



# P2P File-Sharing Network Liability for Infringement by their Users

William F. Adkinson, Jr.

March 12, 2004

## A. Introduction

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The last five years have seen an explosion in unauthorized and illegal distribution and copying of music, movies, games and other copyrighted digital content via the Internet (often called “file-sharing”). Peer-to-peer (P2P) file-sharing systems have played a central role in the explosion of Internet piracy. The Internet makes it easy to transfer copyrighted material in digital formats. P2P file-sharing systems combine millions of Internet users and their computers into networks over which files can easily be distributed and copied. Users can make files available for others on the system, and search tools make it easy for other users to find the files they want. Indeed, the file-sharing explosion was marked by the launch of P2P pioneer Napster in late 1999; by early 2001, Napster claimed over 70 million participants who were copying nearly three billion files per month – predominantly copyrighted music.<sup>1</sup>

Faced with unprecedented levels of piracy, the recording industry brought legal actions, ultimately obtained injunctions that led to the demise of Napster and of a similar file-sharing system, Aimster.<sup>2</sup> But new file-sharing systems immediately rose to take Napster’s place, and file-sharing continued to grow. The record and movie industries challenged these new systems, but

last April in the *Grokster* decision, they suffered a major setback as Judge Stephen Wilson held that two P2P file-sharing services, as currently designed, could not be held liable for infringements committed on their system.<sup>3</sup>

This paper examines the issues raised by these efforts to impose liability on P2P file-sharing systems. This controversy implicates conflicts between concerns that rampant Internet piracy may undermine creativity and concerns that innovation may be stifled if P2P file-sharing systems are held liable for the infringing conduct of their users.

## B. Secondary liability for copyright infringement

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This conflict arises largely because systems typically do not directly infringe on copyrights themselves. Their users do, by distributing and copying files over the system. Therefore, the content industries have sought to hold P2P systems liable based on theories of secondary liability – alleging that the P2P systems contribute to and profit from the infringing conduct of their users.

There are two main strands of secondary liability for copyright infringement (frequently blurred in the case law) – contributory infringement and vicarious liability. Generally “one who, with knowledge of the infringing activity, induces, causes or materially contributes to the infringing conduct of another, may be held liable as a ‘con-

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<sup>1</sup> See Todd Pack, *Pirating of Music Flourishes Despite Napster’s Unplugging*, ORLANDO SENTINEL, Sept. 7, 2001, at B1.

<sup>2</sup> *A&M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004, 1019 (9th Cir. 2001) (“Napster”); *In re Aimster Copyright Litigation*, 334 F.3d 643 (7th Cir. 2003) (“Aimster”).

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<sup>3</sup> *MGM Studios, Inc. v. Grokster, Ltd.*, 259 F. Supp. 2d 1029 (C.D. Cal., April 25, 2003).

tributory' infringer...."<sup>4</sup> Thus two elements must be shown – knowledge of the direct infringement and activity that materially furthers that infringement. Vicarious liability is generally imposed in “cases in which a defendant ‘has the right and ability to supervise the infringing activity and also has a direct financial interest in such activities.’”<sup>5</sup> Again there are two basic elements – the right and ability to supervise the infringing activity and a direct financial interest in it.

Secondary liability is an especially important tool in copyright enforcement. Often, those who facilitate or profit from infringement may be in the best position to prevent or police violations. And suing a multitude of individual direct infringers may be impractical or expensive, rendering copyright protection illusory. However, secondary liability can create disincentives to innovation and entrepreneurship. Generally products have legitimate uses as well as infringing ones, and liability may inhibit firms from beneficial pursuits. Indeed, the Supreme Court in *Sony Corp. of America v. Universal City Studios*<sup>6</sup> limited the circumstances in which liability for contributory infringement may be imposed on a firm simply because it provided a product that was used for infringement.

The conflict arises in part due to the misperception that lawsuits are directed against technologies generally, rather than the specific businesses and the manner in which they implemented the technology. Secondary liability need not be imposed in a blanket fashion. It may frequently be imposed based on particular conduct and remedies may be limited to avoid interfering with legitimate uses of a technology.

### C. Napster, Aimster and Grokster

Indeed, despite the considerable controversy surrounding *Napster*, the decision was unsurprising. Napster was designed to facilitate infringement by its users. The Napster business was built almost entirely around helping users find copyrighted music files. Napster knew that it was used predominantly for massive infringement. Its valuable user base was drawn predominantly by the opportunity it afforded to illegally pirate copyrighted works.<sup>7</sup>

And Napster could impede its users' infringing activity. Napster operated a central server that compiled lists of available files, performed searches, and provided users with file location information they could use to download files.<sup>8</sup> The remedy required Napster to filter out copyrighted files identified on its system.<sup>9</sup> Napster was free to facilitate the transfer of materials that were not copyrighted or for which distribution was authorized. Assuming that technologies for selectively eliminating access to infringing files were available, this relief seems well-tailored to protect copyright holders while enabling legitimate uses of Napster.

*Aimster* presented similar facts. The defendant largely tried to argue that it could not be held liable since the encryption system it used prevented it from having specific knowledge of its users' infringing activity. Judge Posner, affirming a grant of a preliminary injunction, dismissed this “ostrich-like” reliance on encryption, declaring that “[w]illful blindness is knowledge in copyright law.”<sup>10</sup> More generally, Judge Posner emphasized the importance of balancing of the benefits and burdens of imposing liability, endorsing a prag-

<sup>4</sup> Napster at 1019 (quoting *Gershwin Publ'g Corp. v. Columbia Artists Mgmt., Inc.*, 443 F.2d 1159, 1162 (2d Cir. 1971)).

<sup>5</sup> Napster at 1022 (quoting *Gershwin Publ'g Corp. v. Columbia Artists Mgmt., Inc.*, 443 F.2d 1159, 1162 (2d Cir. 1971)).

<sup>6</sup> 464 U.S. 417 (1984).

<sup>7</sup> Napster at 1022-24

<sup>8</sup> Napster at 1011-13.

<sup>9</sup> Napster at 1027.

<sup>10</sup> *Aimster* at 646, 650.

matic consideration of the relevant factors. He offered a colorful illustration:

A retailer of slinky dresses is not guilty of aiding and abetting prostitution even if he knows that some of his customers are prostitutes.... But the owner of a massage parlor who employs women who are capable of giving massages, but in fact as he knows sell only sex and never massages to their customers, is an aider and abettor of prostitution...<sup>11</sup>

Applying this realism, he dispatched Aimster's claims of possible noninfringing uses, finding that there was no "indication from real-life Aimster users that their primary use of the system" was noninfringing activity.<sup>12</sup> And even if substantial noninfringing uses are shown, Judge Posner emphasized that a P2P operator "must show that it would have been disproportionately costly for him to eliminate or at least reduce substantially the infringing uses."<sup>13</sup> But he similarly rejected the notion that "a single known infringing use brands the facilitator a contributory infringer."<sup>14</sup>

In *Grokster*, the content industry plaintiffs argued vigorously that the case was analogous to *Napster*. There was abundant evidence that the defendants' conduct was similar in key respects. They designed and ran their businesses to facilitate infringement, expressly marketing themselves to users as the principal replacements for Napster. They had extensive knowledge of the massive infringement taking place on their systems.

They also designed the systems to enhance users' ability to hide their infringing behavior. KaZaA has even sought to prevent the recording industry from using FastTrack software to identify infringing activity on that system.<sup>15</sup> And they profit from the user base drawn overwhelmingly by the opportunity to obtain copyrighted works for free, largely by receiving money for including "spyware" and other programs with their P2P file-sharing software.<sup>16</sup>

On the other hand, when one limits attention to the operation of defendants' current systems, as Judge Wilson did, the analogy to *Napster* weakens appreciably. The FastTrack and Gnutella software, by design, results in far more decentralized systems than Napster's. By the time the decision was rendered, file-sharing on the system was conducted mainly through users' computers. The KaZaA software designates certain users' computers to act as "supernodes" that collect information and streamline searches. Grokster's gnutella-based software passes search requests from user to user.<sup>17</sup>

As a result, Judge Wilson found that that this was a "seminal distinction": unlike Napster these defendants did not provide the "sites and facilities for direct infringement" or "infrastructure' for file-sharing" that Napster had afforded its users.<sup>18</sup> Instead, they merely provided software that could be used for infringing or noninfringing purposes. Moreover, he reasoned that there should be no liability if defendants can't do anything to "stop ... their users' infringing activity," once they distributed the software.

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<sup>11</sup> Aimster at 651.

<sup>12</sup> Aimster at 653.

<sup>13</sup> Aimster at 653.

<sup>14</sup> Aimster at 651.

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<sup>15</sup> Jon Healey, *Kazaa Owner Cleared to Sue Record Labels, Movie Studios*, L.A. TIMES, Jan. 23, 2004, at C1.

<sup>16</sup> David Kirkpatrick & Christopher Tkaczyk, *Taking Back the Net*, FORTUNE, Sept. 29, 2003, at 117.

<sup>17</sup> Grokster at 1039-43.

<sup>18</sup> Grokster at 1041, 1042.

## D. *Grokster*: A Critique

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Judge Wilson's reasoning suffered from several serious flaws, which can be highlighted by contrasting it with Judge Posner's approach.

First, he brushed aside the defendants' course of conduct in facilitating infringement, looking only at the operation of the current systems once software was distributed. Similarly, he paid little heed to the dominance of infringing uses, and how the defendants were intentionally profiting from the user base that piracy attracted. Judge Posner, in contrast, insisted on evaluating defendants' conduct as a whole and the significance of noninfringing uses in his analysis. (Judge Wilson himself recognizes that defendants' past conduct could render them secondarily liable for damages caused by infringements on their systems, expressly reserving the question.)

Second, Judge Wilson emphasized the limits on defendants' knowledge and ability to prevent infringement. But these were the result of defendants' choices. Indeed, he recognized "the possibility that Defendants may have intentionally structured their businesses to avoid secondary liability for copyright infringement system, while benefiting financially from the illicit draw of their wares."<sup>19</sup> But this did not affect his decision.

Judge Posner scoffed at the suggestion that defendants could avoid liability in this fashion. Of course, if P2P file-sharing systems (or others who facilitate piracy) can avoid liability by simply shielding themselves from knowledge of the activity, they will do so. Honoring such evasions is not sound policy and undermines an important tool for copyright enforcement. It is especially problematic where, as here, the defendants' systems are used predominantly for facilitating infringement on a massive scale. Permitting com-

panies to serve noninfringing users, perhaps in ways that are yet to be developed, is important.

Third, Judge Wilson ignored, or ruled "immaterial," the potential for defendants to exercise control over their users' infringing conduct by making the software "less susceptible to unlawful use."<sup>20</sup> This discounts potential remedies that, while imperfect, could greatly reduce the costs imposed by Internet piracy.

This contrasts with Judge Posner's insistence on broadly considering potential remedies, and in particular his observation that P2P systems should be required to adopt protection measures that are not "disproportionately costly." Sound policy will depend on finding remedies that reflect an appropriate weighting on the competing interests. This can be a daunting task; potential solutions like modifying the underlying software should not be ruled out of bounds. Resolving these issues may be difficult, because the parties have incentives to exaggerate the ease or difficulty associated with protective measures. Failing such a resolution, a harder choice may be faced – whether to adopt a remedy that may effectively shut down a system.

## E. The Policy Considerations

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So let us address the competing policy concerns directly. The content industries claim that, if left unrestrained, infringing activity on P2P systems will dramatically undermine their ability to sell or rent their copyrighted works. They have made such dire predictions regarding the impact of analog technologies before that were not borne out.

However, in the digital environment, predictions of massive uncontrolled piracy are far more plausible. The rise of music file-sharing over P2P networks over the past five years certainly sug-

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<sup>19</sup> *Grokster* at 1046.

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<sup>20</sup> *Grokster* at 1046.

gests that P2P networks are having a dramatic impact on illegal copying. The results could be devastating to the music industry and to the movie industry (especially to the revenues from home viewing of movies).

Of course, content providers are not entitled to earn a profit or to preserve their particular business models. But they are entitled to protection of their ability to earn a return on the rights created by the copyright laws. This is essential for the copyright laws to serve their fundamental purpose of providing incentives for creativity.

Holding P2P file-sharing systems secondarily liable would appear appropriate, even necessary, to make copyright protection a reality on the Internet. While the record industry has brought actions against some individuals using P2P file-sharing systems, there are obvious limits to this approach. In this regard, Judge Posner quotes Randal Picker to good effect: “Chasing individual consumers is time consuming and a teaspoon solution to an ocean problem.”<sup>21</sup>

On the other hand, would granting relief against the *Grokster* defendants retard innovation and offend the policies in *Sony*? That depends on the significance of noninfringing benefits from these file-sharing applications. In this regard, it is important to keep in mind that the focus is not on the technology per se, but the particular products and businesses created and implemented by the defendants.

The defendant’s systems, as presently designed, provide relatively efficient means for non-commercial distribution and copying of files over the Internet. Search tools save on information costs. The systems also save on central system resources by harnessing the bandwidth, storage

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<sup>21</sup> Aimster at 645 (quoting Randal C. Picker, *Copyright as Entry Policy: The Case of Digital Distribution*, ANTITRUST BULLETIN 47, 2002, 442).

capacity and computing capacity of the system users.

But they are inefficient means of commercial economic distribution, since they are poorly suited to ensuring that sellers receive compensation. Indeed, they are used predominantly to traffic in commercially available files, precisely in order to avoid having to make such payments. In contrast, authorized online distributors employ systems designed to require users to observe certain formalities – like paying for a download.

Over the past year, there has been a proliferation of authorized online distribution services. But P2P file-sharing systems undermine the development of such alternatives. Commercially distributed files are likely to make their way on to P2P systems and be available for free, drawing customers from authorized outlets. Indeed, transfers of commercially available files on P2P systems dwarfs the traffic over the servers of authorized dealers.

P2P file-sharing systems can be used for legitimate file-sharing purposes, like the distribution of unprotected works or those for which free distribution is authorized. But at present, the noninfringing uses are small relative to the level of Internet piracy on these systems. Overall, is questionable how much weight should be given to protecting current benefits from the innovations offered by P2P file-sharing systems.

Of course, noninfringing uses of P2P file-sharing systems are likely to be further developed over time. Predicting such developments is impossible – that’s why the successful entrepreneurs earn large returns. But for our purposes, it does mean that liability and especially remedies should be carefully tailored to deal effectively with the piracy problem but leave adequate room for the development of noninfringing uses. I conclude with a consideration of possible remedies.

## F. Remedies

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Recently, attention has been focused on the potential for modifying the system and the software to enable P2P file-sharing systems to monitor and police infringements.<sup>22</sup> Several questions are central to an evaluation of such remedies. First, to what extent would they effectively protect content from infringement? Would they need to be updated either to respond to hacks or to update information? Is it possible to force upgrades or modified software on the many millions of users who have already downloaded P2P file-sharing software? How expensive and difficult would it be for operators of P2P file-sharing services to implement and maintain them? What would be the costs and benefits? Will there be a need for continuing judicial scrutiny to ensure compliance?

Attention has focused on one possible software modification -- including filtering features that would identify copyrighted works and impede their transfer. The P2P file-sharing systems and content industries vigorously disagree regarding the efficacy and feasibility of such approaches. This is an especially hard question to answer in light of the sharp divergences of interest and the potential for innovations to make the impossible commonplace.

Such a solution would have to be evaluated based on its feasibility and the costs it imposes on P2P file-sharing systems, as well as the benefits to copyright owners. If it is possible to police infringement in this manner, secondary copyright liability is a potentially attractive option. It can provide protection for content while still permitting noninfringing uses. Indeed, this approach was adopted in designing the *Napster* remedy.

Apart from technical feasibility, the P2P systems argue that they cannot implement such a solution. But they have the ability to exercise control over the design of the software they used, either by designing it directly or by choosing the software they offer. Similarly, they have insisted that they cannot exercise any control once the consumer has received the software (apparently also a function of design choices they and KaZaA made). But KaZaA reportedly disconnected all of the StreamCast users from the FastTrack system, after a royalty dispute arose.<sup>23</sup> This suggests that KaZaA can exercise substantial control over software held by its existing user base.

Ultimately, the remedy issues are perhaps the most important but least well-developed in the case. I would tentatively favor a remedy along the lines of the *Napster* injunction -- requiring that defendants filter out or otherwise protect identified copyrighted works. This would require a detailed consideration of feasibility and cost issues. Hopefully the Ninth Circuit will direct Judge Wilson and the parties to focus on adopting a cost-effective solution for policing the illegal traffic in copyrighted files over P2P file-sharing networks.

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<sup>22</sup> Drew Clark, *Intellectual Property: Recording Industry, File-sharing Firms; Feud Over Technology*, NAT'L J. TECH DAILY, January 28, 2004.

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<sup>23</sup> See Roger Parloff, *The Real War Over Piracy: From Betamax to Kazaa*, FORTUNE, Oct. 27, 2003, at 148.