

GATEKEEPERS, PIGGYBACKERS, AND FREELOADERS: COPYRIGHT INFRINGEMENT IN MULTISIDED MARKETS

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Draft of January 2006

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Many, if not most, copyright cases of indirect liability for copyright infringement arise in multisided markets: One of the litigating parties is a market intermediary that connects members of different distinct groups. Such intermediaries are commonly known as platforms. Thus far, courts and scholars have not identified the prevalence of platforms in cases of indirect liability for copyright infringement. As a result, despite the passionate debate over the impact of alleged indirect infringers on the interests of copyright holders and on relevant industries, the actual economic functioning of these market participants has been mischaracterized. This Article examines the present common forms of multisided markets in which copyrighted works are traded and identifies three generic types of alleged indirect infringers: gatekeepers, piggybackers, and freeloaders. Gatekeepers are market intermediaries that are in the position to disrupt copyright infringement by withdrawing cooperation from infringers. Piggybackers offer parties that connect through a platform certain services and charge them for these services. Piggybackers' services may circumvent the platform and decrease its value, but may also enhance the platform's performance and increase its value. Freeloaders operate a platform whose operation costs are externalized to third parties. The existing literature has focused on gatekeepers and has downplayed the differences across various alleged indirect infringers. This Article refines the characterization of alleged indirect copyright infringers and presents several legal and policy implications related to the justifications for the imposition of indirect liability for copyright infringement, the applicability of present law, the controversial "substantial noninfringing use" test, product design, and the Digital Millennium Copyright Act. The Article further shows how the presented analytical framework is consistent with the traditional analysis of copyright cases.

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INTRODUCTION

Many, if not most, copyright cases of indirect liability for copyright infringement arise in multisided markets: One of the litigating parties is a market intermediary that connects members of different distinct, groups. Such intermediaries are commonly known as *platforms*.¹ Platform systems are subspecies of networks but unlike generic

¹ In economics literature, multisided markets are often referred to as “platform markets.” For accessible introductions to platform economics, see David Evans, *The Antitrust Economics of Multi-Sided Platform Markets*, 20 YALE J. REG. 325 (2003); David S. Evans & Richard Schmalensee, *The Industrial Organization of Markets with Two-Sided Platforms*, NBER Working Paper Series No. 11603 (Sep. 2005). For prominent works on the properties of platform markets, see Bernard Caillaud & Bruno Jullien, *Chicken & Egg: Competition Among Intermediation Service Providers*, 34 RAND J. ECON. 309 (2003); Jean-Charles Rochet & Jean Tirole, *Platform Competition in Two-Sided Markets*, 1 J. EUR. ECON. ASS’N. 990 (2003). See also DANIEL F. SPULBER, MARKET MICROSTRUCTURE: INTERMEDIARIES AND THE THEORY OF THE FIRM

networks, such as email and telephone networks, that connect members of the same group, platforms connect members of different distinct groups.² To illustrate, in *Sony v. Universal City Studios*,³ television channels connected owners of copyrighted television programs, audiences, and advertisers. VCR Manufacturers sold equipment that enabled audiences to tape television shows and to skip commercials. The copyright holders sued VCR manufacturers, among other grounds, for undermining the audience-advertisers connection by enabling VCR users to skip commercials with the fast-forward button. In *A&M Records v. Napster*⁴ and in *Metro-Goldwyn-Mayer Studios v. Grokster*,⁵ file-sharing services established networks of users who swapped copyrighted files and connected (or planned to connect) these networks of users to advertisers from whom they collected (or planned to collect) revenues.⁶ Copyright owners sued these file-sharing services for facilitating copyright infringement by their users. Traditional brick-and-mortar retailers that connected concessionaires and shoppers were held vicariously liable for sales of bootleg recordings by the concessionaires.⁷ Flea-market operators that facilitated interactions between vendors and shoppers were found liable for sales of counterfeit recordings by vendors.⁸ In the e-commerce era, *eBay.com* and *Amazon.com* connect buyers and sellers and have been sued for indirect copyright infringement due to copyright infringement engaged by some sellers.⁹ In the same fashion, dance halls,¹⁰

(1999); *Conference on Two-Sided Markets*, 2005 COLUM. BUS. L. REV. 509 (2005).

² For a comprehensive survey of network economics, see Joseph Farrell & Paul Klemperer, *Coordination and Lock-In: Competition with Switching Costs and Network Effects*, in 3 HANDBOOK OF INDUSTRIAL ORGANIZATION (forthcoming).

³ 464 U.S. 417 (1984).

⁴ 239 F.3d 1004 (9th Cir. 2001).

⁵ 125 S.Ct. 2764 (2005).

⁶ Napster was sued during its penetration stage in which it collected no revenues. Its potential revenue sources included various forms of advertising and marketing to its users. *A&M Records, Inc. v. Napster, Inc.*, 114 F.Supp.2d 896, 902 (N.D. Cal. 2000). *Grokster* and *StreamCast* took advantage of Napster's fallout, had a very short penetration stage, and started collecting revenues from advertisers soon after it launched its platform. *Grokster*, • U.S. at •.

⁷ *Shapiro, Bernstein & Co., Inc. v. H. L. Green Co., Inc.*, 316 F. 2d 304, 308 (2d Cir. 1963);

⁸ *Fonovisa, Inc. v. Cherry Auction, Inc.*, 76 F. 3d 259 (9th Cir. 1996). See also *Hard Rock Cafe Licensing Corp. v. Concession Services, Inc.*, 955 F.2d 1143 (7th Cir. 1992) (holding that a flea-market operator may be

liable for trademark infringements of vendors).

⁹ See, e.g., *Hendrickson v. eBay, Inc.*, 165 F.Supp.2d 1082 (C.D. Cal. 2001); *Hendrickson v. Amazon.Com, Inc.*, 298 F.Supp.2d 914 (C.D. Cal. 2003); *Corbis Corp. v. Amazon.com, Inc.*, 351 F.Supp.2d 1090 (W.D. Wash. 2004).

¹⁰ See, e.g., *Dreamland Ball Room, Inc. v. Shapiro, Bernstein & Co.*, 36 F.2d 354 (7th Cir. 1929); *KECA Music, Inc. v. Dingus McGee's Co.*, 432 F.Supp. 72 (D.C.Mo. 1977). Cf. *Deutsch v. Arnold*, 98 F.2d 686 (2d Cir. 1938) (holding that a landlord who leased premises to a direct infringer for a fixed rental and did not participate directly in any infringing activity was not liable for contributory infringement).

clubs,¹¹ and concert promoters¹² that connected audiences with singers, music bands, and orchestras that played unauthorized copyrighted compositions were held liable as indirect infringers. In the days of the silent motion pictures, some exhibitors who connected movie distributors, moviegoers, and musicians who played music during show times, were found liable for unauthorized performances of copyrighted compositions by the musicians.¹³ These examples are offered to provide some anecdotal evidence for the prevalence of multisided markets in cases of alleged indirect liability for copyright infringement. The list could have been extended much further.

Indirect liability, or third-party liability, is often sought to be imposed on a party who is not the most-immediate wrongdoer.¹⁴ It is imposed for facilitating the wrongdoing and, in certain circumstances, for not exercising the power to deter wrongdoing or the power to force internalization of the costs of wrongdoing. Indirect liability, although controversial in certain contexts, is imposed in all areas of the law.¹⁵ Arguments in favor of indirect liability for copyright infringement have traditionally relied on practical convenience: The relative ineffectiveness of enforcement against direct infringers, the relative low enforcement costs for the third party, and the third party ability to eliminate infringement opportunities.¹⁶ For example, in *Grokster*, Justice Souter, writing for the Court, noted:

When a widely shared service or product is used to commit infringement, it may be impossible to enforce rights in the protected work effectively against all direct infringers, the only practical alternative being to go against the distributor of the copying device for secondary liability on a theory of contributory or vicarious infringement.¹⁷

¹¹ See, e.g., *Shapiro, Bernstein & Co. v. Veltin*, 47 F.Supp. 648 (W.D.La.1942); *M. Witmark & Sons v. Tremont Social and Athletic Club*, 188 F.Supp. 787 (D.Mass.1960).

¹² *Gershwin Publishing Corp. v. Columbia Artists Management, Inc.* 443 F. 2d 1159 (2d Cir. 1971).

¹³ See, e.g., *Harms et al. v. Cohen*, 279 Fed. 276 (E.D. Pa. 1922); *M. Witmark & Sons v. Pastime Amusement Co.*, 298 F. 470 (D.C.S.C. 1924).

¹⁴ See generally Reinier H. Kraakman, *Gatekeepers: The Anatomy of a Third-Party Enforcement Strategy*, 2 J. L. ECON. & ORG. 53 (1986); Reinier Kraakman, *Third-Party Liability*, in THE PALGRAVE DICTIONARY OF ECONOMICS AND THE LAW vol. 3, 583 (1998).

¹⁵ *Sony*, 464 U.S., at 435. Cf. The Protection of Lawful Commerce in Arms Act of 2005 (shielding firearms manufacturers and dealers from liability for crimes committed by others with their products).

¹⁶ Douglas Lichtman & William Landes, *Indirect Liability for Copyright Infringement: An Economic Perspective*, 16 HARV. J. L. & TECH. 395, 396 (2003) (“the argument in favor of [indirect] liability is that third parties are often in a good position to discourage copyright infringement either by monitoring direct infringement or [by] redesigning their technologies to make infringement more difficult.”); William Landes & Douglas Lichtman, *Indirect Liability for Copyright Infringement: Napster and Beyond*, 17 J. ECON. PERSP. 113 (2003).

¹⁷ *Grokster*, ● U.S. at ●. See also *in re Aimster Copyright Litigation*, 334 F.3d 643, 645-56 (7th

Thus far, courts and scholars have not identified the prevalence of platforms in cases of indirect liability for copyright infringement.¹⁸ As a result, despite the passionate debate over the impact of alleged indirect infringers on the interests of copyright holders and on relevant industries, the actual economic functioning of these market participants has been mischaracterized. This Article examines the present common forms of multisided markets in which copyrighted works are traded and identifies three generic types of alleged indirect infringers: *gatekeepers*, *piggybackers*, and *freeloaders*. A *gatekeeper* is a market intermediary that is in the position to disrupt copyright infringement by withdrawing cooperation from infringers.¹⁹ Internet service providers (ISPs) are a prime example of gatekeepers.²⁰ A *piggybacker* offers parties that connect through a platform certain services and charges them for these services. As discussed below, services offered by piggybackers may circumvent the platform and decrease its value, but may also enhance the platform's performance and increase its value. Examples of piggybackers include sellers of "advertising removers" that lower the platform's value and providers of videogame enhancers that may increase the platform's value. A *freeloader* operates a platform whose operation costs are externalized to third parties. A prime example of freeloaders is file-sharing services that attract users through facilitation of almost a costless trade in copyrighted works while infringing copyrights of others.

The existing literature has focused on gatekeepers and has downplayed the differences across various alleged indirect infringers. This Article refines the characterization of alleged indirect copyright infringers and presents several legal and policy implications related to the justifications for the imposition of indirect liability for copyright infringement, the applicability of present law, the controversial "substantial noninfringing use" test, product design, and the Digital Millennium Copyright Act. The Article further shows how the presented analytical framework is consistent with the traditional analysis of copyright cases.

The plan of this paper is as follows. [TBC]

Cir. 2003) (J. Posner):

Recognizing the impracticability or futility of copyright owner's suing a multitude of individual infringers ... the law allows a copyright holder to sue a contributor to the infringement instead, in effect as an aider or abettor. ... If a breach of ... a copyright license ... can be prevented most effectively by actions taken by a third party, it makes sense to have a legal mechanism for placing liability for the consequences of the breach on him as well as on the party that broke the contract.

¹⁸ Alleged indirect liability for copyright infringement may arise when platforms are not involved. See, e.g., *Universal Pictures Co. v. Harold Lloyd Corp.*, 162 F.2d 354, 365-366 (9 Cir. 1947) (finding a screenwriter who provided his employer with copyrighted materials of his former employer liable for contributory infringement).

¹⁹ Kraakman, at 53.

²⁰ See Assaf Hamdani, *Who's Liable for Cyberwrongs?*, 87 CORNELL L. REV. 901 (2002).