably has not been destroyed as a result. CompuServe, Inc. v. Cyber Promotions, Inc., 962 F. Supp. 1015, 1028 (S.D. Ohio 1997).

properly crafted legislative response to spam, which would consider the public interest and the rights of all parties.[121]

The shortcomings inherent in using trespass to chattels to remedy cyberspace issues have become more obvious now that courts have started using the doctrine to regulate spiders. Since spiders are essential to the Internet, there are substantial benefits to the public from spider activity. In *TicketMaster* and *eBay*, for instance, the spiders arguably provided a useful service to the public by aggregating data from multiple services and providing cost-comparison information to consumers.[122]

In addition to its benefits, spider activity also produces few detrimental effects to the public or the property owner. The harms recited in *eBay*, *Register.com*, and *TicketMaster* have all been vague and attenuated, or even disproved.[123] And while it is certainly conceivable that a spider might overburden or even crash a server, theories other than trespass to chattels already provide remedies for nuisance-like behavior, even on the Internet.[124] Furthermore, there is no apparent plague of troublesome spider activity, for which trespass to chattels might provide a useful remedy.[125]

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121. For instance, spam regulations implicate First Amendment rights. While *Cyber Promotions* examined the First Amendment question, its analysis seems out of date and the issue could in any case profit from a thorough legislative examination. State legislatures have weighed in on this question. *See* Kelin, *supra* note 15 (discussing state legislative responses and ultimately recommending that federal legislation is needed). It is also worth noting that in many situations, legislation has been spurred by courts refusing to stretch laws and doctrines too far. *See, e.g.*, *U.S. v. LaMacchia*, 871 F. Supp. 535 (D. Mass. 1994). The *LaMacchia* court's refusal to find the defendant guilty of wire fraud prompted Congress to pass the "No Electronic Theft Act." H.R. REP. NO. 105-339, at 3-5 (1997). In this respect, the use of trespass to chattels in the spam cases may actually have delayed an effective legislative response to spam by providing an easy, if problematic, solution for ISPs.

122. Brief of Amici Curiae [28 law professors] In Support of Bidder's Edge, Inc., Appellant, Supporting Reversal, No. 00-15995 (Jun. 22, 2000), *available at* http://www.jurist.law.pitt.edu/amicus/biddersedge_v_ebay.pdf. The amicus brief was submiteed for Bidder's Edge's appeal to the Ninth Circuit, before eBay and Bidder's Edge settled.

123. This was also true to some extent in the spam cases. *See infra* Part III.B.3.

124. See Burk, *supra* note 33, at 53, for a discussion of why trespass to chattels is inappropriate for the Internet and comparing it to other theories. Burk specifically proposes a theory of cyber nuisance. *Id.*

125. In fact, the Restatement specifically notes that not all interference with chattel property is actionable. "Use of force"—private action, in other words—is the appropriate remedy for interferences that are not legally actionable. *See supra* note 47 and accompanying text. A variety of technical means are available on the Internet as private action against spiders, spammers and others: IP blocking, use of the afore-mentioned robots.txt standard, programming servers to prioritize particular types of uses, allowing users to

By using trespass to chattels to curtail spider activity, courts have created a new form of property protection for property owners. This property protection affords a back-door form of intellectual property protection for databases and collections of facts that would not otherwise be protected by copyright.[126] Although some businesses might welcome legal protection for databases,[127] it is not the place of courts to create such a protection.

B. Doctrinal Evolution

1. Novel Chattels

Cyberspace trespass to chattels cases have assumed that computers, electronic networks, and computer processing power are chattels. While computers are undoubtedly chattels, it is questionable whether electronic

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easily deploy spam-filters, and even simple methods such as establishing password-access to databases. Part of the complaint in *eBay*, *Register.com*, and the spam cases has been that the technical means employed (IP blocking and use of robots.txt) have failed. This is par for the course with Internet technology—a constant race. Having to constantly deploy new technical methods for keeping ahead, however, should not be considered the sort of harm for which court remedies are in order. Moreover, the existence of alternative technical means that were not explored by the courts or attempted by the property owners renders problematic the granting of relief on the grounds that all available technical means failed.

126. The court in *TicketMaster* explicitly noted its concerns about creating "back-door" copyright protection. "The major difficulty with many of plaintiff's theories and concepts is that it is attempting to find a way to protect its expensively developed basic information from what it considers a competitor and it cannot do so." TicketMaster Corp. v. Tickets.com, Inc., No. 99-07654, 2000 WL 1887522 (C.D. Cal. Aug. 10, 2000), *aff'd* 2 Fed. Appx. 741 (9th Cir. 2001). *See generally* Bruce P. Keller, *Condemned to Repeat the Past: The Reemergence of Misappropriation and Other Common Law Theories of Protection for Intellectual Property,* 11 HARV. J.L. & TECH. 401 (1998) (discussing the history of common law torts in intellectual property and the current uses of misappropriation in hot news cases and trespass to chattels in *CompuServe, Inc., v. Cyber Promotions, Inc.*, 962 F. Supp. 1015 (S.D. Ohio 1997)).

127. eBay has lobbied Congress to craft new legislation protecting databases and overrule *Feist*. David E. Rosenbaum, *Bill to Protect Databases Creates Strange Bedfellows*, N.Y. TIMES, June 5, 2000, at A14, *available at* http://www.nytimes.com/library/tech/00/06/biztech/articles/05databases.html. For more background information, and the library perspective, see American Library Association, Office of Government Relations, *Database Protection Legislation*, http://www.ala.org/washoff/database.html (last visited Feb. 8, 2002). While such legislation would be in line with protections recently granted in Europe, it is questionable whether it would actually be constitutionally permissible. *See generally* J. H. Reichman & Pamela Samuelson, *Intellectual Property Rights in Data?* 50 VAND. L. REV. 51 (1997). *See* Burk, *supra* note 33 (discussing the ways in which trespass to chattels is being employed effectively as a new form of intellectual property).

networks and computer processing power also qualify as chattel.[128] Although it may make sense to consider the processing power of one's chattel as some form of personal property,[129] it is unclear what sorts of protection this property requires, especially since the function of this personal property is to be part of a network accessible to the public. Computer owners may want to ensure that the processing power is available for their own purposes, that it functions fully, and that there is no risk of anybody else making property claims on that processing power.[130] The trespass to chattels doctrine, designed to ensure that a single, indivisible piece of tangible property is available to its owner, might not be suitable in this situation.[131] Furthermore, if processing power and network connection are a form of chattel, what effect does allowing the public access to the chattel via the Internet have on the owner's rights?[132] And what rights does the public have as a result? The courts have not examined these questions.

Finally, the question of whose chattel is being trespassed has not been adequately addressed. In *CompuServe* and the spam cases, it seems apparent that the harm, if any, is actually suffered by the individual users, who rent access to the ISP's processing power and disk space for their e-mail accounts. To the extent that spammers are trespassing, they are in some sense trespassing against the individual users' disk space or time, and not against the ISPs.

2. *Novel Trespasses*

The new cyberspace trespass to chattels has married the doctrines of trespass to land and trespass to chattels, blurring the traditional boundaries between them. The land formulation of trespass is a strict formulation,

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128. Chattel property traditionally has been material items or living property (*e.g.*, animals) that can be physically damaged, injured, or physically taken away. *See* KEETON, *supra* note 32, at 84-86.

129. *See* Melvin Albritton, *Swatting Spiders: An Analysis of Spider Activity on the Internet*, 3 TUL. J. TECH. & INTELL. PROP. 137, 148-52 (2001) (arguing that computer processing power should be treated as a form of chattel).

130. For instance, computer owners would want to be able to prevent members of the public from establishing easements on their property.

131. Computer processing power is inherently divisible, and computers used as servers are designed to facilitate multiple tasks and multiple processes.

132. Placing a traditional chattel, such as a horse, in the position of the cyber-chattel sheds some light on the theoretical inconsistencies. If the owner were generally using the horse to give rides to any and all comers, would taking a ride under a false name be considered a trespass? It makes more sense for deceptive horseback riders, and deceptive spiders, to be held liable for the real problem—the false and misleading identification information that prevents property owners from effectively employing technical means of self-help.

with no harm requirement, that protects the owner's interest in inviolability.[133] Traditionally, trespass to chattels required an actual physical trespass, and intangible impacts have not generally qualified as trespass to chattels.[134] However, beginning with *Thrifty-Tel*'s recognition of electronic signals as a trespass, courts have eliminated the requirement for a physical trespass and recognized intangibles—electrons—as adequate to support a trespass to chattels claim. The elimination of the requirement for a physical trespass blurs the boundary between trespass to chattels and trespass to land,[135] and it also blurs the boundary between trespass to land and nuisance.[136] As doctrinal boundaries blur, the historic balances between owners' interests and the public interest have shifted in favor of the owners.

3. *Novel Harms*

As the cyberspace trespass to chattels doctrine has evolved, the requirement for harm has virtually disappeared, allowing vague, attenuated and indirect harms. While the chattel that was allegedly trespassed in each case was the *server*—the actual computer—the harms alleged and considered have rarely been harms actually suffered by the server. In *eBay*, the court rejected all of the alleged harms and instead found a *potential* harm by aggregating the effect of multiple actors.[137] In the more recent *Intel* decision, the court effectively ruled that third-party harm constituted harm to the chattel.[138] In stretching trespass to chattels, courts have allowed various novel and indirect harms, including loss of corporate goodwill,[139] alleged psychological distress suffered from reading e-mail,[140] and the time wasted by employees[141]—surely a novel form of property in the twentieth century. The actual harm that spam or spiders cause servers has rarely

133. *See supra* Part I.B.

134. *Id.*

135. *See, e.g.*, Intel v. Hamidi, 114 Cal. Rptr. 2d 244 (Ct. App. 2001). Throughout the decision, the majority cites to cases dealing with trespass to land, ignoring the traditional distinctions between the actions. *Id.*

136. *See* Burk, *supra* note 33.

137. *eBay, Inc. v. Bidder's Edge, Inc.*, 100 F. Supp. 2d 1058, 1067 (N.D. Cal 2000). And, as some commentators have noted, the harm was not only potential, it was speculative—it's questionable whether the market would support dozens of Internet auction site aggregators in the real world. *See* Elkin-Koren, *supra* note 19, at 204.

138. Intel Corp. v. Hamidi, 114 Cal. Rptr. 2d 244, 250 (Ct. App. 2001).

139. This was true in the spam cases generally. *See supra* Part I.B.3.

140. *Intel*, 114 Cal. Rptr. 2d at 250.

141. *See id.* and the spam cases generally.

been calculated.[142] This may be because the harm to servers is difficult to measure; or, if measured, would seem insignificant or slight. Where use of available computer resources has been actually alleged, the use has rarely been found sufficient to constitute "harm."[143] Courts' recognition of these indirect and speculative harms has removed an important limit on the doctrine—a connection between the alleged harm and the remedy imposed.

However, even in those situations in which there is an actual, direct harm alleged—e.g., excessive use of server resources—trespass to chattels is not well tailored to address the harm.[144] The reconfigured trespass to chattels—stripped of its harm requirement—is a strict formulation of a property right. In the realm of communications and network technologies this strict formulation creates absurd results. As the dissent in *Intel* points out,

> Under Intel's theory, even lovers' quarrels could turn into trespass suits by reason of the receipt of unsolicited letters or calls from the jilted lover. Imagine what happens after the angry lover tells her fiancé not to call again and violently hangs up the phone. Fifteen minutes later the phone rings. Her fiancé wishing to make up? No, trespass to chattel.[145]

By misconstruing what is fundamentally a communications technology as real property or even chattel property, courts have granted owners of

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142. Of the dozen cases so far, the harm to the server has been calculated by the court in two: *Am. Online, Inc. v. Christian Bros.*, Dec. 16, 1999, N.Y.L.J. 35 col. 2 (S.D.N.Y. 1999), and *CompuServe*, 962 F. Supp. 1015. Although the *eBay* plaintiffs and defendants helpfully tried to calculate it for the court, the court did not allow those harms, finding the numbers too questionable.

143. See, e.g., *eBay*, where the court found that the harms actually alleged by eBay were "flawed." *eBay, Inc. v. Bidder's Edge, Inc.*, 100 F. Supp. 2d 1058, 1063 (N.D. Cal 2000). As discussed *supra* the court found harm in a potential harm rather than in the harms actually alleged.

144. The question of what an appropriate remedy might be is not addressed in this Note. However, the first step would be to define the interests of the relevant parties—communicators on the Internet and owners of Internet-accessible servers. Assuming that some kinds of actions could be harmful, there might be several approaches. At least one commentator has suggested nuisance might be more appropriate than trespass to chattels. *See* Burk, *supra* note 33, at 52-54. Other options include some of the legislation recently tailored to address telecommunications-specific situations, such as spam faxes and spam with false header information. *See, e.g.*, Kelin, *supra* note 15.

145. Intel v. Hamidi, 114 Cal. Rptr. 2d 244, 262 (Ct. App. 2001) (Kolkey, J., dissenting). This dissent is not the only place where these concerns have been raised. *See also* Burk, *supra* note 33, at 34, 35-36 (raising the specter of other uses of telecommunications devices being the subject of trespass to chattels claims—for instance, the electric company and commercial advertisers on televisions and radios)

publicly-accessible Internet servers an absolute right to exclude that does not apply to any other communications medium (e.g., televisions and telephones). An owner merely has to withdraw permission for a use to be deemed harmful and trespassory and therefore subject to injunction and even damages. By removing the harm requirement from trespass to chattels, courts have created an absolute property right, akin to trespass to land, but without the limiting doctrines and balances of real property law.[146]

4. *No Limiting Elements*

By uprooting trespass to chattels from all its traditional restraints, the doctrine has become completely malleable, able to fit any and all situations. With trespasses as they have now been defined, and without a harm requirement, it would be difficult to conceive of anything that might *not* constitute a trespass; trespass is effectively defined purely at the owner's will and can encompass almost any kind of act.[147]

C. Underlying Assumptions of Cyberspace Trespass to Chattels

While courts have preferred to work within the familiar realm of property law, the extent to which "property" is a proper fit for the communications that take place on the Internet should be given more thorough consideration in the courts. Some of the underlying assumptions displayed in the cyberspace trespass to chattels cases highlight the difficulties in treating Internet communications devices as purely property.

First and most obviously is the assumption held by the property owners and most of the courts: that property ownership is absolute. This assumption, in cyberspace, fails to distinguish between the *real property or land*, and *personal property or chattel*. By applying, without discussion,

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146. In fact, the doctrine is not only imbalanced, it is so far removed from its precursor that it is an entirely new doctrine. *See* Intel v. Hamidi, 114 Cal. Rptr. 2d 244, 258-265 (Ct. App. 2001) (Kolkey, J., dissenting). *But see* Richard Warner, *Border Disputes: Trespass to Chattels on the Internet*, 47 VILL. L. REV. 117 (2002) (arguing that trespass to chattels can provide appropriate balance in some kinds of relationships, e.g., the relationship between eBay and Bidder's Edge).

147. In fact, one commentator seemed to think this was a good thing, and that courts should just be up-front and apply trespass to land doctrine to Internet servers. Ballantine, *supra* note 53, at 212. Ballantine seems unconcerned with the possibility that other real property doctrines—e.g., adverse possession or easements—might put a crimp in the owner's style. Perhaps only those aspects of real property doctrine that favor property owners will be adopted. Other commentators have advocated strong property rights for website owners without going so far as to advocate a trespass to land regime. *See, e.g.*, I. Trotter Hardy, *The Ancient Doctrine of Trespass to Web Sites*, 1996 J. ONLINE L. art. 7 (1996), *available at* http://www.wm.edu/law/publications/jol/95_96/hardy.html.

the stricter form of property protection traditionally granted to land, courts avoid analysis of both the rationales behind the strict property protection given to land, and the carefully crafted policy compromises that have modified those strict property protections.[148]

Second, courts coping with new technologies and new forms of communications on the Internet often apply ill-fitting analogies from common law. Property owners alleging trespass to chattels have encouraged the view that telecommunications devices—such as computers connected to the Internet—are best analogized to real property. In contrast, the alleged trespassers have viewed Internet servers as better analogized to telecommunications devices such as telephones and televisions and argued that property owners, by connecting their servers to the Internet, have necessarily opened themselves up to certain kinds of interactions.[149] Courts have been persuaded by the analogy to land, perhaps because popular metaphors such as the "information superhighway" underlie their thinking. But the Internet is *not* a highway or even a private road, and the problems inherent in treating telecommunications devices as land are beginning to make themselves felt.[150] The sense that communications devices, as used in communications, are *not* equivalent to traditional private property is arguably the working assumption for many Internet users. Many Internet users share the sense that the Internet is a cooperative venture and fear the walling off of portions of the Internet or sense that it is unfair to take advantage of the Internet's benefits in a one-sided manner—taking the good without contributing, or taking the good without also taking the bad.[151]

Finally, courts seem to have operated under the assumption that for every problem there lies a legal remedy. Spam is an annoyance, and courts have—perhaps rightly—felt that something should be done about it. Com-

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148. *See* O'Rourke, *supra* note 21 (discussing whether "property" and "trespass to chattels" are the appropriate analogies for cyberspace).

149. *See, e.g.*, *Intel v. Hamidi* amicus briefs from Electronic Frontier Foundation, at 27, and American Civil Liberties Union, Northern California, on the Face Intel website, *available at* http://www.faceintel.com/ (last visited Feb. 8, 2002), and http://www.intelhamidi.com (last visited Feb. 8, 2002); Am. Online, Inc. v. Cyber Promotions, Inc., 948 F. Supp. 436, 442 (E.D. Pa. 1996) (in a second opinion, the court denied Cyber Promotions' motion for reconsideration); and also the spidering cases discussed *supra* Parts II.A.-C.

150. *See* Intel v. Hamidi, 114 Cal. Rptr. 2d 244, 258-265 (Ct. App. 2001) (Kolkey, J., dissenting).

151. *See* Burk, *supra* note 33, at 48. Although not finding these arguments persuasive, Judge Whyte acknowledged these fears briefly in *eBay*, noting that both sides argue as if they must win or it will be the end of the Internet. *eBay, Inc. v. Bidder's Edge, Inc.*, 100 F. Supp. 2d 1058, 1072 (N.D. Cal 2000).

plaints about spammers, troublemakers, and perceived "free-riders" have appealed to courts' sense of fair play. Courts have responded to a sense of urgency in these cases, issuing preliminary and permanent injunctions despite harms that were vague, indirect, tenuous, or completely nonexistent.

IV. CONCLUSION

Trespass to chattels has met some of the stopgap needs of ISPs and generated some intriguing scholarship on the theory of property. However, it is not the right legal approach for dealing with the problems caused by non-permissive communications. Relaxing the doctrine of trespass to chattels from its traditional restraints has created a completely malleable doctrine that poses a real threat to the fundamental activities underlying the Internet. The spidering and noncommercial e-mail cases which have pushed the use of trespass to chattels doctrine beyond spam—*Intel*, *eBay*, *TicketMaster*, and *Register.com*—demonstrate some of the risks in the application of trespass to chattels to cyberspace. Courts considering cyberspace cases should be cautious when applying trespass to chattels and should consider more appropriate common law or statutory remedies.

ADDITIONAL DEVELOPMENTS—CYBERLAW

IN RE DOUBLECLICK PRIVACY LITIGATION

154 F. Supp. 2d 497 (S.D.N.Y. 2001)

The United States District Court for the Southern District of New York ruled on whether Internet cookies violate Title II of the Electronic Communications Privacy Act ("ECPA"), the Federal Wiretap Act, and the Computer Fraud and Abuse Act. The court held that the plaintiff had failed to adequately plead violations of each of the above statutes.

Doubleclick acts as an intermediary, helping advertisers place ads on web sites. Doubleclick uses "cookies" to collect information from users, tracking web usage and submission information. As a user navigates a participating web site or submits information, this usage information is added to Doubleclick's cookie and is sent to Doubleclick's computers. Doubleclick processes this information to determine the appropriate advertisement to display as a "banner" ad on the web page. Plaintiffs brought a class action suit under three federal law claims and four state law claims. The federal claims were under Title II of the ECPA, the Federal Wiretap Act, and the Computer Fraud and Abuse Act. On defendants' motion to dismiss on the pleadings, the district court found for the defendants. As a result, the state claims, under common law and New York law, were not considered by the district court.

Title II of the ECPA prohibits unauthorized access to information (e.g., "hacking"). It provides an exception for conduct authorized by a user of the service, regarding communication of or intended for that user. Doubleclick argued that its conduct fell under this exception. The court held that the exception was not an affirmative defense. Thus, Doubleclick did not have the burden of proving its actions fell within the exception. Next, the court held that the websites that posted the ads were the "users" referred to in the exception. Finally, the court held that the website's authorization of Doubleclick's access and the information posted by individual users to web sites was information "intended for" the websites. Thus, the court held that there was no issue for the court to decide under the ECPA claim.

Doubleclick also claimed that its conduct fell within the exception to the Federal Wiretap Act, which provides that intercepting an electronic communication is lawful unless done for the purpose of committing a criminal or tortious act. The court held that in determining the purpose of a defendant's action, it was not enough to prove that the act was tortious. The plaintiff must also show that the act was done with tortious purpose. Since the plaintiffs did not plead that Doubleclick acted with tortious purpose, the court held there were no issues remaining to be tried under this act.

The Computer Fraud and Abuse Act provides relief for those who suffer damage or loss as a result of unauthorized access to computer information. The statute defines "damage" as a loss of at least $5,000 during any one year. Plaintiffs argued that the statute defined "loss" differently from "damage," and that they should not be subject to the $5,000 limitation. The court held that "loss" was not intended as an exception to the $5,000 limit, and, therefore, that the plaintiff did not plead damages that were entitled to relief.

KONOP V. HAWAIIAN AIRLINES, INC.

236 F.3d 1035 (9th Cir. 2001)

The Ninth Circuit ruled on whether an employer's intrusion into an employee's private website violates the Electronic Communications Privacy Act ("ECPA"). Deciding that accessing messages in transit and accessing stored messages were legally indistinguishable activities, the court held that the employer's action could constitute a violation of the ECPA.

Plaintiff was a pilot working for defendant. Plaintiff maintained a website that criticized his employer. The website was available only to employees, and not to managers or union representatives. The vice president of defendant company used the names of two employee pilots to access the plaintiff's website. Thereafter, the plaintiff was placed on medical suspension. Plaintiff brought suit alleging tort claims, retaliatory suspension, federal labor claims, and federal wiretap claims under the ECPA and Stored Communications Act. The district court dismissed all but the retaliatory suspension claim on summary judgment. The district court ruled for the defendant on the suspension claim after a bench trial. Plaintiff appealed the grant of summary judgment on the wiretap and labor claims and final judgment of retaliation claim.

On the wiretap claim, the Ninth Circuit held that the plaintiff had raised a material question of fact and summary judgment should not have been granted. Under the ECPA, which amended the Federal Wiretap Act, there is no difference between intercepting messages in transit and accessing communications in storage. Further, private messages should not be differently protected simply because they are transmitted by different modes of communication (i.e., voicemail versus e-mail). The court held that exceptions to the ECPA do not apply because the website was not publicly available and was accessed using the account of an employee that was not party to the communication.

On the labor claim, the defendant asserted that there was a lack of jurisdiction, that the plaintiff forfeited his right to protection, and that the claims lacked sufficient evidentiary support. However, the court held that statutory provisions are properly triable in federal court, and that the postings on the protected site raised a triable issue as to whether the plaintiff was participating in a protected activity.

NETWORK SOLUTIONS, INC. V. UMBRO INTERNATIONAL, INC.

259 Va. 759 (S. Ct. 2000)

The Virginia Supreme Court heard the issue of whether a domain name is a form of property that is subject to garnishment. The court, by a vote of five to two, did not sanction the garnishment of Network Solutions, Inc.'s services under the present Virginia garnishment statutes, although domain names are being bought and sold in today's marketplace.

Umbro International, Inc. ("Umbro") obtained a default judgment against the registrant of the Internet domain name www.umbro.com, a Canadian corporation that was the judgment debtor. It went on to obtain a *writ of facias* and institute garnishment proceeding against the judgment debtor. In the garnishment summons, Umbro named Network Solutions, Inc. ("NSI") as the garnishee and sought to garnish thirty-eight Internet domain names that the judgment debtor had registered with NSI. NSI opposed the motion and garnishment on the grounds that the judgment debtor's domain name registration agreements with NSI were contracts for services, and, thus, not subject to garnishment. The lower court ruled that the domain names were "valuable intangible property subjected to garnishment", and ordered NSI to deposit control of all the judgment debtor's domain name registrations into the court's registry for sale by the sheriff's office.

Reversing the lower court's decision, the Virginia Supreme Court dodged the question of whether a domain name was a form of intellectual property, and held that domain names are not subject to garnishment under Virginia state law. Under Virginia Code section 8.01-511, a garnishment summons may be issued with respect to "a liability on any person other than the judgment debtor . . . ." The court held that a domain name registered by NSI was not a liability within the meaning of this statute, explaining that a domain name registration resulted from a contract between the registrar and registrant to use a unique domain name for a specific period of time. A contract for services cannot be a liability as the term is used in the statute. Therefore, it cannot be garnished. The court further reasoned that allowing the garnishment of NSI's services would open the door to garnishment of "practically any service."

In his dissent, Justice Compton disagreed that the right to use a domain name was a contract for services. Rather, Justice Compton found that domain name was a form of intangible personal property, and, therefore, that the judgment debtor, by virtue of the domain name registration agreement with NSI, had a current possessory interest in the property. Justice Compton would thus affirm the judgment of the lower court and hold the domain names subject to garnishment.

UNITED STATES V. COHEN

260 F.3d 68 (2d. Cir. 2001)

The Second Circuit ruled on the issue of whether Internet gambling from a foreign country violated the law as an illegal transmission of bets in foreign commerce, a transmission of communication entitling recipient to receive money as a result of bets, and providing information assisting betting. The court held that the defendant violated 18 U.S.C. § 1084 and that the safe harbor provision contained in 18 U.S.C. § 1084(b) did not apply to the defendant.

The defendant operated a sports-betting service from Antigua. Gamblers would send money to Antigua and communicate by telephone or the Internet to place bets. The defendant was arrested for illegal transmission in foreign commerce of bets or wagers under 18 U.S.C. § 1084(a)(1), transmission of communication entitling recipient to receive money as a result of bets under 18 U.S.C. § 1084(a)(2), and providing information assisting betting under 18 U.S.C. § 1084(a)(3). The defendant was convicted and appealed. The following six issues were on appeal: (1) whether the Government was required to prove a "corrupt motive" in connection with the conspiracy in this case; (2) whether the district court properly instructed the jury to disregard the safe harbor provision contained in section 1084(b); (3) whether Cohen "knowingly" violated section 1084; (4) whether the rule of lenity requires a reversal of Cohen's convictions; (5) whether the district court constructively amended Cohen's indictment in giving its jury instructions; and (6) whether the district court abused its discretion by denying Cohen's request to depose a foreign witness.

The Second Circuit upheld the conviction in its entirety. The defendant argued that corrupt motive was a necessary element for conviction. The court disagreed, reasoning that ignorance of the law is no excuse, and that all that was required for a conviction under these laws was that the defendant knowingly committed the illegal acts. The defendant then argued that certain actions fell within a safe harbor provision for permissible communications. The court found that defendant's conduct did not fit under any safe harbor provision, principally because gambling was illegal in the locations in which the gamblers placed their bets. Defendant also lost on arguments of lenity, improper amendment of charges, and failure to grant a motion to depose a foreign witness.

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CONSTITUTIONAL LAW

BARTNICKI V. VOPPER

By Richard D. Shoop

Federal and state anti-wiretapping statutes expressly prohibit the dissemination of illegally intercepted communications, even by third parties who played no role in the interception.[1] In *Bartnicki v. Vopper*,[2] the Supreme Court held that anti-wiretapping laws violate the First Amendment by prohibiting all disclosures of intercepted information, particularly when the banned information is of significant public concern.[3] *Bartnicki* is one of several recent cases questioning the constitutionality of prohibitions against publishing illegally acquired information.[4]

The *Bartnicki* decision is consistent with the substantial First Amendment protection that the Court has historically allowed publishers of truthful information.[5] However, there are serious concerns about applying *Bartnicki*'s holding. First, the Court did not define the crucial elements of "publication" and "public interest." Second, the Court expressly limited *Bartnicki's* relevance and did not adequately justify using strict scrutiny. Furthermore, the concurring opinion by Justices Breyer and O'Connor significantly reinterpreted the majority's holding. Finally, these issues are exacerbated by political and public sentiment that is increasingly wary of expanding the First Amendment rights of the press. Although *Bartnicki* could have had a profound effect on the rights of traditional mass media as well as on the expanding field of electronic publishing, the ambiguity and fragility of the holding suggest that it will only be of limited utility to either courts or lawmakers.

This Note first examines the federal and state wiretapping statutes at issue in *Bartnicki* and describes the factual and legal background of the case, with an emphasis on the *Daily Mail* line of cases that the Court relied

1. 18 U.S.C. § 2511 (2001); 18 PA. CONS. STAT. § 5703 (2001) (the federal and Pennsylvania state "anti-wiretap statutes").

2. 53 U.S. 514 (2001).

3. *Id.* at 518.

4. *See, e.g.*, Boehner v. McDermott, 191 F.3d 463 (D.C. Cir 1999), *cert. granted*, 532 U.S. 1050; Peavy v. WFAA-TV, Inc., 37 F. Supp. 2d 495 (N.D. Tex. 1999), *aff'd in part, rev'd in part*, 221 F.3d 158 (5th Cir. 2001).

5. *See, e.g.*, Fla. Star v. B.J.F., 491 U.S. 524 (1989); Smith v. Daily Mail Publ'g Co., 443 U.S. 97 (1979); Okla. Publ'g Co. v. Dist. Ct., 430 U.S. 308 (1977); Cox Broad. Corp. v. Cohn, 420 U.S. 469 (1975) (discussing cases involving "publication of truthful, lawfully obtained information").

on.[6] The analysis then explores the implications of *Bartnicki's* holding. Finally, the paper critiques the standard of review applied and the significance of Breyer and O'Connor's narrow concurrence.

I. BACKGROUND: ANTI-WIRETAPPING STATUTES

By the mid-1900s, telephone, wire, and radio communication was widely used in the United States, and political attention had become focused on growing concerns about the privacy rights of private citizens.[7] In 1968, Congress enacted Title III of the Omnibus Crime Control and Safe Streets Act ("Title III").[8] Title III was enacted to protect the privacy of wire and oral communications and to establish standards authorizing restrictions on the interception of private communications.[9] By 1985, however, advances in telecommunications and electronic surveillance technology had frustrated many of the protections of Title III.[10] Congress responded, enhancing Title III by passing the Electronic Communications Privacy Act of 1986 ("ECPA").[11]

The ECPA modified Title III to include virtually every type of electronic communication, specifically cellular telecommunications, within scope of the Act.[12] Title III prohibits the interception of wire, oral, and electronic communications, except where expressly authorized by war-

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6. The *Daily Mail* line of cases are named for Smith v. Daily Mail Publishing Co., 443 U.S. 97 (1979), and also includes New York Times Co. v. United States, 403 U.S. 713 (1971), Landmark Communications, Inc. v. Virginia, 435 U.S. 829 (1978), and Florida Star v. B.J.F., 491 U.S. 524 (1989).

7. *See* Stephen L. Sapp, *Private Interceptions of Wire and Oral Communications Under Title III: Rethinking Congressional Intent*, 16 AM. J. CRIM. L. 181, 184 (1989).

8. *See id.* at 181. Title III replaced the Federal Communications Act of 1934 (the "FCA"), which governed only law-enforcement electronic surveillance. The FCA was enacted partly in response to Supreme Court decisions such as *Katz v. United States*, 389 U.S. 347 (1967), in which the Court held that warrantless wiretapping was a violation of the Fourth Amendment. *See* Sapp, *supra* note 7, at 183-84.

9. *See supra* note 7, at 183-84; *see also* Francis M. Hamilton III, *Should 'Clean Hands' Protect the Government Against §2515 Suppression Under Title III of the Omnibus Crime Control and Safe Streets Act of 1968?* 53 WASH. & LEE L. REV. 1473, 1476-79 (1996).

10. *See* Thomas R. Greenberg, *Email and Voicemail: Employee Privacy and the Federal Wiretap Statute*, 44 AM. U. L. REV. 219, 231 (1994). For example, it was uncertain if "private" cellular phone calls were protected by the Act. John R. Kresse, *Privacy of Conversations Over Cordless and Cellular Telephones: Federal Protection Under the Electronic Communications Privacy Act of 1986*, 9 GEO. MASON U. L. REV. 335, 337 (1987).

11. *See* Greenburg, *supra* note 10, at 232.

12. 18 U.S.C. § 2510(12) (2001).

rant.[13] Violation can invoke criminal and civil penalties.[14] Furthermore, the statute forbids dissemination of illegally acquired information, including publication by a third party who is innocent of intercepting the information.[15]

In addition to the federal statute, most states have anti-wiretapping provisions similar to Title III.[16] For example, Pennsylvania Statute Title 18, section 5703, also at issue in *Bartnicki*, is nearly identical to the federal anti-wiretapping statute. Both the federal and Pennsylvania anti-wiretapping statutes outlaw the dissemination of illegally intercepted communications.[17] Under both statutes, it is irrelevant that the defendant did not participate in the wiretapping activity;[18] a person who disseminates information violates the anti-wiretapping statutes so long as she "knew or had reason to know" that the communication was illegally acquired.[19] This is precisely the issue in *Bartnicki*.

II. CASE SUMMARY

In May of 1993, teacher's union negotiator, Gloria Bartnicki, called union president, Anthony Kane, on a cellular phone and engaged in a colorful conversation about ongoing negotiations with the local school board.[20] At one point, Kane suggested "blow[ing] up the front porches" of school board members to motivate negotiations.[21] An unidentified party intercepted and recorded the call and anonymously delivered a tape to Jack Yocum, the president of a taxpayers association opposed to the demands of the teacher's union.[22] Yocum then distributed the recorded con-

13. 18 U.S.C. 2511(2) (2001).

14. 18 U.S.C. 2511(4) and (5) (2001).

15. Specifically, §2511(1)(c) prohibits "intentional[ly] disclos[ing], or endeavor[ing] to disclose, to any other person the contents of any wire, oral, or electronic communication, knowing or having reason to know that the information was obtained through the interception of a wire, oral, or electronic communication in violation of this subsection . . ." 18 U.S.C. 2511(1)(c).

16. Brief for Petitioner at addendum, Bartnicki v. Vopper, 53 U.S. 514 (2001) (Nos. 99-1687 and 99-1728) (listing the homologous statutes in all 50 U.S. states).

17. *Bartnicki*, 53 U.S. at 526.

18. 18 U.S.C. § 2511(1)(c) (2001) and 18 PA. CONS. STAT. § 5703(a) (2001).

19. Other sections of the statutes qualify the prohibition against use and dissemination to make limited exceptions in the case of law enforcement. *See, e.g.*, 18 U.S.C. § 2516(1) (". . . judge may grant in conformity with section 2518 of this chapter an order authorizing or approving the interception of wire or oral communications by the Federal Bureau of Investigation . . .").

20. *Bartnicki*, 53 U.S. at 517.

21. *Id.*

22. *Id* at 518.

versation to two members of the media, including radio talk-show host Fredrick Vopper.[23] Vopper later broadcast the intercepted conversation during a radio program discussing the school board negotiations.[24]

Bartnicki and Kane brought an action against Yocum, Vopper, and other representatives of the media, alleging a violation of federal and state anti-wiretapping statutes.[25] The District Court denied both sides' motions for summary judgment, holding that imposing liability on Vopper and other media defendants would not violate the First Amendment.[26] However, the District Court certified two questions for appeal: first, whether the anti-wiretapping statutes violate the First Amendment by prohibiting broadcast of newsworthy information, when the information was illegally intercepted but not by agents of the broadcasters. Second, do the anti-wiretapping statutes violate Yocum's First Amendment rights by prohibiting him from distributing the anonymously intercepted information to media defendants?[27]

On appeal, the Third Circuit Court of Appeals reversed, finding that the anti-wiretapping statutes deterred significantly more speech than necessary to protect the privacy interests at stake.[28] The Supreme Court granted certiorari.[29]

A. Supreme Court's Analysis

In a six to three decision, the Supreme Court affirmed the Appellate Court's decision, holding that First Amendment protection extends to the dissemination of illegally intercepted communications if they were lawfully obtained and relate to a matter of public concern.[30] First, the Court determined that strict scrutiny was the most appropriate standard of review for a First Amendment analysis of the anti-wiretapping statutes.[31] Second, the Court placed *Bartnicki* in the context of the *Daily Mail* line of cases that limit restrictions on the publication of matters of public concern.

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23. *Id.* Vopper's talk-show persona is Fred Williams.

24. *Id.*

25. *Id.* The state statute is 18 PA. CONS. STAT. § 5703 (2001). Both state and federal statutes are also known as wiretapping statutes or anti-wiretapping statutes.

26. Bartnicki v. Vopper, 200 F.3d 109, 113 (3d Cir. 1999).

27. *Id.* at 113-14.

28. *Id* at 129.

29. Bartnicki v. Vopper, 530 U.S. 1260 (2000) *cert. granted.*

30. *See Bartnicki*, 53 U.S. at 533-34.

31. The First Amendment of the U.S. Constitution provides in part that "Congress shall make no law... abridging the freedom of speech, or of the press." U.S. CONST. amend. I.

1. Strict scrutiny is appropriate for "pure speech."

Two standards of review determine if a particular statute unconstitutionally restricts speech under the First Amendment: strict scrutiny and intermediate scrutiny.[32] A statute is subject to strict scrutiny when it is either facially discriminatory or was enacted with a discriminatory motivation of singling out and restricting constitutionally protected speech.[33] This test is often described as looking for "content-based" restrictions on free speech.[34] A statute subject to strict scrutiny is only valid if it is "necessary to serve a compelling state interest and... [it is] narrowly drawn to that end."[35]

Intermediate scrutiny, on the other hand, does not have a presumption of First Amendment invalidity, but is instead a balancing test. Courts applying intermediate scrutiny seek to balance explicit government interests against the right of free expression.[36] Intermediate scrutiny is generally appropriate where the government aims to regulate the non-communicative effect of an act,[37] such as a statute aimed at reducing littering by banning the distribution of handbills.[38] Thus, intermediate scrutiny is appropriate for so-called "content neutral" restrictions on speech.[39] In such cases, "the correct result... reflects some 'balancing' of the competing interests."[40]

Determining the appropriate level of scrutiny is important and often difficult. As a further complication, the Court has irregularly supplemented the content-neutral/content-based test with a distinction between laws that regulate "speech" and laws that regulate "conduct."[41] Unfortunately, the Court has not consistently explained exactly what this distinction means.[42] "Conduct" is usually described as physical actions, and

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32. LAWRENCE TRIBE, AMERICAN CONSTITUTIONAL LAW, 794. (2d ed. 1988).

33. *See id.*

34. *See Bartnicki*, 53 U.S. at 525-26.

35. TRIBE, *supra* note 32, at 799 (quoting from Perry Educ. Ass'n v. Perry Local Educators' Ass'n, 460 U.S. 37, 45 (1983)).

36. *Id.* at 791.

37. *See* TRIBE, supra note 32, at 798 n.17 (intermediate scrutiny is appropriate when the government is regulating the speech *regardless* of the content).

38. *See, e.g.,* Schneider v. State, 308 U.S. 147 (1939) (purpose of keeping streets clean is insufficient grounds for prohibiting public distribution of handbills).

39. *See Bartnicki*, 53 U.S. at 543-45 (Rehnquist, C.J., dissenting).

40. TRIBE, *supra* note 32, at 791.

41. *See id.* at 825-32.

42. Professor Tribe vehemently criticizes the speech/action distinction as having no analytical substance, and being *impossible* for the Court to ever clearly define. *Id.* at 830.

"pure speech" is usually described as a communicated idea.[43] Generally, the more a statute impinges on "pure speech," the more likely strict scrutiny applies.[44] Electing either strict or intermediate scrutiny can critically sway the Court's determination of the validity of a statute.

The *Bartnicki* Court agreed with the petitioners that the anti-wiretapping statutes were "content neutral," but still applied strict scrutiny.[45] The majority affirmed the Third Circuit's finding that the wiretapping statues were prohibitions of "pure speech," similar to "the delivery of a handbill or pamphlet," and thus are the kind of speech that the First Amendment is intended to protect.[46] Furthermore, the Court concluded that *Bartnicki* fit within existing case law where strict scrutiny was appropriate.[47]

2. *Bartnicki fits within the Daily Mail Line of Cases*

The second step in the Court's analysis was to examine related case law. The majority relied on *New York Times Co. v. United States*[48] and the *Daily Mail* cases.[49] The *Daily Mail* line of cases expanded the media's First Amendment protections when publishing truthful information concerning a matter of public significance—even when state law protects the information.[50] Following the *Daily Mail* line of cases, the Court held that the anti-wiretapping statute at issue in *Bartnicki* was too restrictive in prohibiting publication of truthful information on matters of significant public concern.[51]

In *New York Times*, the Court held that the government could not prohibit the publication of information of public concern, even when the information had been stolen by a third party.[52] The New York Times and the Washington Post violated an injunction against publishing excerpts of the "Pentagon Papers" that had been illegally leaked to them by a former gov-

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43. *See id* at 826.

44. *See* Note, *The Content Distinction in Free Speech Analysis after Renton*, 102 HARV. L. REV. 1904 (1989).

45. *See* Bartnicki v. Vopper, 53 U.S. 514, 525-27 (2001).

46. *Id.* at 526-27.

47. *See id.*

48. 403 U.S. 713 (1971).

49. *See supra* note 6.

50. *See Bartnicki*, 53 U.S. at 526-28. The "protection" applied in each case is different. In *Florida*, it was statutory protection of the identity of rape victims; in *Landmark* it was statutory protection of a state judicial inquiry; and in *Daily Mail* it was statutory protection of the identity of juvenile criminal offenders. *Bartnicki* is the statutory protection of illegally acquired information.

51. *See id.* at 528-31.

52. 403 U.S. at 714.

ernment employee.[53] *New York Times* was concerned predominantly with prior restraints on free speech. The case enhanced the press' First Amendment protections when publishing truthful information of public concern.[54]

This theme was extended in *Landmark Communications, Inc. v. Virginia.*[55] The *Landmark* Court held unconstitutional a Virginia statute that made it illegal to divulge information regarding the proceedings of a state judicial inquiry.[56] The Virginia-Pilot Newspaper had published an article that accurately reported on a pending inquiry by the Virginia Judicial Inquiry and Review Commission.[57] The Court subjected the Virginia statute to strict scrutiny and held that only a showing of "clear and present" danger to the administration of justice could justify the restriction on free speech that the statute created.[58] The Court again held that it was unconstitutional to penalize a third party for publishing truthful information of public interest.[59]

Similarly, in *Smith v. Daily Mail Publishing Co.*,[60] the Court invalidated a West Virginia statute making it a crime for a newspaper to disclose the name of any youth charged as a juvenile offender.[61] Under strict scrutiny, the Court held that when "a newspaper lawfully obtains truthful information about a matter of public significance then state officials may not constitutionally punish publication of the information, absent a need to further a state interest of the highest order."[62] This is known as the *Daily Mail* principle.[63]

Finally, the Court in *Florida Star v. B.J.F.*[64] explicitly reaffirmed *Daily Mail* and *Landmark*, overturning a state law that made it illegal to publish a rape victim's name in "any instrument of mass communica-

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53. The "Pentagon Papers" revealed classified government material on policy-making in Viet Nam. *See* RONALD D. ROTUNDA AND JOHN E. NOWAK, 4 TREATISE ON CONSTITUTIONAL LAW: SUBSTANCE AND PROCEDURE § 20.17 (3d ed. 1999).

54. *See id.*

55. 435 U.S. 829 (1978).

56. *See id.* at 845-46.

57. *Id.* at 831.

58. *See id.* at 837-38, 844.

59. *See id.* at 839.

60. 443 U.S. 97 (1979).

61. *Id.* at 105-6.

62. *Id.* at 103.

63. Cherly M. Sheinkopf, *Balancing Free Speech, Privacy and Open Government: Why Government Should Not Restrict the Truthful Reporting of Public Record Information*, 44 U.C.L.A LAW REV 1567, 1574 (1997).

64. 491 U.S. 524 (1989).

tion."[65] The Florida newspaper had obtained and published a rape victim's name from the police as a result of an administrative error.[66] The Court, applying the same strict scrutiny standard and rationale as in *Daily Mail*, held that a flat prohibition on publishing such information was unconstitutional because it was not a narrowly tailored means of achieving the state's interest in protecting the rape victims.[67]

3. *The Holding of Bartnicki*

The Court found the anti-wiretapping statutes unconstitutional because the state's asserted interests in enforcing the statutes did not sufficiently justify the prohibitions against free speech.[68] First, the Court was unconvinced that applying the anti-wiretapping sanctions against publishers innocent of the wiretapping would deter the unlawful conduct by the party that actually intercepted the communication.[69] The punishment is too remote to the offending eavesdropper.[70] Furthermore, the Court found no empirical evidence that the statute had actually deterred illegal wiretapping.[71] Second, although the Court acknowledged that privacy is an important interest, it declared that privacy concerns may give way to a compelling public interest in the illegally acquired information.[72] This is supported by the *Daily Mail* principle, as well as by an implicit belief that public figures, even limited public figures as in *Bartnicki*, are subject to a higher level of public interest.[73]

Under *Bartnicki*, when a publisher has obtained an illegal communication in a manner lawful in itself, but from a source who has obtained it

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65. *Id.* at 526.

66. *Id.* at 526-28.

67. *See id.* at 541.

68. *See Bartnicki v. Vopper*, 53 U.S. 514, 529-32. Under strict scrutiny, a statute is constitutional under the First Amendment if the state's interest that justifies the statute outweighs the restrictions on free speech, and only when the statute is narrowly drawn to achieve those interests. *Id.*

69. *See id.* at 531.

70. *Id.* at 529-30.

71. *Id.* The Court rejected the argument that the anti-wiretapping law would "dry up the market" for illegally intercepted communications by making disclosing them illegal. *Id.* at 526.

72. *Id.* at 532-34. The Court does not explicitly define what matters are of public or general interest, a lack that the dissent criticizes. *Id.* at 542 (Rehnquist, C.J., dissenting).

73. *See id.* at 527-28 (citing *N.Y. Times Co. v. Sullivan*, 376 U.S. 254 (1964) and related cases); *see also id.* at 534 ("[M]onths of negotiations over the proper level of compensation for teachers at the Wyoming Valley West High School were unquestionably a matter of public concern, and respondents were clearly engaged in a debate about that concern."); *Id.* at 535 (Breyer, J., concurring).

unlawfully, the government may *not* punish the ensuing publication of that information based on a defect in the chain.[74] The *Bartnicki* Court limited its holding in four ways: (1) the publisher must have played no part in intercepting the conversation; (2) the publisher must have acquired the information lawfully; (3) the published information must concern a matter of public concern; and (4) the information must be truthful.[75] In a strongly worded concurring opinion, Justice Breyer agreed with the majority's limitations, but narrowed the holding even further.[76]

4. *Breyer's concurrence and Rehnquist's dissent: reinterpreting Bartnicki*

Justices Breyer and O'Connor concurred with the majority, while Chief Justice Rehnquist, joined by Justices Scalia and Thomas, dissented.[77] Breyer's concurrence calls for the application of a more equitable test than the majority applied, balancing "speech-restricting and speech-enhancing consequences" of the statute.[78] The concurrence repeatedly emphasizes that *Bartnicki* must be limited to the facts of the case, and specifically to instances where the disclosed communication exposed a threat of personal harm.[79] Thus, the concurrence recasts *Bartnicki's* holding quite narrowly.

In his dissent, Chief Justice Rehnquist argued that the majority blatantly misapplied the standard of review, and thus reached the wrong conclusion. He asserted that the anti-wiretapping statutes should have been found constitutional under intermediate scrutiny.[80] The dissent found no justification for strict scrutiny, and distinguished the *Daily Mail* cases.[81] Unlike *Bartnicki*, the *Daily Mail* cases concerned content based censorship, and the information in the *Daily Mail* cases was publicly available and was lawfully obtained.[82] Thus, the anti-wiretapping statutes should

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74. *Id.* at 527 (quoting from *Boehner v. McDermott*, 191 F.3d 463, 484-85 (1999) (Sentelle, J., dissenting)).

75. *Id.* at 525-28.

76. *See id.* at 540-42 (Breyer, J. concurring).

77. *Id.* at 535-36 (Breyer, J. concurring), 541 (Rehnquist, C.J., dissenting).

78. *Id.* at 537 (Breyer, J., concurring).

79. *See id.*

80. *Id.* at 544 (Rehnquist, C.J., dissenting).

81. *Id.* at 541-46 (Rehnquist, C.J., dissenting).

82. *Id.* The third point (censorship of the media) arguably does not distinguish the *Daily Mail* cases from *Bartnicki*, as it was also about censorship of the media. Rehnquist's point may be a more sophisticated argument about scienter. The anti-wiretap laws of Bartnicki only circumscribes a publisher when she is aware that the information was illegally acquired. Thus, it is not absolute censorship, as in the *Daily Mail* cases, but it is qualified censorship.

have been subjected to intermediate, not strict, scrutiny since *Bartnicki* dealt with content-neutral regulations of speech.[83] Under intermediate scrutiny, the state's interest in protecting privacy by the anti-wiretapping statutes outweighs the publisher's interests in disseminating the information.[84] Therefore the anti-wiretapping statutes should have been found constitutional.

The dissent predicted that *Bartnicki* would have a profound chilling effect on the speech of "millions of Americans who rely upon electronic technology to communicate each day."[85] However, an analysis of *Bartnicki* does not support this dire prediction.

III. ANALYSIS

This section of the paper will argue that *Bartnicki'si* decision is limited utility for a variety of reasons. First, *Bartnicki* gives only minimal guidance to lawmakers and courts. Two key terms in the *Bartnicki* holding are left undefined: the class of information that is of "public concern" and the type of "publication" justifying First Amendment protection. Second, the *Bartnicki* Court intentionally restricted the scope of the holding. *Bartnicki* could have broadly extended First Amendment protection to all downstream publishers of protected information. For example, trade secrets are protected by statutes that are quite similar in scope and language to the anti-wiretapping statutes found unconstitutional by *Bartnicki*.

Finally, the *Bartnicki* decision is fragile because the Court fails to adequately justify its choice of strict scrutiny and because Justices Breyer's concurrence narrowly recasts the holding. *Bartnicki* rests on unstable ground in the current political climate calling for increased media accountability. Taken together, the ambiguity, limited scope, and fragility of the *Bartnicki* decision result in a holding that is of questionable long-term utility to courts and lawmakers.

A. What constitutes "public concern," and who is a publisher under *Bartnicki*?

Bartnicki may give First Amendment protection to a publisher who played no part in illegally acquiring information if the published informa-

83. *Id.* at 547 (Rehnquist, C.J., dissenting).

84. *Id* at 549-53 (Rehnquist, C.J., dissenting). The statute "dries up the market" for illegal wiretaps. The dissent also argues that the state's interest was even greater given the clandestine nature of wiretap activity, and the difficulty of enforcing the statute against those directly responsible for the activity. *Id.* at 551.

85. *Id.* at 542 (Rehnquist, C.J., dissenting).

tion is of public concern. But *Bartnicki* gives little guidance in understanding what constitutes "public concern," and who is a publisher. The Court alternatively used the terms "public interest," "public importance," and "general interest" to describe public concern.[86] It was obvious to the Court that the intercepted conversation discussing the teacher's union negotiations was of public concern, but it is not so obvious how the Court reached this conclusion. There are legal frameworks that a court could adapt to determine if speech is of public concern, including newsworthy speech, and private speech or right-to-publicity speech.[87] However, the majority did not clearly define this crucial term, a lack the dissent was quick to note.[88]

Furthermore, it is not at all apparent that the "public concern" standard in *Bartnicki* should in fact be identical to the "newsworthy" standard alluded to by the *Daily Mail* line of cases. The information at issue in *Bartnicki* was fundamentally different from the information at issue in the *Daily Mail* cases because it was illegally acquired. It is impossible to separate the fact that the information was illegally acquired from the essence of the information.[89] Some information is "newsworthy" only because it was illegally acquired from a speaker who thought that he was speaking privately.

Justice Breyer's concurring opinion heightens the confusion. The concurrence recast *Bartnicki's* holding by restricting the definition of "public concern" to "a threat of potential physical harm to others."[90] This suggests that information of "public concern" should be limited to disclosures regarding public health or safety such as the commission of a crime or a tort.[91] Significantly, these limitations are only articulated by Breyer's concurring opinion, and not by the majority.[92]

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86. *Id.* at 533-34. (reserving the question of whether "trade secrets" or pure "gossip" are matters of significant enough concern to merit first amendment protection).

87. *See generally* William E. Lee, *The Usual Suspects: Journalists as Thieves*, 8 WM.& MARY BILL RTS. J. 53 (1999) (describing newsworthy and public speech); Justin H. Wertman, *The Newsworthiness Requirement of the Privilege of Neutral Reportage is a Matter of Public Concern*, 65 FORDHAM L. REV. 789 (1996) (discussing constitutional classifications of speech).

88. *See Bartnicki*, 53 U.S. at 542 (Rehnquist, C.J., dissenting).

89. *See id.* at 545 (Rehnquist, C.J., dissenting).

90. *Id.* at 536 (Breyer, J., concurring).

91. *See id.* at 537-38 (Breyer, J., concurring). Breyer's definition of "public concern" is much more restrictive than a "newsworthy" test for speech of "public concern."

92. *See id.* The strong wording of Breyer's concurring opinion on this matter is noteworthy. The outcome of Bartnicki might have been much different had Stevens been more explicit in defining "public concern" more broadly.

The second undefined element of *Bartnicki* is the publication requirement. Knowing what constitutes adequate publication is critical, because the *Bartnicki* Court asserted that publishing matters of public importance could outweigh privacy concerns.[93] This implies that First Amendment protection is appropriate only because the public is informed of an especially relevant matter. It remains unclear whether First Amendment protection only extends to those who disseminate information broadly.[94]

Clearly, the Bartnicki holding is not limited to traditional media publishers.[95] The Court "dr[ew] no distinction between the media respondents and Yocum [the private citizen who anonymously received the illegally intercepted phone call]."[96] Yocum cannot be considered a "publisher" in the traditional sense, although he did provide the press with copies of the illegal communication. If Yocum is a publisher under *Bartnicki*, his distribution of the illegal information was extremely limited.[97]

Unlike the *Daily Mail* cases, the published information in *Bartnicki* was inherently illegal, by action of the anti-wiretapping statutes, and dissemination was *also* outlawed.[98] Ironically, under *Bartnicki*, publication "cleanses" the illegal status of the intercepted information, assuming that it meets the "public interest" test. As a consequence, *Bartnicki* might require some minimum audience in order for First Amendment protection to forgive the dissemination of the illegal communication.

Until *Bartnicki*, the *Daily Mail* principle was consistently restricted to traditional news media. Although Yocum is not clearly a "publisher," it is likely that the Court still grants him the First Amendment protections offered to traditional publishers because his actions led directly to publica-

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93. *Id.* at 534-35.

94. Under *Bartnicki*, how broad is broad enough to justify First Amendment protection over an individual's privacy rights? The answer to this question depends on the definition of "public concern" chosen. For example, under the "threat of physical harm" test for "public concern" of Justice Breyer's dissent, adequate publication might be simply informing the threatened parties.

95. The Internet has eliminated most barriers to entry in the publication arena. Virtually anyone can become a "web publisher" by posting a web page. The role that the *Daily Mail* principle and *Bartnicki* may play in the first amendment protections of a web publisher are discussed infra.

96. *Bartnicki* at 525 n.8. Note that the anti-wiretapping statutes make disclosure to anyone (even a single individual) illegal. 18 U.S.C. § 2511 (2001).

97. Yocum distributed the tape only to Vopper, though he played it for other members of the school board. *Bartnicki*, 53 U.S. at 518-519. It is unclear under *Bartnicki* if Yocum would be entitled to First Amendment protection had Vopper not played it on the air and given it to other media defendants.

98. 18 U.S.C. § 2511(1)(c) (2001); 18 PA. CONS. STAT. § 5703 (2001).

tion.[99] Thus, in the wake of *Bartnicki*, enforcement of anti-wiretapping statutes will require a case-by-case analysis, balancing the public interest in the disclosure of illegally intercepted information against the privacy rights of the individual speaker. A court or legislature must decide to whom *Bartnicki* applies (particularly, who is the "publisher"), the nature of the "public interest" served by disseminating the illegal information, and possibly how effectively the information was disclosed. *Bartnicki* does not give clear guidance in these areas.

Despite these problems, the *Bartnicki* test does have advantages. First, the ambiguity of the holding makes it more adaptable; the lack of clear instructions from the Court allows lawmakers and lower courts greater freedom to interpret the meaning of "public concern" and "publisher." Assessing the public interest in the illegally acquired information on a case-by-case basis may be the best way to resolve such cases.[100] Further, the holding is sufficiently flexible to handle technological developments in communications and publishing technologies. But these benefits may be outweighed by further problems with *Bartnicki*'s holding.

Bartnicki raises questions about the meaning of "publisher" and the importance of the publication audience in determining the application of First Amendment protections. Internet publishing makes these questions particularly poignant. Virtually anyone with access to a computer can publish a web page with a potential audience numbering in the millions.[101] *Bartnicki* does not tell us if web publishers are eligible for the same protection under the First Amendment that is granted to traditional publishers.[102]

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99. *Bartnicki*, 53 U.S. at 525 n.8. It is interesting to speculate on Yocum's status had his communication in *Bartnicki* not led to publication. (Indeed, this was almost the case, as Vopper waited months until broadcasting the intercepted conversation.) Although widespread publication might not have occurred, Yocum did immediately play the tape for the other school board members (the ones "threatened" in the tape). Is this an adequate "publication" (particularly in light of the fact that the target audience was the public most likely to be interested in the illegal information)?

100. Paul M. Smith and Nory Miller, *When can the Courts Penalize the Press Based on Newsgathering Misconduct?* 19 COMM. LAW. 1, 29 (2001).

101. *See* Dick Morris, *Symposium: Democracy and the Internet,* 34 LOY. L.A. L. REV. 1033, 1033 (2001).

102. Web "publications" act and look like traditional media, and often serve the same functions of informing and entertaining. *See generally* Robert M. O'Neil, *The Drudge Case: A look At Cyberspace Defamation*, 73 WASH. L. REV. 623 (1998) (questioning legal ramifications of online publishing). But applying the "special" press privileges to web pages raises concerns about eroding the right to privacy. When each citizen can be his own "press," it is conceivable that First Amendment protections like the *Daily Mail* principle and the *Bartnicki* holding will swallow the right to privacy. *See* Floyd Abrams,

B. The Court explicitly limited *Bartnicki*.

The Court intentionally restricted *Bartnicki's* holding so that it would not expand the *Daily Mail* principle or affect trade secret law. *Bartnicki* presented a question that was reserved in the *Daily Mail* line of cases: is publication of truthful, yet illegally acquired information protected by the First Amendment when the publishing party played no part in the illegal acquisition? The *Bartnicki* Court could have powerfully restated the *Daily Mail* principle, but declined to hold so broadly.

In *Bartnicki*, the Court revisited the *Daily Mail* principle, but only expanded it in the narrowest possible manner. Abstracted, *Bartnicki* fits within the bounds of the *Daily Mail* line of cases in which a publisher is held statutorily liable for publication of "protected" information.[103] *Bartnicki* adapts the *Daily Mail* principle to the subset of cases where the published information was illegally acquired by a third party. Thus, the ultimate origin of the information does not matter under the *Bartnicki* enhancement of the *Daily Mail* principle. The Court intentionally rejected the broad interpretation that publication of truthful information is *always* protected by the first amendment.[104] Instead, *Bartnicki* is a small addition to the class of protections that that Daily Mail principle embraces.[105]

Under a slightly more expansive holding, *Bartnicki* could have invalidated provisions of many states' trade secret laws on constitutional grounds. Anti-wiretapping statutes and trade secret statutes are remarkably similar in their downstream treatment of information that they make ille-

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Transcript of the 1999-2000 Oliver Wendell Holmes Lecturer, 51 MERCER L. REV. 833, 843-845 (2000) (observing that expanding "press" privileges to internet publishers could (ironically) lead to a restriction of the First Amendment protections of the press, thereby inflicting serious harm to the public). Although the *Bartnicki* decision has been heralded as a victory for media advocates, there are serious questions about its effectiveness. *See, e.g.*, Tony Mauro, *Defining the Limits; Supreme Court to Rule on Broadcast of Illegally Taped Conversations*, THE QUILL, September 1, 2000, at 73.

103. As mentioned infra, the Dissent clearly disagrees with this logic, holding that *Bartnicki* is clearly distinguishable from the *Daily Mail* line of cases. The dissent holds a different view of the *Daily Mail* principle, and distinguishes *Bartnicki* on factual difference from the general fact of the *Daily Mail* line of cases. Ultimately, the Majority focuses on the more general principles involved. For example, a publisher is punished under state statue for publishing protected information. The Dissent declines to make this generalization. See *Bartnicki*, 53 U.S. at 545-46 (Rehnquist, C.J., dissenting).

104. *Bartnicki*, 53 U.S. at 529. Even this broad holding could have been modified by a requirement that the information be both truthful and "of public concern" or "public interest."

105. Prior to the *Bartnicki* decision, there was some speculation that the court's holding could dramatically expand the *Daily Mail* principle, perhaps by protecting the publication of *all* truthful information, regardless of its origin. Mauro, *supra* note 102, at 73.

gal. For example, the California version of the Uniform Trade Secret Act, like the anti-wiretapping act, prohibits the disclosure of trade secret information by a third party who "knew or had reason to know" that the information was illegally acquired.[106] Like the anti-wiretapping statute, the trade secret statute prohibits the publication of information that was illegally acquired even by otherwise innocent parties.[107] However, the *Bartnicki* Court explicitly set aside the issue of trade secrets.[108] Thus, *Bartnicki* was inapplicable in a recent California appellate trade secret case, *DVD Copy Control Ass'n v. Bunner*.[109]

C. *Bartnicki* is a Fragile Holding.

The vagueness of the holding in *Bartnicki* may eventually lead to its downfall. Because courts and legislatures may be uncertain as how best to apply *Bartnicki*, similar challenges are likely to occur. Furthermore, the Court, looking at a *Bartnicki*-like case, might reach a different outcome for numerous reasons. First, the majority opinion is weakened by the lack of a clear justification for the application of strict scrutiny in *Bartnicki*.[110] Although the anti-wiretapping statutes are admittedly "content neutral," the Court concludes that intercepted conversations are "pure speech" and therefore deserve strict scrutiny.[111] Only scant support is given for this conclusion.[112] It seems more likely that the Court is applying strict scrutiny because the facts of *Bartnicki* comport with the *Daily Mail* line of cases.[113] However, this is troublesome both procedurally and because

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106. Uniform Trade Secret Act of the California Civil Code §3426.1 (b) defines "misappropriation" as "Disclosure or use of a trade secret of another without express or implied consent by a person who. . . (B) At the time of disclosure. . . knew or had reason to know that his or her knowledge of the trade secret was: (i) Derived from or though a person who had utilized improper means to acquire it. . . " 5 CAL. CIV. CODE § 3426.1 (2001).

107. The anti-wiretapping statutes prevent disclosure of information from one who "know[s] or ha[s] reason to know that the information was obtained" illegally (through interception). 18 U.S.C. § 2511(1)(c) (2001).

108. *Bartnicki*, 53 U.S. at 533 ("We need not decide whether that interest is strong enough to justify the application of [the anti-wiretap statute] to disclosures of trade secrets. . .").

109. DVD Copy Control Ass'n v. Bunner, 93 Cal. App. 4th 648 n.7 (Cal. Ct. App. 2001) (finding that the *Bartnicki* was not applicable both because the Court in *Bartnicki* expressly declined to consider trade secret information and because *Bartnicki* was not a trade secret case).

110. *See Bartnicki*, 53 U.S. at 543-44 (Rehnquist, C.J., dissenting).

111. *Id.* at 525-26.

112. *Id.* at 544-45 (Rehnquist, C.J., dissenting).

113. This is never explicitly stated in *Bartnicki*. After holding that *Bartnicki* fit with the *Daily Mail* line of cases, the Court immediately applied strict scrutiny to *Bartnicki*

questions remain about the appropriateness of this categorization.[114] Moreover, the application of strict scrutiny in *Bartnicki* was arguably dispositive.[115]

Second, the concurring justices only conditionally agreed with the majority. Breyer and O'Connor's two votes were critical in achieving the majority. Had the majority opinion more explicitly embraced a broader definition of public concern, it seems likely that Breyer and O'Connor would have joined the dissent, and Rehnquist's opinion would have carried the *Bartnicki* decision.[116]

Finally, political and public opinion may be against First Amendment protection for the press. In the years immediately following the Watergate scandal, the public and political climate favored strengthening the rights of the press and making government less "opaque."[117] This is the atmosphere that helped engender the *Daily Mail* principle.[118] In recent years, however, this trend has been subsiding.[119] Following the September 11, 2001 terrorist attacks on the Pentagon and the World Trade Center, public support for limiting the access and the immunity of the press has increased.[120] Congress and the Executive Branch appear to be responding. For example, on October 26, 2001, the President signed into law a comprehensive anti-terrorism bill (USA Patriot Act of 2001) that includes provisions for increased governmental wiretapping and heightened penalties for security

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despite acknowledging that the anti-wiretapping statues were content-neutral. *Id.* at 525-26 and n.9.

114. *See id.* at 543-47 (Rehnquist, C.J., dissenting).

115. Certainly the dissent found it dispositive. *Id.* at 544-45 (Rehnquist, C.J., dissenting)

116. Indeed, it has been suggested that Stevens' published opinion was modified to accommodate Justices O'Connor and Breyer. This may be why Stevens's opinion does not explicitly state his standard of review (justifying strict scrutiny) as well as the uncertainty in describing "public interest." Cynthia Cotts, *Supremes Secretly Stiff the Press,* THE VILLAGE VOICE, June 12, 2001, at Nation 31.

117. *See* Cotts, *supra* note 116, at Nation 31; Symposium, *Undercover Newsgathering Techniques: Issues and Concerns: Media Misbehavior and the Wages of Sin: The Constitutionality of Consequential Damages for Publication of Ill-Gotten Information,* 4 WM. & MARY BILL OF RTS. J. 1111 (1996) (discussing the role of the media in the pubic realm).

118. *See generally* Sheinkopf, *supra* note 63 (examining legislative restrictions on speech and the public record).

119. Cotts, *supra* note 116, at Nation 31.

120. *See, e.g.,* James R. Lorence, Editorial, *Public Pulse: CNN Crosses line,* OMAHA WORLD-HERALD, October 22, 2001 Sunrise edition at 6B; Jeff Zeleny, *Print Media Asked to Edit bin Laden,* CHI. TRIB., October 12, 2001, at N2; Carolyn I. Jones, Letters to the Editor, *Press Was Irresponsible to Report Bush's Location,* THE COLUMBUS DISPATCH, September 28, 2001, at 10A.

"leaks."[121] In an atmosphere of heightening privacy, particularly governmental privacy, cases like *Bartnicki* that are on the borders of First Amendment protection may have to contract.

IV. CONCLUSION

Bartnicki provides that publishers who knowingly publish illegally intercepted communications, where they had no part in the interception, might be protected under the First Amendment so long as the published information is of significant public concern. However, this holding is likely to be of only limited value. The *Bartnicki* holding is vague and difficult to apply since the critical tests for "information of public concern" and "publication" are undefined. Moreover, although *Bartnicki* is an extension of the *Daily Mail* principle, the Court deliberately limited the scope of the holding. *Bartnicki's* ultimate usefulness is limited because the vagueness of the holding invites future challenges likely to result in an even more restricted holding.

121. Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA Patriot Act) Act of 2001, S. 1510, 107th Cong. (2001).

ADDITIONAL DEVELOPMENTS—CONSTITUTIONAL LAW

AMERICAN CIVIL LIBERTIES UNION V. RENO

217 F.3d 162 (3d Cir. 2000)

At issue in this case was whether the Child Online Protection Act ("COPA") violates the First Amendment. Because the statute imposed an impermissible burden on protected speech, the Third Circuit affirmed the district court's decision granting the American Civil Liberties Union preliminary injunction to prevent the enforcement of COPA.

The American Civil Liberties Union ("ACLU") and several world wide web publishers brought action in the United States District Court for the Eastern District of Pennsylvania, challenging COPA's constitutionality and seeking to enjoin its enforcement. The district court entered a preliminary injunction preventing the government from enforcing COPA, holding that it placed too great a burden on protected expression. The court applied a two-part test to determine whether the statute is constitutional: (1) whether the statute is narrowly tailored to meet a compelling state interest, and (2) whether the statute is the least restrictive means to achieve that objective. In applying this test, the court reasoned that the high economic cost of implementing an age verification system and the ineffectiveness of such a system would cause web publishers to cease publishing such material or censor more material than necessary. Furthermore, less restrictive means, such as parental blocking and filtering software, would likely be as effective as COPA.

The Third Circuit upheld this decision. In applying the same test, it based its entire opinion on the constitutionality of the "contemporary community standards" clause to identify material that is harmful to minors in the context of the web. Any statute imposing a content-based restriction on speech is presumptively invalid and subject to strict scrutiny analysis. The court found that COPA creates an impermissible burden because current technology does not permit web publishers to geographically restrict access to their sites, and, consequently, requires them to abide by the most restrictive state's standards. This case was distinguishable, on the facts, from prior, non-web cases because, unlike mail or telephone mediums, the web was not geographically constrained. Defendants in prior non-web cases had the ability to geographically control the distribution of the controversial material, and were therefore not subject to the most restrictive state's standards.

The court distinguished this case from *United States v. Thomas*, 74 F.3d 701 (6th Cir. 1996), in which the Sixth Circuit held that the degree of harm caused by material on the defendant's electronic bulletin board must be judged by the standards of the community in which the disputed material was received. Unlike web publishers, bulletin board operators have control over the geographical distribution of their materials.

The court further determined that the statute was not readily susceptible to a narrow construction that would make it constitutional. The court rejected the government's argument that the "contemporary community standards" language should be interpreted by an "adult" rather than a "geographic" standard, noting that community standards had always been interpreted as a geographic standard. In addition, the court concluded that striking the "contemporary community standards" clause would not salvage COPA's constitutionality because the clause was an integral part of the statute.

The court concluded that granting the preliminary injunction would not violate the public's interest.

CYBERSPACE COMMUNICATIONS, INC. V. ENGLER

142 F. Supp. 2d 827 (E.D. Mich. 2001)

The United States District Court for the Easter District of Michigan considered whether a Michigan state law regulating the dissemination of sexually explicit materials to children violates the First Amendment and/or the Commerce Clause of the United States Constitution. On the First Amendment issue, the court applied a two-part test: (1) whether the statute is necessary to achieve a compelling state interest, and (2) whether the statute is narrowly tailored to achieve that result. The court held that the Act violated the First Amendment by placing undue content-based limitation on speech. Further the court held that because the Commerce Clause precludes the application of a state statute to commerce that occurs outside of a state's borders, Michigan's effort to regulate what information may be transmitted to Michigan's children via the Internet was in violation of the Commerce Clause.

Michigan's 1999 Public Act 33 ("the Act") contained provisions which pertain to dissemination of sexually explicit materials to children over the Internet. Internet companies and the American Civil Liberties Union ("ACLU") brought suit challenging the constitutionality of the Act, seeking to enjoin defendants from enforcing the Act. The district court issued a preliminary injunction on July 29, 1999. This decision was affirmed by the Sixth Circuit and remanded for further proceedings. On remand, the district court granted the plaintiff's motion for summary judgment that permanently enjoined the defendant from enforcing the Act.

The district court based its holding on the Act's undue content-based limitation on speech. The court recognized that the state had a compelling interest to protect minor children from exposure to obscene materials. However, the court found that the defendants failed to demonstrate that less intrusive means would not achieve similar restrictions. The court noted that filters, child-friendly software, or the on/off switch of the computer, all of which are less intrusive, would allow parents to control the information coming into their home via the Internet.

The district court further held that the Act violated the Commerce Clause, which precludes the application of a state statute to commerce occurring outside of a state's borders. The court found that by regulating information transmitted to Michigan's children via the Internet, the Act attempted to control Internet communications that might originate in states and countries outside Michigan. The court denied defendants' request to limit the relief to the challenged provisions of the Act, stating that courts would not "rewrite statutes to create constitutionality."

DENDRITE INTERNATIONAL, INC. V. DOE

342 N.J. Super. 134 (N.J. Super. Ct. App. Div. 2001)

The Superior Court of New Jersey ruled on the issue of whether the First Amendment protects speech in online chat rooms. Applying a case-by-case, multi-step test that analyzes and balances the equities and rights at issue, the court held that all forms of speech, including anonymous speech over the Internet, are protected.

Plaintiff is a publicly traded product and service company for pharmaceutical and consumer packaged goods. In its quarterly report to the Securities and Exchange Commission, plaintiff announced new licensing methods for its newer products. Some commentators viewed this announcement as a way to manipulate its future financial reports and to give the appearance of larger revenues despite no actual revenue increase. Individuals in online stock chat rooms derisively commented about plaintiff's announcement. Defendant placed nine such negative messages about the plaintiff in a Yahoo! chat room. Defendant's postings suggested that the plaintiff intentionally acted in bad faith by giving the appearance of earnings without improving the company. The plaintiff filed suit for defamation and misappropriation of trade secrets. During discovery, the plaintiff moved to obtain the defendant's identity from Yahoo!. The motion judge denied plaintiff's motion. The plaintiff's request for interlocutory appeal was granted.

The Superior Court of New Jersey upheld the motion judge's decision. The court held that the plaintiff must establish a *prima facie* case against the defendant in order to overcome the protection provided to the defendant by the First Amendment. The typical standard to evaluate a discovery request is a generous motion-to-dismiss standard. However, there is a higher burden of proof where the right to free speech is at risk. The plaintiff is required to show that an act giving rise to civil liability actually occurred and the discovery is aimed at revealing the identity of the person who committed the act. The court reasoned that the First Amendment protected all speech, including anonymous speech over the Internet. The court advised that trial courts must carefully balance the need for injured parties to seek redress and the essential right to anonymously participate in online forums.

DVD COPY CONTROL ASSOCIATION V. BUNNER

93 Cal. App. 4th 648 (Cal. App. 6th. 2001)

The Court of Appeal of California, Sixth Appellate District, examined whether the publication of decryption software on the Internet is protected by the First Amendment or violates the Uniform Trade Secrets Act ("UTSA"). The court held that the defendant's use of DeCSS was protected by the First Amendment.

Plaintiff DVD Copy Control Association ("DVDCAA") brought suit against the defendant, claiming that he had violated the UTSA and a click wrap license by using DVD decryption software called DeCSS to play an encrypted DVD on a system not controlled by the DVDCAA's content scrambling system ("CSS"), and by republishing or linking to DeCSS on the Internet. The defendant argued that enjoining him from disclosing DeCSS on the Internet would violate his First Amendment rights because it constituted an unconstitutional prior restraint. The Santa Clara County Superior Court granted DVDCAA a preliminary injunction, holding that CSS, which embodied DVDCCA's trade secret, had been reverse engineered. Since the UTSA allows for reverse engineering, the publication of CSS would only be illegal if the user was subject to the licensing agreement. That issue would not be resolved without discovery, but the balance of hardships favored a preliminary injunction for DVDCAA. The defendant would only have to remove the trade secret information from their websites and would be free to publicly debate the matter until resolved at trial. Without the injunction, however, the plaintiff may lose the trade secret permanently.

Bunner appealed the lower court's decision, claiming that he did not decrypt the software and that the First Amendment protected his publication of the decryption software on the web. He first claimed that he did not decrypt DVDCAA's software because the "master keys" on a CSS-encrypted DVD could be derived exclusively from the DVD itself without recourse to decryption technology. General copying of DVDs was not feasible because removal media did not have the capacity to hold the enormous files necessary for movies. Second, Bunner argued that he republished the DeCSS source code on his website so programmers could improve the code and Linux users could use it to play DVDs. At the time, he had no knowledge that CSS contained trade secrets, and believed that it had been created either independently or through legal reverse engineering. Furthermore, he contended that CSS was no longer a trade secret because it had been previously published on the Internet.

The Fourth Circuit reversed the lower court on two grounds—the UTSA's "improper means" requirement and the First Amendment. The UTSA prohibits appropriation of trade secrets by "improper means." A plaintiff claiming misappropriation has the burden of identifying those trade secrets. While Bunner did not use improper means to obtain DVDCCA's proprietary information, DVDCCA would likely have proven that Bunner knew CSS was a trade secret. However, the court concluded that DeCSS is speech and, therefore, protected by the First Amendment. While source code can be compiled, it retains its fundamentally expressive nature and remains the preferred mode of communication among programmers. The preliminary injunction was overturned, because it unduly restrained free speech.

ELDRED V. RENO

239 F.3d 372 (D.C. Cir. 2001)

The United States Court of Appeals for the District of Columbia Circuit addressed Copyright Clause and First Amendment constitutional challenges to the Copyright Term Extension Act of 1998 ("CTEA"). The Court held that the statutory extension of copyright durations was constitutional.

Plaintiff, corporations, associations and individuals using works in the public domain for vocational and personal uses, filed suit against the Attorney General claiming that CTEA was unconstitutional. The plaintiffs alleged that the extension of copyright protection provided for in CTEA violated their First Amendment freedom of expression rights and conflicted with the Copyright Clause's goal of "promoting the Sciences and Useful Arts." The plaintiffs argued that: (1) the extension of copyright protection by CTEA violates freedom of speech under the First Amendment, (2) CTEA cannot retroactively extend already existing copyright protection because, as the work already exists, it lacks the originality required for the grant of copyright protection, and (3) CTEA violates the constitutional requirement that copyright protection endure for a "limited time." The district court entered judgment on the pleadings in favor of the defendant and dismissed the plaintiffs' claim in its entirety, holding that the extension is permissible since the "limited time" clause is subject to the discretion of Congress.

The D.C. Circuit affirmed the decision of the district court, holding that CTEA does not violate freedom of speech under the First Amendment because copyright protection only covers particular instances of expression and not the ideas expressed therein. Due to exceptions for expression based on the idea/expression dichotomy, the court held that copyrights are categorically immune from challenges under the First Amendment. Plaintiffs lack any cognizable First Amendment right to exploit the copyrighted works of others. Rejecting the plaintiffs' second argument, that existing works are not original for purposes of the extension of copyright protection, the court found that the test for originality only applies when the work is initially created. The fact that a work has copyright protection demonstrates that it fulfilled the originality requirement. Stating that the preamble to the Copyright Clause does not limit the power of Congress to define the duration of copyright protection, the Appellate court also rejected the plaintiffs' third contention. In sum, the Appellate court affirmed the district court's decision that the CTEA is a proper exercise of Congress's power under the Copyright Clause of the Constitution.

On February 19, 2002, the United States Supreme Court granted Plaintiffs' Petition for *Certiorari*.

GUEST V. LEIS

255 F.3d 325 (6th Cir. 2001)

The Sixth Circuit ruled on the protection afforded by the First and Fourth Amendments, the Electronic Communications Privacy Act ("ECPA") and the Privacy Protection Act ("PPA") for preventing the seizure of an entire computer when only a fraction of the information on it is connected to possible illegal activities.

Plaintiffs were users and operators of Internet bulletin board systems. The Regional Electronic Computer Intelligence Task Force ("RECI") downloaded obscene images from the bulletin boards. Based on these images, the RECI obtained search warrants and seized computer equipment associated with the bulletin boards. The plaintiffs brought suit against the RECI, the Sheriff, and the Sheriff's Department for violations of the First and Fourth Amendments, the ECPA and the PPA. The district court granted the defendants' motion for summary judgment on all claims. Plaintiffs appealed.

The Sixth Circuit affirmed the district court's decision. On the Fourth Amendment count, plaintiffs claimed that their expectation of privacy had been violated. The court held that there was no expectation of privacy when a privacy disclaimer is posted or when the information is provided to a third party, nor is there privacy for a delivered e-mail. Plaintiffs also claimed that the defendants exceeded the scope of the warrant. The court held that if the plaintiffs could not show that the defendants accessed files beyond those specified in the warrant, plaintiffs could not show invasion of privacy. Further, the court held that it is reasonable to seize an entire computer because it is difficult to search the computer in a suspect's home.

As to the First Amendment claim, plaintiffs alleged that the defendants unlawfully placed a restraint on their speech because the material in question had not yet been determined obscene in an adversarial proceeding. The court held that evidence for a criminal prosecution that would be preserved (i.e., not destroyed) need not first be determined obscene to avoid violation of First Amendment rights. The court ruled that governmental search with a warrant does not violate the privacy created by the ECPA. Regarding the PPA claim, the court held that when protected materials are co-mingled on a computer with criminal evidence, seizure of the computer is warranted; officials cannot, however, search PPA-protected materials.

KYLLO V. UNITED STATES

533 U.S. 27 (2001)

The Supreme Court decided whether law enforcement's use of thermal imaging on citizens' homes violates their Fourth Amendment rights. The Court held that "[w]here . . . the Government uses a device that is not in general public use, to explore details of the home that would previously have been unknowable without physical intrusion, the surveillance is a 'search' and is presumptively unreasonable without a warrant."

A United States Department of the Interior agent suspected defendant Danny Kyllo of growing marijuana in his home. Indoor marijuana growth requires high-intensity lamps that give off significant heat. To investigate the defendant, the agent used a thermal imager to search for heat emanating from the defendant's home. Upon collecting high thermal measurements, the agent used these measurements and additional evidence to secure a warrant to search the defendant's home. The search yielded 100 marijuana plants. The defendant was indicted on one count of manufacturing marijuana. The district court granted the defendant's motion to suppress the evidence from the search, and entered a conditional guilty plea. On appeal, the Ninth Circuit remanded for a hearing on the intrusiveness of thermal imaging. The district court then held that the thermal scan was nonintrusive, and, therefore, permissible, because it cannot penetrate into the structure or reveal intimate details of the home. The Ninth Circuit initially reversed, but the opinion was withdrawn. A subsequent Ninth Circuit panel affirmed the district court. This panel reasoned that the defendant showed no expectation of privacy because he did not conceal the heat escaping from his home, and that the thermal scan did not reveal intimate details of his life.

The defendant appealed. The Supreme Court reversed and held that the thermal imaging was an unlawful search. A Fourth Amendment search occurs when the government violates a subjective expectation of privacy which society recognizes as reasonable, as previously stated by the Court in *Katz v. United States,* 389 U.S. 347 (1967), a case involving the use of an electronic listening device. The Court viewed use of electronic listening devices, thermal imagers and satellite scans as unreasonable searches. When sense-enhancing technology is used to obtain information about the interior of the home that could not otherwise have been obtained without physical intrusion into a constitutionally protected area, and the technology used to search the home is not in general public use, an impermissible search has occurred.

The government argued that it only detected heat radiating off the walls of the house, and that this is different from sound traveling through the walls. The Court rejected this argument, stating that such a distinction is mechanical and would result in permitting searches with more sophisticated technology in the future. The Court further stated that all details of the home are intimate details because of their inaccessibility to government officials. "In the home, our cases show, *all* details are intimate details, because the entire area is held safe from prying government eyes." To consider some details of the home intimate and others not, would result in ambiguity for the courts and for law enforcement officials.

NATIONAL A-1 ADVERTISING, INC. V. NETWORK SOLUTIONS, INC.

121 F. Supp. 2d 156 (D.N.H. 2000)

The United States District Court for the District of New Hampshire ruled on the issue of whether Network Solutions, Inc.'s ("NSI") refusal to register second-level domain names under its "decency policy" violated the plaintiff's First Amendment rights. The court recognized no constitutionally protected right to include particular words or phrases in the space occupied by second-level domain names.

The plaintiff sought to register with NSI a number of domain names that contained allegedly offensive words. NSI refused to register those domain names under its decency policy. The plaintiff brought an action against NSI, seeking a declaration that NSI's refusal to register its proposed domain names violated its First Amendment right to freedom of speech.

The district court granted NSI's motion for summary judgment, and held that NSI's actions did not violate the plaintiff's First Amendment rights. The court noted the First Amendment only "proscribes governmental conduct, not conduct undertaken by private citizens," and that NSI was not a state actor at the time of registration. In its analysis, the court first noted there was no evidence that the government sought to evade its responsibilities by delegating them to private entities such as NSI. Second, there was no evidence that the government imposed any regulatory restrictions on registering second-level domain names. Finally, the court was not persuaded that the relationship between the government and NSI could properly be viewed as "symbiotic."

The court further held that even if NSI qualified as a government actor, it did not violate the plaintiff's First Amendment rights because the space occupied by second-level domain names was not designed, intended, or traditionally employed to act as a forum for speech. The court explained that second-level domain names essentially serve the utilitarian role of identifying computer addresses. "That some people might want to express points of view or attempt to convey a particular message by converting the second-level domain name space into a message-carrying vehicle, does not operate to convert that space into a 'forum' for speech."

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BUSINESS LAW

CONTRACTUAL ASSENT AND ENFORCEABILITY IN CYBERSPACE

By Ryan J. Casamiquela

Online vendors often seek to bind online consumers with contracts, frequently in the form of license agreements with standardized terms.[1] Importantly, online vendors differ in the manner in which they present their license agreements and consequently, in the amount of notice they provide their consumers. Some automatically splash their license on the screen and require consumers to click an "I agree" icon; others merely create a link to their license and do not require a clicking acceptance.[2] Courts have considered these various methods of online presentation, holding some licenses binding on consumers and others not.[3] Courts have begun to utilize

1. Online contractual agreements—particularly between businesses and consumers—often take the form of license agreements. Vendors use license agreements to avoid the first sale doctrine. *See infra* note 135. The first sale doctrine gives buyers "first sale" rights to use and/or distribute their particular copy of a copyrighted work. Using licenses, vendors avoid the first sale doctrine because they are "licensing" their product. Accordingly, vendors can impose terms and restrictions on how buyers use their particular copy. Online license agreements often have standardized terms, which commonly represent a unilateral list of terms that the consumer accepts on a "take-it-or-leave-it" basis. Because they are used in mass-market transactions, vendors argue that the standard lists ease transaction costs.

2. Some vendors worry that traffic and revenue would decrease if a license splashes on the user's screen and forces the user to click "I accept." If the vendor merely creates a link to the license and disregards a clicking acceptance, this would speed-up the transaction, maintain consumer interest, and ultimately, increase revenue. *See* IAN BALLON, E-COMMERCE AND INTERNET LAW § 27.03[2] (2001) (explaining how online businesses have to make choices in weighing the legal risks and their business objections).

3. *See, e.g.*, Specht v. Netscape Communications Corp., 150 F. Supp. 2d 585 (S.D.N.Y. 2001) (finding the online license unenforceable); In re Realworks, Inc. Privacy Litig., No. 00C1366, 2000 WL 631341 (N.D. Ill. May 8, 2000) (enforcing online license); Pollstar v. Gigmania, Ltd., 170 F. Supp. 2d 974 (E.D. Cal. 2000) (questioning the level of consumer assent in some online licenses); Register.com, Inc., v. Verio, Inc., 126 F. Supp. 2d 238 (S.D.N.Y. 2000) (enforcing the online license); Hotmail Corp. v. Van$ Money Pie, Inc., No. C 98-20064, 1998 WL 388389 (N.D. Cal. Apr. 16, 1998) (affirming online license as binding); Caspi v. Microsoft Network LLC, 732 A.2d 528 (N.J. App. Div. 1999) (upholding online license with "I agree" icon); Groff v. Am. Online Inc., No. PC 97-0331, 1998 WL 307001 (R.I. Super. May 27, 1998) (finding online license valid).

two broadly defined categories—clickwrap and browsewrap—in order to help characterize the various methods of presentation.[4]

A clickwrap license is an agreement in which the vendor requires the consumer to click an "I accept" icon or click-check an unchecked box for the agreement to take effect.[5] The vendor may place the icon at the conclusion of an agreement, where the consumer must scroll downward through the entire list of terms to click on it. Alternatively, a court will likely characterize an online license as a browsewrap if the vendor utilizes a small link to the license, instead of automatically presenting it.[6] Indeed, the vendor may even tuck the link in the corner of an interior webpage of the site so that consumers are unlikely to notice it. The characterization of an online license as either clickwrap or browsewrap is increasingly important because courts have found consumer assent to exist in the former, but not the latter.[7]

Beyond the recent cases dealing with online licenses, the case law surrounding shrinkwrap licenses is a useful guide to understanding what constitutes consumer assent in the online world.[8] Accordingly, Part I of this Note begins by analyzing the major cases surrounding shrinkwrap licenses and their relevance to licenses in cyberspace. Next, this Note discusses the recent decision in *Specht v. Netscape Communications Corp.*,[9] to understand how courts analyze what constitutes consumer assent online. Finally, this Note sets forth various methods courts may use to strike or modify terms of an online license, even where the court finds consumer assent to the overall agreement. These methods include the unconscionability doctrine, consumer protection statutes, and federal preemption. This Note contends that courts will likely continue to find consumer assent in clickwrap licenses, but should rely on methods for striking or modifying terms within an online license.

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4. *See, e.g.*, *Netscape*, 150 F. Supp. 2d 585; *Pollstar*, 170 F. Supp. 2d 974.

5. *See supra* note 3.

6. *See supra* note 4.

7. *See id.*

8. A shrinkwrap license is similar to an online license, in that it is a standard, unilateral list of terms that the consumer accepts on a "take-it-or-leave-it" basis. Like online licenses, shrinkwrap licenses are ubiquitous, used in mass-market transactions between producers and consumers. Consumers encounter shrinkwrap licenses after they purchase software either at a store or over the phone. When the consumer brings the software home (or receives the software via delivery), the consumer tears open the plastic shrinkwrap around the box or package. Inside the shrinkwrap, the consumer will discover the "shrinkwrap license" and can finally read its terms.

9. 150 F. Supp. 2d 585.

I. LEGAL BACKGROUND

Outside cyberspace, software vendors use shrinkwrap licenses. Like an online license, a shrinkwrap license represents a standard, unilateral list of terms the consumer accepts on a "take-it-or-leave-it" basis.[10] Software vendors typically enclose shrinkwrap licenses within the software packages consumers purchase.[11] Courts addressing consumer assent online have cited and relied upon the case law surrounding shrinkwrap licenses.[12]

A. Early Law Surrounding Shrinkwrap Licenses

In the late 1980s and early 1990s, a few courts found shrinkwrap licenses unenforceable, based on a lack of consumer assent.[13] For example, in *Step-Saver Data Systems, Inc. v. Wyse Technology,*[14] the Third Circuit relied on section 2-207 of the Uniform Commercial Code ("UCC") to hold that buyer Step-Saver failed to assent to seller The Software Link's ("TSL") shrinkwrap license.[15]

The court's analysis turned on which party was the offeror and which was the offeree.[16] The court held that buyer Step-Saver was the offeror, and that seller TSL was the offeree.[17] Specifically, the court reasoned that Step-Saver made a telephone offer to buy the merchandise, and that vendor TSL accepted Step-Saver's telephone offer when TSL initiated the software shipment.[18] At this point, Step-Saver and TSL had a contract,

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10. An important difference between a shrinkwrap license and an online license is that the online presentation gives the consumer the theoretical opportunity to read the license agreement *before* any exchange of money and product takes place.

11. Transactions between merchants, however, may involve more negotiation over terms. For example, a party could bargain for a limited duration of use and installment payments covering the time and use of the product. Arguably, this type of transaction more accurately describes a "licensing" transaction. *See* Microsoft Corp. v. DAK Indus., 66 F.3d 1091 (9th Cir. 1995); Softman v. Abode, No. CV 00-04161, 2001 WL 1343955 (C.D. Cal., Oct. 19, 2001).

12. *See, e.g.*, *Netscape*, 150 F. Supp. 2d 585; *Pollstar*, 170 F. Supp. 2d 974.

13. *See, e.g.*, Step-Saver Data Sys. v. Wyse Tech., 939 F.2d 91 (3rd Cir. 1991); Arizona Retail Sys., Inc v. Software Link Inc., 831 F. Supp. 759 (D. Ariz. 1993); *see also* Vault Corp. v. Quaid Software Ltd., 847 F.2d 255 (5th Cir. 1998) (using federal law to preempt a state statute that allowed vendors to use shrinkwrap licenses with terms in direct conflict with federal policy).

14. 939 F.2d 91.

15. 939 F.2d at 94.

16. *Id.* at 98.

17. *Id.*

18. *Id.*

with both explicit and implicit terms.[19] Since the parties formed a contract during the telephone conversation, the court viewed the shrinkwrap license enclosed in the later shipment as an attempt to modify the terms of the existing contract.[20] Since the enclosed shrinkwrap license contained material terms to which the parties failed to agree, the court utilized UCC section 2-207(3) to strike the terms of the shrinkwrap license.[21] The court held that UCC "gap fillers" could replace the stricken terms.[22]

B. A Change in the Shrinkwrap Debate

In *ProCD, Inc. v. Zeidenberg*,[23] the Seventh Circuit found consumer assent to a shrinkwrap license. The decision dramatically influenced the debate surrounding the enforceability of shrinkwrap licenses.[24] The court distinguished this case from prior decisions, including *Step-Saver*, by noting the presence of a consumer and a vendor in the transaction, rather than two merchants.[25] Refusing to apply UCC section 2-207 to a consumer-

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19. *Id.* The court used UCC section 2-207(3) to hold that the *conduct* of both parties indicated that a contract had been formed at the conclusion of the telephone conversation, even though there was a lack of detailed terms and extensive writing between the parties.

20. *Id.* Although the case involved only one standardized form, the court saw the case as a modified version of the classic "battle of the forms" situation. *Id.* at 99 (arguing that there is no reason that the spirit of UCC section 2-207 cannot apply in situations involving only one form).

21. UCC section 2-207(3) provides:

> Conduct by both parties which recognizes the existence of a contract is sufficient to establish a contract for sale although the writings of the parties do not otherwise establish a contract. In such case the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of this Act.

UCC § 2-207(3) (2000).

22. 939 F.2d at 99. "Gap fillers" are supplementary terms incorporated under other provisions of the UCC. In short, they are default rules that provide, for example, minimum warranties under sections 2.314 and 2.315. *See id.*

23. 86 F.3d 1447 (7th Cir. 1996).

24. *See, e.g.*, Peerless Wall & Window Coverings, Inc. v. Synchronics, Inc., 85 F. Supp. 2d 519, 527 (W.D. Pa. 2000), *aff'd*, 234 F.3d 1265 (3rd Cir. 2000); M.A. Mortenson Co., Inc. v. Timberline Software Corp., 140 Wash. 2d 568 (2000). *But see* Klocek v. Gateway, Inc., 104 F. Supp. 2d 1332, 1339 (D. Kan. 2000). In *Klocek*, the court declined to enforce a shrinkwrap license, explicitly stating that it would not follow *ProCD*. The court employed a similar analysis to that in *Step-Saver*, and held that the offer and acceptance occurred at the moment the vendor initiated the shipment of the purchase. The court acknowledged that UCC section 2-207 generally applies to the "battle of the forms" situation, but then emphasized that "nothing in its language precludes application in a case which involves only one form." *Klocek*, 104 F. Supp. 2d at 1339.

25. 86 F.3d at 1452 (stating that *ProCD* was the first case to address directly the issue of the enforceability of a shrinkwrap license in a consumer transaction). Accord-

vendor transaction, the court found consumer assent under Wisconsin's version of UCC section 2-204.[26]

The court emphasized that the offeror, as the master of the offer, had the ability to dictate how and when an offeree accepts the offer.[27] First, in contrast to *Step-Saver*, the court concluded the vendor was the offeror.[28] Then, the court explained that "a vendor, as master of the offer, may invite acceptance by conduct, and may propose limitations on the kind of conduct that constitutes acceptance."[29] Vendor ProCD could propose the method by which the buyer would accept his offer. Consequently, ProCD dictated that the buyer's acceptance occurred after the purchase, when the buyer had the opportunity to review the shrinkwrap terms and failed to return the merchandise for a refund.[30] In contrast to *Step-Saver*, contract formation extended after the purchase, such that the shrinkwrap license was not a modification of an existing agreement, but instead contained important terms that completed the contract.[31]

In *Hill v. Gateway 2000 Inc.*,[32] the Seventh Circuit extended its holding in *ProCD*. The court emphasized that parties may form a contact through a layered process.[33] The buyer orders the product and the vendor initiates its delivery. Then, the buyer receives the delivery and, within a certain time frame (e.g., 30 days), inspects the enclosed shrinkwrap license.[34] If the buyer does not return the product within the stated period, the buyer assents to the shrinkwrap license and the parties finally form a contract.[35]

Under Uniform Computer Information Transaction Act ("UCITA"),[36] courts would enforce layered shrinkwrap licenses as found in *ProCD* and

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ingly, the Seventh Circuit distinguished itself from the prior decisions of *Step-Saver*, *Arizona Retail Systems, Inc. v. Software Link Inc.*, 831 F. Supp. 759 (D. Ariz. 1993), and *Vault Corp. v. Quaid Software Ltd.*, 847 F.2d 255 (5th Cir. 1998). *Id.*

26. *Id.*

27. *Id.*

28. *Id.*

29. *Id.*

30. *Id.* at 1452-53.

31. *Id.*

32. 105 F.3d 1147 (7th Cir. 1997).

33. *Id.* at 1150.

34. *Id.*

35. *Id.* at 1148. *See also* Brower v. Gateway 2000, Inc., 246 A.D.2d 246, 250-51 (N.Y.App. Div. 1998) (holding that shrinkwrap license terms delivered following a mail order are not modifications to the contract, but part of the original agreement between the parties still in the process of contract formation).

36. UNIF. COMPUTER INFO. TRANSACTIONS ACT, *available at* http://www.law.upenn.edu/bll/ulc/ucita/ucita01.htm (Aug. 23, 2001) [hereinafter

Hill.[37] Courts would also enforce online licenses under UCITA, presuming the vendor had required the consumer to manifest assent to its terms.[38] The future influence of UCITA is questionable, however. Although two states have adopted this model statute,[39] the vast majority of states have refused to consider it or have postponed its enactment indefinitely.[40] Even if states were to enact UCITA, federal law and policy could preempt it.[41]

UCITA]. UCITA, a model contract law statute promulgated by the National Conference of Commissioners on Uniform State Laws ("NCCUSL"), has sought to supplement Article 2 of the UCC. UCITA was promulgated to increase uniformity among the various jurisdictions, specifically in the context of transactions involving information technology. *See* Charles H. Fendell & Dennis M. Kennedy, *UCITA Is Coming!!! Part Two: Practical Analysis for Licensor's Counsel*, 17 COMPUTER LAW 3 (2000).

37. UCITA, *supra* note 36, § 208 cmt. 3 (supporting "layered contracting" as found in *ProCD* and *Hill*.)

38. Seemingly, a clickwrap license with an "I agree" icon or an unchecked box gives the consumer the opportunity to manifest assent under the statute. *See* UCITA *supra* note 36, § 208(1) ("A party adopts the terms of a record, including a standard form, as the terms of the contract if the party agrees to the record, such as by manifesting assent.").

39. Virginia has almost fully adopted UCITA, while Maryland's adoption is qualified. For a concise history and analysis on state responses to UCITA, see Brian D. McDonald, *The Uniform Computer Information Transactions Act*, 16 BERKELEY TECH. L.J. 461 (2001).

40. For a recent update on UCITA and its adoption, *See* Carol A. Kunze, *What's Happening to UCITA in the States, at* http://www.ucitaonline.com/whathap.html (last visited Jan. 25, 2002).

41. Some commentators believe that the Patent and Copyright Acts would preempt a state statute like UCITA. *See, e.g.*, David Nimmer, *The Metamorphosis of Contract into Expand*, 87 CAL. L. REV. 17 (1999) [hereinafter Nimmer, *Metamorphosis*]. To be clear, the viability of preemption of private agreements (like a shrinkwrap agreements) is unclear because of the right to contract. *See infra* Part IV.C.1. But, the possibility of federal preemption of state statutes is clear, especially if a court views a state law as in direct conflict with federal policy. *See* Computer Assocs. Int'l, Inc. v. Altai, Inc., 982 F.2d 693, 695-96 (2d Cir. 1992); Vault Corp. v. Quaid Software, Ltd., 847 F.2d 255 (5th Cir. 1988) (using the Copyright Act to preempt a state statute in conflict with an alleged reverse engineering policy surrounding section 117). *But see*, ProCD, Inc. v. Zeidenberg, 86 F.3d 1447, 1453-54 (7th Cir. 1996) (giving examples from criminal and trade secret law to assert that property rights can originate from both federal and state law); Raymond T. Nimmer, *Breaking Barriers: The Relations Between Contract and Intellectual Property Law*, 13 BERKELEY TECH. L.J. 827, 827-30 (1998) (viewing federal intellectual property as "default rules" working with and potentially altered by state contract law); Joel Rothstein Wolfson, *Contact and Copyright Are Not at War: a Reply to "The Metamorphosis of Contract into Expand,"* 87 CALIF. L. REV. 79 (1999).

C. The Relevance of *ProCD* in Cyberspace

The *ProCD* decision is the nearest a federal appeals court has come to addressing consumer assent in clickwrap and browsewrap agreements.[42] Although not a clickwrap or browsewrap license, the shrinkwrap license in *ProCD* has characteristics similar to those in cyberspace. In *ProCD*, for instance, the shrinkwrap license automatically presented itself on the consumer's computer screen after the software was loaded, but before the software would run.[43] The consumer could not bypass the license and use the program without indicating his acceptance of the license terms.[44] Thus, the shrinkwrap license in *ProCD* shares important characteristics with online clickwrap licenses.[45] In contrast, the shrinkwrap license in *Step-Saver* was in hardcopy form, enclosed within the delivered package.[46] Consequently, the software program did not require an indication of assent to run.

Furthermore, the *ProCD* court addressed the enforceability of a license agreement between a software vendor and a consumer.[47] The use of an online license—whether clickwrap or browsewrap—often involves transactions between a vendor and a consumer. In contrast, the transaction in *Step-Saver* included a software producer and a value-added retailer that integrated the software into a product to sell to consumers.[48]

In *Specht v. Netscape Communications Corp.*, the court found that the decision in *ProCD* had important implications for online agreements.[49] Accordingly, the court relied on precedent from the Seventh Circuit in *ProCD* to address the issue of consumer assent in cyberspace.

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42. Other Circuits have not expressly adopted the Seventh Circuit position regarding shrinkwrap licenses.

43. *ProCD*, 86 F.3d at 1452.

44. *Id.*

45. *See* Specht v. Netscape Communications Corp., 150 F. Supp. 2d 585, 595 (S.D.N.Y. 2001) (noting that the shrinkwrap license in *ProCD* has similar characteristics to online licenses). *See also infra* Part III.A.

46. 939 F.2d at 95-96.

47. *See supra* note 25.

48. 939 F.2d at 95.

49. 150 F. Supp. 2d at 592.

II. CASE SUMMARY

A. Facts of the Case

Defendant Netscape provided free copies of the software program "SmartDownload" on its website.[50] Visitors clicked on a box indicating a desire to download the Netscape software.[51] The software program proceeded to download itself onto visitors' hard drives.[52] Netscape argued that downloading the software indicated assent to the license on Netscape's website.[53] Netscape did not require visitors to click on an "I accept" button or otherwise indicate their acceptance to the license agreement before they were able to download the "SmartDownload" software.[54] On the specific webpage where the downloading took place, the only reference to Netscape's license agreement appeared in the text of a link which read: "Please review and agree to the terms of the Netscape SmartDownload software license agreement."[55] This link was visible only if the visitor scrolled down the webpage.[56] The issue was whether there was consumer assent, given the link's placement and wording, and the general features of the website that might put the visitor on notice of such a license.[57]

B. The District Court's Decision

Judge Hellerstein of the Southern District of New York held that Netscape failed to provide sufficient notice of its license and consequently, found that the plaintiffs did not assent to the browsewrap license.[58]

The court viewed *ProCD*, not *Step-Saver*, as the relevant authority in evaluating consumer assent online.[59] The court noted that the shrinkwrap agreement in *ProCD* had presentation characteristics similar to a typical clickwrap license.[60] Accordingly, the court found clickwrap licenses gen-

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50. *Id.* at 587.
51. *Id.* The clicking of this box had no connection to viewing or accepting the terms of the license agreement. *Id.*
52. *Id.*
53. *Id.* at 588.
54. *Id.*
55. *Id.*
56. *Id.*
57. *Id.* at 587.
58. *Id.* at 595-96.
59. *See id.* at 595.
60. *See id.*

erally enforceable.[61] The court did not question *ProCD*'s holding that consumers assent to the terms of shrinkwrap licenses.[62]

Because the court in *Netscape* viewed clickwrap agreements as valid, the court framed the law such that clickwrap presentation would equal assent, while browsewrap presentation would not.[63] Consequently, the court created a test for determining whether an online license represents a clickwrap or a browsewrap license.[64]

III. DISCUSSION

In *Netscape*, the court recognized two procedural characteristics as important when characterizing an online agreement as a browsewrap or a clickwrap license.[65] The presence of both characteristics indicates a clickwrap license, their absence a browsewrap license.[66] The court derived the two characteristics from the shrinkwrap license in *ProCD*.[67] The shrinkwrap agreement in *ProCD* gave "[the consumer] no choice, because the software splashed the license on the screen and would not let [the consumer] proceed without indicating acceptance."[68] First, ProCD required the customer to affirmatively indicate acceptance of the license.[69] The software program needed this affirmative action before it could run.[70] Second, the software automatically presented the license.[71] The consumer did not need to click on a link to view the license.

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61. *See id.* at 595-96.

62. For arguments against the finding of assent in clickwrap and shrinkwrap agreements, see generally Zachary M. Harrison, *Just Click Here: Article 2B's Failure to Gurantee Adequate Manifestion of Assent in Click-Wrap Contracts*, 8 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 907 (1998); Jeffery A Moddisett & Cindy M. Lott, *Cyberlaw and E-Commerce: A State Attorney General's Perspective*, 94 NW. U. L. REV. 643 (2000) (emphasizing that click-through agreements remain a take-it-or-leave-it proposition without any satisfaction of a meeting of the minds test); and Roger E. Schechter, *The Unfairness of Click-On Software Licenses*, 46 WAYNE L. REV. 1735, 1742-43 ("The fine print, the legalese, and the keen desire to load the software and take it for a spin all tend to encourage the consumer to rip open the envelope or click on the 'I accept' button-without giving much thought to the purported license at all.").

63. 150 F. Supp. 2d at 595.

64. *See id.* at 595-96. For a detailed discussion see *infra* Part III.

65. *See id.* at 595-96.

66. *See id.*

67. *See id.*

68. *Id.* at 592 (quoting *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447, 1452 (7th Cir. 1996)).

69. *ProCD*, 86 F.3d at 1452.

70. *Id.*

71. *Id.*

In recent cases, other courts have suggested that the absence of one factor may not preclude the finding of consumer assent if other features of the website put the consumer on notice.

A. An Affirmative Indication of Assent

Clicking an "I agree" icon or click-checking an unchecked box often represents consumer assent.[72] In *Netscape,* the court emphasized that defendant Netscape did not require its consumers to affirmatively indicate their acceptance of its online license.[73] Significantly, the court stressed that the "mere act of downloading . . . [was] hardly an unambiguous indication of assent. The primary purpose of downloading was to obtain a product, not to assent to an agreement."[74] Thus, the requisite affirmative act must be independent from an act indicating a desire for a product. The court found that clicking an "I agree" icon placed at the end of a license would have "no meaning or purpose other than to indicate assent"[75] to its terms.

However, in *Register.com v. Verio Inc.*,[76] the district court enforced an online license, even where the consumer did not click an icon or check a box to indicate acceptance of the terms.[77] The *Netscape* court would have viewed this license as a browsewrap license because the vendor did not require a separate, affirmative acceptance of the license terms.[78] The software vendor in *Verio* automatically presented the terms in clear view and in close proximity to its important query service.[79] Online consumers would easily notice the terms.[80] Accordingly, the court in *Verio* found that simply submitting a query constituted both a desire to use the service and an indication of the consumer's acceptance of its license terms.[81] Also, the court noted that a paragraph next to the query read: "[b]y submitting this query, you agree to abide by these terms."[82] The court found that this strong language left "no question that by proceeding to submit a WHOIS

72. *See infra* note 97 (listing cases upholding online licenses with clicking requirement).

73. 150 F. Supp. 2d at 595.

74. *Id.*

75. *Id.*

76. 126 F. Supp. 2d 238 (S.D.N.Y. 2000).

77. *Id.* at 248.

78. 150 F. Supp. 2d at 594-95.

79. 126 F. Supp. 2d at 248. Consumers used the query function in order to check the availability of websites with their desired domain name. *See id.*

80. *Id.*

81. *Id.*

82. *Id.*

query, Verio manifested its assent to be bound by Register.com's terms of use . . . "[83] Thus, the clicking of an "I agree" icon was not an essential requirement, given the other features of the website that put the consumer on notice.

B. The Automatic Presentation of the License

The *Netscape* court emphasized that ProCD's software program automatically "splashed" the license onto the consumer's computer screen.[84] In contrast, the consumers in *Netscape* needed to click on a link located within a "small box of text,"[85] in order to view the license. The small box of text read: "Please review and agree to the terms of the Netscape SmartDownload software license agreement before downloading and using the software."[86] The court criticized both the small size of the reference link and the mild request "please review."[87] These words suggested a mere invitation and did not "indicate that a user *must* agree to the license terms before downloading and using the software."[88] With stronger language and more prominent print, other courts may find that a link provides a level of notice tantamount to an automatic "splash."

In *Pollstar v. Gigmania,*[89] the online vendor utilized conditional language stating its online services and "uses [were] subject to the license agreement."[90] This language served as the textual link to the agreement.[91] The textual link was in small gray print on a gray background and the vendor failed to underline the text.[92] In addition, the court noted that some blue colored links failed to function, perhaps causing consumers to assume that all colored links would also fail.[93] In sum, the court found that the website did not put visitors on notice and termed the license a browsewrap license.[94] The court cited *ProCD* and noted that, "unlike the shrinkwrap license held enforceable in *ProCD v. Zeidenberg*, the license agreement at

83. *Id.*
84. 150 F. Supp. 2d at 592.
85. *Id.* at 595.
86. *Id.*
87. *Id.* at 596.
88. *Id.*
89. 170 F. Supp. 2d 974 (E.D. Cal. 2000).
90. *Id.* at 981.
91. *Id.*
92. *Id.*
93. *Id.*
94. *Id.* But, the court hesitated to rule that browsewrap agreements are unenforceable. The court denied the motion to dismiss, preferring to defer its ruling on the enforceability issue, even though the court found that notice was questionable in browsewrap licenses. *Id.* at 982.

issue is a browsewrap license."[95] The court also noted that the "shrinkwrap license [in *ProCD*] appears on the screen when the CD or diskette is inserted . . . ."[96] The license's automatic presentation in *ProCD* contrasted starkly with the small gray link in *Pollstar*.

C. The Two Characteristics Considered Together

If both characteristics are present, courts will likely find consumer assent. When the vendor automatically presents the license to the consumer and requires the clicking of an "I accept" icon, the vendor puts the consumer on notice of the standard terms of the license. Given such a presentation, courts have enforced the online license, often terming it a clickwrap agreement.[97]

Courts generally will not enforce a license when these two characteristics are absent. When the vendor does not require a clicking acceptance and provides an unnoticeable link to the license, courts find the level of notice minimal and consumer assent absent.[98] *Netscape* is one example of such a case.[99]

But, when one characteristic is present and the other absent, the outcome is less clear. Courts will likely consider enforcing a license with only one characteristic if other design elements of the website put the consumer on notice. For example, if a vendor creates a prominent link to the license and places the link directly adjacent to an "I accept" icon, a court may find an acceptable level of notice. Courts may consider whether the vendor has the link underlined or in a distinguishable color, or if condi-

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95. *Id.* at 981.

96. *Id.*

97. *See, e.g.*, Caspi v. Microsoft Network LLC, 732 A.2d 528 (N.J. App. Div. 1999) (upholding clickwrap license when user was prompted by vendor to view license and had opportunity to click either "I Agree" or "I Don't Agree"); Groff v. Am. Online Inc., No. PC 97-0331, 1998 WL 307001 (R.I. Super. May 27, 1998) (validating a clickwrap license where user needed to click "I agree" at the conclusion of the agreement in order to proceed with the online service); *see also* In re Realworks, Inc. Privacy Litig., No. 00C1366, 2000 WL 631341 (N.D. Ill. May 8, 2000); Hotmail Corp. v. Van$ Money Pie, Inc., No. C 98-20064, 1998 WL 388389 (N.D. Cal. Apr. 16, 1998).

98. An extreme example of an unnoticeable link to a license is in *Ticketmaster Corp. v. Tickets.com Inc.*, CV 99-76542000, 54 U.S.P.Q.2d (BNA) 1344 (C.D. Cal. Mar. 27, 2000). In this "deep-linking" case, the customer could hyperlink from a web page of Tickets.com directly to an interior web page of Ticketmaster, thereby bypassing the home page of Ticketmaster (where the vendor placed the link to the license agreement). On this interior page, the customer could proceed to buy tickets without ever noticing or viewing the link to license agreement. The court found no assent and held the license unenforceable. *Id.*

99. *See Netscape*, 150 F. Supp. 2d at 594; *see also Pollstar*, 170 F. Supp. 2d 974.

tional language occupies the text of the link. A prominent, colorful link next to an "I accept" icon may prove sufficient for a finding of consumer assent.

Courts may also find consumer assent in the absence of a clicking acceptance, if the consumer is somehow put on notice. For example, if the vendor automatically places the terms in plain view on the main webpage of the site, a consumer is arguably on notice of these terms and his use of the website may constitute assent. *Verio* is an example of a court finding assent in this type of situation.[100]

In sum, a clicking acceptance and automatic presentation prove to be the two fundamental characteristics in finding consumer assent in cyberspace. As noted above, however, courts may find assent if the overall website presentation still puts the consumer on notice of the binding license.

IV. THE ENFORCEABILITY OF TERMS

Where the court finds consumer assent, an enforceable agreement exists. Such a finding would not, however, preclude a court from striking or modifying particular terms within the agreement. The *Netscape* court did not address the issue of striking particular terms as illegal because it found the entire license agreement unenforceable. Assuming an enforceable agreement, however, courts might modify or eliminate terms by relying upon several legal doctrines: 1) the unconscionability doctrine, 2) state and federal consumer protection laws, or 3) copyright preemption.

A. The Unconscionability Doctrine

The courts may employ the unconscionability doctrine to strike terms from an online agreement. UCC section 2-302 codifies the traditional common law doctrine of unconscionability.[101] Generally, courts recognize

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100. Although plaintiff Register.com succeeded in its suit, the online vendor has changed its website to conform more closely to the ruling in *Netscape*. At the time of publication, the website utilizes an unchecked box that must be clicked-checked for the consumer to complete his online transaction. Interestingly, however, the license agreement is not longer in plain view, as it was previously. Instead, Register.com has placed a blue colored link to the license, and has placed the link adjacent to the unchecked box. Thus, a consumer could simply check the box without having read the license. *See* register.com, *at* http://www.register.com (last visited Jan. 25, 2002).

101. UCC section 2-302(1) states:

> If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the

that both substantive and procedural unconscionability must be present for a court to alter the terms of an otherwise enforceable contract.[102] Substantive unconscionability exists when an agreement contains terms overly harsh and one-sided.[103] Procedural unconscionability occurs when a party lacks a meaningful choice in entering into the contract.[104] This could include a situation where the party lacks a reasonable opportunity to read and understand the terms of a contract due to time pressure and the vendor's intent to hide terms in a maze of legalese.[105]

Courts are unlikely to find an online license procedurally unconscionable. If the court finds consumer assent to the license as a whole, the website provides sufficient notice to the consumer. In short, the procedural or presentational characteristics of the website are reasonable. If the court then strikes terms for reasons of procedural unconscionability, the court would contradict its initial finding of sufficient notice and consumer assent. Indeed, the court's evaluation of whether the license is a clickwrap or a browsewrap license is already a quasi-procedural unconscionability analysis. Further, unlike shrinkwrap licenses where consumers read the license terms when they open the package, online licenses provide the opportunity to view terms before the consumer completes the purchase.

Courts have been reluctant to use this doctrine.[106] Even though UCC section 2-302 gives judges wide discretion to "police the bargain," commentators note that unconscionability is easy to assert but especially difficult to prove.[107] Even in noteworthy examples where significantly harsh

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> application of any unconscionable clause as to avoid any unconscionable result.

UCC 2-302(1) (2000).

102. Arthur Allen Leff, *Unconscionability and the Code—The Emperor's New Clause*, 115 U. PA. L. REV. 485, 487 (1967).

103. *Id.*; *see also* Williams v. Walker Thomas Furniture, 350 F.2d 445 (D.C. Cir. 1965); M.A. Mortenson Co. v. Timberline Software Corp., 140 Wn.2d 568 (1999) (explaining that substantially unconscionable terms should be "shocking to the conscience" or "monstrously harsh").

104. *See supra* notes 102 and 103.

105. *See id.*

106. David L. Shapiro, *Courts, Legislatures, and Paternalism*, 74 VA. L. REV. 519, 534-37 (1988) (arguing that courts, absent legislative guidance, are unwilling to interfere with sales agreements that people entered into for their interests).

107. One commentator notes:

> Despite the charter granted to courts by the Uniform Commercial Code's unconscionability provision [§ 2-302], such decisions remain especially rare in the realm of commercial and consumer sales. The landmark decisions declining enforcement of written provisions—decisions like Henningsen v. Bloomfield Motors, Inc., and Williams-

terms and arguably unfair procedural elements exist, courts hesitate to modify an otherwise enforceable agreement. In *M. A. Mortenson Co. v. Timberline Software Corp.*,[108] the plaintiff lost two million dollars because his bid analysis software contained an "obscure bug."[109] The Washington Court of Appeals held the remedies limitation clause in the shrinkwrap license to be enforceable.[110] The court reasoned that the plaintiff was on notice because of the widespread industry practice of using shrinkwrap licenses to limit liability.[111] Although the parties never discussed the clause, the court cited Comment 3 to UCC section 2-719 to stress that limitations on consequential damages are "merely an allocation of unknown or undeterminable risks."[112] The court viewed risk allocation as essential to keeping companies in business and making software affordable.[113] With these economic issues in the background, courts prove even more reluctant to "police" the terms of an otherwise enforceable agreement.

B. Unconscionability Revisited in Consumer Protection Statutes

Since the consumer movement of the 1960s and 1970s, federal and state governments have created numerous acts addressing unfair and deceptive trade practices, and consumer protection.[114] Although this legislation primarily addresses "fraudulent and illegal" activities, many acts explicitly address unconscionable contract provisions and unfair trade practices.[115] Some commentators argue that courts will use various types of

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> Thomas Furniture Co.—are beginning to stand out in the casebooks as curiosities.

Id.; *see also* BALLON, *supra* note 2, at § 26-32.

108. 140 Wn.2d 568 (1999).

109. *Id.* at 576.

110. *Id.* at 589.

111. *Id.* at 587.

112. *Id.*

113. *Id.*

114. The Federal Trade Commission Act ("FTCA") inspired the creation of state acts which created a state agency with the power to enforce the states' laws on deceptive practices. Currently, every state has enacted state statutes directed at providing consumers with some degree of protection against a broad range of unscrupulous or misleading trade practices. In addition, the Federal Trade Commission ("FTC") has taken a greater role in regulating electronic commerce than any other governmental agency. *See* BALLON, *supra* note 2, at § 31.02[1] (2001) (discussing the FTC's preeminent role in shaping U.S. law on data privacy, unfair and deceptive advertising practices, the effect on competition from proposed mergers, and online fraud).

115. JOHN P. DAWSON ET AL., CONTRACTS 694-95 (1998) (estimating that 15 to 20 of these state acts have unconscionability provisions); *see also* Marshall A. Leaffer & Michael H. Lipson, *Consumer Actions Against Unfair or Deceptive Acts or Practices:*

consumer protection statutes, in place of the common law doctrine of unconscionability, to modify harsh and unfair terms in private agreements.[116] For example, the Magnuson-Moss Act mandates that vendors employ minimum standards for their warranty polices.[117] This federal act, along with state laws, applies in cyberspace.[118] Courts have emphasized that the Act functions as a supplement to state consumer protection laws,[119] finding that it "leaves room for further state regulation."[120] The Magnuson-Moss Act enables consumers to require vendors to conspicuously disclose the terms of a written warranty (including terms regarding consequential damages) prior to the sale.[121] The Act also enables consumers to use the "unconscionability" language of state statutes to supplement their consumer protection.[122] Together, federal and state law provides consumers alternative methods for demonstrating procedural and substantive unfairness.

C. Copyright Preemption

In the future, courts may also use the Copyright Act to preempt terms within online licenses.[123] However, the preemption of contractual terms

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The Private Uses of Federal Trade Commission Jurisprudence, 48 GEO. WASH. L. REV. 521 (1980) (listing numerous state acts that address unconscionable contract provisions); Anthony P. Dunbar, *Consumer Protection: The Practical Effectiveness of State Deceptive Trade Practices Legislation*, 59 TUL. L. REV. 427 (1984).

116. *See* BALLON, *supra* note 2, at §§ 26.02[6], 31 (emphasizing that the scarce application of common law unconscionability should not mislead online vendors into thinking that this doctrine will not serve as a limitation in the future, given the increasing legislative attention to consumer protection issues in cyberspace); DAWSON, *supra* note 115, at 695 ("The main point here is that common law and UCC approaches to unconscionability have been expanded, and that, in general, much of the law of consumer protection is currently the work of statutes and not common law doctrines.").

117. 15 U.S.C. §§ 2301-2312 (1994).

118. Since cyberspace defies state boundaries, online vendors of consumer goods or services must comply with both federal statutes and state laws of all states from which they accept orders. *See generally*, BALLON, *supra* note 2, at § 31 (2001). It should be noted that even if many states were to adopt UCITA, the model law provides that conflicting state consumer protection laws or regulations would supersede UCITA terms. Proposed UCC § 2B-105(d) (Aug. 1, 1998 Draft).

119. *See id.*; Motor Vehicle Mfrs. Ass'n v. Abrams, 899 F.2d 1315, 1319-21 (2nd Cir. 1990); Automobile Importers of Am., Inc. v. Minnesota, 871 F.2d 717, 721 (8th Cir. 1989); Chrysler Corp. v. Texas Motor Vehicle Comm'n, 755 F.2d 1192, 1205-06 (5th Cir. 1985).

120. *Automobile Importers*, 871 F.2d at 721.

121. 15 U.S.C. §§ 2302-2303 (1994).

122. *See supra* notes 114 and 115 and accompanying text.

123. Generally speaking, the United States Constitution mandates that federal law preempt state laws in direct conflict. U.S. CONST. art. VI, § 2.

faces important obstacles. First, courts and commentators disagree on whether federal law can preempt terms within a private contract, as compared to a state statute. Second, enforcement of the first sale doctrine and other provisions of the Copyright Act[124] demands that courts characterize the vendor as selling rather than "licensing" their software to the consumer. Given the widespread use of shrinkwrap and clickwrap agreements to "license" software, this characterization may prove difficult.

1. *The Preemption of Private Agreements*

There is no consensus among courts and commentators as to whether federal law can or should preempt terms within private agreements, including online licenses. In a widely cited case regarding copyright preemption, *Vault Corp. v. Quaid Software Ltd.*, the court addressed the preemption of a state statute, not a private agreement between parties.[125] Some commentators argue that the case law and the preemption clause of the Copyright Act[126] support the reading that the Copyright Act cannot preempt the terms of a private contract.[127] Arguably, allowing parties to fashion the terms and conditions of their transactions is more efficient and desirable than using the government to estimate the expectations of the parties.

However, there are strong arguments that federal law can and should preempt the terms of a private agreement. First, courts may construe terms within private agreements by applying federal copyright law and policy.[128] These cases stress the importance of preventing parties from privately undoing the relative rights that Congress took pains to balance and allocate.[129] Commentators claim that the Copyright Act properly gives copyright owners, licensees, and the public at large the precise economic incen-

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124. *See infra* note 135.

125. 847 F.2d 255 (5th Cir. 1988).

126. Courts apply the preemption clause (Section 301) by using an "extra element" test. In short, if a state statute has an "extra element" not explicitly present in the Copyright Act, then such a statute survives preemption. *See id.*

127. Some courts have stated that the contract itself is an "extra element," consequently holding that such "agreed-to" terms are immune from preemption. *See, e.g.*, ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996); National Car Rental Sys. v. Computer Assocs. Int'l, 991 F.2d 426, 431 (8th Cir. 1993). Citing these cases, some commentators conclude that "agreed-to" contract provisions escape federal preemption. *See* MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT § 1.01(B) (2001).

128. Mark A. Lemley, *Intellectual Property and Shrinkwrap Licenses*, 68 S. CAL. L. REV. 1239, 1272 (1995) (collecting cases).

129. *See id.*

tives to innovate.[130] Because producers use shrinkwrap and clickwrap licenses in mass-market transactions,[131] courts would be giving producers the opportunity to re-write copyright law if federal law did not preempt private contracts.[132] Furthermore, the freedom to contract argument does not retain force in the context of shrinkwrap and clickwrap licenses.[133] These licenses are unilateral agreements that consumers accept on a take-it-or-leave-it basis. Although the freedom to contract has appeal where parties to commercial deals actually negotiate their use and terms, shrinkwrap licenses do not represent a meeting of the minds as is traditionally required by contract law. As such, courts are better left construing these unilateral terms with help from federal legislation that allocates incentives and liabilities in balance.

2. *Licensing Around the First Sale Doctrine*

Courts will likely refrain from striking an entire "license" as illegal under the first sale doctrine.[134] Rather, courts should use this doctrine to

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130. *See, e.g.*, Thomas L. Irving et. al., *The Significant Federal Circuit Cases Interpreting Section 112*, 41 AM. U. L. REV. 621 (1992); Lemley, *supra* note 128.

131. *See infra* note 137.

132. *See* Nimmer, *Metamorphosis, supra* note 41, at 40 (arguing that the enforcement of shrinkwrap licenses would effectively change the federal law); *see also* Charles R. McManis, *The Privatization of American Copyright Law*, 87 CALIF. L. REV. 173 (1999) (stressing that if federal law failed to preempt these license agreements, a licensor could re-write federal copyright simply by drafting a license in the manner they found in their interests).

133. In *The Metamorphosis of Contract into Expand*, David Nimmer criticizes the argument that a shrinkwrap license is similar to a traditional, private agreement affecting only two parties. *See* Nimmer, *Metamorphosis, supra* note 41, at 40-41.

134. In most cases, a court would not disregard the entire "license agreement," if the court found a sale of goods rather than a "license" of goods. Congressional notes surrounding section 109(a) explicitly state that vendors can contract around the first sale doctrine. *See* Notes of Comm. on the Judiciary, H.R. REP. NO. 94-1476 (1976), *reprinted in* 1976 U.S.C.C.A.N. 5659. However, the notes also state that if the intellectual property owner/vendor brings suit, the terms are enforceable only for a breach of contract claim, not for a copyright infringement claim. *Id.*; *see also* Lemley, *supra* 128, at 1273; David A. Rice, *Licensing the Use of Computer Program Copies and the Copyright Act First Sale Doctrine*, 30 JURIMETRICS J. 157 (1990). For example, if Microsoft sold one million copies of Windows to distributor A and their contract limited distributor A from reselling the copies in their component parts, Microsoft could not claim infringement and enjoin distributor A from its actions. But, Microsoft could sue under a breach of contract theory and receive expectation damages for distributor A's actions. Consequently, courts would preempt terms within a license agreement that conflict with the first sale rights of buyers, but only if the seller's claim is for copyright infringement. In short, under the committee notes, buyers retain a property right to distribute and use their copy under the first sale doctrine, but could face liability in the form of expectation damages if they vio-

preempt certain terms within an online license. This preemption depends, however, on the court characterizing the producers as selling rather than "licensing" their products.

When a buyer purchases a copy of a copyrighted product, the buyer attains certain "first sale" rights in their purchased copy.[135] Generally, the buyer can resell, dispose, or otherwise control the use of his copy. Of course, the producer can enjoin the buyer from reproducing his copy, but the producer lacks title to the tangible piece of property, which the buyer owns.[136]

Software vendors get around the first sale doctrine because they "license," rather than sell, their products to consumers.[137] Consumers only attain their rights under the first sale doctrine when they purchase a copy of the software. For example, when a consumer buys Windows 2000 in the store, the consumer merely receives a license from Microsoft to use the product. Although this license is indefinite, Microsoft would claim no "first sale" occurs since the shrinkwrap license within the package fails to transfer ownership to the consumer.[138]

In a recent case, *Softman v. Adobe,*[139] the district court held that a commercial transaction between a software producer and a distributor was actually a disguised sale, rather than a purported "license" of goods.[140] The court cited the Ninth Circuit decision in *Microsoft v. DAK* to stress that "it is well-settled that in determining whether a transaction is a sale, a lease, or a license, courts look to the economic realities of the exchange."[141] The court noted that distributor Softman paid for the merchandise in full and accepted the risk of any subsequent damage to the copies,

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late their contract. Courts would enforce the overall agreement, but preempt certain terms within it.

135. Section 109(a) states: "the owner of a particular copy . . . lawfully made under this title . . . is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy." 17 U.S.C. § 109(a) (1994).

136. In *The Metamorphosis of Contract into Expand,* David Nimmer distinguishes between tangible and intangible property within a copyrighted product. He explains that while a software publisher that distributes its products does not part with their intangible property (copyright), the publisher does part with the tangible property of the copy. *See* Nimmer, *Metamorphosis, supra* note 41, at 36.

137. Whether in the form of shrinkwrap licenses, online licenses, or bargained-for licenses involved in business-to-business exchanges, licensing dominants the transactional practice of the software industry. *See generally,* BALLON, *supra* note 2, at § 21.

138. *See* Microsoft Corp. v. DAK Indus., 66 F.3d 1091 (9th Cir. 1995)

139. 171 F. Supp. 2d 1075 (C.D. Cal. 2001).

140. *Id.* at 1086-87.

141. *Id.* at 1084 (citing *DAK*, 66 F.3d 1091, and *United States v. Wise*, 550 F.2d 1180 (9th Cir. 1997)).

and any risk associated with their resale and marketing.[142] On this evidence, the court found that the "first sale" occurred and that the producer transferred ownership to the buyer.[143] Accordingly, Softman attained the first sale right to re-distribute the merchandise in the manner it desired, despite contradictory terms in the license.

While some courts have reached the conclusion that producers sell, rather than license their software,[144] other courts have held otherwise.[145] These courts relied on the fact that licensing was the standard practice of the software industry.[146] But, these cases are also distinguishable because the consumers either adulterated or counterfeited the product.[147]

In the future, courts may look beyond the industry practice of "licensing" and analyze the underlying facts of the transaction. If courts find that producers actually "sell" their software, buyers will own the software and courts may preempt terms in conflict with ownership rights under the Copyright Act.[148]

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142. *Id.*

143. *Id.* at 1086-87.

144. *See, e.g.*, RRX Indus., Inc v. Lab-Con, Inc., 772 F.2d 543, 546 (9th Cir. 1985); Novell, Inc. v. CPU Distrib., Inc., No. H-97-2326, 2000 LEXIS 9975 (S.D. Tex. May 4, 2000); Applied Info. Mgmt., Inc. v. Icart, 976 F. Supp. 149, 155 (E.D.N.Y. 1997).

145. *See* Adobe Sys., Inc. v. One Stop Micro, Inc., 84 F. Supp. 2d 1086, 1093 (N.D. Cal. 2000); Microsoft Corp. v. Harmony Computers & Elecs., Inc., 846 F. Supp. 208, 212 (E.D.N.Y. 1994).

146. Indeed, *One Stop* had extensive extrinsic evidence on the industry practice. *See One Stop*, 84 F. Supp. 2d 1086.

147. *See id.* at 1093 (noting that the consumer destroyed the bar code and serial numbers, peeled off "education version" stickers from the software, and admitted to trying to resell as retail the Adobe product at a price below market); *Harmony*, 846 F. Supp. at 212 (stating that defendants tried to sell counterfeit Microsoft products).

148. Importantly, consumers also receive user rights under section 117 of the Copyright Act. However, courts have held that in order to obtain rights under section 117 of the Copyright Act, the consumer must be the *owner* of the copy he possesses. *See* DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354, 1359 (Fed. Cir. 1999). If the consumer is merely a "licensee," this could jeopardize the finding of ownership. *But see id.* at 1360-61 (noting that if the transaction more accurately characterized a sale of goods, rather than a license of goods, ownership of title would transfer and the rights associated with section 117 should preempt the conflicting terms within the license). Section 117 gives the owner of a particular copy the right to make both archival copies and copies (in RAM) that are necessary in order for the program to run. 17 U.S.C. § 117 (1994). Also, some cases indicate that section 117 gives owners the right to reverse engineer or alternatively, modify their copy, to the extent necessary to run on their particular computer. *See, e.g.*, *Applied Information Mgmt.*, 976 F. Supp. at 155 (E.D.N.Y. 1997).

V. CONCLUSION

Courts possess effective methods for striking or modifying terms within online license agreements. These methods should prove increasingly important because courts will likely enforce clickwrap licenses. Even if the court finds that the consumer assents to the clickwrap agreement, the court should utilize the unconscionability doctrine, consumer protection statutes, and federal preemption to strike unfair terms of the license.

Many consumer protection statutes explicitly address "unconscionable" contract provisions, while others contain a range of mandatory standards for fair trade practices.[149] Courts may rely on such laws as alternatives or supplements to the common law unconscionability doctrine. In addition, courts may conclude that federal preemption of contractual terms is necessary, given the ubiquity of shrinkwrap and clickwrap licenses, and their potential to radically alter the balance of rights codified in federal intellectual property laws.[150] Finally, courts should increasingly find that a vendor's "license" of goods actually represents a disguised sale of goods.[151] If vendors "sell" their products, courts will likely preempt terms that contradict "first sale" rights under the Copyright Act. The preemption and striking of terms within online licenses should maintain the integrity of federal intellectual property law, consumer protection law, and traditional ideals of good faith and fair dealing.

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149. *See supra* notes 115 and 116 and accompanying text.

150. *See id.*

151. *See* Microsoft Corp. v. DAK Indus., 66 F.3d 1091 (9th Cir. 1995); Softman v. Adobe Sys. Inc., No. CV 00-04161, 2001 WL 1343955 (C.D. Cal. Oct. 19, 2001); *see also supra* note 139 to 144 and accompanying text.

THE GRAMM-LEACH-BLILEY ACT

By Jolina C. Cuaresma

On November 12, 1999, with overwhelming bipartisan support from both houses of Congress,[1] President Clinton signed the Gramm-Leach-Bliley Act ("GLBA") into law.[2] Enactment of the GLBA, also known as the Financial Services Modernization Act of 1999, was a revolutionary event in the world of financial services. For that industry, the GLBA marked the end of regulation that addressed the perceived defects in the banking system thought to have caused the Great Depression.[3] For consumers, it marked Congress' tentative attempt to ensure that private financial companies protect their customers' financial information.

Congress enacted the GLBA to address the need for increased competition in the financial services industry. The Act also acknowledges privacy concerns regarding consumer financial information. This Note focuses on the privacy provisions of the GLBA in light of this allowance for competition among financial institutions.[4] It examines whether the GLBA establishes sufficient legal protections for individual privacy rights in personal financial information. Part I provides an overview of the GLBA and describes the Act's regulation of the financial system, as well as its specific requirements regarding privacy protection. Part II explains why financial services institutions value access to personal financial information and why privacy regarding such information has become a contested issue. Part III analyzes the problems with the GLBA's privacy provisions and suggests that the financial services sector still has the upper hand in controlling information. This Note concedes that the GLBA is not a complete

1. The vote in the House of Representatives was 362 to 57. 145 CONG. REC. H11,513, 11,531 (1999). The vote in the Senate was 90 to 8. 145 CONG. REC. S13,883, 13,917 (1999).

2. Pub. L. No. 106-102, 113 Stat. 1338 (1999) (codified as amended in scattered sections of 12 U.S.C. and 15 U.S.C.).

3. 145 CONG. REC. S13,883, 13,915-16 (1999) (statement of Sen. Gramm).

4. Financial institution is defined as "any institution the business of which is engaging in financial activities" as described in the amended section of 4(k) of the Bank Holding Company Act of 1956. Pub. L. No. 106-102, § 509(3)(A), 13 Stat. 1338, 1443 (current version at 15 U.S.C. § 6809 (2001)). In a presentation on June 18, 2001, the Federal Trade Commission defined financial institution as one that "must be *significantly engaged* in financial activities." Examples include mortgage lenders, companies that sell travelers' checks, and check-cashing businesses. The Gramm-Leach-Bliley Act: Privacy of Consumer Financial Information, *at* http://www.ftc.gov/privacy/glbact/glboutline.htm.

defeat for privacy advocates because Congress has established some limits to the private sector's use of personal information. Nevertheless, as long as society remains information-driven and efficiency is valued at a premium, informational privacy concerns will remain secondary considerations.

I. THE PASSAGE OF THE GLBA

A. The GLBA Restructures the U.S. Financial System

The GLBA redesigned the regulatory structure that had been in place since the Great Depression. The regulations adopted in the early 1930s were not part of a "well-considered overall blueprint,"[5] but were made in "immediate response to developments and crises as they occurred."[6] Because the regulatory structure developed in such an ad hoc manner, the GLBA's reforms answer a long-felt need for coherence.[7]

The 1920s, marked by a succession of bank failures, culminated in the stock market crash of 1929.[8] The economic depression that followed led to more market failures, decreased public confidence, and engendered cries for government intervention.[9] In response to these calls for reform, Congress passed the Glass-Steagall Act.[10] Passed during the Roosevelt administration, the Glass-Steagall Act directly responded to the belief that the stock market crash resulted from the lack of separation between lending and underwriting activities that had allowed banks to engage in speculative investments.[11] Under the Glass-Steagall Act, Congress separated commercial banking[12] from investment banking,[13] thereby prohibiting

5. GEORGE G. KAUFMAN, THE U.S. FINANCIAL SYSTEM: MONEY, MARKETS, AND INSTITUTIONS 340 (5th ed. 1992).

6. *Id.*

7. The GLBA represents twenty years of effort by industry lobbyists and lawmakers to reform the industry's regulatory structure. Adam Nguyen & Matt Watkins, *Financial Services Reform*, 37 HARV. J. ON LEGIS. 579, 579 (2000).

8. HELEN M. BURNS, THE AMERICAN BANKING COMMUNITY AND NEW DEAL BANKING REFORMS 1933-1935, 3-6 (1974).

9. *Id.*

10. 48 Stat. 162 (1933), *repealed by* Gramm-Leach-Bliley Act, Pub. L. No. 106-102, § 101, 113 Stat. 1338, 1341 (2001). The Glass-Steagall Act is also referred to as the Banking Act of 1933.

11. *Bankers as Brokers*, BUS. WK., Apr. 11, 1983, at 70. *See generally* KAUFMAN, *supra* note 5, at 366-67.

12. Commercial banks generally accept deposits and issue loans. KAUFMAN, *supra* note 5, at 364. For an extensive description of commercial banking activities, see *id.* at 162-74.

commercial banks from underwriting most securities.[14] With the goal of eliminating conflicts of interest, Congress sought to prevent these firms from engaging in similar activities.[15]

The Glass-Steagall Act, however, was unsuccessful in maintaining these legal barriers.[16] Had it been effective, the Act would have minimized direct competition between commercial banks and securities firms.[17] Instead, by 1990, the largest banks were able to participate in almost all of the securities activities that they had engaged in before the Glass-Steagall Act.[18]

Several factors explain the deficiencies of the Glass-Steagall Act. First, designed as remedial legislation, the Glass-Steagall Act could not anticipate the development of new financial services and instruments.[19] Investment banks began to offer new products that effectively served the same needs as traditional commercial banking products. For example, investment banks introduced checkable interest-earning money market funds, a product that rivals traditional non-interest-earning checking accounts.[20] Second, the slower growth in traditional lending activities prompted commercial banks to pursue securities activities that were not expressly prohibited to them under the Glass-Steagall Act.[21] In response to these and other developments in the industry, regulatory agencies and

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13. Investment banks generally underwrite new debt and securities issued by private or government entities that require funding. Underwriting involves purchasing these securities and then reselling them to individual or institutional investors. *Id.* at 145. For an extensive description of investment banking activities, see *id.* at 144-50.

14. BURNS, *supra* note 8, at 81. Commercial banks were still allowed to underwrite state and local government issued securities. *Id.*

15. Congress sought to prohibit banks from shifting default risk to unsuspecting investors. For example, a bank with an insolvent client could improve its client's financial position by underwriting securities. The bank could then sell these low-grade securities to unsuspecting investors. The bank would no longer have an insolvent client, but investors would bear the risk of default. *Bankers as Brokers*, *supra* note 11.

16. For a chronology of what U.S. bank regulatory agencies have allowed at the insistence of the banking industry, see Paul J. Polking & Scott A. Cammarn, *Overview of the Gramm-Leach-Bliley Act*, 4 N.C. BANKING INST. 1, 1-2 (2000). *See also Bankers as Brokers*, *supra* note 11 (reporting that banks have chipped away at the Glass-Steagall Act by expanding services and acquiring other financial institutions). For a discussion regarding whether banks should be permitted to engage in investment banking activities, see KAUFMAN, *supra* note 5, at 373-78.

17. This Note uses the term "securities firm" interchangeably with "investment bank."

18. KAUFMAN, *supra* note 5, at 368.

19. *Id.* at 367.

20. *Id.*

21. *Id.* at 368.

courts made discretionary changes to the original regulatory framework without a well-conceived plan.[22]

Against this backdrop, the GLBA comes as no surprise. The Act's primary objective is to increase the competition of the financial services industry through a statutory framework.[23] The latter seems to have been the stronger impetus. In his speech urging fellow senators to vote for the GLBA, Senator Paul Sarbanes (D-MD), the then-ranking Democrat on the Senate Banking, Housing and Urban Affairs Committee, explained:

> Very frankly, the issue for Congress is not whether these affiliations should occur, because they have occurred in one way or another, but whether they should take place on an orderly basis in the context of a responsible statutory framework, or instead, on an ad hoc basis as permitted by the regulators.[24]

Thus, at first glance, the GLBA seems to merely change regulations to reflect market developments. However, closer examination of its provisions shows that the Act makes sweeping changes in the financial services sector that go well beyond what had been permitted by regulators on an ad hoc basis.

B. The GLBA Increases Efficiency in the U.S. Financial System

The GLBA repeals the sections of the Glass-Steagall Act that had restricted commercial banks from affiliating with securities firms.[25] The GLBA also amends the Bank Holding Company Act of 1956 ("BHCA"),[26] which had required banks to divest their nonbanking interests. Prior to the GLBA's enactment, banks could only engage in those activities that were closely related to banking.[27] Under the new statute, Congress allows affiliations between banking and securities firms[28] and the creation of financial holding companies that can engage in a wide variety of financial activities.[29] Thus, commercial banks, securities firms, and insurance compa-

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22. *Id.* at 373.

23. Pub. L. No. 106-102, 113 Stat. 1338, 1338 (1999).

24. 145 CONG. REC. S13,783, 13,787 (1999) (statement of Sen. Sarbanes).

25. The GLBA repeals sections 20 and 32 of the Glass-Steagall Act. Pub. L. No. 106-102, § 101, 113 Stat. 1338, 1341 (1999).

26. 70 Stat. 133 (1956), *amended by* Gramm-Leach-Bliley Act, Pub. L. No. 106-102, § 102, 113 Stat. 1338, 1341-42 (1999) (current version at 12 U.S.C. § 1843(c)(8) (2001)).

27. Nguyen & Watkins, *supra* note 7, at 580.

28. Pub. L. No. 106-102, § 101, 13 Stat. 1338 (1999).

29. *Id.* § 102. Section 102 amends the BHCA by allowing "financial holding companies" that can engage in banking, securities underwriting, and insurance activities.

nies are no longer formally restricted to a limited scope of financial activities. Furthermore, because the GLBA facilitates mergers among these financial institutions,[30] companies can now choose between entering into new product lines and services on their own or joining forces with an entrenched firm. The end result is that the GLBA restructures the marketplace by enabling one-stop shopping for financial services.[31]

One advantage of such one-stop shopping is increased efficiency.[32] The ability to provide a full array of financial services should result in lower average costs to consumers through economies of scale.[33] Companies already have the capital resources necessary to engage in these activi-

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Gramm-Leach-Bliley Summary of Provisions, *at* http://www.senate.gov/~banking/conf/grmleach.htm.

30. Nguyen & Watkins, *supra* note 7, at 583. The GLBA makes merging easier because regulators no longer play a discretionary role. However, mergers in the financial services sector date back to the 1980s. Bank of America acquired Charles Schwab in 1981. *Bankers as Brokers*, *supra* note 11. NationsBank, the fourth-largest bank at the time, acquired Montgomery Securities, a securities firm, in 1997. David Greising et al., *Love Among the Heavyweights*, BUS. WK., July 14, 1997, at 55. Citibank, a bank holding company, merged with Travelers, an insurance company to form the world's largest financial services company in 1998. Matt Murray, *Fed Approves Citicorp-Travelers Merger*, WALL ST. J., Sept. 24, 1998, at A3. When Citibank and Travelers announced their not-then-legal merger, they hoped that their lobbying power would persuade Congress to modernize the financial services sector. Robert W. Dixon, *The Gramm-Leach-Bliley Financial Modernization Act: Why Reform in the Financial Services Industry was Necessary and the Act's Projected Effects on Community Banking*, 49 DRAKE L. REV. 671, 676 (2001).

31. James Hamilton, *Gramm-Leach-Bliley Act Creates Financial Dynamic for the Next Century*, *at* http://www.bankinfo.com/compliance/reform.html. However, with depressed economic conditions since the GLBA's enactment, mergers in the short term are unlikely. Dixon, *supra* note 30, at 688. Furthermore, many of the mergers might have already occurred because congressional legislation tends to follow the market developments by roughly ten years. Raphael Soifer, *Banking Services: Banks Fail to Get in on the Act—The Take-up Rate Among International Banks to Become Financial Holding Companies in the US Has Been Relatively Low*, THE BANKER, Oct. 1, 2000, at Vol. 150, No. 896. *But see* Emily Thornton, *Here's Where the Easy Money Ends*, BUS. WK., Dec. 18, 2000, at 96 (reporting that the GLBA has triggered a "shakeout" in the financial services sector referring to mergers, acquisitions, and firms exiting the industry).

32. James Hamilton, *Gramm-Leach-Bliley Act Creates Financial Dynamic for the Next Century*, *at* http://www.bankinfo.com/compliance/reform.html. Proponents believe that with firms free to compete in a wide range of financial activities, there will be enhanced competition, resulting in more efficient companies that can better serve their clients. *Id. But see* Nguyen & Watkins, *supra* note 7, at 584-89 (proposing possible anticompetitive consequences and the creation of firms that are "too big to fail" such that the government would have to bail them out in times of financial crisis because failure would damage the economy).

33. KAUFMAN, *supra* note 5, at 373.

ties.[34] Furthermore, the GLBA allows companies to take advantage of information by allowing financial supermarkets to share information among affiliates.[35] As one banking executive put it, "[t]he Act eliminates [legal] barriers without imposing significant obstacles to customer information sharing . . . thereby enabling a financial holding company efficiently to provide a broader range of services to its overall customer base."[36] This means that a firm engaged in both banking and insurance operations can correlate information gathered from both activities to make even better decisions about customers. Thus, under the GLBA, resources, including information, will be used more efficiently.

C. Limits to the GLBA's Push For Efficiency

Since the GLBA fosters the use of information, it was inevitable that privacy advocates would lobby to include reasonable limits on the use and dissemination of such information. After much debate regarding the use of financial information,[37] drafters of the GLBA added in a plethora of privacy provisions. These provisions represent the first piece of federal legislation to establish a minimum federal standard of privacy for financial information.[38]

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34. *Id.* at 375-76.

35. The GLBA could have required databases that hold information gathered from different financial activities remain separate, thereby applying the concept of a "Chinese Wall," which is already familiar to investment banks. In addition to underwriting activities, investment banks provide retail investors with recommendations regarding which securities to buy, sell, or hold. Thus, there is an inherent conflict in underwriting securities (performed by dealers) and providing investment advice (provided by research analysts). Accordingly, investment banks have tried to create a barrier between underwriting and research activities. For example, the two departments are often located on different floors and research analysts do not report to the dealers. Emily Thornton, *Commentary: Wall Street's Chinese Walls Aren't Strong Enough*, Aug. 27, 2001, *at* http://www.businessweek.com/magazine/content/01_35/b3746057.htm. *See also* Rick Wayman, *What is the "Chinese Wall" and Why is it in the News?*, *available at* http://www.investopedia.com/articles/analyst/090501.asp.

36. Polking & Cammarn, *supra* note 16, at 37-38.

37. Much of the discussion surrounding the GLBA was not about whether regulatory reform was necessary. Instead, the debate focused on companies' use of personally identifiable financial information. *See generally* 145 CONG. REC. S13,783 (1999); 145 CONG. REC. H11,513 (1999).

38. While Congress has passed several laws protecting informational privacy, no federal law has applied to private companies' use of financial information. *See* Right to Financial Privacy Act of 1978, 12 U.S.C. § 3401 (2001) (providing limits to when banks are obligated to release customer information to government agencies); Privacy Act of 1974, 5 U.S.C. § 552(a) (2001) (providing limits on federal agencies' collection, use, and disclosure of personally identifiable information).

The GLBA establishes certain limits on companies' reliance on information. Subtitle A, which addresses the disclosure of customers' nonpublic personal information,[39] contains numerous provisions that require financial institutions to establish limitations governing the disclosure of nonpublic information to nonaffiliated third parties[40] and to provide their customers with a notice of the company's privacy policy.[41] Protection for this information lies in three sections: (1) section 501 requires institutions to establish a privacy policy, many of them for the first time;[42] (2) section 503 requires that the privacy policies be disclosed at the time of establishing a customer relationship;[43] and (3) section 502 prohibits firms from disclosing information to nonaffiliated third parties, subject to certain exceptions.[44]

In addressing the dissemination of nonpublic personal information, section 502 is at the heart of the GLBA's privacy provisions. Section 502(b)(1) provides in pertinent part:

> A financial institution may not disclose nonpublic personal information to a nonaffiliated third party unless—

39. "Nonpublic information" has three components as defined by Section 509(4) of Subtitle A: i) personally identifiable financial information provided by a consumer financial institution; ii) resulting from any transaction with the consumer or any services performed for the consumer; or otherwise obtained by the financial institution; and iii) that the term does not include publicly available information. Pub. L. No. 106-102, §§ 501-10, 113 Stat. 1338, 1436-46 (1999). The GLBA contains another set of privacy provisions. Subtitle B, which protects consumers from fraudulent access to their information, imposes criminal penalties on persons who fraudulently obtain customer information through false pretenses. *Id.* §§ 521-27.

40. Section 509(5) defines "nonaffiliated third party" as "any entity that is not an affiliate of, or related by common ownership or affiliated by corporate control with, the financial institution, but does not include a joint employee of such an institution." *Id.* § 509.

41. Federal agencies, including the Federal Trade Commission, have the task of issuing and implementing rules to carry out the purposes of this subtitle. *Id.* § 504.

42. *Id.* § 501. Section 501(b)(1) requires that companies meet agency-specific standards that are intended to ensure confidentiality of customer information. *Id.*

43. *Id.* § 503. Privacy policy notices must be sent to consumers annually thereafter. Privacy notices must include the following: the categories of nonpublic personal information that the firm collects and discloses, categories of affiliates and nonaffiliates with whom the firm shares information, and an explanation of the consumer's right to opt-out. *Id.*

44. *Id.* § 502.

> (A) such financial institution clearly and conspicuously discloses to the consumer, in writing or in electronic form . . . that such information may be disclosed to such third party;
>
> (B) the consumer is given the opportunity, before the time that such information is initially disclosed, to direct that such information not be disclosed to such third party; and
>
> (C) the consumer is given an explanation of how the consumer can exercise that nondisclosure option.[45]

Accordingly, consumers must affirmatively prevent companies from sharing their nonpublic personal information with nonaffiliated firms. If consumers fail to opt-out, their inaction provides firms with an implied consent to share information with any nonaffiliated company.

However, there are many exceptions even to this minor requirement of implied consent. Firms are only required to disclose that information is in fact shared and to enter into confidentiality agreements with third parties in limited circumstances: when companies hire nonaffiliated third parties to perform services, when firms contract with third parties (e.g. a company hires an outside agency to market its own products or services), and when companies enter into joint agreements[46] to co-offer products.[47] Additionally, under the section entitled "General Exceptions,"[48] firms can share information with nonaffiliates without consent for "a proposed or actual sale, merger, transfer, or exchange of all or a portion of a business or operating unit"[49] and for "institutional risk control."[50]

II. THE BALANCE BETWEEN INFORMATIONAL PRIVACY RIGHTS AND ECONOMIC EFFICIENCY

While the Glass-Steagall Act has been criticized as a knee-jerk reaction to the crises of its time, it is clear that the GLBA is also a response to current trends. This section will describe the current understanding of the

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45. *Id.* § 502(b)(1).

46. Section 509(10) defines "joint agreement" as "a formal written contract pursuant to which two or more financial institutions jointly offer, endorse, or sponsor a financial product or service." *Id.* § 509(10).

47. *Id.* § 502(b)(2). When nonaffiliated third parties receive nonpublic personal information, they are prohibited from disclosing that information to other nonaffiliated third parties. *Id.* § 502(c).

48. *Id.* § 502(e).

49. *Id.* § 502(e)(7).

50. *Id.* § 502(e)(3)(C).

trade-off between the need for efficiency in information systems and the right to privacy. Part III will argue that, like the Glass-Steagall Act, the GLBA is very much a product of its contemporary conception of that balance.

A. The Use Of Information Results in Increased Efficiency

We live in the "information age."[51] While information has always had some value,[52] information started accruing real market value with the advent of computer technology.[53] In the 1960s, the federal government and large private corporations used mainframe computers to store records in computerized form.[54] Even then, these entities realized that this development would improve "operational efficiency."[55] Using computer technology to better sift through personal financial information has allowed companies to increase efficiency (and profits) by increasing revenues while cutting excess costs. Consequently, reliance on databases in digital form has only increased.

Companies gather personal information in order to make strategic decisions about people.[56] Firms use computerized information to generate

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51. ANNE WELLS BRANSCOMB, WHO OWNS INFORMATION? FROM PRIVACY TO PUBLIC ACCESS 1 (1994). *See also* FRED H. CATE, PRIVACY IN THE INFORMATION AGE 2 (1997) (describing society as "increasingly information-based"); Paul Schwartz, *Data Processing and Government Administration: The Failure of the American Legal Response to the Computer*, 43 HASTINGS L.J. 1321, 1326 (1992) ("Information has become the basis of the American economy.").

52. BRANSCOMB, *supra* note 51, at 1-2.

53. *Id.* at 1-3.

54. PRISCILLA M. REGAN, LEGISLATING PRIVACY: TECHNOLOGY, SOCIAL VALUES, AND PUBLIC POLICY 69 (1995).

55. *Id.* at 70. Before computers, if a business wanted to record information about its customers, it had to collect data and record by hand, and then store in physical files that were labor-intensive to maintain. CATE, *supra* note 51, at 14.

56. JAMES RULE ET AL., THE POLITICS OF PRIVACY 154 (1980). *See also* REGAN, *supra* note 54, at 70 (explaining that data collection serves the needs of firms to make precise decisions about people); PAUL M. SCHWARTZ & JOEL R. REIDENBERG, DATA PRIVACY LAW 310 (1996) ("To identify prospective customers and design products tailored for those customers, direct marketing depends on the collection of massive quantities of personal information."); DIRECT MARKETING ASSOC., CUSTOMER RELATIONSHIP MANAGEMENT, A SENIOR MANAGEMENT GUIDE TO TECHNOLOGY FOR CREATING A CUSTOMER-CENTRIC BUSINESS EXECUTIVE SUMMARY, *at* http://www.the-dma.org/library/publications/customerrelationship.shtml ("Information about how customers interact with a company and use its products and services resides in data available from every customer interaction. That information is valuable - in fact, vital - in marketing, sales, service, organizational efficiency, and overall profitability."). For a discussion on how use of predictive models may have an adverse impact on certain segments of the population,

profiles that are used to predict response rates to various promotional offers.[57] For example, credit card firms can provide pre-approved credit without exposing themselves to significant default risk because targeted individuals have been selected based on substantial amounts of prescreened information. Similarly, banks can make better lending decisions without having to first establish a long-term relationship with each individual customer.[58] Such ready availability of information not only decreases the cost of doing business, but also increases companies' effectiveness at raising revenues. Furthermore, information is valuable in its own right. Information itself is a product that has monetary value. Some firms that profile their consumers will use the same data to compile marketing lists. These lists are then sold to other merchants to augment traditional sources of income.[59]

Clearly, demand for information is high. And yet, despite this intense demand, supply comes at a relatively cheap price. The costs for collecting, manipulating, storing, and transmitting electronic data are low.[60] The price of computers has declined[61] while advances in technology have significantly improved computing ability to process and store enormous amounts of data.[62] These advances have made information more readily accessible.[63] Databases facilitate rapid searches and organizations can locate a

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see Oscar H. Gandy, *Legitimate Business Interest: No End in Sight? An Inquiry into the Status of Privacy in Cyberspace*, 1996 U. CHI. LEGAL F. 77, 90 (1996).

57. Gandy, *supra* note 56, at 89.

58. Three national credit bureaus, Equifax, Experian, and Trans Union, provide firms with information to make business decisions regarding individuals. *See* SCHWARTZ & REIDENBERG, *supra* note 56, at 286.

59. BRANSCOMB, *supra* note 51, at 22. For example, credit card company American Express records their customers' buying habits in order to compile marketing lists that it sells to other merchants. *Id.* Also, direct marketing companies compile marketing lists and sell the personally identifiable information "to anyone who believes he or she might be able to use such information to turn a profit." *Id.* at 4.

60. CATE, *supra* note 51, at 1-2. This does not mean that information-processing systems are inexpensive. Instead, they perform services at a far lower cost than would be possible without them. *Id. at* 14-15. *See also* Gandy, *supra* note 56, at 81 ("advances in information technology serve to reduce the cost of transforming raw data into strategic intelligence").

61. WILLIAM C. BRAINARD & GEORGE L. PERRY, BROOKINGS PAPERS ON ECONOMIC ACTIVITY 1:2000 128 (2000) (reporting that in 1990-1995, the price of computers dropped 15% annually, and that between 1995-1998, the price decline accelerated to nearly 28%).

62. Schwartz, *supra* note 51, at 1335.

63. RULE ET AL., *supra* note 56, at 11 ("The new technologies . . . lead people to collect, store, and use all sorts of personal information which previously could not be

specific entry from volumes of records in fractions of a second.[64] Furthermore, in a networked society, the information in databases can be "seamlessly combined with other data sources to generate ever more comprehensive records of individual attributes and activities."[65]

This ability to selectively cull and collect information, as well as the capacity to correlate existing information, has been described as effectively being able to "create" new information.[66] As such, "personally-identified information is profligate."[67] It is this ubiquitous dissemination of information that has many people concerned about their privacy rights.[68]

B. The Right to Privacy

There is no single meaning behind the phrase "right to privacy."[69] Rather, the right has been invoked in a wide spectrum of issues. It ranges from protection for the most intimate of matters to protection for data. As-

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treated in these ways."). *See also* REGAN, *supra* note 54, at 69 ("[w]ith computerization[,] more information would be collected and retained and then disclosed or exchanged.").

64. REGAN, *supra* note 54, at 70.

65. Julie E. Cohen, *Examined Lives: Informational Privacy and the Subject as Object*, 52 STAN. L. REV. 1373, 1374 (2000). *See also* BRANSCOMB, *supra* note 51, at 3 ("[I]nformation that formerly resided in encoded scribblings on sheets of paper in dispersed locations, difficult to find, laborious to collect, and virtually impossible to correlate, can now be collected easily . . . . Collections of data now wind their way as patterns of electronic impulses into vast database where, by virtue of their comprehensive nature and instant cross-accessibility, they become commodities more valuable than the sum of their independent parts."); DAVID SADOFSKY, THE QUESTION OF PRIVACY IN PUBLIC POLICY 35 (1993) ("As computer technology advances, the ability to join . . . files [of the IRS, private credit agencies, criminal justice administrations, banks, telephone companies, and medical institutions] grows.").

66. A. Michael Froomkin, *Regulation and Computing and Informational Technology: Flood Control on the Information Ocean: Living with Anonymity, Digital Cash, and Distributed Databases*, 15 J.L. & COM. 395, 488 (1996) (quoting COLIN BENNETT, REGULATING PRIVACY: DATA PROTECTION AND PUBLIC POLICY IN EUROPE AND THE UNITED STATES 18 (1992)). It is important to note that the ability to create new information can lead to gathering data for the sake of gathering data. Joel R. Reidenburg, *Privacy in the Information Economy: A Fortress or Frontier for Individual Rights?*, 44 FED. COMM. L.J. 195, 203 (1992) ("Often, information may be gathered 'because it's there.'").

67. Cohen, *supra* note 65, at 1382.

68. *See infra* note 113.

69. There is no consensus on the concept of privacy. *See* JULIE C. INNESS, PRIVACY, INTIMACY, AND ISOLATION 3 (1992) ("[W]e find chaos; the [legal and philosophical] literature lacks an accepted account of privacy's definition and value."); ALAN F.WESTIN, PRIVACY AND FREEDOM 7 (1967) ("Few values so fundamental to society as privacy have been left so undefined in social theory or have been the subject of such vague and confused writing by social scientists.").

sertions extend from the right to make personal choices regarding contraception, marriage, and abortion[70] to the right to be free from government trespass.[71] Underlying these claims is the concept of the "right to be let alone."[72] Courts and legislatures, however, have declined to grant such sweeping protection.[73]

Currently, no single comprehensive privacy law exists.[74] Instead, general privacy rights stem from disparate sources. The U.S. Constitution,[75] state constitutions,[76] federal and state statutes,[77] and common law[78] all

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70. The Supreme Court addressed the right to privacy in the following cases: *Griswold v. Connecticut*, 381 U.S. 479 (1965) (striking down state statute that made it illegal for married persons to purchase contraception); *Loving v. Virginia*, 388 U.S. 1 (1967) (striking down state statute that prohibited interracial marriage); *Roe v. Wade*, 410 U.S. 113 (1973) (striking down Texas state law that prohibited all abortions except those necessary to protect the life of the mother).

71. U.S. CONST. amend. IV. For a discussion on the Fourth Amendment and the right to privacy, see DARIEN A. MCWHIRTER & JON D. BIBLE, PRIVACY AS A CONSTITUTIONAL RIGHT 92-93 (1992).

72. *See* Charles M. Horn, *Financial Services Privacy at the Start of the 21st Century: A Conceptual Perspective*, 5 N.C. BANKING INST. 89, 90-92 (2001). *See also* REGAN, *supra* note 54, at 34 (noting that privacy is "a common term denoting the ways in which one's 'right to be let alone' could be invaded").

73. For example, in *Bowers v. Hardwick*, the Supreme Court held that the right to privacy does not include the right for consenting adults to engage in homosexual oral or anal sexual activity, even in the privacy of their home. 478 U.S. 186 (1986).

74. CATE, *supra* note 51, at 98.

75. While the U.S. Constitution does offer limited privacy protection, *see supra* note 70, the Constitution does not provide an express right to privacy. CATE, *supra* note 51, at 98. Furthermore, the Constitution applies only to government action. *Id. at* 50.

76. The state constitutions of Alaska, California, Hawaii, Montana, South Carolina, Washington, Massachusetts, Rhode Island, and Arizona provide a general right to privacy. Scott A. Sundstrom, *You've Got Mail! (And the Government Knows It): Applying the Fourth Amendment to Workplace E-Mail Monitoring*, 73 N.Y.U. L. REV. 2064, 2076-77 (1998).

77. *See, e.g.*, ALA. CODE § 41-9-642 (2001) ("Disclosure of criminal histories or other information that may directly or otherwise lead to the identification of the individual to whom such information pertains may not be made to any person, agency, corporation or other legal entity that has neither the 'need to know' nor the 'right to know' as determined by the commission . . . ."); CAL. CIV. CODE § 1798.53 (2001) ("Any person, other than an employee of the state or of a local government agency acting solely in his or her official capacity, who intentionally discloses information, not otherwise public, which they know or should reasonably know was obtained from personal information maintained by a state agency. . . shall be subject to a civil action, for invasion of privacy, by the individual to whom the information pertains."); IOWA CODE § 235A.12 (2001) ("The general assembly finds and declares that a central registry is required to provide a single source for the state-wide collection, maintenance and dissemination of child abuse information. . . . The purposes of this section . . . [is] to facilitate the identification of victims or potential victims of child abuse by making available a single, statewide source of

provide some level of privacy rights depending on the competing interests involved. Without a broad right to privacy, however, protection is area-specific and narrow in scope.

In the area of informational privacy, the private sector lacks a set of privacy rights that addresses the acquisition, storage, disclosure, and use of all personally identifiable information.[79] Without a comprehensive privacy regime, regulations controlling the use of personal information in the private sector respond to narrowly tailored issues.[80] This narrow tailoring "presents an inherent limitation for thorough data protection."[81] While federal and state laws provide targeted protection for individuals in answer to defined problems, this issue-specific approach ignores the fact that information gathered in a given context often has substantial uses in other contexts. Such specific regulations, therefore, fail to address secondary uses of information.[82]

Privacy opponents have also invoked their First and Fifth Amendment rights.[83] In asserting freedom of speech rights, such users of information have argued that a right to informational privacy would prevent such users

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child abuse data . . . and to provide maximum safeguards against the unwarranted invasions of privacy which such a registry might otherwise entail.").

78. Long before the U.S. Supreme Court decided that the federal constitution provides some privacy protection, the right to privacy was derived from common law. *See supra* note 70. In a famous law review article, attorneys Samuel Warren and Louis D. Brandeis (later a Supreme Court justice) argued that common law principles dictated that everyone should own the "facts relating to his private life." *The Right to Privacy*, 4 HARV. L. REV. 193, 205 (1890).

79. Reidenberg, *supra* note 66, at 208. This reluctance to broadly regulate industry stems from the deep-seeded "fear of government intervention into private activities." *Id.* at 209.

80. *See id.*

81. SCHWARTZ & REIDENBERG, *supra* note 56, at 215. This targeted approach leads to "a patchwork of uneven, inconsistent, and often irrational privacy protection." CATE, *supra* note 51, at 80 (1997). *See also* JUDITH WAGNER DECEW, IN PURSUIT OF PRIVACY: LAW, ETHICS, AND THE RISE OF TECHNOLOGY 149 (1997) ("[T]he patchwork of legal protections is peculiar."). For example, there is stronger legal protection for information regarding a customer's video rentals than medical records. CATE, *supra* note 51, at 80-81. The Video Privacy Act of 1988 makes it illegal for video stores to disclose their customers' names, addresses, and the specific videotapes rented. Video Privacy Act of 1988, 18 U.S.C. § 2710 (2001). For a general discussion regarding privacy protection for medical information, see RICHARD C. TURKINGTON & ANITA L. ALLEN, PRIVACY LAW 198-227 (1999).

82. SCHWARTZ & REIDENBERG, *supra* note 56, at 270 (1996).

83. *See* Cohen, *supra* note 65. The First Amendment limits the government's regulation of speech. U.S. CONST. amend. I. The Fifth Amendment prohibits the government from taking private property without just compensation. U.S. CONST. amend. V.

from disseminating information, a protected form of speech.[84] Also, companies argue that because information is needed to reach their target audience, privacy restrictions hamper their "right to communicate with consumers."[85] In response, courts have acknowledged that the First Amendment does provide some protection for commercial speech.[86] To reinforce their position, companies have argued that they actually own the information. The Supreme Court has acknowledged the validity of this claim by extending the takings clause to protect stored data,[87] thus recognizing the property status of information. Consequently, opponents claim that government prohibitions that "substantially interfere with a private party's use of data that have been collected or processed, may require compensation under the Fifth Amendment."[88] Such arguments have contributed to the difficulty in limiting the use of personal information.

III. DISCUSSION

Though the GLBA provided Congress with an opportunity to revisit informational privacy, the GLBA clearly erred on the side of economic efficiency. At the same time, the GLBA can still be viewed as a partial victory for privacy advocates. How well this partial victory will fare in today's climate of increased concerns over national security remains to be seen. Nevertheless, the GLBA's privacy protections are not insignificant, as outlined below.

A. The GLBA Provides Some Privacy Protection

This Note defines informational privacy as "an individual's claim to control the terms under which personal information—information identifiable to the individual—is acquired, disclosed, and used."[89] This Note sug-

84. Eugene Volokh, *Freedom of Speech and Information Privacy: The Troubling Implications of a Right to Stop People from Speaking About You*, 52 STAN. L. REV. 1049, 1050-51 (2000).

85. Gandy, *supra* note 56, at 98. For an in-depth analysis of First Amendment implications, see Cohen, *supra* note 65, at 1409 (explaining that the flaw in asserting First Amendment principles is that it "assum[es] that the collection, processing, and exchange of personally-identified data are 'speech'").

86. *See, e.g.*, Central Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n, 447 U.S. 557 (1980).

87. Ruckelshaus v. Monsanto Co., 467 U.S. 986 (1984).

88. CATE, *supra* note 51, at 72.

89. Information Infrastructure Task Force, Privacy and the National Information Infrastructure: Principles for Providing and Using Personal Information (1995), *available at* http://www.iitf.nist.gov/ipc/ipc/ipc-pubs/niiprivprin_final.html. This definition is consistent with other proposed definitions. *See* WESTIN, *supra* note 69, at 7 (defining

gests that because an individual does not effectively control the terms under which his financial information is used, the claim to financial information privacy is a weak legal right at best.[90] The lack of protection becomes clear when we examine the problems that riddle Subtitle A of the GLBA: (1) The definition of nonpublic information is unclear; (2) Merely receiving information about a firm's privacy policy does not provide consumers with privacy protection; (3) Consumers cannot prevent disclosure of information to affiliates; (4) Consumers have limited control over the dissemination of information to third parties; and (5) Individuals have no recourse for violations.

1. *Nonpublic Information Does Not Necessarily Mean Private Information*

Many privacy advocates note that "[t]he boundaries between what is considered to be public information and what is considered to be private have been moving targets for several generations now."[91] This boundary is especially important because the Act does not restrict firms from sharing publicly available information.[92] In promulgating their rules, federal agencies[93] agree that information is "publicly available" if a financial institution has a "reasonable basis" to believe it is lawfully available to the general public from government records and widely distributed media.[94] In recognizing that media includes the Internet, the Federal Trade Commission acknowledged that information obtained from an Internet site can be considered public if the site is available to the general public. With the increasing breadth of the Internet, the line between private and public will continue to shift.

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informational privacy as "the claim of individuals, groups, or institutions to determine for themselves when, how, and to what extent information about them is communicated to others"); REGAN, *supra* note 54, at 70 (characterizing informational privacy as "the rights of individuals to control information about themselves"); Horn, *supra* note 72, at 91 (defining personal financial privacy as "the right of an individual to control the collection, disclosure and use of personal information concerning his or her financial transactions and affairs").

90. *But see* CATE, *supra* note 51, at 23 (proposing that general informational privacy is merely a social value rather than a legal right). However, even before the GLBA's enactment, Congress has provided some degree of informational privacy. *See supra* note 38.

91. BRANSCOMB, *supra* note 51, at 8.

92. Subtitle A expressly deals with only nonpublic personal information. Pub. L. No. 106-102, §§ 501-10, 113 Stat. 1338, 1436-45 (1999).

93. *See supra* note 41.

94. *See* Horn, *supra* note 72, at 108. A more restrictive definition of "publicly available" would have required that information have actually been obtained from a public source.

2. *Consumers are Not Empowered by Receiving Access to a Firm's Privacy Policy*

As noted earlier, section 503 requires that financial institutions provide consumers with their privacy policy.[95] During congressional hearings, proponents emphasized that the bill forces financial institutions to establish a privacy policy and to disclose that policy for the first time in U.S. history.[96] Proponents stressed that the required disclosures give consumers the most powerful tool that exists in a free society in protecting privacy: "if you do not like the bank's policy, you can take your business somewhere else."[97] There are glaring loopholes, however. Nothing in the Act, for example, prevents firms from sharing information about a former customer. Nor does the Act prohibit companies from changing their privacy policies after a consumer has signed on. Should an existing customer be dissatisfied with his firm's privacy policy, taking his business elsewhere does not prevent the old firm from sharing the information that they have already gathered about him with other affiliated firms.

3. *Consumers Cannot Prevent Disclosure of Information to Affiliates*

Even though Congress explicitly directs each financial institution to "respect the privacy of its customers,"[98] customers cannot opt-out of information sharing between affiliates. Allowing a single company to engage in banking, securities, and insurance activities increases the secondary uses of such information. For example, once a banking division obtains nonpublic personal information, there is no legal roadblock to prevent it from sharing that information with its insurance and securities divisions. As noted earlier, these affiliates can correlate existing data to create new information.[99] These exchange opportunities severely restrict an individual's ability to control access to his personal financial information.

This problem is further exacerbated by the fact that the GLBA fosters mergers among financial institutions.[100] Even without mergers, the mere existence of financial supermarkets and the resulting cross-sharing of in-

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95. Pub. L. No. 106-102, § 503, 113 Stat. 1338, 1439 (1999).

96. *Id.* § 503(a). While privacy policies must be disclosed at the time of establishing customer relationships for future customers, the Act does not address the concerns of existing customers who are dissatisfied with their companies' privacy policies.

97. 145 CONG. REC. S13,883, 13,913 (1999) (statement of Sen. Gramm).

98. Pub. L. No. 106-102, § 501, 113 Stat. 1338, 1436-37 (1999).

99. *See supra* notes 66-67 and accompanying text.

100. *See supra* note 30.

formation significantly decreases privacy.[101] Allowing and encouraging mergers only aggravates an already precarious situation since a merger will most likely result in a broader customer base from which to gather information.

Although individuals can take precautions to prevent this cross-sharing of information, such safeguards are not foolproof. An individual can choose to use separate entities for his financial needs. However, separate entities may use joint agreements[102] or contract out to third parties to service the individual's needs. Thus, information sharing may be unavoidable.

4. *Consumers Have Only Limited Control Over the Dissemination of Information to Third Parties*

As noted earlier, firms can share information if consumers fail to opt-out or if the purpose of the sharing falls under one of the many statutory exceptions. Failing to opt-out is remarkably easy. Due to the extensive use and value of information, companies have little or no incentive to facilitate the opt-out process. Privacy advocates describe the notices as "deceptive"[103] and argue that the opt-out language is buried in "legalese."[104] Furthermore, the GLBA does not provide any guidelines or standards for the opt-out process. As a result, each process is likely to include unique hurdles, requiring consumers to muddle through a different opt-out process for each firm. Moreover, many opt-out procedures are cumbersome. For example, some companies require their customers to first request an opt-out form, wait for the form to arrive by post, and then return the opt-out form by post.[105]

Additionally, even the statutory exceptions provide firms with significant discretion. Since firms are allowed to share information for proposed mergers or acquisitions,[106] the existence of a mere proposal is typically

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101. *See supra* notes 66-67 and accompanying text.

102. *See supra* note 46 and accompanying text.

103. Eric Roston, *How to Opt Out of Database Sharing; Who's Got your Number?*, TIME, July 2, 2001, at 46.

104. Don Oldenburg, *Protecting Your Financial Privacy*, WASH. POST, June 27, 2001, at C12.

105. Kathy Kristof, *Choice words for opting out; Consumers run into trouble with privacy forms*, CHI. TRIB., Aug. 7, 2001, at 7N. *See also* Robert MacMillan, *Few Net Banks Offer Clear Privacy Protections*, NEWSBYTES, Aug. 29, 2001 (stating that The Center for Democracy and Technology had reported that less than one-third of banks offer an online opt-out and some firms require customers to first call to request an opt-out form that would be sent via U.S. mail).

106. Pub. L. No. 106-102, § 502(e)(7), 113 Stat. 1338, 1438 (1999).

enough to allow companies to trade nonpublic information on their respective consumers. Also, even if an individual specifically avoided financial supermarkets and took his business to several different firms, there is no guarantee that someday these separate entities will not become part of a larger financial conglomerate. Maybe the most disconcerting exception is the "disclosure of nonpublic information for required institutional risk control."[107] Congress not only failed to define "institutional risk" control in this section, but failed to discuss it anywhere in the Act. This exception seems to allow broad discretion for information sharing.

5. *Firms Have Little Incentive to Comply*

Finally, the GLBA does not provide any remedies for individuals should a firm fail to comply with any of the disclosure provisions. Various federal regulators, state insurance authorities, and the Federal Trade Commission have responsibility for enforcing these provisions.[108] However, according to Section 505(b)(1), enforcement equates to implementation of standards.[109] As one commentator pointed out, "the law establishes . . . overlapping regulatory supervisory enforcement mechanisms to identify and correct abusive policies and practices rather than to remedy or resolve individual rights affected by specific infractions. The structure is thus somewhat illusory, lacking in any recourse for an individual to remedy the infringement of his or her privacy."[110] Without the threat of monetary remuneration, adherence to these privacy provisions may not be a high priority for firms faced with a barrage of economic pressures. This lack of remedies further compromises the individual's right to privacy.

B. The Trade-off between Privacy and Efficiency

The natural conclusion from the above analysis is that the GLBA does not create a strong right to informational privacy because of the inherent trade-off between efficiency and privacy. There is no question that information spawns efficiency. According to former President Clinton's Information Infrastructure Task Force "[i]nformation is one of the nation's most critical economic resources."[111] Even privacy advocates agree that

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107. *Id.* § 502(e)(3)(C).

108. *Id.* § 505.

109. *Id.* § 505(b)(1).

110. David W. Roderer, *Tentative Steps Toward Financial Privacy*, 4 N.C. BANKING INST. 209, 213 (2000).

111. Information Infrastructure Task Force, *National Information Infrastructure Agenda for Action*, *at* http://www.ibiblio.org/nii/NII-Agenda-for-Action.html. *See also* BRANSCOMB, *supra* note 51, at 7 ("the most developed economies have become information-dependant"); OFFICE OF TECHNOLOGY ASSESSMENT, COMPUTER-BASED NATIONAL

"[i]nformation is the lifeblood that sustains political, social, and business decisions."[112] Under the GLBA, financial supermarkets can more easily correlate information, thereby fostering efficient business decisions. At the same time, there is no question that people want privacy. Surveys show that people are concerned about their growing lack of privacy.[113] Therefore, the issue is when, if ever, does the interest in privacy trump the need for information.

Clearly, privacy does not trump the need for information under the GLBA. Congress could have provided stronger privacy protection. For example, the GLBA could have required firms to affirmatively obtain the consumer's consent to information sharing between third parties by requiring opt-in rather than opt-out. However, companies would have had to expend resources to obtain express consent. This would have come at the sacrifice of efficiency. The GLBA could have also imposed stronger limitations on information sharing among firms. This could been accomplished in two ways: 1) by requiring financial supermarkets to establish walls between databases that hold banking, securities, and insurance information;[114] and 2) by allowing consumers to opt-out of information sharing between affiliates, rather than limiting it to nonaffiliated sharing. Restricting the use of this information in these ways, however, would also have come at the sacrifice of efficiency. By providing consumers only limited control over dissemination of information to third parties and by pro-

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INFORMATION SYSTEMS 47 (1981) ("The more complex a society, the more central information is to its economic activities."), *at* http://www.wws.princeton.edu/~ota/ns20/alphaf.html.

112. Anne W. Branscomb, *Global Governance of Global Networks: A Survey of Transborder Data Flow in Transition*, 36 VAND. L. REV. 985, 987 (1983).

113. Privacy Rights Clearinghouse, *Public Attitudes About the Privacy of Information*, *at* http://www.privacyrights.org/ar/invasion.htm. The 1997 Money Magazine Poll reports that 74% of the public are somewhat or very concerned about threats to their privacy and that 64% are more worried now than 5 years ago. *Id.* In a 1998 survey done by AARP's Public Policy Institute, 81% of respondents opposed the sharing of personal and financial information by affiliates. *Id.* Despite consumer concern regarding privacy, industry reports indicate that only 5% of people opted-out. W.A. Lee, *Opt-Out Notices Give No One a Thrill*, THE AMERICAN BANKER, July 10, 2001, at 1. Companies assert that people are not as concerned about privacy as originally thought. *See id.* However, privacy advocates argue that the notices explaining the opt-out procedures are confusing. *See supra* notes 103-105 and accompanying text . Furthermore, many consumers may not have even read the notices. *See supra* note 104 (reporting that according to a recent American Bankers Association Survey, 41 percent of respondents said they could not recall receiving any privacy notices, 22 percent said they received the notices but did not read them, and 36 percent said they had read the notices they received).

114. *See supra* note 35.

hibiting consumers from seeking recourse for privacy violations, Congress has clearly ruled that efficiency is paramount in today's economy.

C. The GLBA is Still A Partial Victory For Privacy Advocates

Despite the inherently weak nature of privacy restrictions in the GLBA, their inclusion should be viewed as a partial victory for privacy advocates for three reasons. First, the laws do increase privacy protection to a certain extent. Prior to the GLBA, firms were able to utilize information without any real limits.[115] Subsequent to the GLBA, firms further depend on information to make strategic decisions about customers, but the use and exchange of such information is regulated by the government.

Second, inclusion of these privacy provisions represents a notable and significant victory over the business lobby. These privacy provisions were included over strong objections by lobbyists. As the first legislation to impose a federal standard of privacy for financial information on private companies,[116] the GLBA represents a partial victory for privacy advocates. Although companies now have increased access to information, they also bear a corresponding responsibility for ensuring certain levels of privacy of such information.

Third, and finally, the GLBA does not preempt state privacy laws. Privacy advocates are not barred from lobbying states to enact greater privacy protection.[117] To achieve more substantial victories, however, privacy advocates will have to justify trade-offs that would likely result in decreased efficiency.[118]

IV. CONCLUSION

Under the GLBA, companies still have the upper hand in controlling financial information. Many in Congress, however, have already attempted to pass amendments that would provide stronger privacy protec-

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115. *See supra* note 38. *See also* note 59 and accompanying text.

116. *See supra* note 38.

117. Pub. L. No. 106-102, § 507, 113 Stat. 1338, 1442 (1999). However, this may prove problematic because "a system of fifty different legal regimes for privacy is ill-suited to a marketplace such as the Internet, where geographic borders are essentially irrelevant." Robert E. Litan, *Law and Policy in the Age of the Internet*, 50 DUKE L.J. 1045, 1066 (2001) (discussing the interaction between the GLBA and the Internet, and arguing that different standards of privacy imposed by states will increase transaction costs).

118. For a discussion proposing decreasing reliance on information, see RULE ET AL., *supra* note 56, at 153-64.

tion.[119] Yet, the momentum for increased privacy rights may have come to a halt in light of the new public concern over national security.[120] With recent terrorist attacks on the U.S. and the need for greater national security, the government and lobbyists alike have both slowly backed away from privacy legislation. For example, the Federal Trade Commission recently announced that it would no longer pursue stronger consumer privacy laws.[121] Despite these developments, many still believe that the GLBA did not strike the proper balance between efficiency and privacy. Nevertheless, in a society that values information, any substantial trade-off that leads to decreased efficiency may be difficult to defend.

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119. For example, prior to recessing this past August, Reps. Edward Markey (D-Mass) and Joe Barton (R-TX) introduced H.R. 2720 which would require an opt-in process rather than the more troublesome opt-out process. Robert MacMillan, *Bills Would Alter Financial Privacy Protections*, NEWSBYTES, Aug. 29, 2001.

120. With the terrorist attacks of September 11, 2001, advocating the need for increased privacy may now be a difficult proposition. *See* JAMES F. HOGE, JR. & GIDEON ROSE, HOW DID THIS HAPPEN? TERRORISM AND THE NEW WAR 152-54 (2001) (proposing that the "traditional American reverence for privacy" imposes constraints on domestic intelligence operations and that loosening those constraints would have helped to avert the September 11 tragedies).

121. Associated Press, *FTC Chairman to Drop Call for New Internet Privacy Laws*, (Oct. 2, 2001). In response to the change in the administration's position, one privacy advocate stated, "[i]f the speech was delivered on Sept. 10, it would have been viewed as a negative event in the privacy community. Now that it's delivered after the 11th, it's a crisis. It looks like we've lost federal government support." *Id.*

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TELECOMMUNICATIONS

RECENT DEVELOPMENTS—TELECOMMUNICATIONS

CITY OF AUBURN V. QWEST CORP.

260 F.3d 1160 (9th Cir. 2001)

The United States Court of Appeals for the Ninth Circuit examined whether the federal Telecommunications Act of 1996 preempted local ordinances regulating telecommunications companies.

Section 253(a) of the federal Telecommunications Act of 1996 bars all state and local regulations that prohibit or have the effect of prohibiting any company's ability to provide telecommunications services unless the regulation falls within one of the statute's safe harbor provisions. In relation to the present case, section 253(c) permits local ordinances that regulate public rights-of-way. Multiple cities passed such local regulatory ordinances. Under these ordinances, telecommunications service providers wishing to operate in a city had to apply to that city for a franchise. Only franchised telecommunications companies could install facilities in public rights-of-way. In order to obtain a franchise, telecommunications companies had to submit lengthy and detailed application forms, including maps, corporate policies, documentation of licenses, and "such other and further information as may be requested by the city." The ordinances also regulated transferability of ownership and charged fees unrelated to maintenance of the public rights-of-way. Further, each city reserved discretion to grant, deny, or revoke franchises for unnamed reasons. Faced with these requirements, Qwest sought a declaratory judgment that the federal Telecommunications Act of 1996 preempted such ordinances as unreasonable prohibitions on the ability to provide telecommunications services. The district court dismissed Qwest's claim as unripe on the grounds that the analysis would be better-conducted following specific attempts by the cities to enforce their telecommunications ordinances.

However, the Ninth Circuit found the case ripe for judicial resolution. It found that the cities' requirements to obtain a franchise, taken together, had the effect of prohibiting Qwest and other companies from providing telecommunications services and, therefore, created a substantial and unlawful barrier to entry into the telecommunication market. The court held that the ordinances attempted to regulate the telecommunication companies themselves rather than the public rights-of-way. In reaching this decision, the court considered the cities' (1) requirement that the applicant submit proof of its financial, technical, and legal qualifications to provide services, (2) regulation of the transferability of ownership, (3) requirement that the companies provide participating cities with best available rates, and (4) reservation of the right to grant, deny, or revoke franchises based on unnamed factors. Thus, the court held the ordinance's requirements overly burdensome and preempted it as outside the realm of section 253(c).

FEDERAL COMMUNICATIONS COMMISSION FIRST REPORT AND ORDER AND FURTHER NOTICE OF PROPOSED RULEMAKING IN THE MATTER OF: CARRIAGE OF DIGITAL TELEVISION BROADCAST SIGNALS

Congress requires cable broadcasters to provide channels for local television stations. Thus, under sections 614 and 615 of the Communications Act of 1934 ("the Act"), and FCC rules, commercial and noncommercial educational (NCE) television broadcast stations are entitled to request carriage on cable systems located within the station's market. The cable operators must carry the local stations on certain channels and must not degrade the local stations' signals. Cable operators must only carry primary video, and are not required to carry duplicative local stations. Additionally, sections 325 and 336 of the Act relate to retransmission consent and broadcast spectrum flexibility and ancillary and supplementary services.

The television industry is currently undergoing a transition from analog to digital television broadcasting. On January 23, 2001, the FCC released its First Report and Order and Further Notice of Proposed Rulemaking, regarding the impact of the transition from analog to digital television on various regulations on cable television broadcasters.

The first issue was whether cable operators must immediately (during the transition) provide both digital and analog signals of local stations' broadcasts. Such duplicative broadcasting might force cable operators to drop other programming services if channel capacity is limited. The FCC decided not to resolve this dual carriage issue in this order, and requested more comment. However, the Commission did clarify (by amending sections 76.5 and 73.622) that digital-only local commercial and NCE television stations were entitled to mandatory carriage by cable operators.

The FCC then turned to retransmission consent issues. Section 325 of the Act prohibits cable operators from broadcasting the signals of local *commercial* television stations unless the local stations consent or choose mandatory carriage. The Commission held as follows. First, stations that simultaneously broadcast analog and digital signals are permitted to treat the signals differently for carriage purposes. Thus, a station can carry out separate negotiations regarding the two signals with cable operators. Stations that broadcast only digital signals are treated just as analog-only stations. Second, stations that commence digital operations will be treated as new stations for purposes of electing either retransmission consent or mandatory carriage, and thus do not need to wait until the end of the three-year election cycle. Third, at least during the transition phase, when a digital-only or digital-and-analog television station consents to retransmission, it may negotiate with the cable operator for partial carriage of the local digital television signal. Fourth, superstations' digital signals are treated the same as their analog signals for retransmission consent purposes. Thus, cable operators are exempt under section 325(b)(2)(D) of the Act from the obligation to obtain retransmission consent from superstations' analog and digital signals if those signals are available by a satellite or common carrier on May 1, 1991. Fifth, exclusive retransmission consent agreements between digital or analog television broadcast stations and cable operators are prohibited until January 1, 2006. Sixth, "tying" arrangements, in which a television broadcaster requires the cable operator to carry its digital signal as a condition of carrying its analog signal, are not prohibited at this time. The Commission requested more information regarding this issue. Seventh, as NCE stations are not covered by section 325 of the Act, an NCE station can-

not withhold its signal from being carried by any multi-video programming distributor or cable operator. However, an NCE station can negotiate for voluntary carriage, and thus for exclusive digital carriage arrangements for any signals not subject to mandatory carriage under section 615 of the Act.

The FCC then addressed ten issues regarding digital signal carriage requirements. First, the Commission asked whether the new digital technology has changed how channels should be defined for the purposes of section 614(b)(1)(B) of the Act, which provides that a cable operator with more than twelve usable activate channels is not required to devote more than one-third of the aggregate number of usable activated channels for the carriage of commercial television stations. Traditionally, analog channels were defined in 6 MHz blocks. However, the new digital technology allows signals to be compressed so that several signals can fit within a 6 MHz block. The Commission held that channel capacity should not be determined by counting the number of 6 MHz blocks. Instead it should be calculated by taking the total usable activated channel capacity of the system in MHz and dividing it by three. This number is the limit on the amount of system spectrum that a cable operator must make available for commercial broadcast signal carriage purposes. Usable activated channels are defined as previously set out in section 76.5(nn) (section 602(1) of the Act) and section 76.5(oo) (section 602(19) of the Act), and may include the cable spectrum used for internet service, pay-per-view, video-on-demand, and telephony. Once the one-third quota has been met, the cable operator has discretion to choose which signals it will carry. NCE stations are not included in the calculation.

Second, section 614(h) of the Act requires stations to deliver a good quality signal to the principal headend of the cable system, in order to qualify for carriage. As degradation presents unique problems in the digital signal context, the Commission established a new standard for digital signals. Specifically, stations must maintain a minimum signal level of—61 dBm at the principal (cable system) headend.

Third, section 614(b)(3) of the Act requires the cable operator to carry "primary" video in its entirety, along with accompanying audio, closed caption, and, to the extent feasible, program-related material carried in the vertical blanking interval. Section 615(g)(1) of the Act provides similar rules for NCE stations. Digital broadcasts may carry many concurrent signals including multiple high or standard definition digital television programs, making it difficult to determine what is "primary" video. The Commission held that only one video stream (along with program-related content) of multiple simultaneous streams can be considered primary. The broadcaster chooses which stream is primary. Cable operators must provide mandatory carriage for primary video program-related content, but not for separate, independent and unrelated programming streams, or for ancillary or supplementary services under section 336 of the Act. The FCC noted that section 73.624(c) of the Commission's Rules provides examples of such ancillary or supplementary services. An example of unrelated programming might be e-commerce applications. The FCC revised its Rule in section 76.56(e) to modify its three-part test for determining what is program-related to take into account technological differences between analog and digital programming. The Commission also held that program guide data is not program-related, and thus is not subject to mandatory carriage. Finally, the FCC held that section 336 of the Act precludes a digital television station offering video services for a fee from asserting multichannel video programming distributor status under the FCC's rules and claiming program access right pursuant to section 628 of the Act.

Fourth, the Commission found that it did not have enough information to revise its rules implementing section 614(b)(5) of the Act. This section permits a cable operator to

decline to carry a station's signal if it substantially duplicates another local television station's signal. The applicable rule states that two commercial television stations are considered to substantially duplicate each other if they simultaneously broadcast identical programming for more than fifty percent of the broadcast week. An NCE station does not duplicate another NCE station if at least fifty percent of its typical weekly programming is distinct from the other station.

Fifth, the Commission asked how the Act's sections 614(b)(4)(A) and 615(g)(2) material degradation requirements apply to digital signals. First, the FCC believes that material degradation should be measured by consumer perception, not by the amount of digitized information. In order to determine whether the signal has degraded, it should be tested at the input terminal of either the television set or set-top box if the subscriber owns that piece of equipment, or at the output point of the set-top box if the subscriber rents that equipment from the cable operator. Second, because section 614(b)(4)(A) of the Act requires that cable operators provide the same quality of signal processing and carriage for broadcasters' signals as they provide for any other type of signal, mandatory carriage of digital broadcast signals must be provided at the same perceptible quality as other digital programs. Third, the Commission held that a television station may demand that one of its HDTV or SDTV signals be carried on the cable system for delivery in analog format, without violating the nondegradation requirement, at least during the early stages of the transition period. Fourth, the FCC will allow cable operators to remodulate digital broadcast signals.

Sixth, the Commission will not require cable operators to provide subscribers with a set-top box that would allow the viewing of digital broadcast signals by a non-digital cable ready television receiver. Owners of analog television receivers will be able to view analog simulcasts.

Seventh, sections 614(b)(6) and 615(g)(5) of the Act generally provide that television stations carried pursuant to the mandatory carriage provision are entitled to be carried on the same channel number. Nevertheless, the FCC held that in view of the channel display menus made possible by digital signal technology, channel positioning requirements will not be implemented. Accordingly, cable operators are required to pass through program-related channel mapping data.

Eighth, the FCC did not alter its method for assessing a television's market area under section 614(h)(1)(C) of the Act. For both analog and digital signals, Nielsen Media Research determines the relevant market reached by stations' programming. However, the FCC recognized that the technical coverage area of digital and analog signals might not be exactly the same. The FCC will consider changes in signal strength and Grade B contour coverage. All other matters will be decided on a case-by-case basis.

Ninth, the Commission will allow cable operators to place required qualified NEC and low power television stations on unused public, educational, or governmental channels not in use for their designated purposes.

Tenth, the process for filing complaints under section 614(d)(3) of the Act by television stations will be left unchanged.

Next, the FCC turned its attention to possible changes to other Part 76 requirements. First, under sections 653(c)(1) and (c)(2)(A) of the Act, any provision applied to cable operators must apply no greater or lesser to open video systems. Thus, the FCC clarified that open video systems must adhere to the rules adopted for the cable industry, including carrying digital-only television stations.

Second, cable operators must notify their subscribers whenever a digital television signal is added to the cable channel line-up or whenever such a signal is moved to another channel location. However, a cable operator is not required to notify subscribers of the programming available on each possible SCTV digital stream.

Third, the rules regarding cable television relay service microwave stations will remain unchanged in light of the absence of comment.

Fourth, program exclusivity rules implemented in sections 76.92 and 76.101 of the FCC's rules will remain unchanged because there is an inadequate record. Exclusive distribution rights afforded to network and syndicated programming through private agreements will be protected.

Fifth, the Commission interpreted section 623(b)(7) of the Act to require that digital signals be provided to all cable subscribers on the same basic, lowest priced tier as analog signals. However, because the Commission believes that section 623(b)(7) does not apply once competition is present in the franchise area, if a cable system faces effective competition, and is deregulated pursuant to an FCC order, the cable operator can place a broadcaster's digital signal on upper tiers of service or on a separate digital service tier.

Sixth, the rate regulation processes in place should generally be applied to the addition of digital programming. Thus, a cable operator may raise rates to cover the costs of upgrading equipment to supply digital broadcasting to subscribers. However, only subscribers of digital programming should pay the increased rates.

Finally, the FCC issued a further notice of proposed rulemaking. The FCC sought comment on a number of issues including the following: First, is dual carriage needed for a successful transition to digital television and return of the analog spectrum? Specifically, the Commission would like to establish a record of possible harm to television stations in the absence of dual carriage, in anticipation of a First Amendment challenge before the U.S. Supreme Court. Second, as we are in the midst of the transition from analog to digital, the FCC requests comments on how the affected parties expect to complete the transition, how the law applies, the current state of digital technology and availability of programming, the quantity of digital programming, and issues relating to small operators, in order to better formulate future rules and policy. Third, what exactly does "program-related" mean in the digital context? Fourth, what is the available usable channel capacity, and what are the implications of techniques that conserve or recapture cable channel capacity? What are the feasibility and implications (e.g., copyright, advertising rate structure) of a proposal to adopt digital carriage rules that allow cable operators to deliver services from video servers through the internet's channel addressing methodology? Fifth, what is the extent of the prevalence and scope of voluntary carriage agreements in the digital signal context? Sixth, what is the effect of new ownership rules affecting the number of television stations in any given market that can be owned or controlled by a single broadcaster? Seventh, should digital channels be placed on different pricing tiers than analog channels? Eighth, what effect will the addition of digital broadcast services to cable operators' channel line-ups have on the FCC's per channel rate adjustment methodology? Ninth, should the FCC adopt different rules regarding implementation of the Satellite Home Viewer Improvement Act of 1999, for digital broadcasts, than it did for analog broadcasts?

MEDIAONE GROUP INC. V. COUNTY OF HENRICO, VIRGINIA

257 F.3d 356 (4th Cir. 2001)

The United States Court of Appeals for the Fourth Circuit determined whether Henrico County could condition its approval of the transfer of control on an open access provision or whether the federal Communications Act preempted such a conditioned approval.

MediaOne provided bundled services, combining their broadband pipeline with Internet services offered by other Internet Service Providers ("ISPs"). AT&T acquired MediaOne and applied to Henrico County for formal approval of AT&T's control of MediaOne. Henrico County conditioned its approval on MediaOne providing open access to its cable modem platform to all ISPs. AT&T and MediaOne sued the county in federal court arguing that the federal Communications Act preempted this condition on approval. Verizon intervened as a defendant. The district court granted summary judgment to AT&T and MediaOne, finding that the open access conditioned approval violated the Communications Act.

Henrico County and Verizon appealed. The appellate court affirmed the district court's granting of summary judgment. The court found that forcing MediaOne to provide its cable modem platform to an ISP, as a condition for transfer of control, violated 47 U.S.C. § 541(b)(3)(d) of the federal Communications Act. Section 541(b)(3)(d) states that a "franchising authority may not require cable operators to provide any telecommunications . . . facilities . . . as a condition of the . . . transfer of a franchise." The court rejected the County's argument that MediaOne was not required to provide access to "telecommunications facilities" because MediaOne was primarily a "cable system." Instead, the court relied on Section 153(43)'s definition of "telecommunications," as "the transmission, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information as sent and received." The court also found that MediaOne's services could be classified as telecommunications services (rather than mere cable system services) because the Communications Act contemplates multi-use facilities receiving different regulatory classifications depending on the services they provide at a given time. Therefore, although MediaOne maintains a cable system, its facilities are properly classified as telecommunications facilities when they provide transmission paths to the Internet. As such, Henrico County violated section 541(b)(3)(d) when it conditioned the transfer of control of MediaOne on open access to its telecommunication facilities.

TIME WARNER ENTERTAINMENT CO., L.P. V. FEDERAL COMMUNICATIONS COMMISSION

240 F.3d 1126 (D.C. Cir. 2001)

In this case, owners of cable television systems petitioned the United States Court of Appeals for the District of Columbia Circuit for review of FCC regulations promulgated pursuant to the Cable Television Consumer Protection and Competition Act of 1992 ("Cable Act"). The regulations at issue generally dealt with attempts by the FCC to prevent anticompetitive behavior in the cable industry. The court's opinion dealt with five distinct issues.

Section 11(c) of the Cable Act sets two types of limits on Cable operators: horizontal and vertical. The horizontal requirement limits "the number of cable subscribers a person is authorized to reach through cable systems owned by such person, or in which such person has an attributable interest." 47 U.S.C. § 553(f)(1)(A). The goal of this limit is to "ensure that no cable operator or group of cable operators can unfairly impede, either because of the size of any individual operator or because of joint actions by a group of operators of sufficient size, the flow of video programming from the video programmer to the consumer." 47 U.S.C. § 553(f)(2)(A).

The FCC implemented the horizontal requirement by setting a thirty percent limit on the number of subscribers that may be served by a multiple cable system operator. The FCC argued that this number satisfied its statutory obligation under the Cable Act to prevent anticompetitive behavior and promote diversity. The court held that the FCC's regulation failed to pass intermediate scrutiny. First, although the court agreed that the FCC has authority to prevent companies from engaging in anticompetitive behavior, it found that neither Congress nor the FCC presented substantial evidence that companies, either independently or in collusion with other firms, had behaved, or were likely to behave, anticompetitively. Second, the court held that Congress did not give the FCC authority to impose a limit that does more than guarantee a programmer two possible outlets, based solely on the goal of promoting diversity. Under Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984), the court found that Congress's primary concern was not promoting diversity but fair competition. The court reversed and remanded with respect to the thirty percent horizontal requirement.

The vertical requirement limits "the number of channels on a cable system that can be occupied by a video programmer in which a cable operator has an attributable interest." 47 U.S.C. § 533(f)(1)(B). The FCC's rule implementing the vertical limit required that sixty percent of channel capacity (up to 75 channels) be set aside for nonaffiliated firms' programming. Again, the FCC argued that this number satisfied its statutory obligation under the Cable Act to prevent anticompetitive behavior and promote diversity. The court found that the vertical rule failed to pass intermediate scrutiny because the FCC did not justify the rule as not burdening substantially more speech than necessary: "the FCC seems to have plucked the 40% limit out of thin air." The court reversed and remanded with respect to the forty percent rule. Additionally, the court found that there was no basis for the FCC's decision not to exempt cable companies that are subject to effective competition.

The FCC also promulgated rules for attributing ownership for purposes of applying the horizontal and vertical limits. First, under the FCC's rules, ownership of five percent of the voting shares of a company signifies attribution. The court upheld this rule on the grounds that there was adequate evidence that the rule would address situations of influ-

ence over companies. Second, the FCC also defines attribution by an investor who holds an interest in a company exceeding thirty-three percent of equity and debt. Finding that the thirty-three percent debt and equity limit had support in the record, the court upheld the rule.

The FCC eliminated an exemption in the broadcast attribution rules for a minority shareholder in a company with a single majority shareholder. The court found standing, and reversed the FCC's decision on the ground that the FCC offered no affirmative justification for eliminating the exemption.

Finally, the court reversed an FCC interpretation regarding sale of programming to the partnership by a limited partner. In general, a limited partner is exempt from attribution if that partner ensures that it is not materially involved in management, day-to-day control, or controlling programming choices. The FCC interpretation eliminated this exemption when the limited partner is a vertically integrated multiple cable system operator that sells programming to the partnership. Thus, such partners could not sell programming to the partnership. The court reversed this exemption elimination on the grounds that it was not rationally related to the goal of restricting the limited partner from controlling the partnership's programming choices, particularly in light of other means for restricting that control.

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ENTERTAINMENT LAW

HOFFMAN V. CAPITAL CITIES/ABC, INC.

By Chia Heng (Gary) Ho

Fame is valued. Consumers want to feel close to and identify with celebrities.[1] As a result, businesses pay high fees to acquire celebrity endorsements.[2] Because of the value attached to their fame, celebrities often sue to enjoin unauthorized and commercial uses of their names and likenesses.[3] They do so by exercising their rights of publicity, rights the law grants to every individual to protect the commercial value in his or her identity.

To celebrities' delight, the Ninth Circuit has consistently granted famous plaintiffs expansive publicity rights.[4] These rights empower individuals to control whether and how others can use information about public figures, and thereby trigger First Amendment concerns.[5] But Ninth Circuit jurisprudence has yet to directly clash with the First Amendment. That is because the court's publicity cases have dealt mostly with appropriations of identity that function solely as a means of commercial exploitation—appropriations that implicate minimal First Amendment interests.[6] Not all appropriations are this one-dimensional; many seek to simultaneously exploit identities and communicate information. How should a court deal with an appropriation that consists of both commercial and communicative elements?[7]

The Ninth Circuit recently faced this question in a case brought by actor Dustin Hoffman against Los Angeles Magazine, after the magazine

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1. John Gibeaut, Image CONSCIOUS, 85 A.B.A. J. 47 (1999).

2. Eleanor Johnson, *Henley v. Dillard Department Stores: Don Loves His Henley, And Has a Right to It Too*, 45 VILL. L. REV. 169 (2000).

3. *See id.*

4. Erika Paulsrude, *Not the Last Dance:* Astaire v. Best Film & Video Corp. *Proves California Right of Publicity Statutes and the First Amendment Can Co-Exist*, 18 LOY. L.A. ENT. L.J. 395, 397 (1998).

5. Alicia M. Hunt, *Everyone Wants to be a Star: Extensive Publicity Rights for Noncelebrities Unduly Restrict Commercial Speech*, 95 NW. U. L. REV. 1605, 1616 (2001).

6. *See* White v. Samsung Elecs. Am., Inc., 971 F.2d 1395 (1992) (advertisements for electronic product); Abdul-Jabbar v. Gen. Motors Corp., 85 F.3d 407 (1996) (television commercials for automobiles); Midler v. Ford Motor Co., 849 F.2d 460 (1988) (television commercials for automobiles).

7. Roberta Rosenthal Kwall, *The Right of Publicity vs. the First Amendment: A Property and Liability Rule Analysis*, 70 IND. L.J. 47(1994).

used Hoffman's likeness in an article.[8] In its decision, the court ruled against Hoffman on First Amendment grounds.[9] The core of the Ninth Circuit's holding was its characterization of the magazine's appropriation of identity as "communicative" rather than "commercial."[10] This characterization is crucial because "communicative speech" receives maximum First Amendment protection, while "commercial speech" receives only minimum protection.[11] Thus, the validity of a First Amendment defense to publicity rights depends on whether an appropriation of identity is categorized as communicative or commercial. Unfortunately, courts have not clearly delineated the line between these two categories.[12]

A line-drawing device does exist in the often-used "primary message"—or "primary nature of the use"—test.[13] This test weighs the commercial and communicative elements of speech to determine its primary or predominant message.[14] It takes a case-by-case and fact-specific approach, giving judges moderate guidance and considerable discretion. Instead of drawing a clear line, the test aims for a careful balancing of relevant interests.

The *Hoffman* court followed the general contours of the primary message approach. But its terse opinion also suggested (or alluded to) concepts not explicitly associated with the primary message test: the inextricably entwined doctrine and a focus on the medium in which identities are appropriated. It is unclear whether the court intended to incorporate these new concepts into the line-drawing process. Regardless of that fact, this Note will consider whether these concepts may in fact serve as useful additions—guidelines or parameters—to the primary message test.

This Note will take the form of a comparative analysis. Instead of selecting the best line-drawing method, it aims to show the strengths and weaknesses of various concepts and approaches. Furthermore, it seeks to highlight the fundamental problems afflicting attempts to resolve the inherent conflict between free speech and publicity rights.

The discussion is divided into three parts. First, the primary message test is evaluated to see if it does need additional guidelines or parameters.

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8. Hoffman v. Capital Cities/ABC, Inc., 255 F.3d 1180 (2001).

9. *Id.* at 1189.

10. *See id.* at 1184-86.

11. *See* J. THOMAS MCCARTHY, THE RIGHTS OF PUBLICITY AND PRIVACY 7-3, 8-16, 8-17 (2d ed. 2001).

12. *Hoffman*, 255 F.3d at 1184.

13. MCCARTHY, *supra* note 11, at 8-149, 8-150.

14. *Id.*

The discussion then turns to the strengths and weaknesses of the two concepts raised by the *Hoffman* opinion. Lastly, the discussion concludes with a brief analysis of the proposal to import an element of the fair use doctrine into the right of publicity regime. In conclusion, this Note will suggest that none of these concepts or approaches can alone solve the problem at issue. Rather than prematurely devising a definitive test or drawing a bright line, courts should apply a combination of factors in each case to accommodate the relevant interests at issue.

I. BACKGROUND

A. Right of Publicity

1. Historical Development

The right of publicity is the inherent right of every human being to control the commercial use of her or his identity.[15] This right developed within privacy law,[16] a field that initially revolved around the right to prevent intrusive and embarrassing disclosures by the press.[17] A considerably different variation on this theme soon developed in the *Roberson* and *Pavesich* cases.[18] This variation concerned lawsuits challenging unauthorized uses of a person's name or likeness for advertising or trade purposes.[19]

At first, only unknown people complained in courts about uses of their identities in advertising.[20] Thus, courts focused on traditional privacy concepts of personal injury to dignity and state of mind, measured by mental distress damages.[21] But then "famous plaintiffs" began to sue too.[22] They did not want to forbid the commercialization of their identities; they just wanted the right to control their use.[23] But judges could not see how public figures could suffer mental distress when their identities were already in

15. *Id.* at 1-2.
16. *Id.* at 1-9.
17. *Id.* at 1-11.
18. Roberson v. Rochester Folding Box Co., 64 N.E. 442 (N.Y. 1902); Pavesich v. New England Life Ins. Co., 50 S.E. 68 (Ga. 1905).
19. *Id.*
20. MCCARTHY, *supra* note 11, at 1-7.
21. *Id.*
22. *Id.*
23. *Id.*

widespread use in the media.[24] Thus, the claims of public figures were rejected.[25]

But one maverick judge soon realized that the right at issue in these new cases was commercial in nature and could not be confined by traditional privacy law. Breaking the "privacy" mold of thinking, Judge Jerome Frank coined the term "right of publicity" in the *Haelan* decision.[26] He used the term to denote a property right in a person's identity, which is a purely commercial interest, as distinct from a "mental distress" interest.[27] Such a property right can be infringed by the use of a person's identity, without permission, in a commercial context. Building on the foundation set by Judge Frank, scholars like William Prosser and Melville Nimmer further refined the right and developed policy rationales for its existence.[28]

Today, the right of publicity has been recognized at common law or by statute in half of the states.[29] It is an intellectual property right under state law, the infringement of which is the commercial tort of unfair competition.[30] California courts have recognized a common law right of publicity for living persons.[31] Moreover, California Civil Code section 3344 provides a statutory right separate and distinct from the common law right.[32] Because section 3344 only covered living persons, section 990 (renumbered as 3344.1 in 1999) was later enacted to recognize a postmortem right of publicity.[33]

2. *Policy Justifications*

Three policy considerations stand behind the right of publicity given to celebrities. First, the right "vindicates the economic interests of celebrities, enabling those whose achievements have imbued their identities with pecuniary value to profit from their fame."[34] Second, the right provides financial incentives for individuals to expend time and resources to produce

24. *Id.* at 1-38.
25. *Id.*
26. Haelan Labs., Inc. v. Topps Chewing Gum, Inc., 202 F.2d 866 (2d Cir. 1953).
27. MCCARTHY, *supra* note 11, at 1-41.
28. *Id.* at 1-25, 1-47.
29. *Id.* at 6-5.
30. *Id.* at 1-2.
31. *See* Lugosi v. Universal Pictures, 25 Cal. 3d 813, 820 (1979).
32. CAL. CIV. CODE § 3344 (1971).
33. *Id.* at § 3344.1 (1999) (originally enacted as Civ. Code § 990 (1984)).
34. Carson v. Here's Johnny Portable Toilets, Inc., 698 F.2d 831, 838 (6th Cir. 1983).

intellectual and creative works.[35] Third, the right prevents unjust enrichment and deceptive trade practices.[36]

B. The First Amendment

As vital as these policies are, they may conflict with societal interests in free speech.[37] Thus, the First Amendment is a defense against a right of publicity claim.

1. Hierarchy of First Amendment Protection

As an initial matter, it is important to understand that the First Amendment does not fully protect all speech. Courts give different types of "speech" different levels of protection.[38] A major distinction is made between "commercial" and "communicative" speech.

a) Commercial Speech

"Commercial speech" has been narrowly defined as speech that "does 'no more than propose a commercial transaction.'"[39] Courts have consistently placed commercial speech at the bottom of the First Amendment hierarchy. It is entitled to little constitutional protection.[40] In fact, the First Amendment usually does not shield pure commercial speech from liability for an infringement of publicity rights.[41]

b) Communicative Speech

On the other hand, "communicative" speech—speech dealing with matters in the public interest, like news and fiction—receives full First Amendment protection.[42] Courts have consistently stated that "[p]ublication of matters in the public interest . . . cannot . . . be actionable."[43] Despite its special status, "communicative" speech encompasses a broad range of expressions. The Supreme Court has broadly defined the scope of "matters in the public interest" to include "expression about phi-

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35. *Id.*
36. *Id.*
37. *Id.* at 839.
38. MCCARTHY, *supra* note 11, at 8-16.
39. Va. State Bd. of Pharmacy v. Va. Citizens Consumer Council, Inc., 425 U.S. 748, 762 (1976) (quoting Pittsburgh Press Co. v. Pittsburgh Comm'n on Human Relations, 413 U.S. 376, 385 (1973)).
40. MCCARTHY, *supra* note 11, at 7-3.
41. *See id.* at 7-10.1, 7-38 (impermissible use of identity in advertisement and on merchandise, forms the core acts that trigger liability).
42. *See id.* at 8-16.
43. Eastwood v. Superior Court, 149 Cal. App. 3d 409, 421 (1984).

losophical, social, artistic, economic, literary, or ethical matters."[44] A New York Court has stretched the scope even further to include "articles of interest to consumer groups and fashion."[45]

2. *Inherent Conflict Between the First Amendment and Publicity Rights*

In protecting communicative speech, the First Amendment serves two vital goals. First, "to preserve an uninhibited marketplace of ideas and repel efforts to limit . . . debate on public issues."[46] Second, "to foster fundamental respect for individual development and self-realization."[47] The right of publicity may frustrate these goals because it authorizes individuals "to control whether and how information about [them] can be used by other people."[48] More specifically, it may inhibit public debate and censor creative expressions.[49] Because celebrities take on public meaning, some uses of their names or likenesses may serve vital functions in debates on public issues.[50] On the other hand, celebrities also take on personal meaning for individuals and the creative appropriation of their images can be an important avenue of individual expression.[51]

3. *"Mixed Speech"—Exacerbating the Conflict*

The potential for a direct conflict between First Amendment and publicity rights is heightened by the existence of "mixed speech." As previously explained, the categorization of a speech as either commercial or communicative determines the fate of a First Amendment defense. But not all speech is easily categorized. Some speech is "mixed"—embodying both commercial and communicative elements. Thus, the method used to categorize mixed speech stands squarely in the middle of the conflict between the two opposing rights; an inadequate method will hasten a direct clash, while a satisfactory method will resolve the conflict.

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44. Abood v. Detroit Bd. of Educ., 431 U.S. 209, 231 (1977).

45. Welch v. Group W. Prods, Inc., 525 N.Y.S.2d 466, 468 (1987).

46. Comedy III Prods., Inc. v. Saderup, Inc., 25 Cal. 4th 387, 397 (2001) (quoting Guglielmi v. Spelling-Goldberg Prods., 25 Cal. 3d 860, 866 (1979)).

47. *Id.*

48. Hunt, *supra* note 5, at 1616.

49. *See id.*

50. Michael I. Rudell, *Reconciling Right of Publicity with the First Amendment*, N.Y. L.J., June 22, 2001, at 3.

51. *Id.*

4. *Fundamental Problems in Resolving the Conflict*

Two major problems afflict attempts to resolve the conflict between First Amendment and publicity rights. The first problem has long affected other legal areas: should courts engage in a case-by-case inquiry or draw a clear and predictable line? The former sacrifices predictability for accuracy, while the latter sacrifices flexibility for consistency. If courts decide to draw a line, a second problem arises: how does one avoid drawing an arbitrary line? As the following discussion will show, a myriad of nearly irreconcilable interests are at stake in these problems. None of the concepts or approaches to be discussed below can alone address all of them. The *Hoffman* opinion by no means resolves these problems, but it does illuminate the vital issues and suggest possible solutions.

II. CASE SUMMARY

A. Facts

Plaintiff, Dustin Hoffman ("Hoffman"), is a famous actor.[52] Defendant, ABC, Inc., owns Defendant, Los Angeles Magazine, Inc.[53] In March 1997, Los Angeles Magazine ("LAM") published an article entitled "Grand Illusions," which used computer technology to merge photographs of actors and actresses from classic films with photographs of body models wearing Spring 1997 fashions.[54] The article also referenced a "shopping guide" that provided price and store information for the clothing used in the photographs.[55]

The final photograph in the article was an altered still from the movie "Tootsie," which starred Hoffman.[56] The original still showed Hoffman wearing a red evening dress and posing in front of an American flag.[57] Only Hoffman's head and the American flag remained in the new photograph published by LAM.[58] A model's body wearing a gown designed by Richard Tyler and shoes designed by Ralph Lauren replaced Hoffman's body and his red evening dress.[59]

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52. Hoffman v. Capital Cities/ABC, Inc., 33 F. Supp. 2d 867, 869 (1999).
53. *Id.* at 870.
54. *Id.*
55. *Id.*
56. Hoffman v. Capital Cities/ABC, Inc., 255 F.3d 1180, 1183 (2001).
57. *Id.*
58. *Id.*
59. *Id.*

LAM did not seek Hoffman's permission to publish the altered photograph.[60] Consequently, Hoffman filed a complaint in California State Court against LAM's parent company, ABC. The complaint alleged that LAM's publication of the altered photograph misappropriated Hoffman's identity in violation of: (1) the California common law and statutory right of publicity; (2) the California unfair competition statute, Business and Professions Code § 17200; and (3) the federal Lanham Act, 15 U.S.C. § 1125(a).[61] Subsequently, ABC removed the case to federal court and Hoffman added LAM as a defendant.[62]

B. The District Court Decision

The district court found for Hoffman on all of his claims.[63] Only the court's rejection of LAM's First Amendment defense is relevant to our discussion. The court held that LAM's use of Hoffman's identity was commercial speech and therefore was not protected under the First Amendment.[64] In the court's view, no significant editorial message or purpose existed in LAM's use of Hoffman's identity.[65] Moreover, it found that the use of Hoffman's identity was not reasonably related to whatever editorial message LAM claimed the article at issue contained.[66]

C. The Ninth Circuit Decision

The Ninth Circuit reversed the district court's decision. Refusing to characterize LAM's use of Hoffman's identity as "commercial speech," the court granted LAM full First Amendment protection.[67] It found that LAM did not use Hoffman's image in a traditional advertisement printed merely for the purpose of selling a product.[68] In fact, the court saw the article as a combination of fashion photography, humor, and visual and verbal editorial comment on classic films and famous actors.[69] Discounting the commercial elements presented by the designer apparel and the "shopper's guide," the court stated that "any commercial aspects are 'inextricably entwined' with expressive elements, and so they cannot be separated

60. *Id.*
61. *Id.*
62. *Id.*
63. *Id.*
64. *Id.* at 1184.
65. *Id.*
66. Hoffman v. Capital Cities/ABC, Inc., 33 F. Supp. 2d 867, 874-75 (1999).
67. Hoffman v. Capital Cities/ABC, Inc., 255 F.3d 1180, 1186-89 (2001).
68. *Id.* at 1185.
69. *Id.*

out 'from the fully protected whole.'"[70] Absent commercial speech, Hoffman had to prove actual malice on the part of LAM to prevail. The Ninth Circuit thwarted his effort on this front and ultimately rejected all of his claims.[71]

III. DISCUSSION

The Ninth Circuit refused to categorize LAM's use of Hoffman's identity as commercial. Although it followed the general contours of the primary message test, the court's opinion suggests two concepts that may serve as additional guidelines in applying the test. This discussion will analyze the strengths and weaknesses of the primary message test and the concepts suggested by the Ninth Circuit opinion. Also, it will examine another line-drawing approach—the "transformative" test, imported from copyright's fair use doctrine.

A. The "Primary Message" Test

The primary message test determines whether the "primary" or "predominant" message of speech is commercial or communicative.[72] The *Hoffman* opinion referred to the test when it asserted that LAM's article did not "simply advance a commercial message" or when it inquired into LAM's purpose for using Hoffman's identity.[73] The test measures and compares the weight of the free speech interest and the publicity right interest raised by each particular case. Two methods are used to accomplish this task.

1. Method I - Primary Impact

This method determines whether the "primary" or "predominant" impact of speech is commercial or communicative.[74] Two key publicity rights cases—*White v. Samsung Elecs. Am., Inc.*[75] and *Cardtoons, L.C. v. Major League Baseball*[76]—nicely illustrate this method.

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70. *Id.* (quoting Gaudiya Vaishnava Soc'y v. City & County of San Francisco, 952 F.2d 1059, 1064 (9th Cir. 1991)).

71. *Id.* at 1188 (concluding that LAM did not intend to suggest to the ordinary reader that he or she was seeing Hoffman's body in the altered "Tootsie" photograph).

72. MCCARTHY, *supra* note 11, at 8-149, 8-150.

73. Hoffman v. Capital Cities/ABC, Inc., 255 F.3d 1180, 1185 (2001).

74. MCCARTHY, *supra* note 11, at 8-149, 8-150.

75. White v. Samsung Elecs. Am., Inc., 971 F.2d 1395 (9th Cir. 1992).

76. Cardtoons, L.C. v. Major League Baseball Players Ass'n, 95 F.3d 959 (10th Cir 1996).

White involved a dispute over a Samsung VCR advertisement, which depicted "a robot, dressed in a wig, gown, and jewelry . . . consciously selected to resemble [Vanna White]."[77] The advertisement was part of a series that expressed a common theme.[78] Each part of the series "depicted a current item from popular culture and a Samsung electronic product;" each was "set in the twenty-first century and conveyed the message that the Samsung product would still be in use by that time."[79] By "hypothesizing outrageous future outcomes for the cultural items, the ads created humorous effects."[80]

The Ninth Circuit rejected Samsung's First Amendment defense—Samsung claimed its use of White's identity was a parody.[81] The court determined that the advertisement's primary impact was commercial: "The ad's spoof of Vanna White . . . is subservient . . . to the ad's [commercial] message: 'buy Samsung VCRs.'"[82] In other words, the commercial message so completely dominated its communicative counterpart as to render that counterpart irrelevant.

In contrast, the Tenth Circuit in *Cardtoons* upheld a defendant's First Amendment defense for baseball cards that parodied prominent athletes.[83] The cards featured caricatures of baseball players on the front and humorous commentaries about their careers on the back.[84] Despite their unique content, they were produced and formatted just like normal trading cards.[85] In its decision, the court found the primary impact in the cards to be the parody and not their commercial message.[86] In other words, the communicative elements in the cards outweighed the commercial elements to render this consumer product noncommercial.

2. *Method 2—Primary Purpose/Reasonable Relationship*

This method singles out the "primary" or "predominant" purpose for an appropriation of identity. A First Amendment defense against publicity

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77. *White*, 971 F.2d at 1396. Vanna White is the hostess of "Wheel of Fortune," a popular television game show.

78. *Id.*

79. *Id.*

80. *Id.* One advertisement "lampooned current popular notions of an unhealthy diet by depicting a raw steak with the caption: 'Revealed to be health food. 2010 A.D.'" *Id.*

81. *Id.* at 1401.

82. *Id.*

83. Cardtoons, L.C. v. Major League Baseball Players Ass'n, 95 F.3d 959 (10th Cir. 1996).

84. *Id.* at 962.

85. *Id.* at 963.

86. *Id.* at 968-970.

rights requires a reasonable relationship between the appropriated identity and the communicative expression it serves.[87] A defendant loses the defense if it uses an identity as a mere vehicle to attract attention to its communicative expression.[88] The *Hoffman* opinion used this method when it inquired into LAM's purpose for using Hoffman's identity and cited several pertinent facts: LAM did not receive any consideration from the designers featured in the article and Hoffman's identity indeed served viable editorial—as opposed to commercial—purposes.[89] The court concluded that unlike defendants previously found liable, LAM did not use a celebrity's identity *entirely and directly* for the purpose of selling a product.[90]

This method was also used in two other noteworthy cases. In *Duncan v. New York Magazine Co.*, the court validated a First Amendment defense after finding a close relationship between a photograph of plaintiff taken at the St. Patrick's Day Parade and an article that "referred to the . . . festivities and included comments about the parade."[91] In contrast, the court in *Grant v. Esquire, Inc.*, deemed a use of identity to be commercial and unprotectable.[92] In the absence of his permission, Esquire magazine featured actor Cary Grant's photograph with his body digitally replaced by that of a model wearing current fashions.[93] Store and price information were printed below the picture in a caption.[94] In contrast to the facts in *Hoffman*, Grant's picture was not part of an article or of an issue of a magazine devoted to him or anything reasonably related to him.[95] His picture surfaced in the middle of the magazine for no apparent reason and outside of a communicative context—just like an advertisement. Thus, the court concluded that "Mr. Grant's face serve[d] no [purpose] but to attract attention" to the magazine.[96]

3. *Arguments Against the Test*

The test's main weakness resides in its case-by-case and fact-specific nature. This open-ended approach gives judges great discretion in measur-

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87. *See* Delan v. CBS, Inc., 458 N.Y.S.2d 608, 613 (1983) ("[T]here must have existed a legitimate connection between the use of plaintiff's name and picture and the matter of public interest sought to be portrayed.").

88. MCCARTHY, *supra* note 11, at 8-83.

89. Hoffman v. Capital Cities/ABC, Inc., 255 F.3d 1180, 1185 (2001).

90. *Id.*

91. Murray v. New York Magazine Co., 27 N.Y.2d 406, 409 (1971).

92. Grant v. Esquire, Inc., 367 F. Supp. 876, 883-86 (1973).

93. *Id.* at 877.

94. *Id.* at 878.

95. *See id.*

96. *Id.*

ing and weighing the relative importance of the interests at issue; thus, judges have wide leeway in determining the contents of speech. Such measurements and comparisons may be difficult to perform; subjectivity may intrude and mistakes may result. Consequently, the test may overprotect or underprotect First Amendment interests under different circumstances.

Moreover, the test lacks explicit guidelines and parameters. Thus, it may produce inconsistent and unpredictable results. Although judges have much experience in performing balancing tests, the mere potential for inconsistency can be a problem. The Constitution frowns upon inconsistency when First Amendment rights are involved.[97] The void-for-vagueness doctrine requires rules affecting free speech to be predictable.[98] Unpredictable rules may "'inhibit the exercise of [First Amendment] freedoms'" by making speakers "'steer far wider of the unlawful zone' . . . than if the boundaries of the forbidden areas were clearly marked."[99] A case-by-case inquiry may not be capable of clearly marking the boundary between commercial and communicative speech. This possibility bodes ill for people who create "mixed" works that are simultaneously communicative and commercial. Without knowing whether their speech will be protected, these "speakers" may refrain from fully exercising their First Amendment rights.

4. *Arguments for the Test*

The strengths of the test also reside in its case-by-case and fact-specific nature. Each application of the test carefully weighs the free speech and publicity right interests at issue. The test refrains from drawing arbitrary lines. Instead, it looks beyond the surface of a speech into the relative importance of the specific interests at issue. Nothing is presumptively commercial or communicative under the test. Consumer products and even advertisements may theoretically be protected if they convey a primarily communicative message; on the other hand, seemingly communicative speech may lose protection under certain circumstances. The test actively seeks out free speech interests and protects them when they exist. As a result, the test faithfully follows the literal and narrow definition of

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97. RONALD D. ROTUNDA, TREATISE ON CONSTITUTIONAL LAW—SUBSTANCE & PROCEDURE §20.9 (3d ed. 1999).

98. *Id.*

99. *Id.* at 109 (quoting Cramp v. Bd. of Pub. Instruction, 368 U.S. 278, 287 (1961), and Bagget v. Bullitt, 377 U.S. 360, 372 (1964) (quoting Speiser v. Randall, 357 U.S. 513, 526 (1958)). *See also* Stephen R. Barnett, *First Amendment Limits on the Right of Publicity*, 30 TORT & INS. L.J. 635, 645 (1995).

commercial speech: speech that "does no more than propose a commercial transaction."[100] Arguably, such a flexible approach better protects free speech than any method that draws a bright line.

Furthermore, the test's refusal to draw a bright line doesn't automatically translate into inconsistent and unpredictable results. In fact, courts applying the test have uniformly found liability in speech that directly proposes commercial transactions, while consistently excluding other speech from the reach of publicity rights. Instead of drawing lines, the test provides speakers with a spectrum for guidance. Speakers can usually be assured of First Amendment protection as long as they do not veer too close to the commercial end of the spectrum.

B. Concepts Suggested by the Hoffman Opinion—Useful Additions for the Test?

1. Concept I: The Inextricably Entwined Doctrine

a) The Doctrine

The Ninth Circuit drew on Supreme Court's "inextricably entwined" doctrine in categorizing LAM's speech. The Supreme Court devised the doctrine to deal with "mixed" speech whose commercial and communicative elements are intertwined and inseparable. The Court always treats such mixture as noncommercial, because "[it] cannot parcel out the speech, applying one test to one phrase and another test to another phrase . . . ."[101] In other words, the Court will exercise judicial restraint and resolve uncertainties in favor of the First Amendment.

b) Arguments For and Against the Doctrine

This doctrine may effectively limit the judicial discretion granted by the primary message test and make the test more predictable. The doctrine forbids courts from arbitrarily singling out a primary message from a true mixture of commercial and communicative elements; it forces them to categorize such mixture as communicative.

But "inextricably entwined" can be an amorphous term. The doctrine may encourage abuses of discretion and produce unpredictability if it is applied without an explicit limit. Different judges may disagree about the

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100. Va. State Bd. of Pharmacy v. Va. Citizens Consumer Council, Inc., 425 U.S. 748, 762 (1976) (quoting Pittsburgh Press Co. v. Pittsburgh Comm'n on Human Relations, 413 U.S. 376, 385 (1973)).

101. Riley v. Nat'l Fed'n of the Blind, Inc., 487 U.S. 781, 796 (1988). *See also* Board of Trs. v. Fox, 492 U.S. 469 (1989); White v. Samsung Elecs. Am., Inc., 971 F.2d 1395, 1401 n.3 (9th Cir. 1992).

degree to which elements are "entwined." The solution may be to grant "inextricably entwined" status to a speech as long as its communicative and commercial elements have some tenuous relationship; consequently, the doctrine will be inapplicable only in extreme situations. Courts seem to follow this formulation of the doctrine, since they have consistently held that the doctrine does not apply where the noncommercial element is simply tacked onto commercial speech that only proposes a commercial transaction—namely, when no reasonable relationship exists between the two components.[102]

Note that this formulation of the doctrine renders most mixed speech protectable as long as their commercial elements are tangentially connected to communicative counterparts—even when the speech takes the form of an advertisement. In other words, the doctrine serves First Amendment interests by resolving uncertainties in favor of free speech. Furthermore, the doctrine, if added to the primary message test, can ensure that the test would never underprotect First Amendment interests. This fact will delight First Amendment advocates. On the other hand, proponents of publicity rights may argue that this doctrine is overly broad—it deprives plaintiffs of compensation even when the commercial and communicative elements in a speech are barely related. These arguments present a clear example of the inherent tension between free speech interests and economic/publicity interests.

2. *Concept II: A Focus on the Medium in Which an Identity is Used*

a) The Concept

The Ninth Circuit emphasized the medium in which LAM's use of Hoffman's identity appeared in. Much of its reasoning relies on the fact that the appropriation of Hoffman's identity occurred in an article and in a magazine. In the court's words: "LAM did not use Hoffman's image in a traditional advertisement . . . 'Grand Illusions' appears as a feature article on the cover of the magazine . . . [it is] a part of the issue's focus on Hollywood past and present."[103] In a sense, the Ninth Circuit could not allow the article's commercial attributes to trump the serious free speech interests implicated by the medium itself. Note that the court did not inquire deeply into the primary message or purpose of LAM's use of Hoffman's identity. Instead, it may have presumed that a magazine would contain

102. *See Board of Trs.*, 492 U.S. at 473-75; *White*, 971 F.2d at 1401 n.3 (9th Cir 1992).

103. Hoffman v. Capital Cities/ABC, Inc., 255 F.3d 1180, 1185 (2001).

some communicative message or purpose. Though the court did not explicitly state this presumption, it's worth evaluating whether such a presumption might be a valuable addition to the primary message test.

Under this rebuttable presumption, courts will presume that mediums "traditionally" considered by the First Amendment to be in the public interest—news, books, magazines, films, etc.—cannot carry a predominantly commercial message or purpose. On the other hand, mediums such as consumer products or advertisements are presumed to be commercial because they do not "regularly" carry communicative messages or purposes.[104]

b) Arguments for a "Presumption" Based on Medium

i) Enhances Predictability by Drawing a Definable Line

This presumption may effectively dilute the case-by-case and open-ended nature of the primary message test. The presumption arguably draws a definable line between protected and unprotected speech and limits courts' discretion in singling out a "primary" message. Creators working in mediums presumed to be communicative will be able to freely express themselves without fearing potential liability. This is desirable because the mediums protected under the presumption are ones commonly recognized to be instrumental in driving public discourse.

ii) Necessity for Incorporating First Amendment Limits

Because publicity rights may clash with the First Amendment, some courts and commentators have suggested that "First Amendment values should be integrated in some form directly into the cause of action for infringement of the right of publicity."[105] A medium presumption may serve as such a built-in First Amendment limit; it practically exempts certain mediums from liability because they implicate too many First Amendment interests.

Proposals for these limits are by no means novel. Numerous intellectual property regimes avoid collisions with speech rights by incorporating First Amendment principles into their frameworks. Copyright law offers a good example. Like the right of publicity, copyright law restrains what may be said and heard in public.[106] Despite this fact, the Supreme Court

104. *See* Guglielmi v. Spelling-Goldberg Prods., 25 Cal. 3d 860 (1979).

105. MCCARTHY, *supra* note 11, at 8-53.

106. Paul Goldstein, *Copyright and the First Amendment*, 70 COLUM. L. REV. 983, 984 (1970).

"has made clear that copyright law is substantively constitutional."[107] Moreover, it suggested that First Amendment protections have been built into copyright law in the form of the idea-expression distinction and the fair use doctrine.[108] These "protections" allow public interests to trump copyrights in appropriate circumstances. Moreover, these "protections" enable copyright and the First Amendment to accommodate one another in spite of their conflicting interests.[109]

iii) Numerous Legal Authorities Support Medium Presumptions and Exemptions

a) Case Law

The medium presumption may find support in existing judicial opinions. Certain media—books, films, magazines, music, fine art, etc.—have received broad immunity from the right of publicity.[110] Courts have consistently distinguished certain "newsworthy" and "entertainment" mediums from consumer products and advertisements. One court has said that "[m]ore so than posters, bubble gum cards, or some other such 'merchandise,' books and movies are vehicles through which ideas and opinions are disseminated and, as such, have enjoyed certain constitutional protections, not generally accorded 'merchandise.'"[111]

Furthermore, some courts have implicitly considered medium as a factor in applying the "primary message" test. In *Guglielmi v. Spelling-Goldberg Prods.*, the court categorized a television film as communicative speech in rejecting a publicity claim brought by the estate of actor Rudolph Valentino.[112] In reaching this decision, the court distinguished motion pictures from "merchandise" such as pens and soaps.[113] It stated that "[merchandise], unlike motion pictures, are not vehicles through which ideas and opinions are regularly disseminated."[114] Indeed, most infringing uses of identity have been found in advertisements or merchandise. Take for example some famous Ninth Circuit decisions in favor of celebrities—

107. Mark A. Lemley & Eugene Volokh, *Freedom of Speech and Injunctions in Intellectual Property Cases*, 48 DUKE L. J. 147, 166 (1998).

108. *Id.* at 166-67. *See also* Harper & Row, Publishers, Inc. v. Nation Enters., 471 U.S. 539, 560 (1985).

109. Goldstein, *supra* note 106, at 988.

110. Hunt, *supra* note 5, at 1618.

111. *See* Hicks v. Casablanca Records, 464 F. Supp. 426, 430 (S.D.N.Y. 1978).

112. *See generally* Guglielmi v. Spelling-Goldberg Prods., 25 Cal. 3d 860 (1979).

113. *Id.* at 874.

114. *Id.*

White, *Midler*, and *Abdul-Jabbar*.[115] All three cases involved advertisements.[116] Courts have even denied protection to consumer products that featured strong communicative elements—for example, T-shirts and dishes with printed "messages."[117]

b) State Statutes

Some state publicity statutes have language granting an exemption for uses of identity in certain media which the legislature felt should be immunized by the First Amendment.[118] For example, such language shows up in California Civil Code Section 3344.1, which makes liable any person who, without consent, uses a deceased personality's name or likeness "in any manner, *on or in products, merchandise, or goods, or for purposes of advertising or selling, or soliciting purchases* . . . ."[119] An express exemption within section 3344.1 precludes liability for the use of a deceased celebrity's persona in: "a play, book, magazine, newspaper, musical composition, film, or radio or television program . . . material that has political or newsworthy value . . . [or a] work of fine art . . . ."[120]

When express exemptions are absent, some courts have found ways to evade First Amendment problems by "interpret[ing] the common law or statute" to exempt certain mediums from liability.[121] The practices of New York courts offer a good example. Although the New York statute prohibits the unauthorized use of identity "for the purposes of trade,"[122] New York courts have interpreted the phrase "purposes of trade" to exclude for-profit media that contain informative or entertainment elements.[123]

c) The Restatement of Unfair Competition

The Restatement of Unfair Competition also contains exemptions for certain media.[124] It phrases the kind of unauthorized use that causes infringement as use for "purposes of trade"—namely, in advertising, on merchandise, or in connection with commercial services.[125] The Restate-

115. *See* cases cited *supra* note 6.

116. *Id.*

117. *See* MCCARTHY, *supra* no125
te 11, at 7-39; Shamsky v. Garan, Inc., 167 Misc. 2d 149 (1995).

118. MCCARTHY, *supra* note 11, at 8-54.

119. CAL. CIV. CODE § 3344.1(a)(1) (1999); Comedy III Prods., Inc. v. Saderup, Inc., 25 Cal. 4th 387, 395 (2001); Paulsrude, *supra* note 4 , at 407.

120. CAL. CIV. CODE § 3344.1(a)(2) (1999).

121. MCCARTHY, *supra* note 11, at 8-53.

122. *Id.* at 8-54, 8-54.1.

123. Delan v. CBS, Inc., 458 N.Y.S.2d 608, 613 (1983).

124. Johnson, *supra* note 2, at 197.

125. *Id.*

ment then proceeds to exclude uses of identity in news reporting, commentary, entertainment, or works of fiction and nonfiction from the category of commercial speech.[126]

iv) The Presumption Creates an Acceptable Balance Between the Conflicting Interests and Goals

The medium presumption may achieve an acceptable balance between the goals of the First Amendment and publicity rights. While the presumption provides favorable treatment to media that have "traditionally" implicated serious free speech interests, it nonetheless leaves the right of publicity intact. Celebrities can still vindicate the economic interests in their identities. The rules do allow finding for infringement in advertisements and consumer products under most circumstances. These findings will by no means be rare; most appropriations of identity occur in such media. In the end, the presumption still gives celebrities sufficient incentives to contribute their talents to society and prevents unjust enrichment on the part of exploiters.

d) Arguments Against a Presumption Based on Medium—Does the Presumption Draw Arbitrary Lines and Deny Protection to Speech that Deserve it?

It may be clear that "newsworthy" and "entertainment" speech deserve protection and commercial exploitations of identities do not. But what about that speech which falls between these two extremes? Who is entitled to profit from the depiction of celebrities in a variety of non-advertising, non-news reporting and nonnarrative contexts, such as baseball cards, collectible plates, T-shirts, figurines, calendars, and posters?[127] Should control rest with the creator of the work, or the celebrity who is being used? The medium presumption provides no certain answers. On the one hand, an application of the presumption to these "consumer products" may produce as much uncertainties as a case-by-case inquiry. Courts and statutes have yet to explicitly address all of these "intermediates." Thus, the presumption is arguably an amorphous concept; drawing a line between commercial and communicative *media* can be a difficult task.

On the other hand, with its preference for media "traditionally" protected by the First Amendment, the presumption arguably excludes all "consumer products" from the category of communicative speech—recall the categorization of "merchandise" as commercial in statutes and case

126. *Id.*

127. Tyler Trent Ochoa, ETW Corp. v. Jireh Publishing Inc.: *Introduction: Tiger Woods and the First Amendment*, 22 WHITTIER L. REV. 381, 384 (2000).

law. But consumer products may do more than propose a commercial transaction. Are T-shirts and mugs intrinsically different from songs or art when they both convey vital messages? They are all mass-marked to consumers. Some commentators have argued that both may act as "equally legitimate . . . vehicles for First Amendment expression . . . [t]he content is the same, only the medium is different."[128] In a sense, the medium presumption oversimplifies the problem by focusing on the medium, rather than the content—messages and purposes—behind it. As a result, it violates the literal definition of commercial speech by deeming speech to be commercial even if they do more than propose a commercial transaction.

Of course, the presumption may be extended to cover certain consumer products, like the baseball cards in *Cardtoons*. But what about figurines and calendars? Where should the extension stop? Not surprisingly, this line is as arbitrary as any other. Moreover, such extensions make the presumption seem like a stopgap measure rather than a real solution. In summary, a double-dilemma is at work here: If a bright line is not drawn, the medium presumption can be an unpredictable rule; but any line-drawing can be challenged as arbitrary.

D. The Transformative Test (Fair Use Approach)

Most courts have refused to provide protection for advertisements that contain communicative elements. This fact raises the troubling issue about the use of publicity rights to suppress criticism of the celebrity's "image."[129] Some courts and commentators have addressed this concern by suggesting the importation of the "transformative" factor from fair use doctrine into the right of publicity regime.[130] They argue that this factor better protects free speech interests.[131] The transformative test measures the extent to which a use of an identity "adds something new, with a further purpose or different character" to the appropriated identity.[132] The test, which requires a case-by-case and fact-specific inquiry, provides advantages similar to that of the primary message test. It does not draw arbitrary lines and carefully balances the free speech and publicity interests

128. *Id.* at 386.

129. *See* David S. Welkowitz, *Catching Smoke, Nailing Jell-O to a Wall: The Vanna White Case and the Limits of Celebrity Rights*, 3 J. INTELL. PROP. L. 67, 95-100 (1995) (arguing that celebrities sometimes use the right of publicity to bypass the limits on defamation imposed by New York Times Co. v. Sullivan, 376 U.S. 254 (1964) and its progeny).

130. *See* Comedy III Prods., Inc. v. Saderup, Inc., 25 Cal. 4th 387, 395 (2001); Barnett, *supra* note 99.

131. *Id.*

132. Barnett, *supra* note 99, at 21.

raised by each case. All uses of identity are potentially protectable, even advertisements.

Despite its strengths, the transformative test also suffers from the potential for unpredictable and inconsistent results. Furthermore, the test allows judges to act as critics in judging the content of works to determine their degree of "transformativeness." The task is a difficult one and verges on literary and aesthetic value judgments for which courts are unsuited.[133] Perhaps the test will only introduce confusion into the legal framework of publicity rights.[134] But proponents of the test have pointed to the fact that courts have applied the test in copyright cases for years and have yet to abandon it. Regrettably, the *Hoffman* Court did not address these contrasting views—it only referred to the test in a footnote. Thus, the debate will surely continue as right of publicity litigation intensifies.

IV. CONCLUSION

The "mixed" speech found in LAM and other media presents "a stark example of the inherent conflict between two seemingly reasonable legal positions."[135] On the one hand, if the magazine is making money from a celebrity's image, shouldn't the celebrity get a share of the profits? On the other hand, shouldn't the First Amendment protect the magazine's right to publish anything it wants? Four concepts or approaches have been presented in this Note; none are perfect. The primary message test may be accurate but unpredictable. The inextricably entwined doctrine ensures that the primary message test will not underprotect speech, but it may be a hard doctrine to define. The medium presumption provides a definable but potentially arbitrary line. The "transformative" test gives judges excessive discretion and may produce unpredictability. One dilemma shows up repeatedly in this analysis—a case-by-case inquiry is potentially unpredictable, but a bright line may be arbitrary. A perfect solution is hard to devise.

But it is worth noting that the right of publicity is a relatively recent legal invention; intense litigation on this right has only begun in the past few years. Instead of immediately drawing bright lines, one may argue that courts "would do better to feel their way from case to case, setting forth in each those factors that seem to bear on the resolution of that case

133. *Id.* at 21.

134. MCCARTHY, *supra* note 11, at 8-58 ("It seems strange to propose to bring clarity to right of publicity law by importing into it some undefinably [sic] modified version of one of the most obscure and unpredictable aspects of copyright law.").

135. Ochoa, *supra* note 127, at 383.

. . . only to eventually arrive at a consensus of relevant factors on the basis of this accumulated experience."[136] In other words, the approaches examined here might work together to address the relevant interests in different cases on an experimental basis. But it is clear that none of them can individually solve the problem on its own.

136. Nabisco, Inc. v. PF Brands, Inc., 191 F.3d 208, 227 (2d Cir. 1999) (commenting on the approach that should be taken toward the new federal antidilution statute).

COMEDY III PRODUCTIONS V. SADERUP

By Gil Peles

In *Comedy III Productions v. Saderup*,[1] the California Supreme Court developed a comprehensive test for resolving tensions between the right of publicity and the First Amendment's guarantee of freedom of expression.[2] As with copyright, the intellectual property right of publicity can conflict with societal interests in free speech.[3] Unlike copyright law, the right of publicity does not systematically incorporate First Amendment safeguards, such as the idea-expression dichotomy or fair use, into its protective regime.[4] To reconcile this conflict, the court created a test influenced by copyright's fair use doctrine. More specifically, the court focused on whether the allegedly infringing use was "transformative."[5]

In *Comedy III*, the court compared a Gary Saderup silkscreen painting of The Three Stooges to the works of other artists, including Andy Warhol.[6] In so doing, it found that Saderup's silkscreen was not sufficiently transformative to rise to a level of privileged expression under the First Amendment.[7] Warhol's works "convey[ed] a message that went beyond commercial exploitation . . . [to become] a form of ironic social comment,"[8] while Saderup's works lacked the proper "message" or "social comment."[9] In making this comparison, the court failed to create a clear test to determine how much "social comment" must be included in order to be considered "transformative."[10] This Note will analyze the California Supreme Court's modified fair use test and argue that the court's "trans-

1. 25 Cal. 4th 387 (2001).
2. *Id.* at 404.
3. *See* Carson v. Here's Johnny Portable Toilets, Inc., 698 F.2d 831, 841 (1983) (describing how the right of publicity conflicts with the First Amendment guarantee of expression, and comparing this conflict with copyright law).
4. *See* Sid & Marty Krofft Television Prods., Inc. v. McDonald's Corp., 562 F.2d 1157, 1163 n.6 (describing the idea-expression dichotomy as a fundamental safeguard) (1977); *see also* Kalem Co. v. Harper Bros., 222 U.S. 55, 63 (1911) (explaining the use of the idea-expression dichotomy in order to limit the copyright monopoly).
5. *Comedy III*, 25 Cal. 4th at 404.
6. *Id.* at 408-09 (providing Warhol's depictions of Marilyn Monroe, Elizabeth Taylor, and Elvis Presley as examples).
7. *Id.* at 409.
8. *Id.* at 408.
9. *Id.*
10. *Id.* at 404.

formative" test is too vague to provide proper guidance. While the *Comedy III* court was correct in finding a need for a First Amendment test, its specific guidelines require clarification. More specifically, the court should have further defined its requirement of expression while also taking into account the potential economic harm that a celebrity might incur.

I. BACKGROUND

A. Origins of the California Right of Publicity

The right of publicity is the right of a person to control the commercial use of his or her identity.[11] Recognition of this right originated within the domain of "privacy" rights.[12] Although this right was guaranteed for the average citizen, the extent in which it applied to famous people was not clear.[13] Proponents reasoned that if a person's image is already widespread, it does not hurt his or her "privacy" for it to be further disseminated.[14] Therefore, a movement began for celebrities to be able to control their identity.[15] William Prosser and Melville Nimmer initially proposed the formation of an official "right of publicity" which incorporated aspects of privacy, property, and tort law.[16] Later, the right of publicity came to be viewed as a type of intellectual property.[17] This allowed the rights existing in many fields to converge into one category.[18] Consolidation of the right of publicity into the category of intellectual property recognized economic investment in a celebrity identity and thus gave it commercial value.[19]

Today, the California right of publicity exists both as a statutory and common law right.[20] Civil Code section 3344 authorizes recovery of damages by any living person whose "name, photograph, or likeness" has been used without his consent for commercial purposes.[21] In 1979, eight years after the enactment of the statutory right of publicity, the California Su-

11. *See generally* J. THOMAS MCCARTHY, THE RIGHTS OF PUBLICITY AND PRIVACY, 1-37 (2d ed. 2001).

12. *See, e.g.,* Haelen Lab., Inc. v. Topps Chewing Gum Inc., 202 F.2d 866, 868 (2d Cir. 1953) ("We think that, in addition to and independent of that right of privacy . . . a man has a right in the publicity value of his photograph . . . .")

13. *See* MCCARTHY, *supra* note 11, at 1-7.

14. *See id.* at 1-39.

15. *Id.* at 1-7.

16. *Id.*

17. *Id.* at 6-14.

18. *Id.*

19. *Id.* at 1-39.

20. Comedy III Prods.v. Saderup, 25 Cal. 4th 387, 391 (2001).

21. CAL. CIVIL CODE § 3344 (West 2001).

preme Court recognized a common law right of publicity.[22] The common law right of publicity was intended to augment statutory law.[23]

California enacted a second statute authorizing rights of publicity to be assignable after death to reconcile the difference between statutory and common law.[24] Section 990 states that any person "who uses a deceased personality's name . . . or likeness . . . for purposes of selling goods . . . without prior consent from the persons specified . . . shall be liable for any damages sustained by the person or persons injured as a result thereof."[25] A "deceased personality" is described as a person whose "name, voice, signature, photograph, or likeness has commercial value at the time of his or her death."[26] The California statutory right of publicity can therefore be assigned to a designee after death.

B. First Amendment Conflict

The First Amendment goals of preserving an uninhibited marketplace of ideas and fostering self-expression free of government restraint may conflict with the right of publicity.[27] Celebrity personas contain some type of public meaning and interest.[28] Use or discussion of this meaning serves the First Amendment purpose of fostering expression.[29] According to Professor Roberta Kwall, "we must have the ability not only to write about, but also to interpret, the thought process of illustrious individuals who have shaped our society."[30] A First Amendment interest therefore exists in the use of a celebrity's image for public debate.

At the same time, courts have found a public interest in allowing a celebrity to control his image, and therefore to enforce his right of publicity.[31] Three policy considerations lie behind this right. First, the right of

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22. *See* Lugosi v. Universal Pictures, 25 Cal. 3d 813, 842 (1979). The common law right of publicity does not provide a cause of action that survives the death of a person owning the right.

23. *Id.* The common law right was not assignable due to its origination in privacy law.

24. CAL. CIV. CODE § 3344.1 (West 2001) (formerly CAL. CIV. CODE § 990 (West 1984)).

25. *Id.* at (a)(1).

26. *Id.*

27. Roberta Rosenthal Kwall, *The Right of Publicity vs. the First Amendment: A Property and Liability Rule Analysis*, 70 IND. L.J. 47, 66 (1994).

28. *See id.*

29. *See id* at 67.

30. *Id.*; *see also* Guglielmi v. Spelling-Goldberg Prods., 25 Cal. 3d 860, 866 (1979) (describing the publicity conflict with the California state Constitution's reiteration of the First Amendment).

31. Carson v. Here's Johnny Portable Toilets, Inc., 698 F.2d 831, 838 (1983).

publicity furthers economic interests of celebrities to enable those whose identities have monetary value to profit from their fame.[32] Second, the right encourages production of creative works by providing financial incentive for individuals to expend the type of investment necessary to produce them.[33] Third, the right serves both individual and societal interests by preventing the communal use of another's identity without compensation as unjust enrichment and deceptive trade practices.[34] A balance is therefore necessary between a public interest in the First Amendment, and the right of publicity.

C. Balancing the Right of Publicity with First Amendment Concerns

Courts have employed several tests in balancing First Amendment rights with a celebrity's right of publicity. In *Zacchini v. Scripps-Howard Broadcasting Company*,[35] the United States Supreme Court considered whether to allow an entire circus act to be broadcast on the evening news.[36] The Court found that, although public figures are afforded less First Amendment protection, the First Amendment "[does] not immunize the media when they broadcast a performer's entire act without his consent."[37] From an economic viewpoint, the Court found that an entertainment act "is the product of petitioner's own talents and energy, the end result of much time, effort, and expense . . . . [I]f the public can see the act free on television, it will be less willing to pay to see it at the [circus]."[38]

More recently, the appellate court in *Cardtoons v. Major League Baseball Players Association* looked toward "social purpose" to balance the First Amendment with the right of publicity.[39] In *Cardtoons*, a baseball card company produced comic book style artwork of baseball players. The court found that, by poking fun at baseball players, the defendant provided "an important form of entertainment and social commentary."[40] To decipher the importance of the defendant's commentary, the court balanced the "underprotection" and "overprotection" of the right of publicity in question. According to the court:

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32. *Id.*
33. *Id.*
34. *Id.*
35. 433 U.S. 562 (1977).
36. *Id.* at 563.
37. *Id.* at 575.
38. *Id.*
39. Cardtoons, L.C. v. Major League Baseball Players Ass'n, 95 F.3d 959, 976 (10th Cir. 1996).
40. *Id.*

> Underprotection of intellectual property reduces the incentive to create; overprotection creates a monopoly over the raw material of creative expression. The application of the Oklahoma publicity rights statute to Cardtoons' trading cards presents a classic case of overprotection. Little is to be gained, and much lost, by protecting the [Major League Baseball Player's Association's] right to control the use of its members' identities in parody trading cards.[41]

While admitting that protection of the right of publicity is "not nearly as compelling as those [arguments] offered for other forms of intellectual property,"[42] the court found societal value in allowing Cardtoons to produce their cards.

The court in *Cardtoons* considered *Zacchini* to be a "red herring" because it "overstated" the economic incentive argument.[43] While economic incentive may be a compelling argument for other forms of intellectual property, "most sports and entertainment celebrities with commercially valuable identities engage in activities that themselves generate a significant amount of income" and therefore do not have the same interests as many copyrights or trademark owners do.[44] Consequently, the conflicting economic analysis of *Cardtoons* and *Zacchini* illustrates an ongoing debate about where to draw the line in the gray area between the First Amendment and the right of publicity.

Another test in balancing a celebrity's right of publicity with the First Amendment is expressed in *Estate of Presley v. Russen*,[45] where the court looked at whether the alleged infringer's appropriation served a social benefit.[46] In this case, the court considered whether a new show entitled "Big El," which copied the format of an Elvis Presley show, deserves First Amendment protection.[47] According to the court, the purpose of the copied shows "must be examined to determine if it predominantly serves a social function valued by the protection of free speech."[48] If the new show meets this social function test, then it deserves First Amendment protection.[49] This particular show was found not to merit protection because it

41. *Id.*
42. *Id.*
43. *Id.* at 973.
44. *Id.*
45. 513 F. Supp. 1339 (D.N.J. 1981).
46. *Id.* at 1356.
47. *Id.* at 1352.
48. *Id.* at 1356.
49. *Id.*

lacked "its own creative component."[50] Big El's use was found not to serve a social function because it copied the original show without making any creative changes.[51]

II. CASE HISTORY

A. District Court Decision

Gary Saderup is an artist who specializes in making charcoal-type drawings of celebrities.[52] The drawings are transformed into lithographic and silkscreen masters in order to produce items such as prints or shirts.[53] Comedy III Productions owns the rights to all items bearing an image of the Three Stooges.[54] Without obtaining permission from Comedy III Productions, Saderup sold lithographic drawings and shirts bearing a charcoal drawing of the Stooges.[55] The products made no claims or endorsement of the Stooges, but contained a likeness of them. Saderup's profits from the sale of Stooges lithographs totaled approximately $75,000.[56]

Comedy III Productions brought an action against Saderup seeking damages and injunctive relief for his alleged violations of California Civil Code section 990.[57] Comedy III alleged that Saderup's use of the Stooges' likeness constituted a violation of the Stooges' publicity rights.[58] The trial court found for Comedy III and entered judgment against Saderup, awarding damages of all gross income plus attorney fees and costs.[59] The court further issued a permanent injunction to restrain Saderup from violating the statute by future use of the Three Stooges' likeness.[60]

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50. *Id.* at 1359.

51. *Id.*

52. Comedy III Prods. v. Saderup, 25 Cal. 4th 387, 393 (2001).

53. *Id.*

54. *Id.* Comedy III Productions was formed by Larry Fine, Moe Howard, and Curly Joe Dirita in 1959. Fine, Howard, and Dirita were three of the six actors who played the Three Stooges. *See The Three Stooges Official Website, at* http://www.threestooges.com/bios/curlyjoe.htm (last visited November 16, 2001).

55. *Comedy III*, 25 Cal. 4th at 393.

56. *Id.* at 394.

57. 68 Cal. App. 4th 744, 747 (Cal. Ct. App. 1998) (noting that California Civil Code § 990 requires consent for any use of a deceased individual's likeness on products, merchandise, or goods).

58. *Id.* Comedy III alleged a statutory (rather than common law) claim as section 990 allowed them to own the rights through assignment. The common law right is not assignable.

59. *Id.* at 747-48.

60. *Id.* at 748.

B. Appellate Court Decision

The Court of Appeal affirmed in part and reversed in part.[61] The court lifted the injunction, reasoning that Saderup was not likely to continue to violate section 990 in the future, and that a probability of reoccurrence "is generally a prerequisite for permanent injunctive relief."[62] Second, the court found that the language of the injunction was overly broad, thereby creating the possibility that "the injunction could extend to matters and conduct protected by the First Amendment."[63] The court rejected Saderup's argument that his conduct was protected by the First Amendment, reasoning that the commercial nature of his product placed it in an unprotectable category.[64]

C. California Supreme Court Decision

The California Supreme Court affirmed the appellate court's decision, although the reasoning behind its decision differed from that of the appellate court.[65] The California Supreme Court focused on the First Amendment issue. According to the court, the right of publicity "is often invoked in the context of commercial speech when the appropriation of a celebrity likeness creates a false and misleading impression that the celebrity is endorsing a product . . . . [T]he present case [however] does not concern commercial speech."[66] Although created for financial gain, Saderup's portraits were found to be "expressive" works and were not an advertisement or endorsement.[67] This classification creates a tension between the Stooges' rights of publicity and Saderup's First Amendment right.

The court acknowledged that the right of publicity has a "potential for frustrating" public debate and the right to self-expression.[68] A celebrity's likeness may contribute to important issues in public debate and individual expression.[69] Giving broad scope to the right of publicity has "the potential of allowing a celebrity to accomplish through the vigorous exercise of that right the censorship of unflattering commentary that cannot be constitutionally accomplished through defamation actions."[70] Saderup does not

61. *Id.* at 747.
62. *Id.* at 756 (citations omitted).
63. *Id.*
64. *Id.* at 757.
65. Comedy III Prod. v. Saderup, 25 Cal. 4th 387, 387 (2001).
66. *Id.* at 396.
67. *Id.*
68. *Id.* at 397.
69. *See id.*
70. *Id.* at 398.

lose his First Amendment protection simply because his work entertains or is sold for financial gain.[71] From this perspective, his works can be protected since it furthers the First Amendment goal of fostering expression.[72]

In deciphering how to balance Saderup's First Amendment right against the Stooges' right of publicity, the court imported an element of the copyright fair use defense.[73] A particular fair use factor—"the purpose and character of the use"[74]—was used to determine whether Saderup's work "merely 'supercedes the objects' of the original creation", or "adds 'something new'" to become "transformative."[75] In employing this "transformative" test, the court asked whether a product containing a celebrity's likeness "is so transformed that it has become primarily the defendant's own expression rather than the celebrity's likeness."[76]

In applying this test, the court found that Saderup's work had no significant transformative element or contribution.[77] Furthermore, the fact that the marketability and value of Saderup's work derived primarily from the fame of celebrities weighs against a transformative classification.[78] Due to the lack of transformative elements within Saderup's paintings, the court denied the fair use claim.[79]

III. DISCUSSION

This Part analyzes *Comedy III*'s analytical framework, and critiques its test to balance the First Amendment's conflict with the right of publicity. Part III.A evaluates the court's general claim that copyright fair use can be effectively applied to the right of publicity. It describes how the court correctly found copyright as a proper framework to help resolve First Amendment problems in publicity and from which to import a balancing test. Part III.B examines the *Comedy III* court's fair use test and argues

71. *Id.*

72. *Id.* at 397.

73. Copyright's four fair use factors are: (1) The purpose and character of the use, including whether such use is of a commercial nature; (2) the nature of the copyrighted work; (3) the amount and substantiality of the portion used in relation to the copyright work as a whole; and (4) the effect of the use upon the potential market for or value of the copyrighted work. 17 U.S.C. § 107 (1994).

74. 17 U.S.C. § 107(1) (1994).

75. *Comedy III*, 25 Cal. 4th at 404 (quoting Campbell v. Acuff-Rose Music, Inc., 510 U.S. 569, 585 (1994)).

76. *Id.* at 406.

77. *Id.* at 409.

78. *Id.*

79. The court found Saderup's work to be expressive, but his expression was discounted as being "trivial." *Id.* at 408.

that it does not set adequate standards. Instead, the court should have specifically defined its requirements and designated commercial considerations as a distinct factor.

A. Copyright Fair Use Importation

This section evaluates the *Comedy III* court's general claim that copyright fair use can be properly applied to the right of publicity. The court in *Comedy III* claimed that "common goals" between the right of publicity and copyright would allow fair use to serve a similar benefit.[80] To decipher these common goals, copyright and publicity objectives will be compared. This section concludes that the court correctly found a proper general framework in copyright to resolve Saderup's First Amendment question.

1. Common Goals

Copyright law is designed to "stimulate activity and progress in the arts for the intellectual enrichment of the public."[81] This utilitarian goal is achieved by permitting authors to reap the rewards of their creative efforts, while not conferring unfettered ownership because it could stifle creativity.[82] The right of publicity shares a similar policy.[83] Both the First Amendment and copyright law "have a common goal of encouragement of free expression and creativity, the former by protecting such expression from government interference, the latter by protecting the creative fruits of intellectual and artistic labor."[84] The right of publicity likewise seeks to allow celebrities to control their works, while stimulating creation and free expression.

Due to these common goals and policy interests, the court in *Comedy III* was correct in finding copyright to be a comparable framework. First, by permitting individuals to benefit from their personal efforts, both the right of publicity and copyright provide incentive for creative endeavors. Second, both frequently pose a potential conflict with the First Amendment framework. By utilizing the copyright analogy in right of publicity decisions, courts can inject uniformity and predictability into an area of

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80. *Id.* at 404.

81. Pierre N. Leval, *Toward a Fair Use Standard*, 103 HARV. L. REV. 1105, 1107 (1990).

82. *See id.* at 1109.

83. *See* Dall T.E. Coyne, *Toward a Modified Fair Use Defense in Right of Publicity Cases*, 29 WM. & MARY L. REV. 781, 813 (1988).

84. Comedy III Prods. v. Saderup, 25 Cal. 4th 387, 405 (2001) (citations omitted).

law that often contains conflicting and inconsistent decisions.[85] Furthermore, as copyright is of constitutional origin, judges can draw upon a developed body of case law in their resolution of publicity rights issues.[86]

2. *Fair Use in Copyright*

A publicity fair use test must work to reconcile rights of free expression.[87] Fair use was first instituted in copyright to unify future First Amendment decisions.[88] In *Folsom v. Marsh*, Justice Story found a need to prepare a test that discovered "the value of the materials taken, and the importance of it to the sale of the original work."[89] Story's test was significant because prior to *Folsom*, copyright was marred by inconsistency in First Amendment jurisprudence.[90] Courts applied a number of subjective tests—varying from looking simply at the "quantity" of the work used, to analyzing the intrinsic and societal value in allowing a "fair" quotation of copyrighted material.[91] Justice Story found that the main factors that should be applied in reconciling the First Amendment with copyright interests were an evaluation of the nature of the new work, the value and quantity of the copyrighted portion used, and the economic impact on the original work's current or future market.[92]

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85. Coyne, *supra* note 83, at 814. *See also* Stephen R. Barnett, *"The Right to One's Own Image": Publicity and Privacy Rights in the United States and Spain*, 47 AM. J. COMP. L. 555, 556 (1999) (labeling the current right of publicity a "quilt of inconsistent statutory and common-law interpretations") (citations omitted).

86. Coyne, *supra* note 83, at 814.

87. *See Comedy III*, 25 Cal. 4th at 404.

88. Folsom v. Marsh, 9 F. Cas. 342, 349 (C.C.D. Mass. 1841) (No. 4,901).

89. *Id.* at 348.

90. *See id.* Prior to Justice Story's classification, some judges would vary their tests from looking wholly at the "quantity" of the work appropriated, while others would subjectively try to determine the "value" of the copied work to see if it interfered with the copyright. *See id.* Story found a need to consolidate these views to create a unified fair use test. His test was later codified in 17 U.S.C. § 107.

91. *Id.* Story referred to common law decisions to illustrate the inconsistent ways in which judges reasoned. *See, e.g.*, Wilkins v. Aikin, 17 Ves. 422, 424 (1810) (focusing on the quantity of the material used to determine whether the amount used constituted "fair quotation"); Bramwell v. Halcomb, 3 Mylne & Cr. 737, 738 (1836) (explaining that "[o]ne writer might take all the vital part of another's book, though it might be but a small proportion of the book in quantity. It is not only quantity, but value, that is always looked to." According to this reasoning, it is irrelevant whether the quoted amount was fair, so long as the quotation itself is valuable); Roworth v. Wilkes, 1 Camp. 94 (1807) (inquiring into whether the copied work would serve as a "substitute" for the original); *See also* WILLIAM F. PATRY, THE FAIR USE PRIVILEGE IN COPYRIGHT LAW, 6-7 (2d ed. 1995) (chronicling the development of fair use prior to Folsom v. Marsh).

92. *Id.* at 348.

Justice Story's test properly limited the scope of the copyright monopoly while creating a new unified First Amendment balancing test. The fair use doctrine "permits [and requires] courts to avoid rigid application of the copyright statute when, on occasion, it would stifle the very creativity which that law is designed to foster."[93] The doctrine "offers a means of balancing the exclusive right of a copyright holder with the public's interest in dissemination of information affecting areas of universal concern, such as art, science, history, or industry."[94] As Lord Ellenborough explained, "[w]hile I shall think myself bound to secure every man in the enjoyment of his copyright, one must not put manacles upon science."[95] To this extent fair use is a necessary part of the overall design of copyright. According to Judge Leval, "although no simple definition of fair use can be fashioned, and inevitably, disagreement will arise over individual applications . . . fair use [is] integral to copyright's objectives."[96] Any First Amendment protections therefore must serve copyright's objective of stimulating productive thought and public instruction without excessively diminishing future creative incentive.[97]

While continuing to be "one of the most important and well-established limitations on the exclusive right of copyright,"[98] the fair use doctrine is also viewed as one of copyright's most unpredictable aspects.[99] On one hand, fair use allows for some uniformity in deciding First Amendment use of copyrighted material. On the other hand, fair use cannot become a bright-line rule, because it is applied on a case-by-case basis. However, the case-by-case approach has been necessary to determine expression and market impact in individual artistic cases—a determination similarly necessary in a future right of publicity First Amendment test.

3. *Fair Use in the Right of Publicity*

Absent a First Amendment balancing test, the right of publicity finds itself in a state similar to that of copyright law before fair use was implemented. That is, a need exists for a clear, unified test to resolve future First Amendment questions. As once was the case for copyright law, courts in publicity law cases have employed varied and often conflicting balancing

93. Stewart v. Abend, 495 U.S. 207, 236 (1990) (quoting Iowa State Univ. Research Found. Inc. v. Am. Broad. Cos., 621 F.2d 57, 60 (1980)).

94. Meeropol v. Nizer, 560 F.2d 1061, 1068 (2d Cir. 1977).

95. Cary v. Kearsley, 170 Eng. Rep. 679, 681 (1803).

96. Leval, *supra* note 81, at 1110.

97. *Id.*

98. MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT § 13.05 (2001) (citations omitted).

99. *Id.*

tests in determining the line between First Amendment protection and rights of publicity. Lines of analysis vary from a pure economic analysis,[100] to a social benefit analysis.[101] Moreover, nature and application of the right of publicity has varied substantially between states.[102] By drawing on copyright principles, courts can bring a greater amount of predictability into this area.[103] Such a test must "distinguish between forms of artistic expression protected by the First Amendment and those that must give way to the right of publicity."[104] Application of copyright fair use doctrine into right of publicity decisions can therefore help to achieve a balance between First Amendment free speech interests and the goals underlying the right of publicity; namely, to promote creative endeavors and prevent unjust enrichment.[105]

Furthermore, leading scholars such as Mark Lemley and Eugene Volokh have argued that the current speech-restrictive potential of the right of publicity doctrine may be inherently unconstitutional.[106] They argue that the right of publicity has the potential to restrict speech to a much higher degree than trademark or even libel law.[107] Thus, without a First Amendment balancing test, the publicity doctrine itself may be substantively unconstitutional.[108] Therefore, the court in *Comedy III* correctly realized a need to address inherent right of publicity tensions with the First Amendment. According to the court, the right of publicity in its present form has a potential of allowing a celebrity to censor unflattering commentary in a method that cannot be constitutionally accomplished through

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100. *See* Zacchini v. Scripps-Howard Broad. Co., 433 U.S. 562, 575 (1977).

101. *See* Estate of Presley v. Russen, 513 F. Supp. 1339, 1356 (D.N.J. 1981).

102. Barnett, *supra* note 85.

103. *Id.*

104. Comedy III Prods. v. Saderup, 25 Cal. 4th 387, 403 (2001).

105. Coyne, *supra* note 83 at 821.

106. Mark A. Lemley & Eugene Volokh, *Freedom of Speech and Injunctions in Intellectual Property Cases*, 48 DUKE L.J. 147, 227 (1998) ("The speech-restrictive potential of the right of publicity goes much further than that of trademark law, or even libel law, and it may mean that the doctrine as a whole is substantively unconstitutional . . . ."). Elsewhere, Lemley and Volokh explain the need for a unified First Amendment test: "[t]he result [in publicity cases] is a rather puzzling mix of precedents, with no clear doctrinal line separating those cases in which preliminary injunctions are granted from those in which the prior restraint rule is applied." *Id* at 228.

107. *Id.* at 227 ("The goal of both trademark and defamation law is to identify and suppress false speech about a person or product which may mislead the public. By contrast, nothing in the right of publicity requires that the punished speech be false or misleading.").

108. *See id.*

defamation actions.[109] A new test is needed, one that must incorporate "the principle that the right of publicity cannot, consistent with the First Amendment, be a right to control the celebrity's image by censoring disagreeable portrayals."[110] This new test can be derived from the copyright realm.

B. Improving Fair Use

Given that the court correctly found a need for a First Amendment test, and copyright fair use could indeed provide a useful realm to import guidelines, this section analyzes the *Comedy III* court's transformative test to determine whether it properly satisfies the need for a clear, unified test. This section argues that the test laid out in *Comedy III* was overly vague and does not go far enough to set proper standards. To improve a publicity fair use test, the court should have specifically defined its requirements and designated commercial considerations as a separate factor.

1. Doctrinal Guidelines

First Amendment law should discourage unpredictability in judicial decision making. The void-for-vagueness doctrine mandates that arbitrary laws can hinder speech.[111] It specifies that clear guidelines for triers of fact should be set to prevent arbitrary First Amendment decisions, as unclear rules may cause speakers to steer wider of the unlawful area than is necessary.[112] This would in turn inhibit the exercise of First Amendment freedoms. First Amendment rules must therefore be drawn as narrowly as possible as to avoid uncertainty.[113]

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109. *Comedy III*, 25 Cal. 4th at 398.

110. *Id.* at 403.

111. MCCARTHY, *supra* note 11, at 8-12. *See also* Grayned v. City of Rockford, 408 U.S. 104. (1972). In *Grayned*, the Court noted:

> It is a basic principle of due process that an enactment is void for vagueness if its prohibitions are not clearly defined. Vague laws offend several important values . . . because we assume that man is free to steer between lawful and unlawful conduct, we insist that laws give the person of ordinary intelligence a reasonable opportunity to know what is prohibited, so that he may act accordingly. Vague laws may trap the innocent by not providing fair warning."

Id. at 108-09.

112. *See* MCCARTHY, *supra* note 11, at 8-12; *see also* Connally v. Gen. Constr. Co., 269 U.S. 385, 391 (1926) ("[A] statute which either forbids or requires the doing of an act in terms so vague that men of common intelligence must necessarily guess at its meaning and differ as to its application, violates the first essential of due process of law.") (citations omitted).

113. *See* RONALD D. ROTUNDA, TREATISE ON CONSTITUTIONAL LAW—SUBSTANCE & PROCEDURE § 20.9 (3d ed. 1999).

Apart from the void-for-vagueness doctrine, the court's transformative test must satisfy a test of strict scrutiny. The strict scrutiny doctrine dictates that "when there exists a real and appreciable impact on, or a significant interference with the exercise of the fundamental right [of the First Amendment,] the strict scrutiny doctrine will be applied."[114] To satisfy strict scrutiny, a rule must be "neither vague nor subjectively over- or underinclusive."[115] The rule must further an overriding state interest and also be drawn with narrow specificity in order to avoid an unnecessary intrusion on First Amendment rights.[116] *Comedy III*'s fair use test is arguably both vague and broad, thereby raising a question as to its survival under a strict scrutiny test. To satisfy the guidelines set in the void-for-vagueness doctrine, and the strict scrutiny test, the right of publicity test will need to set clear guidelines.

2. *Clarify Fair Use*

The *Comedy III* test does not set sufficient guidelines. As stated before, the *Comedy III* fair use test asks whether the product in question "is so transformed that it has become primarily the defendant's own expression rather than the celebrity's likeness."[117] "Expression" is vaguely classified as "something other than the likeness of the celebrity."[118] This definition is not useful for developing a test for the right of publicity. Other courts have also applied highly subjective tests when confronted with a publicity First Amendment challenge. For example, *Cardtoons* focused on whether the product provides "social commentary,"[119] *Estate of Presley* asked whether the new show produced a "social benefit",[120] *Groucho Marx Productions, Inc. v. Day & Night* looked for "works designed primarily to promote the dissemination of thoughts,"[121] and *Zacchini* used an economic utility argument that tried to create a balanced test.[122] The California Supreme Court in *Comedy III* wanted to move past these prior stan-

114. Fair Political Practices Comm'n. v. Super. Ct., 25 Cal. 3d 33, 47 (1979) (citations omitted).

115. H-CHH Assocs. v. Citizens for Representative Gov't, 193 Cal. App. 3d 1193, 1207 (1987).

116. *See id.*

117. Comedy III Prods. v. Saderup, 25 Cal. 4th 387, 406 (2001).

118. *Id.*

119. Cardtoons, L.C. v. Major League Baseball Players Ass'n, 95 F.3d 959, 976 (10th Cir. 1996).

120. *Estate of Presley*, 513 F. Supp. at 1356.

121. 523 F. Supp. 485, 492 (1981).

122. Zacchini v. Scripps-Howard Broad. Co., 433 U.S. 562, 575 (1977).

dards and create a new unifying test;[123] however, the guidelines they used to implement the test did not properly achieve this goal.[124]

First, the court's test does not specify evidentiary burdens. The United States Supreme Court case of *Harper & Row Publishers, Inc. v. Nation Enterprises*, classified copyright fair use as an exception and affirmative defense, where the burden of proof is on the party invoking it.[125] The *Harper & Row* view has caused some analysts to consider fair use inadequate in protecting First Amendment guarantees.[126] A publicity test should therefore move away from the affirmative defense classification in *Harper & Row*. *Comedy III* does not specify whether right of publicity fair use will take a different approach. The court suggests that future decisions should look to see if creative elements "predominate in the work."[127] The court does not specify whether the party invoking fair use will have the burden of proof to show the predominate expression, nor does it indicate how lenient a future court should be in deciding what constitutes "creative elements."[128]

Second, the court does not properly define how much expression a work needs to satisfy the transformative test, other than specifying that the new work should be different than the celebrity's likeness.[129] The court provides only one case example that would hypothetically satisfy its test; however, this example is not particularly helpful because, unlike Sad-

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123. *See Comedy III*, 25 Cal. 4th at 406 (noting that decisions using the transformative test will unify right of publicity law by taking "many forms, from factual reporting, to fictionalized portrayal, heavy handed lampooning, to subtle social criticism").

124. Arguably, the court in *Cardtoons* could have been using a pseudo-transformative test when deciding whether the cards' image commented on baseball to a degree that allows societal value. The social benefit analysis in *Estate of Presley* similarly closely resembles that of a "transformative" analysis. Elements that the court looked for to decipher social benefit (did the new "Big El" show merely copy Elvis, or does it add a new creative element?) are nearly identical to that in a broad "transformative" analysis.

125. *See* Harper & Row Publishers, Inc. v. Nation Enters., 471 U.S. 539, 561 (1985).

126. *See* Neil Weinstock Netanel, *Locating Copyright Within the First Amendment Skein*, 54 STAN. L. REV. 1, 21-22 (2001). Netanel argues that since the *Harper & Row* decision:

> Courts have repeatedly invoked the bare possibility of licensing in potential markets for the copyright holder's work to deny fair use. In some cases, indeed, courts have denied fair use even where the copyright owner's avowed purpose is to suppress publication of material that might show the copyright owner in an unfavorable light.

Id.

127. *Comedy III*, 25 Cal. 4th at 407.

128. *Id.*

129. *Id.* at 406.

erup's work, it concerns a parody.[130] In copyright, as well as publicity, parody places itself in an obvious transformative category.[131] It is very easy therefore to point to parody as being "transformative."[132] With regards to situations that do not involve parodies—such as Saderup's work—the court does not specify elements that could have caused his work to be considered transformative. Instead, Saderup's lithograph was discounted as a work with "trivial" expression that is not recognizably "his own."[133] While it may be difficult to create a bright-line rule to determine what constitutes expression, the court could have given further examples of transformative works in addition to clearly defining how "recognizably 'his own'" Saderup's work should have been.[134]

3. *Commercial Considerations*

Finally, to satisfy the strict scrutiny test and the void-for-vagueness doctrine, a publicity fair use test should separate economic and transformative elements. The *Comedy III* court alluded to including an economic harm factor, but it left this test as a vague subsidiary of the transformative consideration.[135] Under the *Comedy III* test, economic considerations can be an optional part of a transformative analysis "particularly in close cases," and as a "subsidiary inquiry."[136] This "subsidiary" inquiry might ask if "the marketability and economic value of the challenged work derive[s] primarily from the fame of the celebrity depicted . . . . "[137] The court further hinted at an economic test when it pointed to *Cardtoons* as properly decided on the grounds that the parody was found to "not likely substantially impact the economic interests of celebrities."[138] It seems then that the court improperly merged aspects of an economic test into the transformative/expression test. A use is more likely to be transformative if it does not impact a celebrity's "economic interests."[139] It is however unclear when this "subsidiary" inquiry would take effect, and how it should

130. *Id.* ("*Cardtoons* . . . is consistent with this 'transformative' test.").

131. *See* Campbell v. Acuff-Rose Music, Inc., 510 U.S. 569, 579 (1994) ("Parody has an obvious claim to transformative value . . . . Like less ostensibly humorous forms of criticism, it can provide social benefit, by shedding light on an earlier work, and, in the process, creating a new one.").

132. *Id.*

133. *Comedy III*, 25 Cal. 4th at 408 (quoting Batlin & Son, Inc. v. Snyder, 536 F.2d 486, 490 (2d Cir. 1976)) (citations omitted).

134. *Id.*

135. *Id.* at 407.

136. *Id.*

137. *Id.*

138. *Id.* at 406.

139. *Id.*

be weighed against the general transformative test. Saderup's situation was considered a close case, but the court did not fully utilize the economic test as they designated.[140]

Instituting an "economic harm" inquiry into a separate factor may therefore add clarity to the new rights of publicity fair use standard. This separate factor can be used in the same way that copyright's fourth fair use factor is applied. Deemed "undoubtedly the single most important element of fair use,"[141] copyright's fourth fair use factor asks a court to consider "the effect of the use upon the potential market for or value of the copyrighted work."[142] The Second Circuit found that this factor can create a balance between "the benefit the public will derive if the use is permitted and the personal gain the copyright owner will receive if the use is denied."[143] The Court in *Campbell* defines this factor as requiring that the court consider "not only the extent of market harm caused by the particular actions of the alleged infringer, but also whether unrestricted and widespread conduct . . . would result in a substantially adverse impact on the potential market for the original."[144] A potential market does not only lie within the original work's current market, but also within the potential future derivative market in which the new work has a potential of causing "market substitution."[145] This definition can be particularly useful in publicity, where a court can ask whether the celebrity realistically would enter the market in question.

The court in *Comedy III* initially rejected application of copyright's fourth fair use factor by labeling the factor as "irrelevant" to the right of publicity.[146] According to the court:

> If it is determined that a work is worthy of First Amendment protection because added creative elements significantly transform the celebrity depiction, then independent inquiry into whether or not that work is cutting into the market for the celebrity's images—something that might be particularly difficult to ascertain in the right of publicity context appears to be irrelevant. Moreover, this "potential market" test has been criticized for circularity: it could be argued that if a defendant has capitalized in any

140. *Id.*

141. *Harper & Row*, 471 U.S. at 566.

142. 17 U.S.C. §107(4) (1994).

143. Wright v. Warner Books, Inc., 953 F.2d 731, 739 (2d Cir. 1991) (citations and internal quotation marks omitted).

144. 510 U.S. at 590.

145. *Id.* at 593.

146. *Comedy III*, 25 Cal. 4th at 405 n.10.

> way on a celebrity's image, he or she has found a potential market and therefore could be liable for such work.[147]

The fourth factor is not applicable because it may be both "difficult to ascertain" and "circular."[148] While ascertaining market harm in a right of publicity context may pose some difficulties, it should not be eliminated. In copyright fair use, courts regularly attempt to determine the market effect of derivative works.[149] A right of publicity determination raises similar questions to copyright derivative works (i.e., whether the related—yet not identical—work harms the original) and can be ascertained in the same way.

Arguably, a separate consideration similar to copyright's fourth fair use factor can improve *Comedy III*'s transformative test. In cases of artwork, where it is unclear whether a work is transformative, such as with Saderup's works, a court can look to economic harm as a determinative consideration. The court can consider whether transformative elements dominate the work to a point that its economic value derives from the artist expression, rather than the celebrity.[150] For example, if an artist utilizes a celebrity's image as a subsidiary device within a painting to further the artist's overarching expressive theme, a court may find that the work does not threaten the type of celebrity market protected by the right of publicity.[151] Economic considerations go beyond mere damages, and "pose[] the issue of whether unrestricted and widespread conduct of the sort engaged in by the defendant . . . would result in a substantially adverse impact on

147. *Id.* (citation omitted).

148. *Id.*

149. *See Campbell*, 510 U.S. at 593 (determining whether a rap song was a derivative work harming the potential market of a Roy Orbison song); *see also* Roy Export Co. v. CBS, 503 F. Supp. 1137, 1146 (S.D.N.Y. 1980) ("The value of the right to use the copyrighted work to make a derivative work, which the copyright owner may sell or himself exercise, would certainly seem to be diminished by the ability of another to use the copyrighted work in order to compete at will with the derivative work.").

150. *See* Meeropol v. Nizer, 560 F.2d 1061, 1070 (2d Cir. 1977) (citations omitted).

151. *See Comedy III*, 25 Cal. 4th at 405 (admitting that artistic works with significant expressive elements "are not, from the celebrity fan's viewpoint, good substitutes for conventional depictions of the celebrity and therefore do not generally threaten markets for celebrity memorabilia that the right of publicity is designed to protect"); *see also* ETW Corp. v. Jireh Publ'g, Inc., 99 F. Supp. 2d 829, 835 (2000) (holding that a painting depicting Tiger Woods does not violate Woods' right of publicity because Woods' image is not the primary point of the painting, but rather it is being used to portray a social message about American life. This could therefore be a work where expressive elements in the painting dominate to a point that its sale does not substantially interfere with Woods' memorabilia market).

the potential market for, or value of, the plaintiff's present work."[152] The potential market in publicity will presumably look at a realistic monetary impact on the celebrity.[153]

An economic consideration would further decipher whether the infringing work performs the same function as the existing market created by a celebrity.[154] In copyright, the "functional" test asks if "regardless of medium, the defendant's work, though containing substantially similar material, performs a different function than that of the plaintiff's."[155] David Nimmer describes the functional test in an example involving a reproduction of copyrighted musical lyrics in an article in a magazine:

> The unauthorized reproduction of the chorus lyrics of songs [is a] noninfringing fair use where such reproductions appear in magazine articles .... [T]he plaintiff and defendant, in a sense, employed the same medium, *i.e.*, the printed page. However, the functions differed in that plaintiff's sheet music was intended to be used for singing or musical performances, while defendant's article was a literary presentation that incidentally included the disputed lyrics. Persons interested in obtaining plaintiff's music for musical purposes would not find that need fulfilled through the purchase of defendant's magazine article.[156]

The copyright functional test therefore finds a use to be fair where its function does not act as a market substitution for the original copyrighted work. In the right of publicity, the functional test can lean towards fair use where expressive elements within a defendant's works cause consumers to purchase those works primarily for the expression, and not the celebrity. Where a consumer purchases a product because of expressive content, the celebrity's future market is likely not being substituted.[157] Separating

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152. NIMMER, *supra* note 98. *See also Campbell*, 510 U.S. at 593 n.23 ("'[P]otential market' means either an immediate or a delayed market, and includes harm to derivative works.").

153. Once again, monetary impact can be determined on a case-by-case basis in the same way that it is accomplished in copyright cases involving derivative works.

154. *See* NIMMER, *supra* note 98, at § 13.05[B][1].

155. *Id.*

156. *Id.*; *see also* Broadway Music Corp. v. F-R Publ'g Corp., 31 F. Supp. 817 (S.D.N.Y. 1940) (holding that a magazine's publication of a musical's song lyrics was fair use).

157. The court alluded to the notion of a fourth factor functional test. However, it refused to specifically classify it as such:

> [W]hen a work contains significant transformative elements ... it is also less likely to interfere with the economic interest protected by the right of publicity. As has been observed, works of parody or other distortions of the celebrity figure are

commercial considerations into a second factor can therefore add clarity to a publicity fair use test in satisfying guidelines set forth in the void-for-vagueness and strict scrutiny doctrines.

IV. CONCLUSION

At one point, copyright law found itself in a predicament. Courts had not found a unified method of deciding the parameters with which the First Amendment permits the unauthorized use of copyrighted works. While some courts focused on subjective standards to decide if the "value" of the work had been appropriated, other courts looked purely to economic harm.[158] When developing the copyright fair use test, Justice Story noted that it is not easy "to lay down any general principles applicable to all [First Amendment] cases."[159] He nonetheless found that copyright law needs to form guidelines that can standardize future First Amendment questions. His test therefore asked four specific questions while designating that the test be used on a case-by-case basis.[160] This designation struck a balance between the need to have both clear guidelines and flexibility where it is needed in the realm of artistic works.

The right of publicity currently finds itself in a predicament. Case law has shown that courts have varied their method of First Amendment balancing to range from a social utility to a pure economic test.[161] In finding a need for a new unified publicity test, the court in *Comedy III* correctly looked at copyright law for guidance. Copyright law shares common goals and dilemmas to the right of publicity. Both recognize that authors should have control over their works, while simultaneously accepting that this control does not confer an absolute ownership.[162] Copyright fair use can therefore serve as a model for a right of publicity test that protects First Amendment rights.

> not, from the celebrity fan's viewpoint, good substitutes for conventional depictions of the celebrity and therefore do not generally threaten markets for celebrity memorabilia that the right of publicity is designed to protect. Accordingly, First Amendment protection of such works outweighs whatever interest the state may have in enforcing the right of publicity. The right-of-publicity holder continues to enforce the right to monopolize the production of conventional, more or less fungible, images of the celebrity.

Comedy III, 25 Cal. 4th at 405.

158. *See* Folsom v. Marsh, 9 F. Cas. 342, 348 (C.C.D. Mass. 1841) (No. 4,901).

159. *Id.* at 344.

160. *Id.* at 350.

161. *See* Zacchini v. Scripps-Howard Broad. Co., 433 U.S. 562, 575 (1977); Estate of Presley v. Russen, 513 F. Supp. 1339, 1356 (D.N.J. 1981).

162. *See* Leval, *supra* note 81, at 1110.

Unfortunately, unlike Justice Story's test, the *Comedy III* court's fair use test does not strike a proper balance between a need for clear guidelines and versatile use. The court did not delineate evidentiary burdens, define "expression," or provide substantial examples of "transformative" works. Furthermore, the court did not develop the role of assessing economic harm within the transformative analysis. To serve a similar function as copyright fair use, the right of publicity fair use test needs to further clarify itself, as part of this improvement should be the placement of economic harm into a separate factor. It may not be easy to lay down general principles applicable to all First Amendment cases.[163] It is necessary to form guidelines that are as specific as possible. An improved right of publicity test can perhaps serve this important function.

163. *Folsom*, 9 F. Cas. 342 at 348.

E.C. DATABASE DIRECTIVE

By Xuqiong (Joanna) Wu

In an effort to harmonize the level of database protection throughout the European Union ("E.U.") and promote the growth of the European database industry,[1] the European Parliament ("Parliament") and the Council of the European Union ("Council") adopted Directive 96/9/EC on the legal protection of databases ("E.C. Directive") on March 11, 1996.[2] The E.C. Directive creates a sui generis right which protects database content from unauthorized "extraction" and/or "re-utilization," in addition to copyright protection which guards the structure and organization of databases.[3] While the copyright protection is similar to that granted by the United States ("U.S.") copyright law,[4] the sui generis provisions create a property-like right in database contents.[5] During the past few years, many E.U. Member States have incorporated the Directive in their national laws,[6] and more than two dozen cases have been decided under this legislation.[7]

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1. *See* J.H. Reichman & Pamela Samuelson, *Intellectual Property Rights in Data?*, 50 VAND. L. REV. 51, 74-76 (1997).

2. Directive 96/9/EC of the European Parliament and of the Council of 11 March 1996 on the Legal Protection of Databases, 1996 O.J. (L 77) 20 [hereinafter E.C. Directive].

3. *Id.* at ch. III, arts. 7-11 (defining the sui generis right).

4. *Id.* at ch. II, arts. 3-6. These articles define the copyright in databases; in particular, Article 3 defines the object of copyright protection of databases as "the author's own intellectual creation" "by reason of the selection or arrangement of [databases'] contents." *Cf.* Feist Publ'ns, Inc. v. Rural Tel. Serv. Co., 499 U.S. 340 (1991) (the landmark United States Supreme Court decision holding that originality must exist in the selection, coordination, or arrangement of contents for a database to qualify for copyright protection). The Court emphasized that "[t]he *sine qua non* of copyright is originality." *Id.* at 345.

5. *See* E.C. Directive, *supra* note 2, at art. 7. *See generally infra* Part I.B.

6. Stephen M. Maurer, *Across Two Worlds: Database Protection in the US and Europe*, at 29-31 (paper prepared for Industry Canada's Conference on Intellectual Property and Innovation in the Knowledge-Based Economy, May 23-24, 2001) (on file with author) (observing that not all Member States voluntarily implemented the E.C. Directive).

7. *See id.* at 32-34 (discussing European case law developed since national implementation of the E.C. Directive); *see also* P. Bernt Hugenholtz, *The New Database Right: Early Case Law from Europe* (paper presented at Ninth Annual Conference on International IP Law & Policy, Fordham University School of Law, New York, Apr. 19-20, 2001), *at* http://www.ivir.nl/publications/hugenholtz/fordham2001.html.

The E.C. Directive has influenced lawmaking in the U.S. as well. Databases created in countries outside the E.U. do not qualify for sui generis right protection under the E.C. Directive unless these countries outside of the European Community ("Community") have a similar level of protection for databases.[8] This reciprocity requirement appears to be driving forward similar legislation in the U.S.[9] The database industry has been lobbying Congress to strengthen database protection in the United States,[10] while the scientific research communities, public policy researchers, and libraries have criticized the legislative attempts to create a property-like right in database contents.[11] Proponents of database rights worry that data-

8. The E.C. Directive contains a provision requiring that database makers be nationals of a member state in the Community or have their habitual residence in the E.U. *See* E.C. Directive, *supra* note 2, pmbl., recital 56. *See also* David Mirchin, *The European Database Directive Sets the Worldwide Agenda*, 39 NFAIS NEWSL. 7, 9 (Jan. 1997), *available at* http://www.pa.utulsa.edu/nfais/pubscat/mirchin.html; Ferris Webster, *A Summary of Database Protection Activities*, Scientific Access to Data and Information, *at* http://www.codata.org/data_access/summary.html (Nov. 30, 2000) (observing that "The EU Directive contains a reciprocity clause .... Though this clause has been frequently cited as a motivation for legislation in other countries, it may violate the principles of the World Trade Organization").

9. Stephen M. Maurer et al., *Europe's Database Experiment*, 294 SCIENCE 789 (2001) (observing the weak database lobbying from 1991 until 1996 when "Congress took the EC's threat seriously").

10. *See* Laura D'Andrea Tyson & Edward F. Sherry, Information Industry Association, *Statutory Protection for Databases: Economic & Public Policy Issues*, http://www.house.gov/judiciary/41118.htm (last visited Feb. 12, 2002).

11. *See, e.g.*, Maurer et al., *supra* note 9; Stephen M. Maurer & Suzanne Scotchmer, *Database Protection: Is It Broken and Should We Fix It?*, 284 SCIENCE 1129 (1999) (arguing that, unless there is a demonstrated immediate need for strong database protection, legislature should not act); William Gardner & Joseph Rosenbaum, *Database Protection and Access to Information*, 281 SCIENCE 786 (1998) (criticizing the Collections of Information Antipiracy Act of 1998, H.R. 2652, and using a hypothetical situation to illustrate the bill's negative effects on scientific research); J.H. Reichman & Paul F. Uhlir, *Database Protection at the Crossroads: Recent Developments and Their Impact on Science and Technology*, 14 BERKELEY TECH. L.J. 793, 796 (1999) (concluding that "a daunting array of legal and contractual restraints on the ability of scientists and engineers to access factual data and information" could compromise the research-based institutions); *European Union Database Directive Sets Dangerous Precedent for Librarians Worldwide*, Association of Research Libraries, *at* http://www.arl.org/info/frn/copy/iff1.html (last modified May 21, 1998). The National Academy of Sciences also conducted a workshop that studied the characteristics of scientific and technical databases, reviewed technologies available and in development for protecting or misappropriating digital contents, and discussed legal and policy options for promoting access to data in the government sector, non-profit sector, and commercial sector. *See* PROCEEDINGS OF THE WORKSHOP ON PROMOTING ACCESS TO SCIENTIFIC AND TECHNICAL DATA FOR THE PUBLIC INTEREST: AN ASSESSMENT OF POLICY OPTIONS (Comm'n on Physical Sciences,

base makers in the U.S. would not qualify for protection in the E.U. and thereby lose their competitive advantages against the European counterparts, since the U.S. does not offer a similar sui generis database right.[12]

This Note discusses developments in the E.U. since the adoption of the E.C. Directive, with a focus on the sui generis right provisions and the development of a body of case law on this topic in the Member States. It also considers whether it is appropriate and constitutionally permissible to adopt similar database legislation in the U.S. Part II briefly describes the origins of the E.C. Directive, and, specifically, how database protection evolved into a sui generis right. Part II also focuses on key E.C. Directive provisions and concepts and how Member States courts have interpreted these provisions. Part III discusses similar developments in the U.S., focusing on whether a new legal regime for database protection is necessary, and whether it provides a viable model for the U.S. This Part also briefly discusses alternatives to a sui generis database right. This Note concludes that a new legal regime, which creates a property right in databases, is neither necessary nor appropriate in the U.S. Instead, alternative legal regimes based on the doctrine of unfair competition, and supplemented by contract law or a modified liability rule may simultaneously promote the growth in the database industry and unobstructed access to data.

I. THE EUROPEAN DIRECTIVE AND CASE DEVELOPMENT

This Part introduces the key provisions on sui generis protection of databases, beginning with historical background and the main driving forces behind the E.C. Directive, and moving to key provisions and concepts in the E.C. Directive and an analysis of their interpretations by courts in the Member States following national implementation. This analysis will

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Mathematics, and Applications ed., 1999), *available at* http://www.nap.edu/books/NI000903/html/.

12. *Cf.* Myths and Facts About S. 2291/Title V of H.R. 2281 (Originally enacted as H.R. 2652): The Collections of Information Antipiracy Act, Association of Research Libraries, *at* http://www.arl.org/info/frn/copy/myth.html (last modified Aug. 24, 1998) (rejecting the argument that H.R. 2652 is required to assure protection for U.S. databases in Europe); *Collections of Information Antipiracy Act of 1998: Hearing on H.R. 2652 Before the Subcomm. on Courts and Intellectual Property, House Comm. on the Judiciary,* 105th Congress (1998) (testimony of Jonathan Band on behalf of the Online Banking Ass'n), *at* http://www.house.gov/judiciary/41148.htm [hereinafter Band testimony]; *Professor Pamela Samuelson's Letter re: Tyson/Sherry Report* (Oct. 23, 1997), *at* http://www.arl.org/info/frn/copy/psamlet.html [hereinafter *Samuelson's letter*] (Oct. 23, 1997).

demonstrate that the E.C. Directive has yet to fulfill its goal of harmonizing database protection in the Member States.[13]

A. History of the E.C. Directive

Database protection in the E.U. originated in 1988, when the European Commission ("Commission") set forth an agenda to harmonize copyright issues involving information technology among the Member States.[14] The issue of database protection did not draw significant attention until 1991, however, when the Supreme Court of Netherlands (Hoge Raad) held, for the first time, that copyright law was an inappropriate "vehicle for database protection,"[15] and the U.S. Supreme Court in *Feist* extended copyright protection only to the original selection, arrangement, and coordination of a compilation of data, but not to the factual contents therein.[16]

These developments in Europe and the U.S. convinced the Commission that copyright law was not the best regime for database protection.[17] Consequently, the Commission presented an initial proposal for database protection to the Council in May 1992[18] and an amended proposal in Oc-

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13. Furthermore, a recent empirical study indicates that the E.C. Directive has yet to fully realize the other goal of strong database protection, which is to promote the growth of European database industry. *See* Maurer et al., *supra* note 9, at 789 (showing a one-time only growth spurt of new companies entering database markets in France, United Kingdom, and Germany after their respective national implementations of the E.C. Directive 1998).

14. P. Bernt Hugenholtz, *Implementing the European Database Directive, in* INTELLECTUAL PROPERTY AND INFORMATION LAW, ESSAYS IN HONOUR OF HERMAN COHEN JEHORAM 183-200 (Jan J.C. Kabel & Gerard J.H.M. Mom eds., 1998), *available at* http://www.ivir.nl/publications/hugenholtz/PBH-HCJ-LIB.doc (discussing the European Commission's *Green Paper on Copyright and the Challenge of Technology*) (on file with author).

15. *Id.* (discussing the Dutch Supreme Court's decision that "a collection of words will only be protected by copyright if it results from a selection process expressing the author's personal views").

16. *Id. Feist Publ'ns, Inc. v. Rural Tel. Serv. Co.*, 499 U.S. 340 (1991), is the landmark decision that explicitly rejected the "sweat of the brow" doctrine in copyright protection of databases and held that the "*sine qua non* of copyright is originality."

17. *E.g.*, Hugenholtz, *supra* note 14, at 3. Although some databases could qualify for copyright protection, traditional copyright did not extend protection to "the essence of the database," that is, the compiled, disparate data. *Id.* The level of traditional copyright protection of databases varied among the Member States. *See, e.g., Proposal Would Harmonize Laws, Extend Safeguards to Data Bases*, 3 EUROWATCH (Mar. 6, 1992) [hereinafter *Proposal Would Harmonize*] (describing that sui generis database protection is based on the Scandinavian catalogue rule).

18. Commission Proposal for a Council Directive on the Legal Protection of Databases, 1992 O.J. (C 156) 4.

tober 1993.[19] After more than two years of inactivity, the Council suddenly adopted a Common Position[20] which was quite distinct from the amended proposal—one of the main distinctions was the absence of compulsory licensing requirement in the Common Position.[21] The Parliament eventually accepted the Common Position as the final version of the Directive in December 1995 and enacted it in March 1996.[22]

Scholars have observed that the Commission based its initial proposal on an unfair competition model, in an attempt to safeguard "the investment of considerable human, technical and financial resources" in the making of databases from the possibility that they "can be copied or accessed at a fraction of the cost needed to design them independently."[23] The unfair competition principle is similar to the traditional common law notion of misappropriation.[24] However, the Council likely did not adopt the unfair competition approach in the end for the following three reasons.[25] An unfair competition regime does not create "transferable economic rights at the outset,"[26] but only provides remedies after an unfair act, (e.g., misappropriation), occurs. Further, an unfair competition principle applies only to questionable acts by a competing party, and not to all potential users.[27] Finally, existing unfair competition laws are not uniform among the E.U. Member States.[28] Instead, the final version of the E.C. Directive creates a sui generis right in databases made by "substantial investment" to prevent unauthorized "extraction and/or re-utilization" of the

19. Amended Commission Proposal for a Council Directive on the Legal Protection of Databases, 1993 O.J. (C 308) 1.

20. *See* Hugenholtz, *supra* note 14, at 3.

21. *See infra* note 29.

22. *See* Common Position Adopted by the Council on the Legal Protection of Databases, 1995 O.J. (C 288) 14 [hereinafter Common Position]; E.C. Directive, *supra* note 2.

23. Reichman & Samuelson, *supra* note 1, at 74-80. *See also Fighting International Piracy of Data Bases: European Commission Proposes to Harmonise Legal Protection in the Community,* RAPID, at 8 (Jan. 29, 1992) (describing the proposal as including some unfair competition principles).

24. Reichman & Samuelson, *supra* note 1, at 81-82 (describing Commission's initial approach as "modeled on existing laws that protected trade secrets or confidential information [to] repress conduct amounting to the 'misappropriation' of an electronic database provider's investment without imposing either legal barriers to entry or the social costs of actual or legal secrecy"). *Id.* at 139-45 (discussing U.S. case law that extended the misappropriation doctrine to offer legal protection of a producer's investment in information goods and identifying a multiplicity of factors that courts should adopt to defend the incentive to invest).

25. Maurer, *supra* note 6, at 28.

26. *Id.*

27. *Id.*

28. *Id.*

compiled data.[29] This database right affords eligible database makers strong, property-like right protection for their contents, which would not otherwise be protected under traditional copyright law in some E.U. Member States.[30] This modification has led some scholars to believe that the legislative history of the E.C. Directive "illustrate[s] how a modest, pro-competitive initial proposal for sui generis protection has been transformed into a virtually absolute monopoly by the backdoor lobbying efforts of publishers and by the coordinated efforts of U.S. and E.U. officials to propagate a protectionist strategy for the global information infrastructure."[31] As discussed below, this modification would also lead to dissimilar protection of databases among Member States that do not have uniform national competition rules.[32]

B. The Directive: Key Provisions/Definitions of Sui Generis Right

The E.C. Directive protects an eligible database from unauthorized extraction and re-utilization of its data through its sui generis right provisions.[33] Chapter I of the Directive sets forth the scope of database protection and defines "database" as "a collection of independent works, data or other materials arranged in a systematic or methodical way and individu-

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29. *See* E.C. Directive, *supra* note 2. The Common Position adopted in July 1995 concluded that "a proper balance between the rights of the maker of a database and the rights of the users no longer hinged on the possibility of obtaining such licences and [the Council] has deleted the provisions allowing for it." Common Position, *supra* note 22 (Recital No. 15 "Non-voluntary licences," in the Statement of the Council's Reasons). In the final version, Recital 47 of the preamble provides that "protection by the sui generis right must not be afforded in such a way as to facilitate abuses of a dominant position. . .[and] the provisions of this Directive are without prejudice to the application of Community or national rules of competition." Given the existing discrepancy between national competition rules adopted by various Member States, it is interesting to see how the Directive would harmonize database protection to different database makers of dominant positions in different countries. *See infra* notes 924-96 and accompanying text.

30. Those E.U. Member States that did not recognize the Scandinavian catalog rule were unlikely to protect factual contents of a database under their copyright law prior to national implementation of the E.C. Directive. *See Proposal Would Harmonize, supra* note 17. On the other hand, for the five Nordic countries (Denmark, Finland, Iceland, Norway, and Sweden) that had "expressly protect[ed] non-original compilations of data . . . the Database Directive is of only limited consequence." Hugenholtz, *supra* note 14, at 15.

31. Reichman & Samuelson, *supra* note 1, at 75.

32. *See supra* note 29; *infra* notes 88-100 and accompanying text.

33. *See* E.C. Directive, *supra* note 2. As noted above, this paper will focus on the sui generis right provisions. Chapter II, Articles 3-6, unifying copyright protection of databases constituting "the author's own intellectual creation" "by reason of the selection or arrangement of their contents," is therefore not discussed here.

ally accessible by electronic or other means."[34] Chapter III grants a sui generis right to a database maker who has demonstrated "qualitatively and/or quantitatively a substantial investment in either the obtaining, verification or presentation of the contents" of the database.[35] The enforcement of this right prevents "extraction and/or re-utilization . . . of the contents of that database,"[36] the substantiality of which a court evaluates "qualitatively and/or quantitatively."[37] The Directive further defines "extraction" as "the permanent or temporary transfer of all or a substantial part of the contents of a database to another medium by any means or in any form" and "re-utilization" as "any form of making available to the public all or a substantial part of the contents of a database by the distribution of copies, by renting, by on-line or other forms of transmission."[38] The sui generis right in eligible databases also serves to prevent "repeated and systematic extraction and/or re-utilization of insubstantial parts of the contents . . . which unreasonably prejudice the legitimate interests of the maker of the database."[39]

The E.C. Directive allows certain exceptions to the sui generis right, an example of which is extraction, but not re-utilization, for educational or scientific research needs "justified by the noncommercial purpose."[40] Further, this sui generis protection lasts for fifteen years, although any substantial modification of a database leads to a renewal of the term of protection.[41]

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34. *Id.* at art. 1. The E.C. Directive excludes from its legal protection "computer programs used in the making or operation of databases accessible by electronic means." *Id.* at para. 3.

35. *Id.* at art. 7.

36. *Id.*

37. *Id.*

38. *Id.*

39. *Id.* The E.C. Directive allows "repeated and systematic extraction and/or re-utilization of insubstantial parts of the contents" which does not "conflict with a normal exploitation of that database." *Id.*

40. *Id.* at art. 9.

41. *Id.* at art. 10. "Any substantial chance, evaluated qualitatively or quantitatively, to the contents of a database. . .which would result in the database being considered to be a substantial new investment, evaluated qualitatively or quantitatively, shall qualify the database resulting from that investment for its own term of protection." *Id.* This prolonged protection of dynamic databases that are continually modified has led many commentators to believe that the right could become perpetual. *See, e.g.*, Hugenholtz, *supra* note 7 (observing that "a regularly updated database is awarded semi-permanent protection" and "a mere 'substantial verification of the contents of the database' would be enough to trigger a new term of protection").

C. The Courts' Responses

Since its enactment, courts in various Member States have handed down more than two dozen decisions under the E.C. Directive.[42] Most of the cases concerned database makers in France, Germany, and The Netherlands,[43] while two involved United Kingdom databases.[44] Commentators also noted that more than half of these cases were about "synthetic data," which, unlike discovered, existing facts, could not have been independently generated by those other than the database maker.[45] Simply put, only the database creators could have generated the contents of these databases.[46]

1. Database Protection

The E.C. Directive provides a two-pronged test to determine whether a database is eligible for protection.[47] First, a database can qualify for protection if it contains information arranged in a qualifying way, e.g., a systematic collection of individually accessible data.[48] Second, the database must be created through a substantial investment.[49]

The first part of the qualifying test is "extremely elastic."[50] For example, factual data—including information about the times and places of

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42. *See* Maurer, *supra* note 6; Hugenholtz, *supra* note 7.

43. Maurer, *supra* note 6; Hugenholtz, *supra* note 7.

44. Hugenholtz, *supra* note 7. One of the two British cases is of particular interest because the British appellate court wanted to refer the case to the European Court of Justice to resolve the discrepancy in different courts' interpretation of the E.C. Directive. *See infra* note 75 and accompanying text.

45. Maurer et al., *supra* note 9.

46. For example, only a telephone company could create a directory of its subscribers in the first place. Likewise, only the organizer of horseracing could access the information regarding event schedules and participants in the first place. *See infra* notes 51-52.

47. *See* E.C. Directive, *supra* note 2, at arts. 1 & 7.

48. *See* E.C. Directive, *supra* note 2. Article 1 loosely defines "database" as "a collection of independent works, data or other materials arranged in a systematic or methodical way and individually accessible by electronic or other means." *Id.* at art. 1. Article 7 grants a sui generis right against "extraction and/or re-utilization" of a database's contents compiled by "substantial investment." *Id.* at art. 7.

49. *Id.* at art. 7.

50. Maurer, *supra* note 6, at 32 ("According to one British judge, the concept of a 'database . . . has a very wide meaning covering virtually all collections of data in searchable form.' In practice, courts have been liberal. According to one German case, even a collection of hyperlinks qualifies as a database.") (citing British Horseracing Bd. Ltd. v. William Hill Org. Ltd., [2001] R.P.C. 31, [2001] 2 C.M.L.R. 12 (Eng. Ch. Pat. Ct.), *available at* 2001 WL 98034, at ¶ 30.

horse races[51] and telephone directories[52]—can qualify as core information in protectible databases. Further, even information in the public domain such as laws and regulations can become contents of a protectible database.[53]

Courts have formulated different factors in determining what constitutes a substantial investment in the creation of a database, and thus qualifies for the sui generis protection under the E.C. Directive.[54] Under one relatively consistent test that may represent a quantitative evaluation dictated by the E.C. Directive, the court looks at the investment itself in monetary terms.[55] For example, the costs of collecting, verifying and maintaining the data in an electronic telephone directory can qualify as "substantial investment,"[56] if the court finds them substantial. Similarly, the costs or investment in hiring someone else to create the database can amount to "substantial investment."[57] Some courts seem to base their quantitative evaluation on the amount of labor involved in collecting and compiling the data.[58] For example, a British trial court held that controlling, verifying and maintaining horseracing information—a four to five-month annual process of compiling, granting and publishing the fixture list for horse racing and maintaining and constantly updating a computer database—was a substantial investment.[59] Moreover, a German court held that

51. *British Horseracing Bd. Ltd.*, [2001] R.P.C. 31.

52. *See, e.g.*, France Télécom SA v. MA Editions Sàrl and Others, [2001] E.C.C. 4, (Trib. Comm. Paris 1999), *available at* 1999 WL 33231726.

53. Vermande/Bojkovski, Pres. Rb., Den Haag , 20 maart 1998, *translated at* http://www.ivir.nl/rechtspraak/vermande-en.html (finding that a commercially published CD-ROM containing laws and regulations can be protected under the E.C. Directive).

54. Maurer, *supra* note 6, at 32-33 (discussing three different tests that courts have used in determining substantiality).

55. *See* E.C. Directive, *supra* note 2, at art. 7.

56. *See France Télécom*, [2001] E.C.C. 4, at ¶ 6 (finding the plaintiff's annual costs in collecting, managing, checking, and maintaining the telephone directory made the directory protectible under the E.C. Directive).

57. At least one commentator noted this "safe harbor" in that databases created by outside employees or contractors could qualify for substantial investment. Maurer, *supra* note 6, at 32 (noting that "[a] Belgian court found that an umbrella organization of self-help groups had made a 'substantial investment' when it hired an outside contractor to prepare a directory"). Two German courts have held that trade fairs that hire professional catalog compilers also make 'substantial investments.'" These cases also raised the issue as to who can qualify as the database maker and thus receive protection under the E.C. Directive. *Id.*

58. *See generally* Hugenholtz, *supra* note 7.

59. British Horseracing Bd. Ltd. v. William Hill Org. Ltd., [2001] R.P.C. 31, [2001] 2 C.M.L.R. 12 (Eng. Ch. Pat. Ct.), *available at* 2001 WL 98034, at ¶ 5. This court also noted that the costs and efforts in creating the actual data, e.g., scheduling the races, did

converting classified advertisements from a newspaper into digital form and the amount of labor in selecting, updating and verifying the ads qualified for substantial investment.[60]

A second judicial test measures substantiality of investment in making a database by inferring "investment by examining the face of the database."[61] Such an evaluation can be either quantitative or qualitative, and, therefore, this test appears to be almost as elastic as the test for qualifying ways of arranging data.[62] For example, a German court held that a catalogue of 251 alphabetically ordered links to sites on parenting-related subjects constituted a protectible database, finding substantial investment in "compiling, *researching,* and up-dating" the list.[63] An "effort [to put] [sic] 'frames' around another provider's Web pages was not 'substantial,'"[64] although a similar web site containing a collection of web pages was held to be a database within the meaning of the E.C. Directive. To the German court, designing a way to display data on a web site is relevant to determining the substantiality of efforts in making the web site, a potentially protectible collection of data under the Directive.[65] The absolute amount of data also matters to another German court: "a single promoter's concert schedule was [therefore] 'insubstantial,' although the combined schedule of 400 such promoters would not be."[66] Finally, merely reproducing data weighs against a finding of "substantial investment."[67] A French court found no substantial investment in making a database of advertised calls for tender in the field of public procurement, because such a maker merely reproduced calls received from the advertisers.[68]

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not "count towards the relevant investment to which database right is directed. On the other hand, the efforts which go into gathering all the data together . . . is relevant." *Id.* at ¶ 34.

60. Hugenholtz, *supra* note 7 (discussing the case of *Berlin Online*, decided by the Landgericht Berlin, Oct. 8, 1998).

61. Maurer, *supra* note 6. For this test, a court makes an evaluation of the investment based on the characteristics of the database at issue, the nature and amount of data compiled, and so on.

62. *See supra* notes 47-52 and accompanying text.

63. Hugenholtz, *supra* note 7 (discussing the case of *Kidnet/Babynet*, decided by the Landgericht Köln, Aug. 25, 1999) (emphasis added).

64. Maurer, *supra* note 6, at 32.

65. Hugenholtz, *supra* note 7 (discussing the case of *baumarkt.de*, decided by the Oberlandesgericht (Court of Appeal) Düsseldorf, June 29, 1999).

66. Maurer, *supra* note 6, at 32.

67. Hugenholtz, *supra* note 7 (discussing the case of *Groupe Moniteur v. Observatoire des Marchés Publics*, decided by the Paris Court of Appeal, June 18, 1999).

68. *Id.*

Despite the broad scope of protection of databases under the E.C. Directive, several Dutch courts have tried to limit the database right by creating a "spin-off" doctrine when finding against substantial investment in creating a database.[69] For example, because the headlines were a spin-off of newspaper publishing, a court found no substantial investment in creating a web site of automatic hyperlinks (in the form of headlines) to newspaper articles.[70] Another appellate court, also applying the spin-off doctrine, held that a collection of real estate objects on a web site did not qualify for the sui generis database right, because individual real estate brokers in the plaintiff organization had designed it for use in an internal network.[71] Further, broadcasters' program listings were also the products of a spin-off activity, reflecting no substantial investment in their making.[72] However, in other cases, several Dutch courts have rejected the defendants' argument that the database in question was a mere spin-off of plaintiffs' core activities.[73] For example, two different courts held that telephone subscriber listings and online telephone directories were not mere spin-off products of the plaintiff company's core activity of providing telephone services.[74]

In sum, the E.C. Directive does not provide a clear guideline for determining whether a database qualifies for the sui generis right. The ambiguity inherent in the word "substantial" makes it difficult for courts in different Member States to interpret the Directive in a consistent manner. A British appellate court, deciding to refer its case to the European Court of Justice ("ECJ") said, "we cannot say that we can resolve the [Directive's interpretation] issues with complete confidence nor that there is no scope for any reasonable doubt, still less that the matter is equally obvious to the courts of other Member States."[75] The ECJ will likely be called upon to formulate a consistent test for: (1) interpreting the Directive; (2) deter-

69. *See* Maurer, *supra* note 6, at 33; Hugenholtz, *supra* note 7.

70. Dagbladen/Eureka Internetdiensten, Rb., Rotterdam, 22 augustus 2000, *translated at* http://www.ivir.nl/rechtspraak/kranten.com-english.html.

71. Hugenholtz, *supra* note 7 (discussing the case of *NVM v. De Telegraaf*, decided by the Court of Appeal at The Hague, Dec. 21, 2000).

72. Hugenholtz, *supra* note 7 (discussing the case of *NOS v. De Telgraaf*, decided by the Court of Appeal at The Hague, Jan. 30, 2001).

73. *See* Maurer, *supra* note 6, at 33; Hugenholtz, *supra* note 7.

74. Hugenholtz, *supra* note 7 (discussing the case of *KPN v. Denda Int'l*, decided by the Court of Appeal at Arnhem, Apr. 15, 1997, and the case of *KPN v. XSO*, decided by the President District Court of the Hague, Jan. 14, 2000).

75. British Horseracing Bd. Ltd. v. William Hill Org. Ltd., [2001] EWCA CIV 1268, [2002] E.C.D.R. 4 (Eng. C.A. 2001), *available at* 2001 WL 825162, at ¶ 45 (July 31, 2001).

mining how much or what kind of time, money, efforts, etc., spent in making a database constitute "substantial investment;" and (3) determining whether any factors limiting the scope of the database right, e.g., the Dutch spin-off doctrine, are feasible.

2. *Prohibited Extraction and/or Re-utilization*

After determining whether a collection of data conforms to the E.C. Directive's definition of "database," and qualifies for the sui generis right based on substantial investment expended in making it, a court must then assesses whether another party infringed the database right.[76]

The Directive defines infringement of protectible databases as the unauthorized substantial "extraction" and/or "re-utilization," or the "repeated and systematic extraction" of insubstantial parts, "evaluated quantitatively and qualitatively."[77] However, courts have not established a definitive test for database infringement. A court may measure the substantiality of extraction and/or re-utilization by looking at the data's value to an infringer, and a few pieces of data of great value to an infringer would be "substantial."[78] According to a British trial court, to determine the substantiality of unauthorized extraction, the extracted data's value to an infringer must be appraised both quantitatively and qualitatively.[79] Courts may also look at the infringer's acts or the infringing activities from a database maker's perspective when making this determination. For example, a German court found substantial extraction because the alleged infringer copied 239 of the 251 links, including the same grammatical errors, in the catalogue of alphabetically ordered links to parenting-related subjects.[80] Therefore, either extracting and re-utilizing core information of great value to an infringer or verbatim copying a substantial part of content from a protectible database can amount to substantial extraction and/or re-utilization prohibited by the E.C. Directive.

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76. *See* E.C. Directive, *supra* note 2, at art. 7.

77. *Id.*

78. Hugenholtz, *supra* note 7 (discussing the case of *NVM v. De Telegraaf*, decided by the President District Court of the Hague (Sept. 12, 2000)). This case was reversed by the Court of Appeal The Hague, because the database did not meet the substantial investment test—the appellate court applied the spin-off doctrine. *Supra* note 71.

79. British Horseracing Bd. Ltd. v. William Hill Org. Ltd., [2001] R.P.C. 31, [2001] 2 C.M.L.R. 12 (Eng. Ch. Pat. Ct.), *available at* 2001 WL 98034, at ¶ 53 (finding that defendant's "relying on taking advantage of the completeness and accuracy of the information taken from the [plaintiff's database]" contributed to a finding of substantial extraction).

80. Hugenholtz, *supra* note 7 (discussing the case of *Kidnet/Babynet*, decided by the Landgericht Köln, Aug. 25, 1999).

Further, two German courts have held that "[t]he use of [a] search engine amounted to repeated and systematic extraction of insubstantial parts of the database that unreasonably damaged the lawful interests of the owner of the database right."[81] In both of these German cases, the search engine systematically bypassed advertisements on the originating web sites and sent extracted information directly to end users and therefore affected the database owners' commercial interests.[82] Similarly, a Dutch court also found "a dedicated search engine" infringed an online telephone directory owner's database right, because it provided its users the extracted data without referring them to the original directory.[83]

In sum, the E.C. Directive does not provide definitive guidelines for determining what constitutes prohibited extraction and re-utilization. The courts have yet to reach a consensus on whether the substantiality of prohibited extraction and/or re-utilization depends on the objective amount of extracted contents or the subjective value of the extracted contents to an alleged infringer or both. As for "repeated and systematic extraction of insubstantial parts," the three decisions on search engines[84] are illustrative of potential judicial treatment, but cannot reflect whether the courts in different Member States would adopt a similar test.

3. *Effect of Competition Rules*

The E.C. Directive provides that, "in the interests of competition, protection by the sui generis right must not be afforded in such a way as to facilitate abuses of a dominant position."[85] As indicated by several cases discussed below, national courts of Member States are willing to apply the Community or national competition rules in deciding cases involving alleged database right infringement.[86] The famous "Magill" decision exem-

81. Hugenholtz, *supra* note 7 (discussing the case of *Berlin Online,* decided by the Landgericht Berlin, Oct. 8, 1998, and the case of *Süddeutsche Zeitung*, decided by the Landgericht Köln, Dec. 2, 1998).

82. *Id.*

83. Hugenholtz, *supra* note 7 (discussing the case of *KPN v. XSO*, decided by the President District Court of the Hague, Jan. 14, 2000). It is not clearly from the source whether the court held the search engine's extraction to be a "repeated and systematic extraction and re-utilization of insubstantial parts."

84. *See supra* notes 81-83 and accompanying text

85. E.C. Directive, *supra* note 2, at pmbl., recital 47.

86. *See* Hugenholtz, *supra* note 7 (discussing several cases where courts applied both competition rules and the sui generis database right and, in particular, the case of *De Telegraaf v. NOS and HMG*, decided by the Dutch Competition Authority which is "[i]nspired by the Magill decision" by the ECJ).

plifies the Community competition rule that prohibits abuse of a dominant position.[87]

Courts in different Member States have attempted to apply the E.C. Directive in conjunction with the Community or their respective national competition rules.[88] At least three Dutch courts found for the alleged infringers, because the database owners, while *not* eligible for the sui generis right for lack of substantial investment in creating the databases in question, abused their dominant positions by refusing to license under reasonable terms.[89] In contrast, a French court held for the plaintiff under both the E.C. Directive and the competition rule, because the plaintiff's electronic telephone subscriber directory qualified for the database right *and* because the plaintiff was willing to license the information for a reasonable fee, and, therefore, did not display anti-competitive behavior.[90]

Other courts have also applied the competition rule by focusing on the alleged infringers' conducts, regardless of whether the databases at issue qualify for protection under the E.C. Directive. For example, the German Supreme Court upheld a plaintiff's database right in its subscriber telephone directories, and additionally considered the defendant's unfair competition behavior of scanning and subsequently publishing the plaintiff's data on a CD-ROM.[91] Further, a French court, without any explicit determination of a database right, found no copyright infringement in the defendant's copying of the contents of agreements in the plaintiff's collec-

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87. In this case, the ECJ upheld the Commission's finding that three broadcasting organizations abused their dominant position by refusing to grant licenses for the publication of their weekly program listings in Magill's TV Guide. Case C-241/91, Radio Telefis Eireann v. Comm'n of the European Communities, 1995 E.C.R. I-743. The Commission ordered the broadcasting companies to "supply [sic] third parties on request and on a non-discriminatory basis with their. . .program listings and permit [sic] reproduction of those listings by such parties. . . .[Further] if the three organizations chose to grant reproduction licences, any royalties requested should be reasonable." *Id.* at ¶ 12. It appears that the European competition rule applied in this case is different from the traditional common law unfair competition principles in the United States. While the former considers the plaintiffs' abuse of dominant position, the latter focuses on whether defendants' conduct amounts to misappropriation. *See* Reichman & Samuelson, *supra* 1, at 139-45.

88. *See* Hugenholtz, *supra* note 7.

89. *Id.* (discussing the case of *KPN v. Denda Int'l*, decided by the Court of Appeal at Arnhem, Apr. 15, 1997, the case of *De Telegraaf v. NOS and HMG,* Dutch Competition Authority, Sept. 10, 1998, and the case of *NOS v. De Telegraaf*, decided by the Court of Appeals of The Hague, Jan. 30, 2001) (emphasis added).

90. *See* France Télécom SA v. MA Editions Sàrl and Others, [2001] E.C.C. 4, (Trib. Comm. Paris 1999), *available at* 1999 WL 33231726 (emphasis added).

91. Hugenholtz, *supra* note 7 (discussing the case of *Tele-Info-CD*, decided by the Bundesgerichtshof (Federal Supreme Court), May 6, 1999).

tion of over 400 collective bargaining agreements.[92] But the court held that the defendant's parasitic behavior amounted to unfair competition.[93] Therefore, unfair competition principles can strengthen database protection, even in the absence of a clear database right.

Although the cases discussed above indicate that national courts in the Community have attempted to reconcile the E.C. Directive and competition rules, the courts have yet to decide upon a potential situation where a database owner, eligible for the sui generis right, abuses its dominant position. For example, whose side would the French court take, had France Télécom displayed anti-competitive behavior by refusing to license under a reasonable fee?[94] It remains uncertain whether competition rules would undercut database right, as the E.C. Directive permits.[95] Perhaps the Office of Fair Trading in the United Kingdom is the first to address such uncertainty: preliminary inquiries, following a complaint by William Hill Organization Ltd., indicated that the British Horseracing Board might have abused its dominant position by setting excessive and discriminatory pricing and restrictive licensing terms.[96] So far, unfair competition principles have strengthened database protection. But applying national unfair competition rules that are not uniform throughout the Community in the database context may defeat an important goal that the E.C. Directive intended to achieve—a Community-wide harmonized level of database protection.

4. *Current Problems Facing Courts*

The decisions discussed above reflect the difficulties that courts are facing in interpreting the E.C. Directive. They further highlight the uncertainties that the E.U. will face in attempting to harmonize the level of database protection among its Member States through the new legal regime of database protection.

First, the E.C. Directive does not offer courts much help in defining the key concepts of the sui generis database right. Because the E.C. Directive defines the database concept and the scope of protection so broadly, courts have not been able to apply consistent tests.[97] As noted by the Brit-

92. *Id.* (discussing the case of *Dictionnaire Permanent des Conventions Collectives*, decided by the Tribunaux de grande instance at Lyon, Dec. 28, 1998).

93. *Id.*

94. This would not have been a problem, had the Commission kept the compulsory licensing requirement as initially proposed. *See supra* note 29.

95. E.C. Directive, *supra* note 2, at pmbl., recital 47.

96. *OFT Investigates British Horseracing Board*, Office of Fair Trading, Press Release PN26/01, *at* http://www.oft.gov.uk/html/research/press-no/pn26-01.htm (June 12, 2001) [hereinafter *OFT Investigates BHB*].

97. *See supra* notes 48-83 and accompanying text.

ish appellate court,[98] the ECJ would have to resolve these uncertainties, if and when cases reach this highest-level court.

Second, the inconsistency displayed by the courts' interpretation of the E.C. Directive suggests that this new law has not reached its first goal of harmonizing database protection in Europe. For example, a spin-off database, not granted protection by some Dutch courts, may qualify for the sui generis protection in the United Kingdom or Germany.

Third, the courts have yet to reconcile the potential tension between the competition rules and the new database right.[99] Whether the Commission will reconsider a compulsory license requirement in amending the E.C. Directive to avoid such a situation remains an open question. Applying national unfair competition rules would further undermine the effort to harmonize the level of database protection in different Member States.[100]

Finally, a recent empirical study has also indicated that the E.C. Directive is yet to reach its goal of promoting and sustaining the growth of the database industry in the Community.[101] Despite that only database makers in the E.U. qualify for the strong property-like right in database contents, the E.C. Directive has not generated enough incentive for U.S. database companies to move to Europe.[102] The E.C. Directive, therefore, has yet to reach its original goals of granting uniform protection of databases among the Member States and of providing sufficient, sustained incentives to invest in the database industry in Europe.

II. DEVELOPMENTS IN THE UNITED STATES

Proponents for additional legal database protection in the U.S. have been lobbying the Congress since *Feist*.[103] It was not until the adoption of

98. *See* British Horseracing Bd. Ltd. v. William Hill Org. Ltd., [2001] EWCA CIV 1268, [2002] E.C.D.R. 4 (Eng. C.A. 2001), *available at* 2001 WL 825162, at ¶¶ 40-47 (CA) (July 31, 2001) (appeal taken from the High Court of Justice, Chancery Division, Patents Court).

99. *Supra* notes 94-96 and accompanying text.

100. *See supra* notes 91-93 and accompanying text.

101. Maurer et al., *supra* note 9.

102. Maurer, *supra* note 6, at 35-36 (discussing that three large biotechnology companies decided against moving to Europe because of the presence of adequate protection of their databases in the U.S., insufficient additional protection by the sui generis right, and other practical concerns). *Compare with* Jasper A. Bovenberg, *Should Companies Set up Databases in Europe?*, 18 NATURE BIOTECHNOLOGY 907 (2000) (discussing incentives to set up bioinformatics database in Europe and potential data access problems associated with highly protected databases).

103. *See* Maurer et al., *supra* note 9.

the E.C. Directive, however, that Congress started a serious discussion about database protection.[104]

This Part first addresses whether the E.C. Directive's reciprocity requirement will force the U.S. Congress to enact additional protection for databases. It then examines protection currently available in the U.S. for the database industry, both legal and technical, to illustrate whether additional legal protection is necessary. This Part further notes that any legislation modeled on the Directive may not survive the scrutiny under the U.S. Constitution. It finally concludes that certain legal regimes alternative to the sui generis database right might nonetheless be permissible in the U.S. from both constitutional and policy perspectives.

A. Database Right in the United States after the E.C. Directive

The E.C. Directive intends to influence worldwide database protection legislation via its reciprocity requirement denying protection to citizens of countries which do not enact database protection statutes granting similar levels of database protection.[105] This requirement may violate the World

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104. *Id.* In fact, heavy debates among congressional staff started in 2000 and the topic of database legislation will likely surface again in 2002. *See* Robert MacMillan, *Congress Likely To Defer Database Protection to 2002,* NEWSBYTES, *at* http://www.newsbytes.com/cgi-bin/udt/im. . .ble?client.id=newsbytes&story.id=170742 (Oct. 2, 2001) (discussing the status of the House Energy & Commerce Committee's version, i.e., Consumer and Investor Access to Information Act, H.R. 1858, 106th Cong. (1999) and the House Judiciary Committee's version, i.e., Collections of Information Antipiracy Act, H.R. 354, 106th Cong. (1999), of database protection in light of the September 11, 2001, terrorist attacks). *See also Database Proposals and Legislation*, Association of Research Libraries, *at* http://www.arl.org/info/frn/copy/database.html (last modified Nov. 16, 2000) (providing a list of hyperlinks to letters, testimonies, statements, and legislation on database protection).

105. Maurer, *supra* note 6, at 29:

> It has been objected that the net effect of the [Directive] seems to amount to a rather cynical attempt to boost the European information technology market at the expense of the rest of the world. We would not quarrel with such an apparently harsh judgment. We are dealing with the realms of Big Money and High Politics. The Commission, having cottoned on to the economic importance of databases, was not about to let the opportunity pass of digging another section of the trench around Fortress Europe and labeling it database right.

(quoting CHRISTOPHER REES, DATABASE LAW 64).

This reciprocity requirement may find its precedent in the Semiconductor Chip Protection Act enacted in 1984 in the United States. Leon Radomsky, *Sixteen Years After the Passage of the U.S. Semiconductor Chip Protection Act: Is International Protection Working?*, 15 BERKELEY TECH. L. J. 1049, 1063-65 (2000) (commenting that the reciprocity requirement in the Semiconductor Chip Protection Act ("SCPA") was to induce similar legislation in other countries). *Cf. Samuelson letter, supra* note 12 (commenting

Trade Organization ("WTO") rules.[106] Nevertheless, the Directive has already revived discussions and legislative attempts on database protection in the U.S.[107]

It is not clear if the E.C. Directive's reciprocity requirement would *compel* the U.S. to create a similar legal regime for database protection. To address this question, one may first ask whether the current situation in the Community, i.e., the strong property right in database contents compiled in the Community by citizens or residents of the Member States of the Community, renders U.S. database companies, which are unprotected by a property right in database contents, vulnerable to their European competitors. Thus far, the answer appears to be no. The U.S. database industry is and will likely remain far more advanced than the European counterparts,[108] even in the absence of a formal database right. Even if the need to protect the U.S. database industry did justify a new legal regime for database protection, one must still ask whether the U.S. should or could follow the model set forth in the E.C. Directive. A sui generis, property right in database contents would directly contradict the current U.S. law and might violate the U.S. Constitution as well.[109]

Commentators generally agree that some form of database protection is necessary to promote the growth of the database industry. However, they disagree on what type of protection is appropriate and constitutionally permissible in the U.S. The remainder of this Note will argue that a model based on unfair competition principles supplemented with liability rules, in combination with the ever-improving technological protection meas-

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that the U.S. has become an advocate for "international treatment," i.e., without national protectionism, because of the bad experience with the SCPA).

106. Webster, *supra* note 8. Article III of the General Agreements on Tariffs and Trade of 1947 prohibits "national treatment," i.e., laws, regulations and requirements that would afford protection of domestic production of "like products." General Agreement on Tariffs and Trade, Oct. 30, 1947, art. III, 61 Stat. A-11, T.I.A.S. 1700, 55 U.N.T.S. 194, 204-06 [hereinafter GATT]. But the reciprocity requirement in the E.C. Directive offers more protection to European database makers than it would do to database makers in other WTO member countries that do not enact sui generis database right.

107. *See* Maurer et al., *supra* note 9.

108. *See* Daniel R. Valente, *Feist Overruled? Database Protection in the Next Century*, 17 THE COMPUTER LAWYER 20, 20 (2000) (quoting Mortimer B. Zuckerman, *The Time of Our Lives*, 127 U.S. NEWS & WORLD REP. 68, 70 (1999), that 31 out of 48 information technology companies with "sustainable competitive advantages" are in the United States). *See also Legal Protection Now Available to Databases, at* http://www.databasedata.org/hr1858/legalprt/legalprt.html (last visited Feb. 12, 2002) (showing statistical data that demonstrates a "phenomenal rate" of growth of the database industry since 1991) [hereinafter *Legal Protection*].

109. *See infra* notes 131-36 and accompanying text.

ures, will achieve the goals of fostering the growth of the database industry while leaving sufficient free space for the education and scientific communities to access and exchange data.

B. The U.S. Database Industry Enjoys Adequate Protection

Proponents of a database right in the U.S. perceive but cannot prove an actual threat to the U.S. database industry by its European counterparts who enjoy a strong sui generis right in their database contents. As discussed below, however, current legal regimes have yet to hinder the growth of the U.S. database industry.[110] In addition, the rapid, pioneering technological developments have put the U.S. database industry in a much more advantageous position than its European competitors.[111]

Current U.S. law does offer some database protection.[112] Although limiting the copyright protection of data, *Feist* would nonetheless grant a database copyright protection if it displayed "a modicum of originality" in the "selection, coordination, or arrangement" of its contents.[113] Indeed, several cases following *Feist* granted copyright protection to databases, including yellow pages of a telephone directory with categorized business listings,[114] a compilation of collectible coin prices listed in the Coin Dealer Newsletter,[115] and a collection of state trademark data organized under

110. *See infra* notes 113-126 and accompanying text.

111. *See infra* notes 127-130 and accompanying text.

112. *See, e.g., Legal Protection, supra* note 108; Paul T. Sheils & Robert Penchina, *What's All the Fuss About Feist? The Sky Is not Falling on the Intellectual Property Rights of Online Database Proprietors,* 17 U. DAYTON L. REV. 563, 564 (1992) (arguing that "properly drafted license agreements for online database services provide proprietors with enforceable remedies against unauthorized copying of database contents, and that causes of action sounding in misappropriation and unfair competition will continue to be effective weapons against 'information aftermarket' speculators"); Amy C. Sullivan, *When the Creative is the Enemy of the True: Database Protection in the U.S. and Abroad,* 29 AIPLA Q.J. 317, 346-52 (2001).

113. Feist Publ'ns, Inc. v. Rural Tel. Serv. Co., 499 U.S. 340 (1991).

114. See Key Publ'ns, Inc. v. Chinatown Today Publ'g Enters., Inc., 945 F.2d 509 (2d Cir. 1991). The Second Circuit, while recognizing "'the copyright in a factual compilation is thin,' [it is not] anorexic." *Id.* at 514 (quoting *Feist Publ'ns*, 499 U.S. at 349.)

115. *See* CDN, Inc. v. Kapes, 197 F.3d 1256 (9th Cir. 1999). Proponents for strong database protection usually cite *Warren Publ'g Inc. v. Microdos Data Corp.,* 115 F.3d 1509 (11th Cir. 1997), *cert. denied,* 522 U.S. 963 (1997), where the court denied copyright protection of listings of cable service providers. However, several commentators believe that the Eleventh Circuit erred in that case. *See, e.g.,* Band testimony, *supra* note 12.

different, searchable fields "such as name of the mark, date of first use, owner of the mark, or description of the goods."[116]

Further, state common law doctrines based on contract law, unfair competition law, and trespass can also protect a database from free-riding misuses, as long as a court finds no preemption of these state law actions by section 301 of the Copyright Act.[117] In *ProCD, Inc. v. Zeidenberg*, the Seventh Circuit upheld a shrinkwrap license agreement that would protect the plaintiff's CD-ROMs of telephone listings from being posted on the Internet.[118] Unfair competition law also prohibits free-riding misappropriation of certain factual data such as "hot news."[119] Finally, frequent accessing and copying auction items' information on eBay's web site by search robots or web crawlers may constitute trespass.[120]

Business method patent protection may afford databases additional protection, since many business method patents offer protection to a novel system of processing certain types of information.[121] For example, the United States Patent and Trademark Office recently granted patent protection to a system used to process adverse event information concerning

116. *See* Corsearch, Inc. v. Thomson & Thomson, 792 F. Supp. 305, 309 (S.D.N.Y. 1992).

117. *E.g.*, Sullivan, *supra* note 112.

118. *See* ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996). Some courts have agreed with the Seventh Circuit. *See, e.g.*, Lipscher v. LRP Publications, Inc., 266 F.3d 1305, 1318 (11th Cir. 2001) (agreeing with the Seventh Circuit that "claims involving two-party contracts are not preempted because contracts do not create exclusive rights.")

119. *See* Int'l News Serv. v. Associated Press, 248 U.S. 215, 242 (1918) (finding that "the [defendant's] entire system of appropriating complainant's news and transmitting it as a commercial product to defendant's clients and patrons amounts to a false representation"). *But see* NBA v. Motorola, Inc., 105 F.3d 841, 851 (2d Cir. 1997) (finding that "if . . . the work is unprotected by federal law because of lack of originality, then its use is neither unfair nor unjustified").

120. eBay, Inc., v. Bidder's Edge, Inc., 100 F. Supp. 2d 1058 (N.D. Cal. 2000).

121. *See, e.g.*, Peter R. Lando, *Business Method Patents: Update Post State Street*, 9 TEX. INTELL. PROP. L.J. 403, 416-422 (2001) (discussing several business method patents involved in recent patent infringement litigations, of which one "is directed to an information handling system including, e.g. a digital information storage, retrieval and display system" and another one's title is "Online Interactive System and Method for Providing Content and Advertising Information to a Targeted Set of Viewers"). This article also presented statistical data on recent patent applications in the area of communications and information processing technologies, e.g., 3068 applications for Class 707 (databases and word processors) and 2658 applications for Class 705 (business methods) in 1999. *Id.* at 411.

medical products.[122] Notably, the granted claims cover new products generated by processing proprietary data with the patented system.[123] Thus, patent protection is available for the use of a database comprising such proprietary information.[124] While the term of patent protection may be shorter than what the European sui generis right could potentially offer to an ever-changing database as a whole, the fifteen-year protection of contents afforded by the database right is comparable to a normal patent term.[125] The relatively short term of patent protection is nonetheless valuable, as it may serve as a "blocking time" during which a protected database maker can enjoy monopoly of the market and establish its trademark or brand name.[126]

The U.S. database industry has also enjoyed tremendous advantages over its European counterpart in terms of technological advancements.[127] The development of encryption technologies, for example, has provided electronic databases strong protection against unauthorized access.[128] Further, the anti-circumvention provision of the Digital Millennium Copyright Act prohibits acts intend to bypass technological protections such as encryption.[129] Finally, electronic "tattooing" which gives database contents an identity can serve to recognize infringing copying immediately.[130]

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122. U.S. Patent No. 6,219,674 (issued Apr. 17, 2001) (describing "systems and methods for creating and using product data to enhance safety of a medical or non-medical products").

123. *Id.* For example, claim 12, a dependent claim of claim 1, of U.S. Patent No, 6,219,674 is directed to a "proprietary product" created using the patented system comprising "at least one adverse event database for storing averse event data associated with a commercially available product."

124. *Id.* It is perhaps worth noting that patent protection, similar to copyright, does not extend to the contents in these databases. But contents, or data, protection is not what is at issue in the debates on database protection. The spotlight of these debates is how to balance database protection, and, therefore, provide incentives to invest in the database industry with the need for free exchange and access to data by scientific and educational communities. *Compare* Tyson & Sherry, *supra* note 10, *with* Reichman & Samuelson, *supra* note 1.

125. *Compare* E.C. Directive, *supra* note 2, at art. 10, *with* 35 U.S.C. § 154 (1994) (Post-GATT patent term is 17 years from the date of the patent issuance).

126. *See* Reichman & Samuelson, *supra* note 1; *Legal Protection, supra* note 108 (acknowledging that "trademark is a valuable form of protection" in certain markets).

127. *See* Valente, *supra* note 108, at 20.

128. *See Legal Protection, supra* note 108.

129. *Id.*

130. *EU's Adoption of Database Directive Raises Issue of Data Protection*, 8 EUROWATCH (Apr. 30, 1996).

C. Why the European Model May Not Work in the United States

Even if additional database protection is necessary in the U.S., the E.C. Directive may not be a good model. The sui generis right in a database may not survive judicial review under the U.S. Constitution. First, the scope of the protection afforded by the Directive, (i.e., substantial investment), reflects the "sweat of the brow" doctrine which was explicitly rejected by *Feist* as exceeding what is permissible under the U.S. Constitution.[131] According to *Feist*, this doctrine's "most glaring [flaw is] that it extended copyright right protection in a compilation beyond selection and arrangement—the compiler's original contributions—to the facts themselves."[132] *Feist* pointed out that the Intellectual Property Clause in the U.S. Constitution[133] mandates originality as a prerequisite for copyright protection and that Congress cannot create a property-like right in database to exceed the limit of or to bypass the Intellectual Property Clause.[134] Second, scholars have identified potential First Amendment issues.[135] If a property right stemming from factual information is vested in one group of people, Congress necessarily takes the right of freedom to access, use, or express such information from another group of people.[136]

D. Viable Solutions for the United States

There appears to be some consensus that databases need both technological and legal protection against free-riding, market-destructive acts.[137] However, the question remains as to which legal regime offers an appropriate level of database protection while surviving constitutional scrutiny in the U.S.[138] The House Judicial Committee and Commerce Committee each presented a bill for database protection, indicating many unresolved differences among congressional members and various lobbying organizations.[139] Scholars have proposed an additional approach based on unfair

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131. Feist Publ'ns, Inc. v. Rural Tel. Serv. Co., 499 U.S. 340, 353-60 (1991).

132. *Id.* at 353.

133. U.S. CONST., art. I, § 8, cl. 8.

134. *Feist Publ'ns,* 499 U.S. at 346.

135. *E.g.,* Yochai Benkler, *Constitutional Bounds of Database Protection: The Role of Judicial Review in the Creation and Definition of Private Rights in Information*, 15 BERKELEY TECH. L.J. 535, 552-57 (2000).

136. *Id.*

137. *Compare* Tyson & Sherry, *supra* note 10, *with* Reichman & Samuelson, *supra* note 1.

138. As noted in Benkler, *supra* note 135, at 588, if it provides content-based protection, a legal regime "must be subject to the strictest First Amendment scrutiny."

139. *See, e.g.,* Letter to all Members of the House of Representatives, Association of Research Libraries (Oct. 8, 1999), *at* http://www.arl.org/info/letters/abercrombie.html

competition principles, but also recognized the difficulties—case-by-case adjudication which creates inconsistency and enormous transactional costs—inherent in such an approach.[140]

Scholars have also proposed a more favorable approach based on a modified liability rule.[141] Combining "a blocking period" to prevent any form of market-destructive appropriation of the protected database contents with a subsequent "automatic license" mechanism may serve as the most balanced model.[142] A problem may nonetheless arise out of a compulsory licensing regime for database protection, because of the wide range, depth, and breadth of what can be defined as protectible data. Therefore, although compulsory licensing requirement succeeded in the music industry,[143] a baseline statutory rate for the automatic licensing mechanism would unlikely work for all types of databases.

Perhaps, instead of letting Congress set a statutory fee for the automatic licensing of databases, different sectors in the database industry can form "Collective Rights Organizations (CROs)"[144] and these CROs, with their expert knowledge and flexibility, can set and change the licensing terms with low transaction costs.[145] Although the modified liability approach is not premised on a property rule entitlement theory, the initial mechanism of "a blocking period" may achieve the same "benign purpose" as property rule entitlements.[146] Just as the initial high transaction

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(supporting H.R. 1858, the Consumer and Investor Access to Information Act of 1999, which "protects databases against commercial piracy while preserving the critically important role that information plays in the progress of science and education," and protesting against H.R. 354, the Collections of Information Antipiracy Act, which "provides overly broad protection for "collections of information" that would reduce the public's access to information and would impose unreasonable and costly burdens on scientific research, scholarship, and education").

140. *See* Tyson & Sherry, *supra* note 10; Reichman & Samuelson, *supra* note 1 (discussing how expensive and inconsistent an unfair competition regime may become due to the case-by-case adjudicating). *See also An Unfair Competition Model for Protecting Databases*, *in* PROCEEDINGS OF THE WORKSHOP ON PROMOTING ACCESS TO SCIENTIFIC AND TECHNICAL DATA FOR THE PUBLIC INTEREST: AN ASSESSMENT OF POLICY OPTIONS, 218-50 (Comm'n on Physical Sciences, Mathematics, and Applications ed., 1999), *available at* http://books.nap.edu/html/proceedings_sci_tech/ch11.html.

141. Reichman & Samuelson, *supra* note 1, at 145-51.

142. *Id.*

143. *See id.* at 148 (comparing the numbers of voluntary licenses with involuntary licenses for the recording of musical works under section 115 of the U.S. Copyright Act of 1976).

144. Robert P. Merges, *Contracting into Liability Rules: Intellectual Property Rights and Collective Rights Organizations*, 84 CAL. L. REV. 1293, 1296 (1996).

145. *See id.*

146. *Id.*

costs associated with property rule entitlements "lead individual [intellectual property right] holders to form CROs,"[147] the strong protection of databases during the "blocking period" may also lead to the formation of CROs in the database industry. The modified liability approach further balances judicial inquiries by focusing on the alleged infringer's behavior during the initial "blocking period" and shifting the focus on whether the database owners provide access to their contents under the automatic licensing terms.[148] Such a balanced approach, therefore, addresses what is at issue in the debates on database protection: to provide incentives for investment in the database industry by guarding against market-destructive, free-riding uses, while not to compromise the scientific and educational needs for free exchange and access to data.

III. CONCLUSION

Because the E.C. Directive fails to clearly define several key concepts in its sui generis protection provisions, courts in the Member States have not been able to interpret the database right consistently. Such a strong, property-like right in database contents has not led to persistent, robust growth of the European database industry either. The E.C. Directive, therefore, has yet to realize its goals of harmonizing database protection among the different Member States and advancing the growth of database industry in the Community.

Should the U.S. decide to enact database legislation, a property-like right in databases modeled after the E.C. Directive's sui generis provisions would be unlikely survive scrutiny under the U.S. Constitution. Such a sui generis right in database contents does not serve to advance science and technology, as the research and education communities thrive on freedom of accessing and exchanging data. Congress would have to evaluate any additional legal protection of databases guardedly, in order to strike a proper balance between the necessity to freely access information by the education and scientific research communities and the need to preserve incentives in investments to foster the growth of the database industry.

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147. *Id.*

148. This balance makes sense: an initial "blocking period" can foster the growth of smaller companies and encourage entry into the industry and a subsequent compulsory licensing requirement is necessary if the initial "blocking period" succeeds in bringing the company to a dominant position.

WTO PANEL REPORT ON SECTION 110(5) OF THE U.S. COPYRIGHT ACT

By Helen A. Christakos

A World Trade Organization ("WTO") panel regarding the validity of the exceptions clause to the United States Copyright Act,[1] found that section 110(5)(B) conflicted with both the Agreement on Trade Related Aspects of Intellectual Property Rights ("TRIPS")[2] and the Berne Convention for the Protection of Literary and Artistic Works ("Berne Convention").[3] Rather than appealing the decision or taking some other action, the United States agreed to amend section 110(5)(B) to comport with these international agreements.[4] This sequence of events raises interesting questions about whether the WTO panel correctly interpreted the TRIPS agreement and whether the United States responded correctly.

This Note will discuss the WTO decision and conclude that it interpreted the TRIPS agreement so narrowly that it created a standard that invalidates the laws of many countries. Further, it will be argued that the United States therefore should have appealed the WTO decision; if this appeal failed, the United States should have negotiated with other potential violators of the TRIPS agreement and Berne Convention in order to create a uniform amendment and preserve international consistency. The Note will conclude that the WTO decision and the subsequent reaction by the United States to amend section 110(5)(B) did not serve TRIPS' purpose or bolster the United States' ability to get other nations to comply with TRIPS. This is crucial given China's recent admittance to the WTO.[5] The United States should have considered these overriding objectives in making its decision.

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1. WTO Dispute Panel Report on Section 110(5) of the U.S. Copyright Act, WT/DS160/R § 7.1, at 69 (June 15, 2000), *at* http://www.wto.org/english/tratop_e/dispu_e/dispu_e.htm [hereinafter WTO Panel Report].

2. Agreement on Trade Related Aspects of Intellectual Property Rights, Apr. 15, 1994, 108 Stat. 4809, 33 I.L.M. 81 [hereinafter TRIPS agreement].

3. Berne Convention for the Protection of Literary and Artistic Works, Paris Act of July 24, 1971 (as amended on Sept. 28, 1979), arts. 11(1)(ii), 11bis(1)(ii), *at* http://www.wipo.int/treaties/ip/berne/ [hereinafter Berne Convention].

4. *U.S. Told to Alter its Music Law,* Bloomberg News, Jan. 16, 2001, *at* http://seattlep-I-nwsource.com/business/msic16.shtml

5. WTO Decision on the Accession of the People's Republic of China, WT/L/432, (Nov. 23, 2001), *at* http://www.wto.org/english/thewto_e/acc_e/completeacc_e.htm.

I. BACKGROUND

A. Berne Convention and TRIPS Agreement

1. Overview

The Berne Convention came into force on September 9, 1886, to protect copyright holders across national borders; since then, it has been revised approximately once every twenty years.[6] While member states can bring disputes before the International Court of Justice ("ICJ"), there is no formal process to enforce ICJ decisions. Although the Berne Convention still exists, most of its substantive provisions were incorporated into the TRIPS agreement in 1994.[7]

The General Agreement on Tariffs and Trade ("GATT")[8] was formed after the Second World War to prevent the exorbitant tariffs of the 1930s from occurring again. As a nonlegal entity, GATT had little power.[9] In an effort to strengthen it, its members formed the World Trade Organization.[10] The WTO is a legal entity whose members are required to ensure the conformity of their laws with international obligations.[11] TRIPS codified the rules of trade enforced by the WTO.

To ensure member states' compliance with WTO and TRIPS provisions, the WTO instituted the Dispute Settlement Understanding ("DSU").[12] Under the DSU, disputing states parties are required to attempt to negotiate a settlement.[13] If that fails, they are then required to submit

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6. 8 MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT, § 17.01[B][1], at 5-6 (2000).

7. H.R. REP. NO. 100-609, at 5 (1988).

8. General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A-3, 55 U.N.T.S. 187 (annexed to the Final Act Adopted at the Conclusion of the Second Session of the Preparatory Committee of the United Nations conference on Trade and Employment, as subsequently rectified, amended or modified). GATT was further modified and supplemented and was adopted as Annex 1A of the WTO Charter. 33 I.L.M. 1125, 1127 (1994).

9. Agreement Establishing the World Trade Organization, art. I, *reprinted in* General Agreement on Tariffs and Trade: Multilateral Trade Negotiations Final Act Embodying the Results of the Uruguay Round of Trade Negotiations, Apr, 15, 1994, 33 I.L.M. 1125, 1226-47 [hereinafter WTO Charter].

10. *See generally* WTO Charter, *supra,* note 9, at art. IX:3.

11. *Id.* art. XVI:4.

12. Understanding on Rules and Procedures Governing the Settlement of Disputes, Marrakesh, Apr. 15, 1994, Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, art. 22, 33 I.L.M. 1143 Annex 2, 1233 (1994), *available at* http://www.wto.org/english/docs_e/legal_e/final_e.htm [hereinafter DSU].

13. *Id.* art. 3.7.

the dispute to mediation with a WTO moderator.[14] Should this also fail, the Director General of the WTO, in consultation with the parties, establishes a panel to hear the dispute.[15] After reviewing oral arguments, the panel issues a report.[16] This decision is subject to appeal before the standing WTO appellate body.[17] If the appellate body finds the complaint valid, it instructs the offending state to cease violating TRIPS rules.[18] If the state does not comply, sanctions can be imposed.[19]

2. *United States Participation*

Until the United States joined the Berne Convention in 1989, United States copyright law developed independently of international law. "[C]hanges in American law and in Berne standards . . . narrowed the gap" between the two bodies of law, thereby making it possible for the United States to ratify the Convention.[20] The United States ratified the Berne Convention as non self-executing so it "is not directly enforceable in United States courts."[21] However, should United States law not comport with the Berne Convention, member states can bring suits before the International Court of Justice.

Once most substantive sections of the Berne Convention were subsumed into the TRIPS agreement, the United States ratified the TRIPS agreement in order to create a broader framework for regulating world trade.[22] This agreement was also signed as non self-executing and has no force in United States courts, but member states can bring claims against the United States before a WTO panel under the DSU.

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14. *Id.*
15. *Id.*
16. *Id.*
17. *Id.*
18. *Id.*
19. *Id.*
20. Senate Report on Berne Convention Implementation Act of 1988, S. REP. NO. 100-352, at 1-51 (1988) ("New technologies like satellites, photocopiers, computers, and video and audio recorders have 'internationalized' intellectual property to an unprecedented extent."); *see also* NIMMER, *supra* note 6, § 17.01[C][1][b], at 15.
21. Senate Report on Berne Convention Implementation Act of 1988, *supra* note 20, at 9 ("Rights and responsibilities of authors, copyright owners, users of copyrighted materials, and other parties must be resolved under appropriate domestic law not under Berne itself.").
22. NIMMER, *supra* note 6, § 17.01[C][3], at 18.

B. Specific Provisions of the TRIPS Agreement Related to Broadcasting

Article 9.1 of the TRIPS agreement states that WTO members are required to comply with Articles 1-21 of the Berne Convention.[23] Article 11bis of the Berne Convention gives authors of literary and artistic works the exclusive right to authorize "public communication by loudspeaker or any other analogous instrument transmitting, by signs, sounds or images, the broadcast of the work."[24] Every broadcast is considered to be a new public performance and therefore requires authorization from the license holder.

Whereas Article $11^{bis}(1)$ of the Berne Convention addresses broadcasting to the public, Article 11 addresses public performances. Article 11 gives authors of dramatic, dramatico-musical and musical works the exclusive right to authorize "any communication to the public of the performance of their works."[25] Public performance includes both "communication to the public of the performance of a work" and as "performance by any means or process, such as performance by means of recordings."[26]

Article 13, the exceptions clause to the TRIPS agreement, describes the circumstances under which member states can provide exceptions to authors' exclusive rights.[27] In its decision related to section 110(5) of the United States Copyright Act, the WTO panel considered whether Article 13 applies to the incorporated Berne articles and defined the breadth of Article 13's scope.

Section 110(5)

The precise meaning of the terminology in section 110(5) of the Copyright Act of 1976[28] is ambiguous. In 1998, Congress passed the Fairness in Music Licensing Act ("FMLA") in response to inconsistent court deci-

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23. TRIPS agreement, *supra* note 2, art. 9.1.

24. Berne Convention, *supra* note 3, art. 11bis.

25. *Id.* art. 11(1)(ii), at 13.

26. *Id.* art. 11(1).

27. TRIPS agreement, *supra* note 22, art. 13. Article 13 states that "[m]embers shall confine limitations or exceptions to exclusive rights to certain special cases which do not conflict with a normal exploitation of the work and do not unreasonably prejudice the legitimate interests of the right holder." *Id.*

28. Copyright Act of 1976, Pub. L. No. 94-533, § 110(5), 90 Stat. 2541 (codified at 17 U.S.C. § 110(5) (1994)) ("[C]ommunication of a transmission embodying a performance or display of a work by the public reception of the transmission on a single receiving apparatus of a kind commonly used in private homes unless (A) a direct charge is made to see or hear the transmission; or (B) the transmission thus received is further transmitted to the public.").

sions regarding the meaning of section 110(5).[29] Throughout the amendment process, Congress received pressure from interest groups regarding how broad to make the exception. Two such competing groups were establishment owners who wanted a broadly construed exceptions clause so that they could provide entertainment to their customers, and music producers and copyright holders who wanted to be paid royalties for the use of their works. Even though the FMLA was passed, this conflict between establishment owners and music producers and copyright holders still exists.[30] The establishment lobby is arguably pleased with the current scope of section 110(5) while the music lobby wants the United States to narrow the scope of the exception.

Currently, section 110(5)(A) carves out an exception for transmissions by a "single receiving apparatus of a kind commonly used in private homes" as long as no fee is charged or the transmission is not further broadcast to the public.[31] This "homestyle" exemption[32] is essentially the same text that was included in the Copyright Act of 1976. The House Report accompanying the Copyright Act of 1976 states that its purpose "is to exempt from liability anyone who merely turns on, in a public place, an ordinary radio or television . . . of a kind normally sold to members of the public for private use."[33]

Section 110(5)(B), the "business" exemption, was added by the FMLA to protect businesses that transmit or retransmit nondramatic works.[34] This section carves out an exception that applies to business establishments; the scope of the exception depends on how big the establishment is and whether it serves food or drink.[35] This exemption applies only if no fee is imposed for seeing or hearing the transmission, and the transmission does not extend beyond the establishment.[36] During the debates on the amend-

29. Laura A. McCluggage, *Section 110(5) of the Fairness in Music Licensing Act: Will the WTO Decide the United States Must Pay to Play?*, 40 IDEA 1, *6-*8 (2000).

30 *Id.*

31. 17 U.S.C. § 110(5)(A) (1994).

32. WTO Panel Report, *supra* note 1, at 4.

33. H.R. REP. NO. 94-1476 (1976). The current section 110(5)(A) provides more details than its predecessor in the 1976 act by specifying that no fee may be charged and that the transmission cannot be broadcast to the public.

34. 17 U.S.C. §110(5)(B).

35. *Id.* at § 110(5)(B). For both the second and fourth exceptions, the transmission must be solely by audio means by no more than six loudspeakers, no more than four of which are located in one room, or, if the performance is by audiovisual means by no more than four audiovisual devices, of which not more than one has a diagonal screen size of more than 55 inches, and not more than six audio devices of which no more than four are located in one room.

36. *Id. at* § 110(5)(B).

ment, the House Judiciary Subcommittee on Courts and Intellectual Property heard testimony regarding how this proposed amendment would violate the TRIPS agreement and Berne Convention.[37] Congress passed the bill despite the warning, and one and one half years later, the European Communities ("EC") brought a case before the WTO challenging the legality of section 110(5) as amended by the FMLA.

II. WTO PANEL REPORT

A. History of the Dispute

Proceedings against the United States began at a DSU meeting[38] on January 26, 1999. The EC alleged that sections 110(5)(A) and (B) of the United States Copyright Act, as amended by the FMLA, violated Article 9.1 of the TRIPS agreement and Articles 11(1)(ii) and 11bis(1)(iii) of the Berne Convention.[39] In accordance with the requirements set forth by the DSU, the EC and the United States met to negotiate a settlement regarding section 110(5).[40] No settlement was reached.[41] On April 15, 1999, a panel was formed to mediate the dispute.[42] The panel met with the parties and submitted its final report on May 5, 2000, in which it found that section 110(5) violated the TRIPS agreement and Berne Convention.[43]

B. Panel Decision

The panel began its analysis by first determining whether Article 13 of the TRIPS agreement, the exceptions clause, applied to the articles that were incorporated from the Berne Convention. The panel then went on to flesh out the scope of the article's application to section 110(5) to deter-

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37. *Music Licensing in Restaurants and Retail and Other Establishments, 1997: Hearings on H.R. 789 Before the Subcomm. on Courts and Intellectual Property of the House Comm. on the Judiciary*, 105th Cong. (1997) (statement of Bruce A. Lehman, Assistant Comm'r of Commerce and Comm'r of Patents and Trademarks, statement of Rep. Henry Hyde, letter from Richard W. Fisher, Deputy U.S. Trade Representative to Rep. Mary Bono). *See also* Laura A. McCluggage, *supra* note 29, at *17-*18.

38. WTO Panel Report, *supra* note 1, § 1.1, at 1. The EC initiated the meeting pursuant to Article 64.1 of the TRIPS agreement and Article 4 of the DSU.

39 *Id.* § 3.1, at 7

40. *Id.* § 1.2, at 1.

41. *Id.*

42. WTO Dispute Panel Report on Section 110(5) of the U.S. Copyright Act, WT/DS160/5, p. 1, (April 16, 1999), *available at* http://www.wto.org/english/tratop_e/dispu_e/dispu_e.htm.

43. WTO Panel Report, *supra* note 1.

mine if this provision of the United States Copyright Act violated the TRIPS agreement.

1. The Scope of Article 13

In deciding whether Article 13 of the TRIPS agreement also applied to the incorporated rights granted by Articles 11 and 11bis, the panel first had to determine whether the exceptions were permitted by the Berne Convention.

The revision conference reports of the Berne Convention indicated that the members approved limited exceptions in states' laws.[44] At the 1948 revision conference in Brussels, there was a motion to add a provision allowing states parties to the Convention to maintain the minor exceptions already existing in their national laws.[45] Although the motion did not pass[46], it was noted in the 1948 General Report that the "[c]onference did not question the very existence and maintenance of minor exceptions in national laws."[47] Having determined that exceptions were permitted at the 1948 conference, the panel began to define the breadth of the exceptions at the 1967 conference.

The United States and EC disagreed about what minor exceptions should be permitted.[48] Given these reports, the members of the WTO panel decided that the Berne Convention should be interpreted as permitting minor exceptions.[49] In reading the General Reports of the Berne Convention revision conferences of 1948 and 1967, the panel found that the examples given by the states parties were merely intended as examples of types of minor exceptions that would be permitted.[50] They were not intended to be an exhaustive list.[51]

The panel then addressed the issue of whether the Berne minor exceptions doctrine was incorporated into the TRIPS agreement by virtue of Article 9.1. The wording of Article 9.1 did not expressly exclude the minor exceptions doctrine when Articles 11 and 11bis of the Berne Convention were incorporated into the TRIPS agreement.[52] According to the panel, this fact indicated that the states intended to incorporate the minor excep-

44. *Id.* § 6.48, at 18-19.
45. *Id.* § 6.52, at 19.
46 The motion did not pass because the states parties feared it would broaden the number of minor exceptions.
47. WTO Panel Report, supra note 1, §6.52, at 19.
48. *Id.* § 6.56, at 21-22.
49. *Id.*
50. *Id.* § 6.57, at 22.
51. *Id.*
52. *Id.* § 6.61, at 23.

tions doctrine.[53] The panel cited as support several TRIPS Negotiating Group documents which stated that this principle is a general tenet of international law.[54]

Finally, the panel compared the text of Article 13 to Article 9(2) of the Berne Convention.[55] The two articles are virtually identical except that Article 9(2) applies only to the reproduction right and Article 13 applies to all categories of copyright rights.[56] Given the similarity of the two articles, along with the fact that there are no provisions that limit the application of Article 13 only to the TRIPS agreement, the panel decided that Article 13 also applied to the incorporated sections of the Berne Convention.[57]

2. *Application to Section 110(5)*

The three-prong test of Article 13 permits exceptions if they: (1) are confined to certain special cases; (2) do not conflict with a normal exploitation of the work; and (3) do not unreasonably prejudice the legitimate interests of the right holder.[58] The panel fleshed out the meaning of each prong of the test,[59] beginning with the first prong ("certain special cases"). The panel found that "certain" means that the exception has to be clearly defined by the national legislation.[60] Although not every exception must be accounted for, the first prong of the test requires "a sufficient degree of legal certainty."[61] The term "special" means that the exception has to be the opposite of the normal situation.[62]

The panel then moved to the second prong ("do not conflict with a normal exploitation of the work") and defined normal exploitation as

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53. *Id.* § 6.63, at 23.

54. *Id.* § 6.64-6.65, at 23-24.

55. Berne Convention, *supra* note 3, art. 9(2), at 381 ("[I]t shall be a matter for legislation in the countries of the Union to permit the reproduction of such works in certain special cases, provided that such reproduction does not conflict with a normal exploitation of the work and does not unreasonably prejudice the legitimate interests of the author.")

56. The Article 13 test is described in more detail and applied to section 110(5) in Part II.B.2 *infra*.

57. WTO Panel Report, *supra* note 1, § 6.94, at 31.

58. *Id.* § 6.97, at 31.

59. *See generally* Jane C. Ginsburg, *"Towards a Supranational Copyright Law? The WTO Panel Decision and the 'Three Step' Test for Copyright Exceptions,"* (Columbia Law Sch., The Ctr. for Law and Econ. Studies Working Paper No. 181, 2001) *at* http://papers.ssrn.com/paper.taf?abstract_id=253867.

60. WTO Panel Report, *supra* note 1, § 6.108, at 33.

61. *Id.*

62. *Id.* § 6.109, at 33.

"something less than the full exclusive right."[63] It agreed with the United States that there is a hierarchy between primary and secondary broadcasts, even though this distinction might not be economically significant.[64] It also agreed with the EC that copyright holders should equally benefit from broadcasts and rebroadcasts.[65] Ultimately the panel sided with the United States because the establishments covered by the "homestyle" exemption were not likely to purchase licenses. Since they were not likely to purchase licenses, broadcasting the nondramatic works would not "conflict with the expectation of right holders concerning the normal exploitation of their works."[66]

In defining the terms composing the third prong ("do not unreasonably prejudice the legitimate interests of the right holder"), the panel identified the key issue as drawing a line between reasonable and unreasonable prejudice. They determined that prejudice "reaches an unreasonable level if an exception or limitation causes or has the potential to cause an unreasonable loss of income to the copyright holder."[67] After an extensive economic analysis, the panel agreed with the United States that the loss caused by the homestyle exception was not great enough to unreasonably prejudice the legitimate interests of the right holder.[68]

In order to be valid under Article 13, section 110(5) needed to comply with all three of these requirements.[69] The panel began its analysis by determining whether sections 110(5)(A) and (B) met the first prong of the test. A Congressional Research Service study showed that 16 percent of United States eating establishments, 13.5 percent of United States drinking establishments, and 18 percent of United States retail establishments fall within the parameters described in section 110(5)(A).[70] Since this was clearly not the norm, the panel found that section 110(5)(A) met the requirement that the circumstances be "special." The panel also determined that section 110(5)(A) did not need to be more specific in defining homestyle equipment in order to meet the "certain" requirement.[71]

The panel found that section 110(5)(B) clearly defined the size of the establishments and the kinds of equipment that can be used to qualify for

63. *Id.* § 6.167, at 44.
64. *Id.* § 6.170, at 45.
65. *Id.*
66. *Id.* § 6.216, at 56.
67. *Id.* § 6.229, at 59.
68. *Id.* §§ 6.230-6.272, at 59-68.
69. *Id.* § 6.97, at 31; *see also supra* notes 28, 31-32.
70. *Id.* § 6.142, at 39-40.
71. *Id.* § 6.145, at 40.

the exception. It, therefore, met the "certain" requirement. It was not as clear, however, if it fell within the acceptable scope of "special."[72] A Congressional Research Service study showed that 65.2 percent of all establishments, 71.8 percent of all drinking establishments, and 27 percent of all retail establishments met the size requirements of subparagraph B.[73] These statistics showed that this was the norm as opposed to a special case. Thus, the United States failed to prove that section 110(5)(B) of the United States Copyright Act met the requirements of Article 13 of the TRIPS agreement.[74]

Upon finding that section 110(5)(B) violated sections 11(1)(ii) and 11bis(1)(iii) of the Berne Convention and Article 9.1 of the TRIPS agreement, the panel recommended that the United States bring section 110(5)(B) into conformance with international law.

C. Criticism of the Panel Decision

The panel's narrow application could potentially invalidate exceptions clauses in other nations.[75] This, in turn, could harm the TRIPS agreement goal of creating a uniform copyright standard.

1. Canada

Article 69(2) of the Canadian Copyright Law states:

> In respect of public performances by means of any radio receiving set in any place other than a theatre that is ordinarily and regularly used for entertainment to which an admission charge is made, no royalties shall be collectable from the owner or user of the radio receiving set, but the Board shall, in so far as possible, provide for the collection in advance from radio broadcasting stations of royalties appropriate to the conditions produced by the provisions of this subsection and shall fix the amount of the same that royalties cannot be collected for the public perform-

72. *Id.*

73. *Id.* § 6.118, at 35; *see also supra* note 34.

74. Since the panel found section 110(B) invalid based upon the first prong and did not focus as much on the second two prongs, they will not be discussed here.

75. Exceptions clauses in Australia, Belgium, Finland, Denmark, New Zealand, Philippines, Canada, South Africa, Japan, and Brazil could potentially violate the Berne Convention and TRIPS agreement. WTO Panel Report, *supra* note 1, at 21, n. 67. It is beyond the scope of this note to analyze the copyright exception clauses of many nations. The analysis of the laws in the following countries is intended to be a representative example of the problem.

> ance of a song played on the radio within an establishment other than a theater.[76]

This exemption, which states that royalties *cannot* be collected if a song is played in a venue other than a theater, is broader than the United States exception.[77] This seems to be incompatible with the spirit of Article 11bis(1)(iii) of the Berne Convention, and therefore, with Article 13 of the TRIPS Agreement.[78]

2. *Japan*

The language in article 38(3) of the Japanese Copyright Code, which is virtually identical to the language in section 110(5) of the United States Copyright Code, states:

> It shall be permissible to communicate publicly, by means of a receiving apparatus, a work already broadcast or diffused by wire, for nonprofit-making purposes and without charging any fees to audiences or spectators. The same shall apply to such public communication made by means of a receiving apparatus of a kind commonly used in private homes.[79]

Article 14 of the Supplemental Provisions to the Japanese Copyright Act creates an exemption for playing sound recordings in public.[80] Establishments that use the sound recordings to obtain a profit are not exempt under Article 14.[81] The exemption also does not apply to establishments which: (1) serve food or drinks but advertise music entertainment; (2) permit customers to dance; or (3) show other performances that accompany the music.[82] Given the similarity between Japanese and United States law, it is likely that Japan's law would be found to violate Articles 11 and 11bis of the Berne Convention and Article 13 of the TRIPS Agreement.

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76. Copyright Act, R.S., c. C-30 (as updated to Jan. 1, 1994—Chapter C-42 An Act respecting copyright) art. 69(2) (Can.), *reprinted in* COPYRIGHT AND NEIGHBORING RIGHTS LAWS AND TREATIES, Canada Text 1-01, at 23 (WIPO 1998).

77. McCluggage, *supra* note 29, at *37.

78. *Id.*

79. Japanese Copyright Act, Law No. 48 of 1970, art. 38(3), (as amended by Laws No. 49 of 1978, No. 45 of 1981, No. 78 of 1983, No. 23 of 1984, No. 46 of 1984, No. 62 of 1985, No. 64 of 1986, No. 65 of 1986, No. 87 of 1988, No. 43 of 1989, No. 112 of 1994, and No. 91 of 1995), *reprinted in* COPYRIGHT AND NEIGHBORING RIGHTS LAWS AND TREATIES, Japan Text 1-01, at 9 (Agency for Cultural Affairs, Copyright Division of Japan trans., WIPO 1995).

80. *Id.* art. 14.

81. *Id.*

82. *Id.*

3. *Austria*

Article 56d(1) of the Austrian Copyright Law states that hotels can play films for their guests if: (1) at least two years have passed since the film was first performed in Austria or in a Germanic language; (2) the performance is legally communicated and distributed; and (3) the guests do not have to pay for the movie.[83] Austrian law requires hotels to pay filmmakers for uses that do not meet these requirements;[84] however, like United States law, it does not require the hotels to obtain the permission of filmmakers before showing the films.[85] Austrian law is therefore likely to be held to violate Articles 11 and 11*bis* of the Berne Convention and Article 13 of the TRIPS Agreement.

The panel should not have construed the prongs of Article 13 in the way it did, since the construction is likely to invalidate the copyright exceptions clauses of many countries. The goal of the TRIPS agreement is to create a uniform international standard of copyright protection.[86] Adopting the broader application of the "are confined to certain special cases" prong of the article would reinforce the seemingly consistent standard that already exists.

Furthermore, adopting the strict standard will decrease the legitimacy of and compliance with the TRIPS agreement. Many countries might be required to change their laws under this interpretation of the TRIPS agreement. An international treaty which overrules a seemingly consistent standard is not likely to be seen as legitimate. This lack of legitimacy is not likely to foster compliance which could, in turn, defeat the TRIPS agreement goal of creating a more uniform standard of copyright protection. Nonetheless, the panel adopted the stricter application of the standard.

III. REMEDY

In order to rectify the potential problems with the panel's decision and prevent international inconsistency, this Part addresses how the DSU should be interpreted and how the United States should have resolved the situation. The existing literature on the subject and the relevant sections of

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83. Section 56d(1), Copyright Amendment Law 1996, Federal Law to Amend the Copyright Law and the Copyright Amending Law of 1980, No. 151 (1996), *reprinted in* COPYRIGHT AND NEIGHBORING RIGHTS LAWS AND TREATIES, Austria Text 1-05, at 4 (WIPO trans., WIPO 1997).

84 *Id.*

85 *Id.*

86. DSU, *supra* note 12, art. 3.

the DSU will be presented before arguing that the United States should have appealed the decision. This section will go on to argue that had this appeal failed, the United States should have negotiated a sweeping change of national laws with other potential violators of the TRIPS agreement to set an example of compliance which would enable it to force offending nations, such as China, to comply with TRIPS.

A. Scholarly Interpretations of the DSU

Commentators writing on WTO remedies generally agree that the DSU mandates that an offending state first unilaterally change its laws and, only if this is not done, that compensation be made to the harmed parties. John Jackson, writing on remedies in general, stated "the DSU clearly establishes a preference for an *obligation to perform* the recommendation" and "that compensation shall be resorted to only if the immediate withdrawal of the measure is impracticable . . . ."[87] Applying his interpretation of the DSU to this case, he would likely agree with the United States' decisions not to appeal the decision and to amend section 110(5)(B) to conform with TRIPS and the Berne Convention.

Judith Hippler Bello, writing on the DSU, argues that members have three options once panel hearings have begun. They may change the offending law or omission, retain the law and provide compensation, or retain the law, make no compensation and suffer likely economic sanctions against their exports.[88] Applying her argument to this case, she would likely agree with Jackson that it was preferable for the United States to amend section 110(5)(B), and, if it did not do that, it should compensate the EC.

Laura McCluggage argues the United States "needs to be a good sport and accept defeat gracefully by amending or repealing section 110(5) of the United States Copyright Act."[89] She interprets the DSU as stating that "an offending measure should be removed, and that compensation is only temporary relief while the measure is remedied."[90] She proposes two ways that the United States could change the law. First, it could repeal the amendment and use the old language of the Copyright Act of 1976.[91] The language of the 1976 Act would, however, have to fit within the panel's

87. John H. Jackson, *The WTO Dispute Settlement Understanding—Misunderstandings on the Nature of Legal Obligation*, 91 AM. J. INT'L .L. 60, 62 (1997).

88. Judith Hippler Bello, *The WTO Dispute Settlement Understanding; Less is More*, 90 AM. J. INT'L .L. 416, 417 (1996).

89. McCluggage, *supra* note 29, at *45.

90. *Id.* at *26.

91. *Id.* at *27.

interpretation of Article 13.[92] Second, it could adopt United States Senate Bill 1628 proposed in the 104th Congress since it would meet the three-part test of Article 13.[93] Should the United States choose neither of these options, it could compensate the EC.

United States Senate Bill 1628 stated that in order to qualify for the exemption, an establishment must be less than 5,000 square feet, have a gross annual income not exceeding 20 percent of the gross annual income of small businesses, and broadcast with ten or fewer loudspeakers.[94] This bill would meet the "certain special cases" exception clause that section 110(5)(B) violates because, McCluggage argues, it would allow only a limited number of establishments to qualify for the exception. Furthemore, more than 92 percent of business owners supported Senate Bill 1628.[95] She acknowledges that in a newly introduced bill the ten speaker limit would have to be decreased in order to meet the Article 13 requirements.[96]

Alternatively, McCluggage discusses her interpretation of Article 22. She focuses on the portion of the provision that states:

> The suspension of concessions or other obligations shall be temporary and shall only be applied until such time as the measure found to be inconsistent with a covered agreement has been removed, or the Member that must implement recommendations or rulings provides a solution to the nullification or impairment of benefits, or a *mutually satisfactory solution* is reached.[97]

McCluggage interprets "mutually satisfactory solution" to mean "that if the United States and EC mutually agree on a level of compensation, the case would be settled without amending United States law."[98] McCluggage argues that the United States should first change its law but, if it does not do that, compensating the EC would be a mutually satisfactory solution.

B. Remedy Provisions of the DSU

A careful analysis of Article 22 of the DSU indicates the United States is not required to unilaterally amend section 110(5). Article 22 states:

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92. *Id.* McCluggage wrote this piece before the panel rendered its decision, and, as such, did not fully develop this analysis.

93. *Id.* at 28. Senate Bill 1628 was defeated after publication of her article. She would likely argue that a bill similar to this should now be passed.

94. *Id.*

95. *Id.*

96. *Id.*

97. DSU, *supra* note 12, art. 22. (emphasis added).

98. McCluggage, *supra* note 29, at *42.

> Compensation and the suspension of concessions or other obligations are temporary measures available in the event that the recommendations and rulings are not implemented within a reasonable period of time. However, neither compensation nor the suspension of concessions or other obligations is preferred to full implementation of a recommendation to bring a measure into conformity with the covered agreements.[99]

Article 22 states that changing a law that violates TRIPS is preferred if a mutually satisfactory agreement is not reached. This seems significantly different from requiring a state to unilaterally withdraw its measures.

Furthermore, the phrase "mutually satisfactory solution" should not be narrowly interpreted to involve universal change - as McCluggage argues. The primary aim of the DSU is to achieve a mutually satisfactory solution. Article 3(7), titled General Provisions, states:

> A solution mutually acceptable to the parties to a dispute and consistent with the covered agreements is clearly to be preferred. In the absence of a mutually agreed solution, the first objective of the dispute settlement mechanism is usually to secure the withdrawal of the measures concerned. . . . The Provision of compensation should be resorted to only if the immediate withdrawal of the measure is impracticable. . . . The last resort . . . is the possibility of suspending the application of concessions or other obligations.[100]

It is only if the parties cannot agree upon a mutually satisfactory solution that changing the law and compensation are suggested as possible means of solving the dispute.

This is also seen in the latter part of Article 22.[101] The Article discusses the options of changing the law or compensating injured countries but concludes that these are only temporary measures that are in force until "a mutually satisfactory solution is reached."[102] Again, it is only if the parties cannot mutually come to a solution that these two options are imposed. A mutually satisfactory solution is preferable.

C. A Mutually Satisfactory Solution

As stated before, the United States should have appealed the decision because the construction was too narrow and invalidated the laws of many

99. DSU, *supra* note 12, art. 22.
100. *Id.* art. 3.
101. *Id.* art. 22.
102. *Id.*

countries. Had the United States appealed the decision and lost its appeal, it would have been within its best interest to then negotiate with other countries which have laws that arguably violate the TRIPS agreement[103] to achieve a mutually satisfactory solution. A mutual solution in which many change their laws is better than a unilateral decision in which only the United States changes its laws, because the rights of United States copyright holders will be afforded greater protection.

Further, the United States has historically been a strong proponent of compliance with international treaties and has strongly criticized other nations for not complying with them.[104] For example, in the United States dispute with the EC over banana trade, which the EC lost, the United States was stalwart in insuring EC compliance with the panel decision.[105] If the United States does not make an effort to find a mutually satisfactory solution, it will set a bad precedent, and the United States will be less effective in getting other countries to comply with TRIPS standards.

Now that China has become a party to the TRIPS agreement, it has become important for the United States to be able to enforce the TRIPS agreement against China in order to protect United States copyright holders. Although software piracy slowly began to decline or level off in most regions during the 1990s, piracy is continuing to increase in China.[106] The software piracy rate in China was 90 percent in 1999 and 94 percent in 2000.[107] Worldwide, there was a loss of approximately 10.1 billion dollars in retail software sales because of piracy in China in 2000 alone.[108] The United States is most strongly affected as approximately 70 percent of the worldwide market for software is served by the United States.[109]

The financial losses from piracy have become so severe that some businesses will no longer release software in China and the rest of Asia. It was recently reported that Adobe Acrobat systems may abandon the Chinese and Asian markets because of software piracy in China.[110] Adobe CEO Bruce Chizen stated, "It is a simple business decision... It costs

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103. *See supra* note 75.

104. McCluggage, *supra* note 29, at *43.

105. *Id.*

106. Business Software Alliance, "Sixth Annual BSA Software Piracy Study" 4 (May 2001), *at* http://www.bsa.org/.

107. *Id.* at 3.

108. *Id.* at 6.

109. Business Software Alliance, "Software Piracy: The Facts," (last updated Dec. 29, 2001), *at* http://www.info.gov.hk/ipd/eng/information/studyaids/software_piracy_fact.htm.

110. Kurt Foss, "Will software piracy fears keep Adobe out of China?," Planet PDF (Feb. 4, 2002), *at* http://www.planetpdf.com/mainpage.asp?webpageid=1891.

US$750,000 to localise [sic] an application for the Chinese language and if we are only going to make US$500,000 in revenue it does not make sense for us to go ahead."[111]

The United States can use China's membership in the WTO to combat this piracy. Changing section 110(5) as well as the laws of other countries to comply with the TRIPS agreement would result in a more consistent international standard for copyright. This in turn would make WTO rules easier to enforce against China.

IV. CONCLUSION

The panel applied its interpretation of the prongs of Article 13 too narrowly. The United States should have appealed this decision and argued for a broader application of the Article to maintain legitimacy and compliance with the TRIPS agreement. If the United States had appealed and lost its appeal with respect to this, it should have negotiated with other countries whose laws also violate this new interpretation of Article 13 to change their laws for the purpose of maintaining a consistent international standard. Scholars interpret the DSU too narrowly in limiting offending states options to 1) amending the law contrary to the TRIPS agreement, 2) compensating the damaged nations, or 3) doing nothing and incurring penalties. The main purpose of the DSU is to obtain a mutually satisfactory agreement.

The United States should have negotiated with other potentially offending countries to uniformly change their laws. This would have not only afforded United States copyright holders greater protection but would have also given the United States more clout in compelling China to comport with TRIPS.

111. *Id.*

ADDITIONAL DEVELOPMENTS—FOREIGN AND INTERNATIONAL LAW

TRIPs RESOLUTION ON PUBLIC HEALTH

At the November 2001 World Trade Organization ("WTO") meeting in Doha, Qatar, member nations resolved that the Agreement on Trade-Related Aspects of Intellectual Property Rights ("TRIPs") should be "interpreted and implemented in a manner supportive of WTO Members' right to protect public health."

Pharmaceutical companies filed lawsuits and threatened trade-sanctions against South Africa and Brazil for allegedly violating TRIPs by refusing to enforce patents for an AIDS drug. Thirty-nine of the world's largest pharmaceutical companies sued the South African government to prevent it from importing and producing less expensive generic AIDS drugs. After harsh international criticism, the pharmaceutical companies withdrew their charges. In Brazil, United States pharmaceutical companies threatened to sue Brazil for violating TRIPS by failing to enforce patents for AIDS drugs. Brazil countered by launching a worldwide media campaign that created so much negative publicity for the U.S. pharmaceutical companies that they did not pursue the case. Brazil subsequently announced its intentions to violate a patent for an AIDS drug when negotiations between the government and pharmaceutical companies break down. This announcement triggered the discussion and ensuing resolution regarding the enforceability of pharmaceutical patents at the recent WTO Summit.

The Doha declaration affirms the rights to grant compulsory licenses (overriding patents), and to determine the grounds upon which such licenses are granted. The declaration also acknowledges that each country has the right to determine what constitutes a national emergency. For example, public health crises, including those relating to HIV/AIDS, tuberculosis, malaria and other epidemics, can represent a national emergency. Individual countries are permitted to determine whether to engage in parallel import trade and licensing agreements. The member states recommended further studies to address the issue of nations that do not have the manufacturing capacity in the pharmaceutical sector and might face difficulties issuing compulsory licenses.

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STATUTES AND OTHER TOPICS