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In re Napster Inc. Copyright Litigation: Defining the Contours of the Copyright Misuse Doctrine

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CASE NOTES

IN RE *NAPSTER INC. COPYRIGHT LITIGATION*: DEFINING THE CONTOURS OF THE COPYRIGHT MISUSE DOCTRINE

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I. INTRODUCTION

Napster, Inc. ("Napster"), in a ruling that marked its first significant victory in a battle against the major companies in the recording industry, persuaded Chief Judge Marilyn Hall Patel to further consider whether the recording industry plaintiffs misused their copyrights by attempting to control the digital distribution of music.[1] If ultimately successful, Napster's copyright misuse defense will bar the recording industry plaintiffs from asserting their copyright infringement claims until they cease their illegal activity.[2]

Napster's victory is significant for several reasons. First, and practically, Judge Patel's order provides Napster with some breathing room in this litigation that has condemned the company's music file-swapping service[3] and effectively shut down its business for almost

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1. *See In re* Napster Inc. Copyright Litig., No. MDL 00-1369, 2002 WL 482361, at *21 (N.D. Cal. Feb. 22, 2002). The opinion also considered other issues, including whether plaintiffs "owned" their copyrights.

2. *See id.* at *16.

3. For a background of the case, *see* A&M Records Inc. v. Napster, Inc., 2001 WL 227083 (N.D. Cal. Mar. 5, 2001) (entry of modified preliminary injunction), *aff'd* No. 01-15998, 2002 WL 449550 (9th Cir. Mar. 25, 2002).

one year.[4] Second, from a legal standpoint, Judge Patel's decision is one of the first detailed discussions of the defense of copyright misuse in the Ninth Circuit and provides copyright infringement defendants with a significant arrow in their quiver of defenses against large, and potentially monopolistic, plaintiffs seeking to "secure an exclusive right or limited monopoly not granted by the Copyright Office."[5]

Notwithstanding this victory, Napster still has a significant uphill battle. Judge Patel's decision came in the context of a Rule 56(f)[6] motion for additional discovery.[7] While her decision effectively grants Napster the opportunity to conduct discovery into whether the recording industry plaintiffs misused their copyrights or committed antitrust violations, the ruling, for all intents and purposes, has no true legal adverse consequence for the plaintiffs.[8] Napster needed only to demonstrate—and Judge Patel only concluded—that "there are relevant facts remaining to be discovered . . . that [may] raise an issue of material fact."[9]

Nevertheless, the opinion provides some useful guidance for the parties and sets forth clearly the law of copyright misuse. In addition, Judge Patel—who had to date reserved her harshest judgment for Napster—drafted an opinion that "seems to signal a sea change in the music industry's lawsuit against the peer-to-peer song-swapping service."[10] The recording industry, long under scrutiny for its practices, which in the past have been deemed anticompetitive,[11] now must defend itself against new charges of anticompetitive conduct and

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4. *See* Kevin Featherly, *Napster Case: Is Judge Turning Tables on Labels?*, NEWSBYTES, Feb. 1, 2002, *at* http://www.newsbytes.com/news/02/174154.html.

5. *See* Lasercomb Am., Inc. v. Reynolds, 911 F.2d 970, 977 (4th Cir. 1990).

6. FED. R. CIV. PRO. 56(f).

7. *See In re* Napster Inc. Copyright Litig., No. MDL 00-1369, 2002 WL 482361, at *1 (N.D. Cal. Feb. 22, 2002).

8. *See id.* at *3.

9. *Id.* (alteration added) (quoting Continental Mar. v. Pac. Coast Metal Trades, 817 F.2d 1391, 1395 (9th Cir. 1987)).

10. Featherly, *supra* note 4.

11. The plaintiffs in this case have been through the antitrust ringer before, first with the landmark price-fixing Supreme Court decision in *Broadcast Music, Inc. v. CBS*, 441 U.S. 1 (1979). Plaintiffs also have been investigated for illegally fixing compact discs prices, *see* Press Release, State of Vermont Office of the Attorney General, Music Distributors, Retailers Charged with Price-Fixing (Aug. 9, 2000), *available at* http://www.state.vt.us/atg/press08092000, and presently are under investigation by the Department of Justice for the precise claims raised by Napster in this litigation—that they have attempted to monopolize the digital distribution of music by unlawful means. *See* Jane Black, *Online Music: Cranking Up the Antitrust Volume*, BUSINESSWEEK ONLINE, Oct. 26, 2001, *available at* http://www.businessweek.com/bwdaily/dnflash/oct2001/nf20011026_0654.htm.

justify joint venture arrangements that Judge Patel concluded "look bad, sound bad and smell bad."[12] Napster's new-found right to conduct discovery into the recording industry's practices presents the salacious opportunity for the underdog to knock the giant on its back.

This Case Note—much like Judge Patel's opinion—looks to the history of the law of copyright misuse, the current state of the law, and how the court preliminarily applied the law to the facts before it. Finally, it discusses "what might be" if Napster's discovery ultimately uncovers evidence of copyright misuse.

II. BACKGROUND

The Napster litigation began in December of 1999, when the five major recording industry companies—BMG, Sony, EMI, Universal and Warner—filed suit against Napster for copyright infringement.[13] Napster is a peer-to-peer file-swapping service; the Web site enabled users from around the world to log in and trade music. This Internet music-swapping function is referred to now in the industry as the "digital distribution of music." [14] Plaintiffs contended that "Napster knew of and failed to prevent its users' unauthorized reproduction and distribution of plaintiffs' copyrighted sound recordings."[15] Judge Patel granted plaintiffs' motion for a preliminary injunction and shut down the Napster file-swapping service until the company could prevent such unauthorized reproduction.[16] Napster appealed to the Ninth Circuit, which subsequently affirmed.[17] It is still shut down today.[18]

Napster's copyright misuse claims spring from the recording industry plaintiffs' subsequent entry into the market for the digital distribution of music.[19] In mid-2001, the major recording industry companies formed two joint ventures—MusicNet and press*play*—that enabled the digital distribution of their music.[20] MusicNet is a collaboration between EMI, BMG, and Warner; press*play* is a venture between Sony and Universal.[21] In June 2001, Napster signed a

12. *In re Napster Copyright Litig.*, 2002 WL 482361, at *17.
13. *See id.* at *1.
14. *See* Featherly, *supra* note 4.
15. *In re Napster Copyright Litig.*, 2002 WL 482361, at *1 (citing Compl. ¶¶ 56–80).
16. *See id.*
17. *See* A&M Records, Inc. v. Napster, Inc., 239 F.3d 1004 (9th Cir. 2001).
18. *See* Featherly, *supra* note 4.
19. *See In re Napster Copyright Litig.*, 2002 WL 482361, at *2–*3.
20. *See id.* at *2.
21. *See id.*

licensing agreement with MusicNet, which allowed Napster to access MusicNet's copyrighted materials, and will, when Napster comes back on-line, allow Napster's customers to access this music content as well.[22]

Napster has challenged several provisions of the MusicNet licensing agreement as an attempt by plaintiffs to unlawfully extend their copyright.

III. THE STATE OF THE LAW OF COPYRIGHT MISUSE

Judge Patel first was confronted with the task of delineating the contours of the copyright misuse defense.[23] The copyright misuse defense finds its origins in the law of patent misuse.[24] Although the doctrine has existed for some time, it has not been developed clearly by the Ninth Circuit, and those courts that have confronted it squarely have diverged in their interpretations and applications of the defense and *rarely* have concluded that a defendant in a copyright infringement case could assert it successfully. Moreover, there is a clear split of authority as to how to assert the defense. As will be discussed below, several circuits allow a misuse defense to stand where a defendant can demonstrate a violation of "public policy," whereas other courts require copyright misuse defendants to make a showing that the plaintiff violated the antitrust laws by attempting to extend its copyright.

One of the first cases to consider the copyright misuse defense, *Lasercomb America, Inc. v. Reynolds*, set forth the rationale for the defense in great detail.[25] In *Lasercomb*, the court held that "a misuse of copyright defense is inherent in the law of copyright just as a misuse of patent defense is inherent in patent law."[26] Recognizing "[t]he origins of patent and copyright law in England, the treatment of these two aspects of intellectual property by the framers of our Constitution, and the later statutory and judicial development of patent and copyright law in this country persuade[d] [it] that parallel public policies underlie the protection of both types of intellectual

22. *See id.* at *3.
23. *See id.* at *11.
24. *See id.*
25. Lasercomb Am., Inc. v. Reynolds, 911 F.2d 970 (4th Cir. 1990).
26. *Id.* at 973.

property rights,"[27] the Fourth Circuit held that the doctrine of copyright misuse existed as a defense to infringement actions.[28]

Because the *Lasercomb* court relied on the doctrine of patent misuse to ground its holding that the doctrine of copyright misuse existed, it makes sense that a defendant asserting the copyright misuse defense would have to make the same showing as would a patent misuse defendant. In other words, as in a patent misuse claim, where a defendant demonstrates that a plaintiff attempted to extend its copyright beyond its intended use, a copyright misuse claim would stand: "[P]ublic policy . . . forbids the use of the [copyright] to secure an exclusive right or limited monopoly not granted by the [Copyright] Office and which is contrary to public policy to grant."[29]

Thus, under *Lasercomb*, a defendant need not demonstrate that a plaintiff violated the antitrust laws to successfully assert the copyright misuse defense:

> Both the presentation by appellants and the literature tend to intermingle antitrust and misuse defenses. A patent or copyright is often regarded as a limited monopoly—an exception to the general public policy against restraints of trade. Since antitrust law is the statutory embodiment of that public policy, there is an understandable association of antitrust law with the misuse defense. Certainly, an entity that uses its patent as the means of violating antitrust law is subject of a misuse of patent defense. However, *Morton Salt* held that it is not necessary to prove an antitrust violation in order to successfully assert patent misuse.[30]

The copyright misuse doctrine as defined by *Lasercomb* (*i.e.*, a defense that does not require a defendant to prove an antitrust violation, but only to demonstrate a violation of "public policy") has been expressly recognized by four circuits.[31] Several other circuits have been more reluctant to adopt the defense, and instead have adopted the doctrine as a defense to copyright infringement *only* where the defendant can link the misuse to an actual antitrust

27. *Id.* at 974.

28. *See id.*

29. *Id.* at 977.

30. *Id.* at 977–78 (citation omitted).

31. *See* Alcatel USA, Inc. v. DGI Techs., Inc., 166 F.3d 772 (5th Cir. 1999); Practice Mgmt. Info. Corp. v. Am. Med. Ass'n, 121 F.3d 516 (9th Cir. 1997), *amended by* 133 F.3d 1140 (9th Cir. 1998); Bateman v. Mnemonics, Inc., 79 F.3d 1532 (11th Cir. 1996); Lasercomb Am., Inc. v. Reynolds, 911 F.2d 970 (4th Cir. 1990).

violation.[32] Finally, the First Circuit has left open the question as to whether "the federal copyright law permits a misuse defense."[33]

Judge Patel had sufficient guidance from Ninth Circuit precedents to conclude that the defense of copyright misuse existed.[34] In *Practice Management Information Corp. v. American Medical Association*, the plaintiff brought a suit for declaratory relief, arguing that the defendant misused its copyright by negotiating a contract with a federal agency (*i.e.*, the Health Care Financing Administration (HCFA)) in an anticompetitive manner.[35] In that case, the plaintiff argued that the American Medical Association engaged in copyright misuse by agreeing to license its product *only* if HCFA agreed not use a competing diagnostic system. The Ninth Circuit agreed, concluding that the provision clearly restrained trade (*i.e.*, it precluded HCFA from using competing products). As a result, the provision violated public policy and was the basis for a copyright misuse defense.[36]

The *Practice Management* court, adopting the Fourth Circuit test for copyright misuse, concluded that the defense "forbids the use of the copyright to secure an exclusive right or limited monopoly not granted by the Copyright Office."[37] The court, relying on the *Lasercomb* decision, concluded that "a defendant in a copyright infringement suit need not prove an antitrust violation to prevail on a copyright misuse defense."[38] Instead, to prevail on the copyright

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32. Presumably, such courts were concerned with allowing defendants to proceed with misuse claims where they allege only vague and ambiguous "public policy" violations. Requiring an actual antitrust violation provides clearer and more stringent guideposts for the court and the parties. *See* Saturday Evening Post Co. v. Rumbleseat Press, Inc., 816 F.2d 1191 (7th Cir. 1987) (suggesting that the doctrine exists only when a defendant can demonstrate an antitrust violation). In a subsequent case, the Seventh Circuit suggested, in qad. inc. v. ALN Assocs., Inc., 974 F.2d 834 (7th Cir. 1992), that the copyright misuse doctrine may exist separately and independently of a showing of an antitrust violation, but did not define its contours. *See also* United Tel. Co. of Mo. v. Johnson Publ'g Co., Inc., 855 F.2d 604 (8th Cir. 1988) (same standard as set forth in the Seventh Circuit's *Saturday Evening Post* case).

33. Data Gen. Corp. v Grumman Sys. Support Corp., 36 F.3d 1147 (1st Cir. 1994).

34. *See Practice Mgmt.*, 121 F.3d at 520.

35. *See id.* at 520–22.

36. *See id.* at 522; *see also Lasercomb*, 911 F.2d at 977–79 (holding that license agreement, which prohibited licensees from creating their own competing software program for the ninety-nine-year term of the license, "essentially attempts to suppress any attempt by the licensee to independently implement the idea which [Lasercomb's software program] expresses," and was invalid under the copyright misuse doctrine because it ran afoul of the public policy surrounding the grant of a copyright).

37. Practice Mgmt. Info. Corp. v. Am. Med. Ass'n, 121 F.3d 516, 521 (9th Cir. 1997) (quoting *Lasercomb*, 911 F.2d at 977–79, and citing DSC Communications Corp. v. DGI Techs., Inc., 81 F.3d 597, 601 (5th Cir. 1996)).

38. *Id.* (citing Lasercomb Am., Inc. v. Reynolds, 911 F.2d 970, 978 (4th Cir. 1990)).

misuse defense, a defendant need only demonstrate that "the [plaintiff] used its copyright 'in a manner violative of the public policy embodied in the grant of a copyright.'"[39] The court further reasoned:

> So while it is true that the attempted use of a copyright to violate antitrust law probably would give rise to a misuse of copyright defense, the converse is not necessarily true—a misuse need not be a violation of antitrust law in order to comprise an equitable defense to an infringement action. The question is not whether the copyright is being used in a manner violative of antitrust law (such as whether the licensing agreement is 'reasonable'), but whether the copyright is being used in a manner violative of the public policy embodied in the grant of a copyright.[40]

Practice Management is one of only a few cases in which a party prevailed on a copyright misuse claim.[41]

Judge Patel, however, correctly noted that even though *Practice Management* held that it was unnecessary to demonstrate an antitrust violation to raise the copyright misuse defense successfully, that court "still rel[ied] on antitrust-like inquiries in determining what licensing agreements violate public policy. Of the cases reviewed by the court, all mimic the *per se* rules of antitrust."[42] Nonetheless, Judge Patel did not need to decide whether Napster could rely on a violation of public policy to support a copyright misuse claim. Instead, because Napster argued in the alternative—contending both that plaintiffs committed

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39. *Id.* at 521 (quoting *Lasercomb*, 911 F.2d at 977).

40. *Id.*

41. In *Electronic Data Systems Corp. v. Computer Associates Intern., Inc.*, 802 F. Supp. 1463 (N.D. Tex. 1992) ("*EDS*"), the plaintiff alleged that the defendant misused its software copyrights in such a manner that restrained competition; imposed undue restrictions on the use of copyrighted software that extended beyond the permissible bounds of the exclusive rights granted by the copyright laws; and, unlawfully tied the purchase of its copyrighted software to some other products or services. *See EDS*, 802 F. Supp. at 1465–66. The plaintiff brought suit, seeking *both damages and a declaration* that the defendant's misuse of its copyrights rendered the copyrights invalid and unenforceable. The defendant brought a motion to dismiss, arguing that there is no cause of action for "misuse of copyright" and no legal basis for granting affirmative relief based on such a theory. The *EDS* court *denied* the motion to dismiss, concluding that the plaintiff stated a valid cause of action for damages and for declaratory relief. The court suggested, however, that to succeed on a misuse of copyright claim in the affirmative, the plaintiff would have to demonstrate that the misuse of copyright actually violated the antitrust laws. *See id.* at 1466. Thus, it seems as though Napster would face a more rigorous standard if it sought affirmative relief. This is the only case where a party sought affirmative damages for copyright misuse and the court allowed it to proceed beyond the motion to dismiss stage.

42. *In re* Napster Inc. Copyright Litig., No. MDL 00-1369, 2002 WL 482361, at *13 (N.D. Cal. Feb. 22, 2002).

public policy violations and ran afoul of the antitrust laws—Judge Patel left the issue for another day.

Napster argued two independent bases for the misuse defense. First, it contended several of the terms of its licensing agreement with MusicNet were unduly restrictive, and thus, contrary to public policy.[43] Alternatively, Napster contended that even if the court concluded the license agreements were not unduly restrictive, the recording industry plaintiffs nonetheless could not enforce their copyrights because their conduct was "so anti-competitive as to give rise to a misuse defense."[44]

A. Copyright Misuse Based on a Public Policy Violation

Napster first contended that the MusicNet licensing agreement was unduly restrictive and thus in violation of public policy.[45] Although the court did not decide the issue on its merits, Judge Patel strongly suggested that she was concerned about several of the apparently oppressive terms in the agreement. Therefore, she allowed Napster the opportunity to conduct discovery on the issue.[46]

Specifically, Napster alleged that the MusicNet agreement effectively prevented Napster from ever entering into a license agreement with a non-MusicNet member.[47] First, the licensing agreement had a limited period of absolute exclusivity (through March 2002).[48] More important, Napster challenged section 19.1 of the Agreement, which provided that Napster could enter into a licensing agreement with a non-MusicNet distributor (*e.g.*, Sony or Universal) only through MusicNet itself.[49] Thus, if Napster wished to enter into a license agreement with Sony to use Sony's copyrighted music, it could only do so if MusicNet secured the license from Sony.[50] If MusicNet could not secure that license, Napster would be out of luck. *Moreover*, the MusicNet agreement provided that if Napster did attempt to enter into such an individual license with a non-MusicNet company, MusicNet could "terminate the agreement

43. *See id.* at *14.

44. *Id.*

45. *See id.* at *14–*16.

46. *See id.* at *21.

47. *See id.* at *14–*15.

48. *See In re* Napster Inc. Copyright Litig., No. MDL 00-1369, 2002 WL 482361, at *14 (N.D. Cal. Feb. 22, 2002).

49. *See id.*

50. *See id.*

with ninety-day notice."[51] Alternatively, MusicNet could charge Napster higher fees if it failed "to use MusicNet as its exclusive licensor for content."[52]

Facially, this provision is very problematic. Plaintiffs asserted that they anticipated reaching agreements with the other two non-MusicNet distributors—Sony and Universal. Having reached such agreements, they argued, Napster would be able to obtain licensing agreements through any major distributor, and consequently, there was no harm in requiring Napster to "ask permission from MusicNet."[53] Notwithstanding plaintiffs' arguments, Napster has a strong basis to contend that this provision unduly extends plaintiffs' valid copyrights.

As Judge Patel noted, "[t]he critical issue is that the agreement binds Napster to obtain licenses from MusicNet and not its competitors."[54] Section 19.1 seems to extend plaintiffs' copyrights beyond their original purpose. Those copyrights did not confer upon plaintiffs the right to foreclose Napster from entering into other licensing arrangements with other music companies. Given that the MusicNet companies do not control all music content, the agreement effectively could foreclose Napster from a significant portion of commercially available music (*i.e.*, that content from non-MusicNet distributors). Additionally, the agreement seems rather unseemly, as it allows MusicNet to be the ultimate arbiter of whether Napster could freely negotiate with non-MusicNet distributors of on-line music.

Plaintiffs made several arguments to support their position that Napster could not rely on the copyright misuse defense. First, they contended that MusicNet was an entity separate from plaintiffs, and as a result, plaintiffs were not responsible for the actions of the joint venture.[55] Although the court ultimately did not rule on this issue, Judge Patel suggested strongly that this argument was meritless, stating that "plaintiffs cannot hide behind the shell of a joint venture to protect themselves from misuse claims. The court views with great suspicion plaintiffs' claims of ignorance as to MusicNet's activities. Surely the three parties to MusicNet discussed their joint venture before entering into it."[56]

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51. *Id.*

52. *Id.*

53. *See id.* at *14–*15.

54. *In re* Napster Inc. Copyright Litig., No. MDL 00-1369, 2002 WL 482361, at *15 (N.D. Cal. Feb. 22, 2002).

55. *See id.* at *15–*16.

56. *Id.* at *15.

Plaintiffs also contended that even if they had engaged in copyright misuse, that should not excuse Napster's infringement. The alleged misuse, according to plaintiffs, did not occur during the time frame when the infringement occurred, and thus should not act as a bar to plaintiffs' suit.[57] Again, the court rejected that claim, noting that the doctrine of copyright misuse "does not prevent plaintiffs from ultimately recovering for acts of infringement that occur during the period of misuse. The issue focuses on when plaintiffs can bring or pursue an action for infringement," and plaintiffs cannot claim infringement while they are misusing their copyrights.[58] In other words, plaintiffs first would have to cure the offending licensing provisions before they could pursue their infringement claim.

B. Copyright Misuse Predicated on an Antitrust Violation

Alternatively, Napster claimed that even if section 19.1 of the MusicNet agreement did not violate public policy, plaintiffs' antitrust violations were sufficient to support Napster's copyright misuse defense.[59] Specifically, Napster alleged that the MusicNet agreement was anticompetitive and facilitated collusion.[60] Concluding that MusicNet and other agreements between plaintiffs "look bad, sound bad and smell bad," Judge Patel allowed Napster to conduct discovery to determine whether plaintiffs—through MusicNet and press*play*—engaged in horizontal price fixing, retail price squeezing, a refusal to deal, and exclusive dealing.[61]

Because the record was largely undeveloped at the time, Judge Patel only cursorily discussed Napster's antitrust claims.[62] However, Judge Patel noted that plaintiffs had failed to present any evidence that their MusicNet joint venture had any procedural protections in place to limit or preclude the possibility of price fixing.[63] According to the court: "[E]ven a naïf must realize that in forming and operating a joint venture, plaintiffs' representatives must necessarily meet and discuss pricing and licensing, raising the specter of possible antitrust

57. *See id.* at *16.

58. *Id.* (Judge Patel quoted *Lasercomb America, Inc. v. Reynolds*, 911 F.2d 970, 979 n.22 (4th Cir. 1990): "Lasercomb is free to bring suit for infringement once it has purged itself of the misuse.").

59. *See id.*

60. *See In re* Napster Inc. Copyright Litig., No. MDL 00-1369, 2002 WL 482361, at *16–*18 (N.D. Cal. Feb. 22, 2002).

61. *Id.* at *17.

62. *See id.* at *16–*18.

63. *See id.* at *18.

violations."[64] Napster was entitled to discovery, according to the court, to determine whether plaintiffs had in place any of the proper protections to ensure that the parties to the joint ventures did not engage in any illegal activity.[65]

C. *Plaintiffs' Unclean Hands Argument*

Because copyright misuse is an equitable doctrine, plaintiffs contended that a party with "unclean hands" like Napster cannot avail itself of the defense.[66] The court preliminarily disagreed.[67]

Like the law of copyright misuse itself, the contours of the unclean hands doctrine in a copyright misuse case also are unclear. Judge Patel noted that one Federal Circuit opinion interpreting Ninth Circuit law, *Atari Games Corp. v. Nintendo of America, Inc.*, recognized in passing that the "doctrine of unclean hands can . . . preclude the defense of copyright misuse."[68] However, Judge Patel also noted that the *Atari* decision did little to explain why the doctrine of unclean hands bars a misuse defense, and several other courts persuasively had reached the opposite conclusion.[69] Judge Patel thus preliminarily disregarded the *Atari* holding.

Instead, Judge Patel was persuaded by the Fifth Circuit decision in *Alcatel USA, Inc. v. DGI Technologies, Inc.*[70] In *Alcatel*, the Fifth Circuit concluded that the doctrine of unclean hands was not generally available to serve as a bar to the copyright misuse defense.[71] Where "plaintiffs seek equitable relief . . . then the defendant's improper behavior serves as no bar to its equitable defenses."[72] On the other hand, if the plaintiff seeks only legal relief, "the defendant's unclean hands may preclude it from advancing equitable defenses."[73] This distinction makes sense. According to Judge Patel,

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64. *Id.* at *17.

65. *See id.* at *21.

66. *See In re* Napster Inc. Copyright Litig., No. MDL 00-1369, 2002 WL 482361, at *18–*21 (N.D. Cal. Feb. 22, 2002).

67. *See id.* at *21.

68. *Id.* at *18 (quoting Atari Games Corp. v. Nintendo of Am., Inc., 975 F.2d 832, 846 (Fed. Cir. 1992)).

69. *See id.* at *19.

70. *See id.* (citing Alcatel USA, Inc. v. DGI Techs., Inc., 166 F.3d 772 (5th Cir. 1999)).

71. *See id.* (citing *Alcatel*, 166 F.3d at 794 n.92).

72. *In re* Napster Inc. Copyright Litig., No. MDL 00-1369, 2002 WL 482361, at *19 (N.D. Cal. Feb. 22, 2002) (quoting *Alcatel*, 166 F.3d at 794 n.92).

73. *Id.*

> [p]laintiffs used this court's open doors to obtain an injunction that eventually forced Napster to disable file-sharing entirely. Because plaintiffs have invoked this court's equitable powers (and it now appears that plaintiffs may have since sullied their hands with misuse), Napster should be entitled to assert equitable defenses. Once plaintiffs used equity as a sword to prevent Napster's continued infringement, they lost the right to employ the unclean hands bar to shield themselves from the consequences of their own potentially inequitable behavior.[74]

In addition, Judge Patel reasoned that the copyright misuse defense is meant to protect not only the private party asserting it, but also the public itself. Thus, "[i]n the interests of right and justice the court should not automatically condone the defendant's infractions because plaintiff is also blameworthy, thereby leaving two wrongs unremedied and increasing the injury to the public."[75] Judge Patel clearly was concerned about the harm that the seemingly troublesome conduct of the recording industry plaintiffs could do to competition and consumers; as a result, the court did not want Napster's misconduct to serve as a shield to allow the recording industry to harm consumers through agreements or collaborate activity that ran afoul of either the antitrust laws or public policy.[76] In the end, Judge Patel allowed Napster to conduct additional discovery because, if Napster's allegations find support in the facts, "plaintiffs are attempting the near monopolization of the digital distribution market."[77]

Thus, it appears that the battleground has shifted. This ruling from Judge Patel does put the recording industry on the defensive for the time being and creates a strong incentive for the plaintiffs to consider settlement. With a Justice Department inquiry looming, the recording industry has every reason to avoid a lengthy private investigation into its potentially anticompetitive practices.

IV. NAPSTER'S PROSPECTS GOING FORWARD

Going forward, Judge Patel does not have significant guidance as to whether the plaintiffs' actions rise to the level of copyright misuse. There are simply no cases with facts similar to those presented in the

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74. *Id.* (citations omitted).

75. *Id.* at *19 (quoting Republic Molding Corp. v. B.W. Photo Utils., 319 F.2d 347, 349–50 (9th Cir. 1963)).

76. *See id.* at *20.

77. *Id.*

Napster litigation. It is important to note that in all of the cases where a defendant successfully asserted the defense of copyright misuse, the license provision at issue drastically increased the scope of the copyright beyond that which was granted by the copyright originally. Thus, the issue for the court will be whether section 19.1 of the MusicNet agreement *substantially* extended the plaintiffs' valid copyrights. Napster must persuade Judge Patel that plaintiffs are using their copyrights to curtail competition. It will be important for Napster to demonstrate both that the *duration* and *breadth* of the agreement are excessive.

In this area, precedents are thin, but will nonetheless help guide the court's decision. Defendants have successfully asserted the defense only in a few instances, including those in which:

- The license restricted the licensee's ability to develop similar software, *for ninety-nine years, whether or not* the similar software was developed using the licensed technology (*e.g.*, reverse engineered), *or* developed independently;[78]
- The license restricted the licensee's ability to use competing products for the duration of the license; and[79]
- The license absolutely restricted the licensee's ability to develop products to compete with the licensor's uncopyrighted products that were related to the copyrighted licensed products.[80]

On the other hand, courts have rejected the copyright misuse defense in the following instances:

- The license prohibited the licensee from developing a product that competed with the licensed product where the licensee attempted to develop that product using reverse engineering (reasoning that it is acceptable to limit a licensee's ability to develop a competing product by copying the licensor's design);[81]
- The licensee had "unclean hands," thus prohibiting it from being able to raise the copyright misuse defense, which the court characterized as an equitable defense. The licensee had

78. *See* Lasercomb Am., Inc. v. Reynolds, 911 F.2d 970 (4th Cir. 1990).

79. *See* Practice Mgmt. Info. Corp. v. Am. Med. Ass'n, 121 F.3d 516 (9th Cir. 1997).

80. *See* Alcatel USA, Inc. v. DGI Techs., Inc., 166 F.3d 772 (5th Cir. 1999).

81. *See* Triad Sys. Corp. v. Southeastern Express Co., 64 F.3d 1330 (9th Cir. 1995).

lied to the Copyright Office to obtain licensor's copyrighted material;[82]

- The license prohibited, in *perpetuity*, use of certain licensed intellectual property to make a product that would compete with the licensed product. The court distinguished *Lasercomb*, which not only prohibited in perpetuity the development of a product based on knowledge learned from license, but also the *independent development* of a product that competed with the licensed product.[83]

Given precedent, Napster will have a difficult battle ahead, although not an impossible one. The MusicNet license is not exclusive for a significant duration and does not prohibit Napster from entering into license agreements with competing ventures, both facts that undermine Napster's misuse claim. However, several of the provisions of the MusicNet agreement do seem excessive, including the section that requires Napster to secure (through MusicNet only) other license agreements for digitally distributed music. This provision effectively requires Napster to seek permission from MusicNet to enter into competing distribution agreements. The agreement also grants MusicNet the right to terminate the agreement if Napster does sign up with a competing recording industry company. Finally, the agreement allows MusicNet to raise its fees if Napster enters into an arrangement with a competing company. Judge Patel likely will find this to be a *de facto* exclusive arrangement because its terms severely punish Napster if it attempts to enter into competitive agreements. Additionally, the agreement requires Napster to make a decision it should not have to make: to sign the agreement and give MusicNet the ability to dictate to Napster with whom the Company can obtain additional agreements for on-line music content, or not to sign the agreement and lose access to the music content owned by the MusicNet joint venture partners. Whether Napster will prevail clearly is an issue that requires additional discovery.

Napster's discovery likely will also yield significant evidence regarding the MusicNet and press*play* joint ventures. It will be interesting to see whether this discovery yields evidence that the parties—competitors in the music industry—have designed their joint ventures to adequately protect against antitrust risk. Although courts

82. *See* Atari Games Corp. v. Nintendo of Am., Inc., 975 F.2d 832 (Fed. Cir. 1992) (applying Ninth Circuit law).

83. *See* Syncsort Inc. v. Sequential Software, Inc., 50 F. Supp. 2d 318 (D.N.J. 1999).

and the government recognize that competitor collaborations "often are not only benign but procompetitive," such collaborations must take special care to protect against certain pitfalls.[84] Specifically, Napster's discovery should answer the following:

- Is the MusicNet venture open to all recording industry participants? If it is not, the court may conclude this is a boycott.[85]
- How restrictive is the venture? Does it repress alternative distribution channels? If it does, the court may conclude the venture unduly restrains competition.[86]
- Does the venture facilitate improper information exchange? Do the participants have access to competitively sensitive information such as pricing, customer lists, volume of sales, or discounts? Have the participants set up firewalls and taken other steps to limit the flow of such information? If the ventures' firewalls are porous, this would suggest, at a minimum, that the recording industry competitors/plaintiffs improperly share sensitive information, providing evidence of collusion in violation of Section 1 of the Sherman Antitrust Act.[87]

In the end, the plaintiffs may decide that it is in their best interest to settle this litigation, rather than to risk exposure associated with such sensitive discovery. With a pending investigation from the Department of Justice, plaintiffs have every incentive to close off one potential battlefront. Nevertheless, even if this litigation settles, Judge Patel's opinion provides a good legal framework as to how to analyze copyright misuse claims, and clearly sets forth the important

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84. FED. TRADE COMM'N & U.S. DEP'T OF JUSTICE, ANTITRUST GUIDELINES FOR COLLABORATIONS AMONG COMPETITORS (Apr. 2000) [hereinafter GUIDELINES], *reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,160 at 20,851–52 (2000) *and available at* http://www.ftc.gov/os/2000/04/ftcdojguidelines.pdf.

85. *Compare* Bascom Food Prods. Corp. v. Reese Finer Foods, Inc., 715 F. Supp. 616, 632 (D.N.J. 1989) (granting preliminary injunction because there was sufficient evidence to establish that there was a horizontal group boycott and that plaintiffs would be unable to compete in the relevant market without access to defendants' products) *with* United States v. Columbia Pictures Indus., 507 F. Supp. 412, 430–31 (S.D.N.Y. 1980) (agreement among motion picture companies forming pay television network joint venture to make movies available to the venture nine months before making them available to competing networks held facially unreasonable).

86. *See* GUIDELINES, 4 Trade Reg. Rep. at 20,861 ("In general, competitive concern is likely to be reduced to the extent that participants actually have continued to compete, either through separate, independent operations or through membership in other collaborations, or are permitted to do so.").

87. *See id.* at 20,853.

unanswered questions that the Ninth Circuit must one day finally confront.