

SECONDARY LIABILITY FOR TRADEMARK AND COPYRIGHT INFRINGEMENT

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As intellectual property owners attempt to enforce their trademarks and copyrights against Internet-based infringers, they are increasingly seeking to impose liability on parties other than the direct infringers. The direct infringers can be hard to catch. Direct infringers that sell counterfeit or other infringing products on the Internet can easily avoid liability. They can easily mask their identities. They can conduct business worldwide from a distant country. They can shut down and reopen under a different domain name with ease. They move their sites to different hosting services in different countries throughout the world. Moreover, the sheer number of such sites can make it impractical or extraordinarily expensive to attempt to shut them down. As a result, intellectual property owners have turned to attempting to impose liability on other parties that have some involvement in transactions involving counterfeit or infringing products, such as search engines involved in selling key words used by the direct infringers, auction sites that facilitate transactions involving infringing products, and credit card companies involved in processing payments for such products.

In an effort to impose liability on these participants in ecommerce, intellectual property owners rely on common law tort principles of secondary liability: vicarious liability and contributory liability. Vicarious liability imposes strict liability on a party because of the party's relationship with the direct infringer. At common law, vicarious liability is established when: (1) the third party has the right and ability to control the actions of the direct infringer; and (2) the third party derives a direct financial benefit from the infringement. One example of strict liability is the liability of an employer for the tortious conduct of its employee. In contrast, contributory liability imposes liability on a third party that acts in concert with or provides assistance or encouragement to the direct infringer. At common law, contributory liability is established when: (1) the defendant knows of the infringement; and (2) the defendant materially contributes to or induces the infringement. Contributory infringement is based on tort law principles of enterprise liability and imputed intent, while vicarious infringement is based on agency principles of *respondeat superior*. Both forms of liability require proof of an underlying direct infringement claim.¹

¹ To establish direct copyright infringement, a plaintiff must show: (1) ownership of a valid copyright, and (2) violation of an exclusive right under 17 U.S.C. § 106. To establish direct trademark infringement, a plaintiff must show: (1) ownership of a valid trademark, and (2) a likelihood of confusion resulting from a defendant's alleged infringing use. 15 U.S.C. § 1114; *Applied Info. Sciences Corp. v. eBay, Inc.*, 511 F.3d 966, 972 (9th Cir. 2007).

Courts do not strictly follow the common law standards for secondary liability. The standards have changed as the courts have grappled with applying the standards to new technologies and new business methods. Moreover, courts do not apply the tests for vicarious infringement and contributory infringement in trademark cases the same way the courts apply the standards in copyright cases. The test for contributory trademark infringement is narrower and more difficult to satisfy than the comparable test for copyright infringement. *Hard Rock Cafe Licensing Corp. v. Concession Services, Inc.*, 955 F.2d 1143, 1150, 21 U.S.P.Q.2d 1764 (7th Cir. 1992) (“[T]he Supreme Court tells us that secondary liability for trademark infringement should, in any event, be more narrowly drawn than secondary liability for copyright infringement.”); *Perfect 10, Inc. v. Visa Intern. Service Ass’n*, 494 F.3d 788, 806, 83 U.S.P.Q.2d 1144 (9th Cir. 2007), *cert. denied*, 128 S. Ct. 2871 (U.S. 2008) (“The tests for secondary trademark infringement are even more difficult to satisfy than those required to find secondary copyright infringement.”). The rationale for applying different standards in the trademark and copyright contexts is not evident in the case law.

This article explores the standards for secondary liability in the context of the Internet, with a focus on how courts have applied the standards in cases against third parties that play some role in ecommerce transactions involving the advertising or sale of counterfeit or infringing products, including internet service providers (ISPs), auction sites, search engines and credit card companies, but which engage in substantial business that does not involve such transactions. This article also will not address liability for business models that have been held to thrive on direct infringement, such as peer-to-peer music sharing sites. This article will also not address statutory safe harbors, such as under the Digital Millennium Copyright Act.

I. Overview Of Vicarious Infringement

Vicarious infringement attaches based on the nature of the relationship between the direct infringer and the accused secondary infringer and on the secondary infringer’s financial benefit from the infringement.

A. The Nature of the Relationship: Right and Ability to Supervise

In copyright cases, a party can only be held vicariously liable for infringement if it has the right and ability to supervise the infringing activity (coupled with a direct financial interest in the infringement). In trademark cases, there is a much stricter standard for vicarious liability. A party must prove evidence of a specific principal-agent relationship (coupled with a direct financial interest in the infringement). A principal-agent relationship exists only if “the defendant and the direct infringer have an apparent or actual partnership, have authority to bind one another in transactions with third parties, or exercise joint ownership or control over the infringing product.” *Hard Rock*, 955 F.2d at 1150. Thus, the accused secondary infringer’s mere ability to control the direct infringer is not enough in trademark cases.

B. Financial Benefit

In trademark cases, to establish the direct financial benefit necessary for vicarious liability, there must be actual profit sharing between the direct infringer and the party charged

with vicarious infringement. In *Hard Rock*, the owner of the Hard Rock trademark sued the owner of a flea market for contributory and vicarious liability, contending that the owner was vicariously liable for trademark infringement by a t-shirt vendor selling counterfeit HARD ROCK t-shirts. The Seventh Circuit suggested that only actual profit sharing between the flea market owner and the t-shirt vendor would establish the financial benefit necessary to prove vicarious infringement. The fact that the t-shirt vendor paid a fee to the flea market owner or attracted customers to the flea market was not sufficient.

To establish financial benefit in copyright cases, there is no requirement that the party charged with vicarious liability *directly* financially benefit from the infringement. In *Fonovisa, Inc. v. Cherry Auction, Inc.*, 76 F.3d 259 (9th Cir. 1996), a copyright owner sued the owner of a flea market for vicarious liability arising from the sale of infringing recordings by a vendor at the flea market. The flea market owner generated revenue from concession stand fees from the vendor and parking and admission fees from customers. The Ninth Circuit held that the flea market owner was vicariously liable for copyright infringement, because the vendor's activities lured customers to the flea market, thereby increasing the flea market's revenues. Thus, the Ninth Circuit imposed liability even though the flea market did not directly profit from the sale of the infringing recordings.

In short, vicarious liability in trademark cases requires a close relationship and profit sharing between the direct infringer and the accused secondary infringer, while vicarious liability in copyright cases requires only the right and ability to supervise the infringer and indirect profit from the infringement.

II. Overview of Contributory Infringement

At common law, contributory infringement attaches when the accused secondary infringer knows or has reason to know of the direct infringement and materially contributes or intentionally induces the direct infringement.

A. Knowledge

The knowledge requirement differs depending on whether goods or services are involved. The Supreme Court has held that, with respect to goods: “[I]f a manufacturer or distributor intentionally induces another to infringe a trademark, or if it continues to supply its product to one whom it knows or has reason to know is engaging in trademark infringement, the manufacturer or distributor is contributorily responsible for any harm done as a result of the deceit.” *Inwood Labs., Inc. v. Ives Labs., Inc.*, 456 U.S. 844, 855 (1982). Thus, actual or constructive knowledge may suffice. Actual knowledge exists where it can be shown that the accused secondary infringer actually knew of specific instances of direct infringement. *See A & M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004, 1020 (9th Cir. 2001). Constructive knowledge exists where it can be shown that the accused secondary infringer should have known of the direct infringement. *Id.* When the alleged direct infringer supplies a service rather than a product, under the second prong of this test, there must be “[d]irect control and monitoring of the instrumentality used by a third party to infringe the plaintiff's mark.” *Lockheed Martin Corp. v. Network Solutions, Inc.*, 194 F.3d 980, 984 (9th Cir.1999).

In copyright cases, the actual knowledge requirement is different. Mere knowledge is not enough. In *Sony Corp. v. Universal City Studios*, 464 U.S. 417 (1984) the Supreme Court did not impose contributory liability where a "staple article of commerce" used in infringement possessed "substantial noninfringing uses." Thus, when a product (in this cases, a Betamax) is capable of both substantial infringing and noninfringing uses, defendant's mere knowledge of the product's infringing use is not sufficient to establish contributory copyright infringement. However, as discussed below, this safe harbor has been limited in cases in which the secondary infringer distributes a product with the object of promoting its use to infringe copyrights. See *MGM Studios, Inc. v. Grokster*, 125 S. Ct. 2764 (2005).

2. Material Contribution or Inducement

The standard for material contribution in trademark cases is somewhat ill-defined. Courts historically only held manufacturers and distributors of infringing products liable for contributory infringement. However, the generally accepted standard is that, if the defendant had *direct control or monitoring* of the instrumentality used by the third party to infringe the plaintiff's mark, contributory infringement may arise. *Lockheed Martin v. Network Solutions*, 134 F.3d 980 (9th Cir. 1999). The amount of control is typically the key issue in determining liability for contributory infringement.

However, the standard is lower in copyright cases. Contributory infringement requires the defendant to engage "in personal conduct that encourages or assists the infringement." *A & M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004, 1019 (9th Cir. 2001). In *Grokster, Ltd.*, the Supreme held that "[o]ne infringes contributorily by intentionally inducing or encouraging direct infringement." 545 U.S. 913, 930, 781 (2005). There are two branches: (1) actively encouraging or inducing infringement through specific acts; or (2) distributing a product distributees use to infringe copyrights, if the product is not capable of 'substantial' or 'commercially significant' noninfringing uses." *Id.* at 942. The defendant's active inducement of infringement trumps the *Sony* defense. Active inducement exists if the defendant distributes that product "with the object of promoting its use to infringe copyright." *Id.*

Merely knowing of the existence of infringing material on the accused secondary infringer's system and failing to take action to remove can be enough. Where "a computer system operator learns of specific infringing material available on his system and fails to purge such material from the system, the operator knows of and contributes to direct infringement." *Id.* at 1022; *Perfect 10 v. Amazon.com, Inc.*, 508 F.3d 1146, 1172 (9th Cir. 2007) (computer system operators can be liable where, knowing that specific infringing materials are present on their systems and able to take "simple measures" to limit infringement, they continue to provide access to the infringing materials).

III. Secondary Liability of Internet Service Providers

In *Louis Vuitton Malletier, S.A. v. Akanoc Solutions, Inc.*, an unpublished case in the San Jose Division of the United States District Court for the Northern District of California, Louis Vuitton sued web hosting companies and their owner for knowingly allowing and encouraging

certain websites to use defendants' services for infringing Louis Vuitton's trademarks and copyrights. Louis Vuitton found that the defendants were hosting web sites selling counterfeit Louis Vuitton goods. After sending defendants several notices concerning these web sites, the sites either remained operable or were moved to different IP addresses owned by defendants. Discovery uncovered several internal communications regarding the complaints from Louis Vuitton and the need to disable the sites.

Defendants moved for summary judgment on the secondary liability claims. However, the court granted the defendants' motion for summary judgment on the vicarious liability claims. With respect to vicarious copyright infringement, the district court held that there was no evidence that the defendants had any direct financial interest in the underlying infringement. With respect to the vicarious trademark infringement claims, the district court held that there was no evidence that the defendants had an apparent or actual partnership with the direct infringers. The district court held that there were genuine issues of material fact regarding the contributory infringement claims and these claims proceeded to trial along with direct infringement claims.

On August 28, 2009, after a jury trial on the merits, the jury returned a verdict in favor of the Louis Vuitton. The jury found that the defendants engaged in contributory trademark and copyright infringement as well as direct trademark and copyright infringement. The jury found that the defendants knew or should have known that its customers were infringing Louis Vuitton's trademarks and copyrights and that the defendants had reasonable means to withdraw its services so that its services could not be used to infringe. The jury awarded \$31 Million in damages on the trademark and copyright claims. Interestingly, the jury verdict form posed the questions regarding liability for contributory trademark and contributory copyright infringement, even though the standards for establishing infringement are different.

IV. Secondary Liability of Auction Sites

In *Tiffany (NJ), Inc. v. eBay, Inc.*, 576 F. Supp. 2d 463 (S.D.N.Y. 2008), Tiffany sued eBay for direct and contributory trademark infringement and dilution, among other claims, on the grounds that eBay facilitated and allowed counterfeit Tiffany products to be sold on its website. There was no dispute that individual sellers, rather than eBay, were responsible for listing and selling counterfeit Tiffany items. However, Tiffany argued that eBay was on notice of the infringement, that eBay had the obligation to investigate and control the illegal activities of these sellers-specifically, and that by preemptively refusing to post any listing offering five or more Tiffany items and by refusing to immediately suspend sellers upon learning of Tiffany's belief that the seller had engaged in potentially infringing activity, eBay was contributorily liable. In response, eBay argued that it was Tiffany's burden to monitor the eBay website for counterfeits and to bring counterfeits to eBay's attention. The key issue was who should bear the burden of policing Tiffany's trademarks on the eBay site.

After a bench trial, the court held that eBay was not liable for contributory trademark infringement. The court applied the *Inwood* standard regarding whether eBay continued to supply its services to sellers when it knew or had reason to know of infringement by those sellers. When Tiffany put eBay on notice of specific items that Tiffany contended were infringing, eBay immediately removed those listings. However, the district court held that the

law “does not impose liability for contributory trademark infringement on eBay for its refusal to take such preemptive steps in light of eBay's ‘reasonable anticipation’ or generalized knowledge that counterfeit goods might be sold on its website. Quite simply, the law demands more specific knowledge as to which items are infringing and which seller is listing those items before requiring eBay to take action.”

The district court applied *Inwood* and *Lockheed Martin* in determining vicarious infringement. The court held that, because eBay provides a service rather than a product, it would “look not only to whether eBay provided the necessary marketplace for the counterfeiting (which it clearly did), but further, to whether eBay had direct control over the means of infringement.” The district court held that “eBay exercises sufficient control and monitoring over its website such that it fits squarely within the *Fonovisa* and *Hard Rock* line of cases.” The court held that eBay retains significant control over the transactions conducted through eBay, eBay has actively promoted the sale of Tiffany jewelry items, eBay profits from the listing of items and successful completion of sales, through insertion fees and final value fees, eBay maintains significant control over the listings on its website, and eBay maintains a classified ad service separate and apart from the eBay listings that are at issue in this action.

Under the *Inwood* test, Tiffany had to prove that eBay continued to supply its services “to one whom it knows or has reason to know is engaging in trademark infringement.” The district court framed the question as whether eBay's generalized knowledge of trademark infringement on its website was sufficient to meet the “knowledge or reason to know” prong of the *Inwood* test. The court concluded that “such generalized knowledge is insufficient under the *Inwood* test to impose upon eBay an affirmative duty to remedy the problem.” The “reason to know” standard can be satisfied by a showing that the defendant was willfully blind to the infringing activity. However, willful blindness means a person must suspect wrongdoing and deliberately fail to investigate. *See Hard Rock*, 955 F.2d at 1149. The court held that eBay was not willfully blind to the infringement:

Put simply, it cannot be said that eBay purposefully contrived to avoid learning of counterfeiting on its website, or that eBay failed to investigate once it learned of such counterfeiting. To the contrary, in the face of such general awareness, eBay took significant steps to prevent counterfeiting by developing the VeRO Program, which seeks to remove individually infringing listings. Moreover, the record reveals that when eBay became aware, through its VeRO Program, of Tiffany's good-faith belief that a listing was infringing, it investigated and removed that listing from its website.

Id.

The case is on appeal to the Second Circuit. The Second Circuit heard oral argument from the parties in August 2009. A decision is likely in the next few months.

V. Secondary Liability of Search Engines

This section addresses the extent to which a search engine may be held secondarily liable for trademark and copyright infringement on third-party web sites, particularly when the search engine caches, indexes, and links to infringing images from third-party web sites. This section does not address liability for key word advertising, which will be addressed as a separate topic at the conference.

In *Perfect 10 v. Google*, 487 F.3d 701 (9th Cir. 2007), Perfect 10, Inc. sued Google for, among other things, infringing (both directly and indirectly) Perfect 10's copyrighted photographs of nude models. Perfect10 brought a similar action against Amazon.com and its subsidiary A9.com. The district court preliminarily enjoined Google from creating and publicly displaying thumbnail versions of Perfect 10's images, but did not enjoin Google from linking to third-party websites that display infringing full-size versions of Perfect 10's images. The district court did not preliminarily enjoin Amazon.com from giving users access to information provided by Google. Perfect 10 and Google both appealed. The district court found that Google was likely to succeed on its fair use defense as to creating and displaying thumbnail images.

The district court then turned to the issue of secondary liability, specifically whether the Ninth Circuit erred in holding that Perfect 10 was not likely to succeed on the merits of its claims for contributory and vicarious copyright infringement.

After reviewing the case law regarding contributory liability, the Ninth Circuit held that a computer system operator can be held contributorily liable if it has *actual* knowledge that *specific* infringing material is available using its system and can take simple measures to prevent further infringement of copyrighted works, yet continues to the infringing works. Applying this test, the Ninth Circuit concluded that:

There is no dispute that Google substantially assists websites to distribute their infringing copies to a worldwide market and assists a worldwide audience of users to access infringing materials. We cannot discount the effect of such a service on copyright owners, even though Google's assistance is available to all websites, not just infringing ones. Applying our test, Google could be held contributorily liable if it had knowledge that infringing Perfect 10 images were available using its search engine, could take simple measures to prevent further damage to Perfect 10's copyrighted works, and failed to take such steps.

Id. However, the court held that there are factual disputes over whether there are reasonable and feasible means for Google to refrain from providing access to infringing images. *Id.* at 1172-73. Therefore, the Ninth Circuit remanded the case to the district court to determine whether Perfect 10 was likely to succeed on the merits under the test enunciated by the Ninth Circuit.

With respect to the issue of vicarious liability, the Ninth Circuit held that Perfect 10 had not demonstrated a likelihood of success in showing that Google has the legal right to stop or limit the direct infringement of third-party websites. The Ninth Circuit held that the district court did not commit clear error in finding that "Google's software lacks the ability to analyze every image

on the [I]nternet, compare each image to all the other copyrighted images that exist in the world ... and determine whether a certain image on the web infringes someone's copyright.” *Id.*

The Ninth Circuit did not reach the issue of whether Google derived direct financial benefit from the direct infringement.

VI. Secondary Liability of Credit Card Companies

In *Perfect 10, Inc. v. Visa International Service Association*, 494 F.3d 788 (9th Cir. 2007), Perfect 10 sued Visa International Service Association, MasterCard International Inc., and several affiliated banks and data processing services, alleging secondary liability under federal copyright and trademark law based on defendants’ processing of credit card payments for websites that infringe Perfect 10’s intellectual property. The district court dismissed the claims for failure to state a claim and the Ninth Circuit affirmed.

With respect to contributory copyright infringement, Perfect 10 argued that, by continuing to process credit card payments for merchants engaged in infringing activities despite having knowledge the infringement, the credit card companies are liable for contributory infringement. The Ninth Circuit disagreed, holding that “[t]he credit card companies cannot be said to materially contribute to the infringement in this case because they have no direct connection to that infringement. Here, the infringement rests on the reproduction, alteration, display and distribution of Perfect 10’s images over the Internet. Perfect 10 has not alleged that any infringing material passes over Defendants’ payment networks or through their payment processing systems, or that Defendants’ systems are used to alter or display the infringing images.”

The Ninth Circuit distinguished this case from *Perfect 10 v. Google* on the grounds that “Google’s search engine itself assists in the distribution of infringing content to Internet users” and “Google substantially assists websites to distribute their infringing copies to a worldwide market and assists a worldwide audience of users to access infringing materials.” In contrast, the credit card companies “in no way assist or enable Internet users to locate infringing material, and they do not distribute it.” *Id.* at 797.

The Ninth Circuit also distinguished the case from the *Fonovisa*, *Napster* and *Grokster* cases: “The swap meet operator in *Fonovisa* and the administrators of the *Napster* and *Grokster* programs increased the level of infringement by providing a centralized place, whether physical or virtual, where infringing works could be collected, sorted, found, and bought, sold, or exchanged.” Moreover, any definition of “site and facilities” that encompasses the credit card companies would also “include a number of peripherally-involved third parties, such as computer display companies, storage device companies, and software companies that make the software necessary to alter and view the pictures and even utility companies that provide electricity to the Internet.”

The Ninth Circuit also rejected Perfect 10’s argument that the credit card companies induced customers to purchase infringing products, holding that Perfect 10 alleged no “affirmative steps taken to foster infringement” and no facts suggesting that the credit card companies promoted their payment system as a means to infringe. *Id.* at 800. The *Grokster*

court defined inducement as providing a service with the object of promoting its use to infringe copyright; mere knowledge of potential or actual infringing uses is not enough. In contrast, Perfect 10 did not allege that credit card companies created or promote their payment systems as a means to foster infringement.

Perfect 10 also argued that the credit card companies were vicariously liable because they have the right and ability to control the content of the infringing websites by refusing to process credit card payments to the websites, enforcing their own rules and regulations, or both. The credit card companies had regulations prohibiting member banks from providing services to merchants engaging in certain illegal activities and requiring the member banks to investigate merchants suspected of engaging in such illegal activity and to terminate such merchants' accounts. *Id.* at 809-10. Based on the Court's ruling in *Google*, the Ninth Circuit held that the credit card companies did not have the ability to directly control the infringing activities of merchants. The Ninth Circuit also rejected Perfect 10's argument that the credit card companies' contractual rights give them then right to control the infringing conduct, reasoning that "the ability to exert financial pressure does not give [the credit card companies] the right or ability to control the actual infringing activity at issue in this case." *Id.* at 804.

The Ninth Circuit also held that Perfect 10 failed to satisfy the more stringent tests for secondary trademark infringement. Perfect 10 failed to plead a viable claim under *Inwood Labs* that the credit card companies intentionally induced infringement of Perfect 10's trademarks. Perfect 10 also failed to plead sufficient facts to establish that the credit card companies had "[d]irect control and monitoring of the instrumentality used by a third party to infringe the plaintiff's mark" under *Lockheed Martin*. The fact that the credit card companies could stop processing credit card transactions for infringing goods did not constitute "direct control." The Ninth Circuit also held that Perfect 10 failed to plead facts sufficient to establish vicarious trademark infringement, stating that "Defendants process payments to these websites and collect their usual processing fees, nothing more."

In dissent, Judge Kozinski claimed that, assuming the truth of plaintiff's allegations, "the credit cards are easily liable for indirect copyright infringement: They knowingly provide a financial bridge between buyers and sellers of pirated works, enabling them to consummate infringing transactions, while making a profit on every sale. If such active participation in infringing conduct does not amount to indirect infringement, it's hard to imagine what would. By straining to absolve defendants of liability, the majority leaves our law in disarray." *Id.* at 810-811. Judge Kozinski quoted *Perfect 10, Inc. v. Amazon.com, Inc.*, 487 F.3d 701 (9th Cir. 2007), for the proposition that Google "could be held contributorily liable if it had knowledge that infringing Perfect 10 images were available using its search engine, could take simple measures to prevent further damage to Perfect 10's copyrighted works, and failed to take such steps." *Id.* citing *Amazon*, 487 F.3d at 729. He then argued that if you substitute "payment systems" for "search engine" in this sentence, "it describes defendants here: If a consumer wishes to buy an infringing image from one of the Stolen Content Websites, he can do so by using Visa or MasterCard, just as he can use Google to find the infringing images in the first place." *Id.* He disagreed with the majority's claim that "Google's search engine itself assists in the distribution of infringing content to Internet users, while Defendants' payment systems do not" and that

“[h]elping users to locate an image might substantially assist users to download infringing images, but processing payments does not.” *Id.*

VII. The Future of Secondary Liability

As the difficulty in stopping counterfeiters on the Internet continues, intellectual property owners will continue to try to expand the boundaries of secondary liability by suing parties involved in some manner in the sale, advertising, payment, shipment or other activities relating to such goods. As a result, the law of secondary liability will continue to be unsettled for some time. It is difficult to reconcile the existing case law. Each time a court addresses the scope of secondary liability in a new context, the standards change. Courts will likely continue to attempt to draw a principled line to define the contours of secondary liability. However, the analysis will likely be result driven, rather than driven by application of any clear principles. Future cases will likely address secondary liability in new contexts such as virtual worlds, social media, and new technologies and media that we do not know of and cannot contemplate at this point in time.