

Intellectual Property

IT, Internet and Outsourcing Bulletin

December 2009

In This Issue...

- Supreme Court Hears Arguments on Business Method Claims—Will They Survive?
- Companies Can't Outsource Competition Law—The Relevance of Competition Law to Outsourcing Transactions
- Federal Circuit Vacates Lucent Damages Award and Provides Guidance for Reasonable Royalty Analysis
- Federal Circuit Limits Overseas Patent Liability: Method Patents
- France Moves towards a "Privacy Privilege" to Oppose Discovery Requests?
- The Biggest Issue Not Being Discussed in United States Patent Law Reform
- Online Service Provider Copyright Infringement in China
- An Additional Theory of Recovery for Software Licensors?
- An Unanswered Question Regarding Gray Market Importations of Copyrighted Material

As we reflect on the past year, we note that there have been significant changes in both the legal and practical realities of intellectual property. These changes have particularly impacted those of us practicing in the areas of technology, the Internet and outsourcing. Through this periodic publication, we are pleased to provide brief updates on current changes and policy implications of an ever-changing intellectual property paradigm. These insights are delivered with the international perspective that our global practice is uniquely situated to provide. We hope you enjoy this issue of our publication, and welcome your thoughts and suggestions for future issues. Best wishes for the New Year.

Daren Orzechowski and Bijal Vakil



Bulletin Editors:

Daren M. Orzechowski
Partner, New York
+ 1 212 819 8704
do@whitecase.com

Bijal V. Vakil
Partner, Palo Alto
+ 1 650 213 0303
bvakil@whitecase.com

Amy Bagdasarian
Associate, Palo Alto
+ 1 650 213 0304
abagdasarian@whitecase.com

Leigh Checchio
Associate, New York
+ 1 212 819 8417
lchecchio@whitecase.com

Tayo Giwa
Associate, New York
+ 1 212 819 8674
tayo.giwa@whitecase.com

The White & Case IT, Internet and Outsourcing Bulletin is prepared for the general information of our clients and other interested persons. This memorandum is not, and does not attempt to be, comprehensive in nature.

The contents of this Bulletin should not be construed or relied upon as legal advice or a legal opinion.

ATTORNEY ADVERTISING.
Prior results do not guarantee a similar outcome.

Supreme Court Hears Arguments on Business Method Claims—Will They Survive?

By David M. Tennant and Monisha Deka (Washington, DC)

On November 9, 2009, the US Supreme Court heard oral arguments in *Bilski v. Kappos*, the appeal of the en banc *In re Bilski* decision from the Federal Circuit regarding the patent eligibility of method/process claims.¹ This case stemmed from a rejection by the United States Patent and Trademark Office (USPTO) Board of Patent Appeals and Interferences of a business method claim for failing to constitute patent eligible “process” subject matter under 35 U.S.C. § 101.² This case was closely watched by the software industry which has relied upon the patent eligibility of method/process claims for the protection of its valuable innovations.

The USPTO applied the prevailing standard for patent eligibility of process claims and concluded that Bilski’s claimed method did not produce “useful, concrete and tangible results.”³ The Federal Circuit affirmed the USPTO’s decision but also set forth a new bright line and definitive “machine or transformation test” for determining patent eligibility of method/process patents, which requires that a claimed process: (1) be tied to a particular machine or apparatus, or (2) transform a particular article into a different state or thing.⁴ The issues and ambiguities created by the Federal Circuit’s “machine or transformation test” did not go unnoticed by the Supreme Court Justices or the 60-plus amici curiae who submitted briefs to the Court. It is unclear whether the Court will provide an unambiguous answer to the question of patent eligibility of method/process claims, but several industries are

eagerly awaiting the Court’s decision. Having attended the oral arguments, we wanted to share some of our observations for those who could not attend.

The Supreme Court’s oral arguments began with the Petitioner (Bilski) advocating a reversal of the Federal Circuit’s “machine or transformation test” and a return to prior tests for patent eligibility. However, skepticism on the bench was apparent. The Justices took turns posing campy examples of business methods in an apparent attempt to attack the underpinnings of the Petitioner’s position and exploring “the line between patent eligibility and ineligibility for method claims.” For example, Justice Breyer made reference to his “great, wonderful, and really original method of teaching antitrust law” that keeps 80 percent of the students awake, which the Petitioner attested would “potentially” be patent eligible. Along the same lines, Justice Kennedy raised the hypothetical example of a method of applying risk to the compilation of actuarial tables which enabled the creation of the insurance industry in England in 1680, and concluded that “it’s difficult for me to think that Congress...would have wanted to give only one person the capacity to issue insurance.” Nonetheless, Petitioner opined that such a method would be patent eligible. Justice Ginsberg approached the issue from another angle and inquired why the US should not include a science or technology limitation to business method patents as is done in Europe and elsewhere.

1 The US patent laws, including 35 U.S.C. §101, provide that any new and useful process, machine, manufacture, or composition of matter is eligible for patent protection.

2 The claim in question was the business method claim below; however, the implications of this case reach all process/method claims.

1. A method for managing the consumption risk costs of a commodity sold by a commodity provider at a fixed price comprising the steps of:

(a) initiating a series of transactions between said commodity provider and consumers of said commodity wherein said consumers purchase said commodity at a fixed rate based upon historical averages, said fixed rate corresponding to a risk position of said consumer;

(b) identifying market participants for said commodity having a counter-risk position to said consumers; and

(c) initiating a series of transactions between said commodity provider and said market participants at a second fixed rate such that said series of market participant transactions balances the risk position of said series of consumer transactions.

3 *State Street Bank & Trust Co. v. Signature Financial Group, Inc.*, 149 F.3d 1368, 1370 (Fed. Cir. 1998) (holding that a claimed invention was eligible for protection by a patent in the United States if it involved some practical application and “it produces a useful, concrete and tangible result.”).

4 *In re Bilski*, 545 F.3d 943, 959 (Fed. Cir. 2008).

Subsequently, the Justices and the Petitioner debated the hypothetical outcome of telephone and Morse code claims under various tests for eligibility for a method patent. Petitioner submitted that Alexander Graham Bell's claim to transmit sound using undulating current would not have passed the transformation portion of the "machine or transformation test" because there is no physical change. Justice Scalia retorted that the transformation of sound to electrical current and back to sound should meet the transformation portion of the "machine or transformation test." They proceeded to debate whether electric current is "physical," but Justice Scalia appeared convinced that the telephone claim would have met the Federal Circuit's "machine or transformation test." Also, the Petitioner compared Justice Kennedy's statement that the use of an alphabet should not be patent eligible to the patented process for using Morse code. In response, Justice Sotomayor pointed out that the patent eligible method claims for the use of Morse code incorporated the use of a telegraph machine.

In general, the Petitioner argued that patent eligibility of process/method claims should be determined with a test broader than the "machine or transformation test." At the conclusion of the Petitioner's oral arguments, there was a sense that a majority of the Justices do not intend to substantially broaden the scope of patent eligible method/process patents. However, the Justices also conveyed reservations to affirming the Federal Circuit's "machine or transformation test" throughout the Respondent's oral argument. For example, Justice Sotomayor requested Respondent to "help us with a test that doesn't go to the extreme that the Federal Circuit did." These reservations were ever more apparent during the discussion of the *State Street Bank* case.

The previous *State Street Bank* "standard" was discussed only with the Respondent, who distinguished the facts in *State Street Bank* by noting that State Street tested the patent eligibility of a "machine," as opposed to the patent eligibility of a "process" as in Bilski's claim. Nonetheless, Justices Stevens, Kennedy and Sotomayor seemed concerned about the potentially far-reaching effect of the Federal Circuit's decision on business method claims, including the *State Street Bank* precedent. Justice Stevens expressed that he did not "understand how...[the computer claim in *State Street Bank*] can be a patent on a machine if the only thing novel is the process that the machine is using." Justice Stevens questioned whether the process in *State Street Bank* taken alone (i.e., without the computer) was patent eligible, and Justice Kennedy expressed the same concern. However, the Respondent continually referred to the underlying "machine" or "computer" in *State Street Bank* as rendering the invention patent eligible. Justice Sotomayor took it a step further and stated, "[In]o ruling in this case is going to change State Street. It wasn't looking at process or the meaning of 'process.' It was looking at something else."

Later, the Court advanced the same concerns it had with the *State Street Bank* precedent in a different context. Chief Justice Roberts inquired as to in which situations the Bilski claim would constitute patent eligible subject matter. The Respondent stated that it envisioned a situation with an interactive computer technique where people sign onto a website to perform some of the personal contact steps of the method. However, Chief Justice Roberts brought up the same concerns that other justices had with *State Street Bank* and inquired whether, under the "machine or transformation test," the simple presence of a computer makes a method patentable over a non-computer version of the method. The Respondent indicated that the Federal Circuit has yet to flush out the implementation of the "machine or transformation test" because the Bilski claim at issue did not involve either a machine or a transformation. The Chief Justice confirmed that the extent to which a machine has to be used in a process in order for the "machine or transformation test" to be met remains unclear.

At the conclusion of its oral arguments, the Respondent pushed for a ruling limited to only the Bilski claim and the "machine or transformation test." While the Justices were posing questions as to the fate of software or medical diagnostic techniques, the Respondent asked that the Court rule on this issue and address any future issues when they come up in other cases.

It remains to be seen whether the Supreme Court will affirm the "machine or transformation test" outright, or whether it will take this opportunity to address patent eligibility of method/process patents as a whole. The Supreme Court majority did not seem to favor the Petitioner's position regarding expansive patent eligibility of business method claims. If the Supreme Court affirms the "machine or transformation test" outright, one would hope the Supreme Court expands on the issues, such as the application of the "machine or transformation test" that concerned the Court during oral arguments. However, the Bilski claim is purely a process claim, so the Supreme Court may decide the broader issues in the future.

Ultimately, the Supreme Court's decision could impact the validity of thousands of issued business method patents and patent applications pending before the USPTO. This, in turn, may impact the bottom line of companies where a significant portion of their valuation is derived from investments in business method patents in the form of software or otherwise, as well as future company strategies and investments in intellectual property. In the event that the Supreme Court's decision renders certain business method patents ineligible, fortunately, businesses may request that the USPTO reissue patents affected by the decision to try and salvage the remaining protectable subject matter. This is certainly an opinion to watch for and, in the meantime, companies should consider how the decision will reshape their patent prosecution strategies going forward.

Companies Can't Outsource Competition Law— The Relevance of Competition Law to Outsourcing Transactions

By James Killick (Brussels) and Ashley Winton (London)

Summary

Over the past two decades, companies have increasingly made use of outsourcing. Often functions perceived as “non core” were outsourced to specialist providers, often located offshore, who then delivered the same services back to the company more cheaply. This was achieved by using cheaper labour, newer technology and by reusing infrastructure developed for other companies with similar requirements. In today's leaner times, outsourcing transactions will continue to be important given their potential cost reductions.

However, companies need to ensure compliance with European competition laws. For example, some types of outsourcing transaction may need to be notified under merger control rules, meaning that prior approval would be needed before the outsourcing can be put into effect. In other cases, contractual restrictions put in place to give the company a competitive advantage may themselves be anticompetitive and subject to challenge.

Competition law is, in the authors' views, seldom given the consideration it deserves by outsourcing practitioners. This article will endeavour to redress the balance.

Introduction—The Different Types of Outsourcing

Outsourcing, and, in particular, offshoring has enjoyed rapid growth. Outsourcing to India alone is estimated to have grown from US\$12.9 billion in 2004 to US\$40.3 billion in 2008, with growth in Business Process Outsourcing (BPO), the outsourcing of back office business functions, being the most pronounced.

The common characteristic of outsourcing is that a specified “outsourcing service provider” will supply the “customer” with certain services that the latter previously performed in-house. There are a number of forms of outsourcing.

- **Alternative sourcing** involves the termination of the business activities within the customer—including laying off the employees who previously carried out those activities and the

dismantling of existing infrastructure. In parallel, the outsourcing service provider begins to deliver the same services to the customer via a supply agreement. Such a transaction is akin to a normal service contract. It is not a concentration within the EC Merger Regulation (ECMR) as there is no transfer of assets or personnel.

- **Captive outsourcing** involves the creation of a unit or subsidiary within a company (typically in a lower cost jurisdiction) which assumes responsibility for a certain category of service. This would not need to be notified under the ECMR since internal restructurings within a single corporate group do not constitute a concentration. Article 81(1) would not apply to such an intra-group arrangement.
- **Outsourcing and Offshoring** involves the transfer of a business unit with associated assets and/or personnel from the customer to the outsourcing service provider. The assets and personnel being transferred can vary. For example, a BPO is less likely to require the transfer of assets than an IT Outsourcing. If the outsourcing provider is geographically proximate to the customer and within the EU, then the staff are likely to be automatically transferred to the provider under the Acquired Rights Directive. If not, the staff will be made redundant and the outsourcing provider will use its own employees. In the past 18 – 24 months, firms such as Dendrite, SAP and Oracle have bought development teams from outsourced partners. There is also a trend for some companies to transfer their captive outsourcing operations to a third party.
- **Joint Venture** sourcing involves an outsourcing/offshoring that is to be owned by a joint venture between outsourcing provider and the customer. The advantage for the customer is that it retains an additional degree of control over the outsourced operations and benefits from any capital appreciation of the outsourced business. This method has been used in both the public and the private sectors.
- **Multisourcing** involves splitting up operations into a number of different functions which get outsourced simultaneously to a number of different outsourcing providers. The client benefits by having direct access to the different contractors—this is more cost effective than hiring a single outsourcing provider who uses subcontractors and takes a margin on the subcontractors'

services. In addition to the service contract, there need to be horizontal agreements between the service providers to regulate their conduct and resolve issues that do not fall at the feet of any one of the providers.

Outsourcing/Offshoring and the ECMR

Outsourcing/Offshoring is the most likely type of outsourcing to raise competition law issues given that the transfer of a team of employees or assets can constitute a concentration under the ECMR. National Competition Authorities such as the UK's OFT take a similar view, considering outsourcing situations involving the transfer of employees and assets to be relevant under UK merger control, provided that the transaction causes the enterprises in question to cease to be distinct.

In addition to satisfying the normal turnover thresholds, there are several requirements for outsourcing transactions that must be met before there is a need to file the transaction with the European Commission.

The Consolidated Jurisdictional Notice makes clear (at paragraph 25) that outsourcing will only constitute a notifiable concentration if the transferred unit can be classified as a "business with market presence." The notice explains this concept further: "This requires that the assets previously dedicated to in-house activities of the seller will enable the outsourcing service supplier to provide services not only to the outsourcing customer but also to third parties, either immediately or within a short period of time after the transfer." In the outsourcing world, this is described as a shared services platform and is a common method for outsourcing providers to reduce costs by sharing a platform or infrastructure. Even if the assets are not used on a shared platform, if they have the "means to develop market access" within a short period of time, then the transfer could also be a concentration.

Thus there will be no concentration where the outsourcing service supplier merely acquires a right to direct its newly transferred employees and assets exclusively for the benefit of the customer. So the outsourcing of an in-house IT business, that is not placed on a shared services platform, for instance, would not need to be notified since the business being outsourced would not be supplying third parties.

Joint Ventures and the ECMR

The Consolidated Jurisdictional Notice makes clear that setting up an outsourcing joint venture will be considered to be concentration, provided it is a "full function" joint venture, i.e., it operates on a lasting basis, performing all the functions of an independent economic entity, and is not dependent on its parents. This can be a difficult issue to judge for outsourcing transactions.

For instance, in the IBM/Fiat case (Case Comp/M.2478), the Commission decided that the joint venture was fully functional since it had significant capitalisation from the outset as well as having an independent management and a staff of almost 5,000 employees. Crucially, whilst the joint venture entity would sell IT services to its founding companies, it would also offer services to third parties. Around 50 to 70 percent of the revenues of the joint venture entity would come from merchant sales to third parties and this was seen as sufficient to fulfil the criterion. Thus, similarly to transfer outsourcing, if the joint venture entity achieves significant sales to third parties, this will increase its likelihood of being classed as full function.

Turnover and the ECMR

To be notifiable to the European Commission under the ECMR, a concentration must have "Community Dimension," satisfying the turnover thresholds in Article 1.

In an outsourcing context, ascertaining the turnover of the business that is being outsourced can be awkward. (The turnover of the acquiring business, i.e., the outsourcing service provider, will generally be easy to ascertain). The Consolidated Jurisdictional Notice (at paragraph 163) makes it clear that the relevant turnover should be calculated on the basis of the previous internal revenues generated by the respective employees whilst in-house. The calculation of the internal turnover of a part of the customer's business will not be easy, given that an IT department, for instance, will rarely be a distinct entity within a company and as a support group, may not have real "turnover." Therefore it will often be necessary to estimate. The Notice makes clear that if the previous internal turnover does not appear to correspond to a market valuation of the activities in question, forecast revenues may be a suitable proxy. Given that there will almost certainly be divergences between previous internal turnover of the outsourced unit whilst still based with the customer and the turnover of the same unit once part of the more efficient outsourcing service provider, this determination may not be as simple as outsourcing parties may imagine it to be.

So whether a merger is indeed notifiable under the ECMR may depend on rather subjective estimates, something which is relatively unusual under the ECMR.

Ancillary Restraints

Ancillary restraints are obligations related to and necessary for the conclusion of a concentration. These can include clauses preventing the customer from competing with the business transferred—in effect preventing the customer from resuming in-house services. Other examples include agreements to guarantee the purchase of a certain quantity of services for a set

period of time. Ancillary clauses are deemed to be necessary for the merger and therefore in principle can fall outside the scope of Article 81(1). (If a merger is below the ECMR thresholds, then the EC ancillary restraints notice does not technically apply. But it remains highly persuasive because other countries' merger control rules apply a similar approach and an analysis under Article 81 may consider ancillary restrictions as being justified by the merger.)

The Commission has indicated that such agreements will only be considered to be ancillary if they are limited in time, generally meaning a duration of less than five years and in some cases less than three years. This may not be long enough in many outsourcing situations, which envisage outsourcing to be indefinite or to last for a long period. But this does not mean that such arrangements are illegal—it simply means that companies who have such agreements will need to carry out a separate analysis of the competition issues associated with the agreement under Article 81, including checking the applicability of block exemptions and the 1978 subcontracting notice and self-assessing possible individual exemption under Article 81(3).

Information Exchange

When a customer outsources services to one of its competitors, or in the case of a transfer of outsourced services from one

supplier to another, or in the case of multisourcing, there are potential information exchange issues that can arise. In an outsourcing situation, suppliers and customers may in some cases need to discuss service levels, costs as well as strategies, notably in negotiations leading up to the conclusion of an outsourcing deal. Whilst some information exchange will be legitimate and necessary, other types of information exchange may be more problematic. Care may be needed.

Conclusion

The above analysis has considered European law and shown that a number of elements of competition law are relevant to outsourcing. Particular care is needed with merger control since any merger filing needs to be undertaken to strict deadlines and approval of the relevant authority may be needed before outsourcing deals can be implemented. The same principles would equally apply under national competition rules both in the EU and around the world.

This article was published in a slightly different form in the April 7, 2009 issue of *Competition Law Insight*.

Federal Circuit Vacates Lucent Damages Award and Provides Guidance for Reasonable Royalty Analysis

By Kevin X. McGann, Daren M. Orzechowski and Aaron Chase (New York)

In a recent decision vacating a jury's US\$358 million award for patent infringement, the Court of Appeals for the Federal Circuit sent a message to district courts and to litigants that it will no longer tolerate awards based on insufficient, irrelevant or unexplained evidence. The court laid blame for the erroneous award at the feet of both the district court, for failing to "scrutinize the evidence carefully," and the parties, observing that the "damages evidence of record was neither very powerful, nor presented very well by either party." The decision, which arguably

requires more of an evidentiary showing from patent plaintiffs, follows recent, well-publicized discussions in Congress concerning patent law reform, particularly in the area of damages.

In *Lucent Tech., Inc. v. Gateway, Inc.*¹ Lucent sued Microsoft for infringement of a patent for a method of entering information on a computer screen without the use of a keyboard. Lucent alleged that the patent was infringed by Microsoft's "date-picker" too—a graphical calendar that allows users to select dates, rather than

¹ 580 F.3d 1301 (Fed. Cir. 2009).

enter them by keyboard—available in its Outlook application and other products. Microsoft argued that the patent was invalid for anticipation or obviousness and that, in any case, its date-picker tool did not infringe. Finding the patent valid and infringed, the jury awarded almost US\$358 million in damages, amounting to roughly eight percent of the value of 110 million units of software sold. Following trial, Microsoft moved to set aside the findings of invalidity and infringement, as well as the damages award. When its motions were denied by the District Court for the Southern District of California, Microsoft appealed to the Federal Circuit.

Applicable law requires that the successful patent owner be awarded damages adequate to compensate for the infringement, but in no event less than a reasonable royalty.² In *Lucent*, the plaintiff advanced only a reasonable royalty theory. In analyzing the jury's award of a lump sum (as opposed to a "running" or "per-unit") royalty of almost US\$358 million (now swollen to over US\$511 million with interest), the Federal Circuit applied the well-established framework from *Georgia-Pacific Corp. v. US Plywood Corp.*³

Georgia-Pacific provides a set of 15 factors that help determine a reasonable royalty that willing negotiators would have agreed to at the time of first infringement. Focusing on *Georgia-Pacific* factor two, "the rates paid by the licensee for the use of other patents comparable to the patent in suit," the court admonished Lucent for the "shortcomings" in its evidence of license agreements offered in support of the award. Of the eight license agreements put into evidence, only four were for lump sum royalties. Of those four, insufficient evidence was presented to allow the court to deduce the subject matter of the agreements, or to answer important questions, such as how an agreement covering a large portfolio of patents could shed light on the value of a license agreement for a single patent. The court was equally critical of the four running royalty license agreements offered by Lucent in support of the award. The court noted that while running royalty agreements can, as a matter of law, be used to support awards for lump sum royalties, because of certain fundamental differences between running and lump sum royalty agreements and the negotiation of such agreements, litigants wishing to do so must explain how a running royalty agreement informs the calculation of a lump sum damages award. This requirement will likely apply to any future damages argument that seeks to rely on an allegedly comparable license agreement with an economic structure that differs from the structure of the proposed award. In particular, a litigant must explain: (a) the types of products covered by the agreement, (b) how valuable or essential the licensed patent rights are and (c) the relationship between the patented technology and

the product sold in the agreement as compared to the product/service at issue in the litigation. Criticizing Lucent for the "evidentiary lacunae" created by failing to explain the relevance of the four running royalty agreements it offered into evidence, the Court of Appeals found that *Georgia-Pacific* factor two weighed strongly against upholding the jury's award.

Weighing other *Georgia-Pacific* factors, and focusing on its conclusion that the infringing date-picker was one "tiny feature" among "hundreds, if not thousands" of other features of an "enormously complex" software program, the Court of Appeals found it "inconceivable" to conclude that a substantial amount of the value of Outlook was a result of the date-picker.

The Court of Appeals also addressed the viability and applicability of the so-called "entire market value" rule, which states that, where a patented feature is the sole reason that consumers buy a product, the royalty can be based on the value of the entire product rather than on merely the value of the feature. Again citing a lack of evidence that the patented method was the basis of consumer demand for Outlook, the court ultimately reached the "unmistakable conclusion" that the date-picker was not the reason consumers purchased Outlook, and, therefore, that the entire market value rule was inapplicable. The court did, however, explain that there is nothing "inherently wrong" with using the value of the entire product as a base for determining a reasonable royalty, so long as an appropriately tailored royalty rate is used. Lucent's expert failed to properly construct his proposed royalty rate in light of the royalty base he sought to apply it to.

Patent litigants would be wise to heed the lessons of *Lucent*. Evidence offered during the damages portion of a trial will be scrutinized, so due time must be given to gathering that evidence and preparing its presentation for trial. Litigants who neglect their damages case to focus solely on liability should not be surprised by unfavorable awards or a failure to sustain a damages claim. In general, regardless of the applicability of the entire market value rule, parties will need to address the relative value of the patented technology to the product or service accused of infringement. This apportionment must be reasonable and supported by the evidence. In addition, for purposes of a *Georgia-Pacific* analysis, only licenses for patents that are reasonably similar in terms of content and value to the patent at issue may be accepted as "substantial evidence" capable of supporting a reasonable royalty damages award. Parties will no longer be able to bring allegedly comparable agreements under analysis without first making these initial evidentiary showings.

² 35 U.S.C. § 284.

³ 318 F. Supp. 1116 (S.D.N.Y. 1970).

Federal Circuit Limits Overseas Patent Liability: Method Patents

By Bijal V. Vakil (Palo Alto) and Jack O. Lever, Jr. (Washington, DC)

On August 19, 2009, in an 11-1 en banc decision, the United States Court of Appeals for the Federal Circuit ruled that 35 U.S.C. § 271(f), which prohibits exporting patented products, does not apply to method patents. The ruling in *Cardiac Pacemakers Inc. v. St. Jude Medical Inc.*¹ makes it clear that United States manufacturers who ship products overseas cannot be held liable for the infringement of method claims that occur abroad. The Court's ruling will impact all companies that do business both in the United States and abroad.

The decision in *Cardiac Pacemakers* overruled the Federal Circuit's 2005 decision in *Union Carbide Chems. & Plastics Tech. Corp. v. Shell Oil Co.*,² which permitted the application of § 271(f) to method claims. In *Union Carbide*, the Federal Circuit found Shell liable for infringement of a method patent under § 271(f) for exporting a catalyst that was a necessary "component" for performing the patented method. The *Cardiac Pacemakers* decision is consistent with the United States Supreme Court's prior decision in *Microsoft Corp. v. AT&T Corp.*³ In *Microsoft*, the Supreme Court held that Microsoft did not supply combinable components of a patented invention when it shipped golden masters of its Windows operating system abroad. Since foreign-made copies of the Windows operating system were installed on computers supplied from places outside the United States, the Supreme Court concluded that Microsoft did not supply "components" from the United States. In that case, the Supreme Court reserved judgment on whether "an intangible method or process...qualifies as a 'patented invention' under § 271(f)."⁴

In this case, Cardiac Pacemakers brought a patent infringement suit against St. Jude for its implantable cardioverter, defibrillators that allegedly practice Cardiac's patent on "a method of heart stimulation using an implantable heart stimulator." In rendering its en banc decision, the Federal Circuit considered whether Cardiac Pacemaker was entitled to damages from sales of the defibrillators supplied from the United States for use in foreign countries. The Federal Circuit emphasized the distinction between components of tangible products and those which are simply components or steps in a method or process. The Federal Circuit rejected Cardiac's argument that the definition of "component" should encompass "the apparatus that performed the process" rather than just the step of that patented method. The Court reasoned that "Congress clearly believed that 'component' was separate and distinct from a 'material or apparatus for use in practicing a patented process.' Thus, a material or apparatus for use in practicing a patent process is not a component of that process. The components of the process are the steps of that process."⁵

In finding that St. Jude was not liable for infringement under § 271(f) for defibrillators that are exported for use abroad, the Federal Circuit concluded that because one cannot supply the step of a method, § 271(f) cannot apply to method claims. As a result, § 271(f) does not encompass products that may be used to practice a patented method in a foreign country.

Manufacturers involved in pending patent litigation cases in which patentees are asserting method claims for products sold for use abroad should consider whether the holding in *Cardiac Pacemaker* could be used to defend against claims of patent infringement.

1 576 F.3d 1348 (Fed. Cir. 2009).

2 425 F.3d 1366 (Fed. Cir. 2005).

3 *Microsoft Corp. v. AT&T Corp.*, 550 US 437 (2007).

4 *Id.* at 452 n.13.

5 *Cardiac Pacemakers Inc. v. St. Jude Medical Inc.*, 576 F.3d 1348, at 1363-64 (Fed. Cir. 2009).

France Moves towards a “Privacy Privilege” to Oppose Discovery Requests?

By Bertrand Liard and Elizabeth Lefebvre-Gross (Paris)

On July 23, 2009, the French Data Protection Authority (Commission nationale de l’informatique et des libertés (CNIL)) released its Deliberation No. 2009-474 concerning recommendations for the transfer of personal data in the context of discovery in US litigation (the Recommendation).

The Recommendation should be taken into account by all parties that find themselves in the position of transferring documents or other information containing personal data from France to the United States in the context of discovery in civil litigation (it does not apply to US criminal litigation or the investigations by governmental agencies).

In the Recommendation, the CNIL, a governmental agency whose stated goal is to protect individuals with regard to the processing of their personal data in France, addressed threats posed to personal data by discovery requests served in US civil and commercial litigation. The Recommendation was issued in response to “an increase in the number of matters concerning the transfer of personal data to the United States, filed principally either by French subsidiaries of American companies or by French companies that have commercial ties with the United States, in the context of ‘Discovery’ proceedings before American courts.” For those familiar with the CNIL’s prior recommendations and privacy-friendly positions, the new Recommendation will not come as a complete surprise; nonetheless, the Recommendation represents an important new authoritative statement regarding the defense of privacy rights in the discovery context.

Conditions for processing

In the Recommendation, the CNIL maintains that individuals whose personal information is divulged in the context of a US proceeding shall have the right to oppose the disclosure on legitimate grounds in all circumstances. Although the practical implications of this are not entirely clear, this would seem to mean that, in the event personal data of employees fall within the scope of a discovery request, such employees would have the right to oppose the production of their data, and their employer would be required to take their opposition into account when responding to the discovery request.

In addition, the Recommendation provides that parties producing personal data must weigh the proportionality and quality of the information and the consequences of the disclosure for the

individuals against the need for the information in the underlying litigation. If personal information is not needed for the purpose of the discovery request to be fulfilled, the personal information should be redacted. In this respect, the Recommendation offers guidance on the circumstances under which the data should be filtered, secured, redacted and/or how it should be utilized once transferred.

Conditions for transfer

Subject to certain limited exceptions, individuals’ consent is required prior to processing of their data. Such consent must have been “freely given.” Such consent cannot be considered to have been freely given to the extent that the consent was obtained through pressure or threats. Individuals must also be provided with specific information with respect to the processing and the transfer of their data to the US.

A one-time transfer of relevant information may be permitted by the exception within the 1978 Law on Data Processing, Data Files and Individual Liberties (Loi n° 78-17 du 6 janvier 1978 relative à l’informatique, aux fichiers et aux libertés) which allows for the transfer of data to a country that does not provide an adequate level of protection for personal data (such as the United States) if the transfer is necessary for a defense in a legal proceeding. Historically, this “self-defense” exception has been the most common means for a party to a litigation to comply with a US discovery request without violating the 1978 Law on Data Processing, Data Files and Individual Liberties, although the exception probably does not apply to a third party to a litigation (e.g., in the case of a third party being issued with a US subpoena for the production of documents). A party seeking to rely upon this exception must provide prior notice to the CNIL, but the CNIL’s permission need not be sought.

Where the transfer of personal data is “on a large scale” and repetitive, the CNIL’s prior permission must be obtained, and the information may be transferred only in compliance with the Recommendation and where the entity to which the information is transferred (a) has adhered to the safe harbor principles, (b) has entered into a contract compliant with the standard contractual clauses enacted by the European Commission or (c) has adopted binding internal regulations (referred to as Binding Corporate Rules).

While the CNIL's position in the Recommendation is consistent with its previous positions, as well as its general outlook and purpose and positions taken at a European Union level, the Recommendation is particularly important, both for its provision of specific rules and for its reaffirmation of the strong French principle in favor of personal data protection—even when such protection comes into conflict with other interests, such as judicial cooperation.

The Recommendation also reaffirms that the Convention on the Taking of Evidence Abroad in Civil or Commercial Matters of 1970 is the only legal way of transmitting information from France to the US in the discovery context and that the orders of US courts

to parties in France to produce documents or information in any other fashion are illegitimate. As a result, this Recommendation will give an additional tool to both parties and non-parties seeking, in the context of US discovery, to resist providing certain information covered by privacy rights under the French data protection regulation. Unfortunately, however, the Recommendation does not fully address the difficulties experienced by French parties in trying to balance their obligations to comply fully with discovery requests served in connection with US litigation with their responsibilities to adhere to the limitations on personal data production found in the Recommendation. How this Recommendation will play out in practice remains to be seen.

The Biggest Issue Not Being Discussed in United States Patent Law Reform

By Bijal V. Vakil and Thomas C. Flynn (Palo Alto)

Seventy years ago, not far from White & Case's Palo Alto office, two engineering graduate students set up a new electronics company in a Palo Alto garage. They, and technology entrepreneurs like them, helped establish Silicon Valley as a center for innovation and technology, greatly contributing to making the United States economy the world's largest and most innovative. Silicon Valley's inventions have drastically changed the way people live, work, and communicate around the world.

Today, Silicon Valley continues to invent. Established and start-up companies in Silicon Valley are at work developing the technologies and devices that have the potential to restart economic growth, including cloud computing, green/clean technologies and medical devices. The competition could be just down the street or around the world. Both could be working on the next big thing, getting ready to bring their inventions to market, and probably thinking about protecting their inventions by applying for a patent in the United States.

There is just one problem. At some point, it is likely that the competitor may face expensive and time-consuming patent litigation. Typically, companies know their competition and may perform patent searches to confirm that their products are free

and clear of claims of patent infringement. Unfortunately, the patent litigation landscape has changed so much that an industry may be faced with suits from patent holders in completely unrelated industries, making the reasonable investigation of patents currently in the field prior to launching a product nearly impossible and extremely cost prohibitive.

In an ever-increasing number of cases, a competitor has no reasonable notice that it would be subject to a patent suit, but nonetheless is subject to significant past damages simply because the patent at issue was marked; albeit in a completely unrelated field. There are numerous real world examples of this glaring hole in the United States patent laws, a few of which are included below:

- An inventor receives a patent and marks it for use with a home alarm system. Years later (since today the United States Patent laws provide for 20 years of protection from the date the patent is filed) a computer manufacturer is subject to suit for alleged use of this patent.
- The patent office issues a patent for transferring data from various databases and the patent holder later alleges infringement by a simple word processing program.

Many commentators agree that this is not fair; if the statute is designed to provide notice to the public, then it needs to do just that. The law is clear that the scope of coverage of a patent does not change as technology evolves. The claims and the specification of a patent do not evolve and take on a broader meaning as technology advances. Terms in patent claims should be construed in the manner contemplated at the time the inventor filed the patent. If a term had a narrow meaning when the patent application was filed, but later takes on a broader definition, the scope of patent protection should not expand. Likewise, if a device was understood to have one mode of operation by a person of ordinary skill in the art at the time of the application, the scope of coverage should not increase as technology develops additional ways of performing the same function.

United States patent laws are old. The reality of inventing and patenting new devices has changed significantly since the founders of the United States included patent protection in the Constitution to “promote the progress of science and the useful arts.” Congress and industry are currently working on patent reform legislation that is under active consideration and may be enacted next year.

An archaic rule, which largely goes unchallenged in patent cases, relates to a limitation on damages. United States intellectual property laws require a patent holder that makes physical products to mark the word “patent” or “pat.” on all manufactured products so that the public is on notice of the patent holder’s rights. Failure to properly mark a product can result in the forfeiture of damages in an infringement case. This statute (Section 287 of Title 35), like most of United States patent law, was enacted over 150 years ago. This section requires patent holders to provide a warning to the public that their products are protected by a patent.

The essential purpose of the marking statute is to provide notice to the public and enable the public to exercise their best efforts to avoid innocent infringement. However, any changes to the marking statute and its implications to large companies in patent cases have been noticeably absent from the discussion relating to patent reform. Courts should keep this purpose in mind when deciding cases where a lawsuit seems to come out of nowhere.

Competitors should be forced to take reasonable steps to learn of any potential claims of patent infringement, but it is simply impossible for a company to have any understanding of potential broad interpretations of patent claims for unrelated products and technology. The old marking laws simply fail to give notice and prevent innocent infringement.

When a lawsuit like this comes from an unrelated industry—when it comes out of nowhere—defendants should be able to argue that they have not received adequate notice, as required by the patent marking statute, to reduce the amount of claimed damages.

The time is ripe to address this issue in the current discussion regarding patent reform. Congress should ensure that patent laws provide competitors with proper notice of patent rights so that they can more credibly assess business opportunities. Courts should consider whether the public has been given adequate notice that a patent might cover products in a particular field. Technological change and scientific advances should encourage invention and invigorate the economy, not stifle legitimate competition in the marketplace.

Online Service Provider Copyright Infringement in China

By Patrick Ma (Beijing) and Rose He (Shanghai)

Introduction

As a result of the increasingly large number of movies and TV shows uploaded to video-sharing websites by unauthorized web users on a daily basis, these days it is common for a popular video-sharing site in China to simultaneously face more than ten copyright infringement lawsuits. Consequently, on September 15, 2009, about 110 online video copyright holders, led by Sohu.com, a major Chinese search engine, established an Anti-Piracy Alliance which announced its plan to file a series of lawsuits against Youku.com, the most popular online video site in China, seeking up to US\$14 million in damages. In response, two days later, Youku filed a lawsuit against Sohu claiming infringement of copyright and reputation. As this incident exemplifies, China is subject to the tug-of-war between technological advancement and copyright protection just like many other countries around the world.

Safe Harbor Protection in China

Similarly to the legal protections afforded to Internet service providers in other countries, video-sharing sites in China mainly rely on "safe harbor" rules to protect themselves from copyright infringement claims arising from their online video dissemination activities. According to the *Provisions on the Protection of the Right to Network Dissemination of Information*¹ promulgated by the State Council on May 18, 2006, internet service providers are exempted from infringement liability if they meet the following conditions:

- Clearly indicating that the information memory space is provided to the service objects and publicizing the name, contact information and websites of the network service provider;
- Not having changed the audio-visual products provided by the service objects;

- Not having, and cannot be reasonably expected to have, any knowledge of infringement of the audio-visual products provided by the service objects;
- Not having directly gained any economic benefit from the audio-visual products provided by the service objects; and
- After receiving a notice from the copyright owner, deleting the allegedly infringing audio-visual products in accordance with these provisions.

Among the five conditions required for safe harbor protection, the third criterion is often the issue disputed in court. Like in many other countries, owners of video-sharing sites in China generally argue that it is impossible for them to monitor and control the content of videos uploaded by Internet users given the huge amount of information exchanged over their sites. Courts do not, however, find that argument persuasive. In determining whether website operators have knowledge of the copyright infringement occurring on their websites, courts examine whether these websites have in the past exercised any monitoring or editorial control over the content that is uploaded onto the site by users.

For example, in the case of *Xinchuan v. Tudou.com*² decided in 2008, the court held that Tudou was unable to shield itself with safe harbor protection because it defaulted in performing its obligation of paying reasonable attention in processing web users' requests for uploading the popular movie "Crazy Stone." The court held that given the obviously large investment required for producing a movie like "Crazy Stone," Tudou should have been aware of the possibility of copyright infringement when the movie was uploaded to its website by users for free dissemination. The court also noted that Tudou exercised a certain degree of monitoring over the content of information uploaded to its site because it would review the information and decide whether or

¹ http://www.sipo.gov.cn/sipo2008/zcfg/flfg/bq/fljxzf/200804/t20080403_369366.html

² http://ipr.chinacourt.org/public/detail_sfws.php?id=16454

not to recommend the uploaded video. Further, since Tudou.com categorizes videos into various channels (e.g., Originals, Music, Movie & TV Series), the court found that Tudou is expected to pay more attention to the Movie & TV series channel because that channel is more prone to infringing activities. The court noted that the “notice and takedown” rule only applies to circumstances where the service provider has no knowledge of or cannot be reasonably expected to know the infringing nature of the video provided by the sites’ users. In sum, the court ruled that if the service provider fails to pay reasonable attention in processing information, it cannot rely on the safe harbor rule for protection.

Copyright Infringement Deterrence

It is not incredibly difficult for copyright owners to win infringement suits in China. However, due to the small damages fees awarded by courts (many awards would be limited to several thousands US dollars) and the huge advertising income that popular video-sharing sites receive, infringement damage awards do not effectively deter further infringement. Consequently, some right holders have begun to include as defendants companies that advertise on infringing websites. For example, in the Alliance’s planned suits against Youku, Coca-Cola has also been named as a joint defendant for advertising its Minute Maid brand juice on Youku.com. The plaintiffs aim to warn advertisers that placing ads on infringing video-sharing sites can land them in court. As a result of this tactic, many large companies may think twice about advertising on video-sharing sites known for infringing content and thus cut down the financial capital flowing to those video-sharing sites. In this way, copyright owners hope to more effectively deter websites from facilitating copyright infringement.

Administrative restrictions are another obstacle that video-sharing sites must overcome in order to operate in China. According to *the Administrative Regulations on Internet Audio-Visual Program Services*³ adopted by the State Administration of Radio, Film and Television (SARFT) and the Ministry of Industry and Information Industry in 2007, in order to engage in internet audio-visual program services, a video site should be either wholly state-owned or state-controlled. Further, the video-sharing site must obtain a “Permit for Disseminating Audio-Visual Programs via Information Network” which is issued by the competent department of SARFT. Unlicensed websites that engage in broadcasting for more than three months can be shut down in certain situations. According to the *Circular of the State Administration of Radio, Film and Television on the Reinforcement of the Administration of the Contents of Internet Audio-Visual Program*⁴ issued on March 30, 2009, to disseminate movies and TV series online, an audio-visual program service provider must also obtain the relevant permits for broadcasting movies and/or publishing TV series. These stringent rules will go a long way in driving many unlicensed video-sharing sites out of the market.

Conclusion

Facing increasing pressure from regulatory bodies and copyright owners, more and more video-sharing sites are beginning to explore various cooperation models with copyright owners, including paying license fees or sharing with the copyright owners a percentage of their advertising revenue. As social media technology continues to advance, cooperation will be key to creating a viable business market for technological innovators while also respecting the rights of copyright owners.

3 <http://www.miit.gov.cn/n11293472/n11293832/n11294042/n11302360/11652700.html>

4 <http://www.miit.gov.cn/n11293472/n11293832/n11294042/n11302360/11652700.html>

An Additional Theory of Recovery for Software Licensors?

By Leigh M. Checchio (New York)

Software owners may now have another avenue through which to obtain redress for violations of terms of use—copyright infringement. According to a decision in the District of Arizona this past summer, if a user is in violation of the terms of use of a software license, then copying of portions of the software program to RAM in the course of running the program is unauthorized, and therefore, an infringement.¹

At the center of the case lies World of Warcraft (WoW), an interactive multiplayer online video game produced and owned by Blizzard Entertainment, Inc. (Blizzard). While playing WoW, gamers explore the fantasy landscape, fight monsters and perform quests and other tasks to acquire power, experience and in-game assets (specifically, gold, the WoW currency) in order to advance in the game. WoW is the most successful of this type of game; since its release in 2004, WoW has amassed over 11.5 million players and earns Blizzard US\$1.5 billion annually.

Various types of software programs and other applications have been developed as add-ons to the WoW-licensed software in order to enhance the user experience of the game. The offending Glider software program produced and sold by MDY Industries, LLC (MDY) is one of such add-ons. When installed and run on the gamer's computer, the Glider program (referred to as a "bot") essentially plays the game for the user while he or she is away from the computer. Specifically, Glider allows the user's character to repetitively perform mundane tasks and other activities (chopping wood, for instance) that earn the player gold. For this reason, using a bot is called "goldfarming" or "goldmining." Glider offers the broadest range of automatic activities and is undetectable by WoW technology, and thus MDY's bot is the most popular of its kind, having sold over 100,000 copies since its release in 2005.

The obvious issue with Glider and other bots is that they allow players who employ them a notable and unfair advantage over those who do not, and they upset the WoW in-game economy. Furthermore, the excess of gold and other in-game assets generated by these programs has created an extra-game economy for WoW assets as well; gold is now sold online via eBay and other avenues. Because of this, such programs have caused upheaval among gamers and are overwhelmingly detested within the WoW

community. Blizzard has received over 500,000 complaints from users about Glider and other bots, the use of which are prohibited under the terms of use of the WoW software license. However, despite expending nearly US\$1 million per year attempting to detect and eliminate them, Blizzard's technology is presently unable to detect Glider.

In October 2008, Blizzard threatened to file suit against MDY in California, to which MDY responded by filing a declaratory judgment action in Arizona on the same day. Blizzard's response contained counterclaims for contributory copyright infringement and voluntary copyright infringement (among others). Blizzard argued that because bots are prohibited under the terms of the WoW software license, a gamer who uses Glider exceeds the scope of the license when certain software components of the WoW software are copied to RAM on the user's computer during play of the game (a necessary step for play), and thus, such copying constitutes direct copyright infringement. Then, as Blizzard alleged, because MDY created and sells Glider with the knowledge that it will be used in violation of the WoW terms of use and thus will infringe Blizzard's copyright, MDY is liable for contributory copyright infringement. Similarly, Blizzard argued, because MDY profits from Glider and has failed to exercise its right to stop use of the infringing bot, MDY is liable for vicarious copyright infringement.

Because it was undisputed that MDY created Glider with the knowledge that gamers would use it in violation of the WoW terms of use and that MDY profited from Glider and continued to sell it, the only issue before the court was whether copyright infringement had occurred. Specifically, the issue was whether a claim of copyright infringement was available to Blizzard as the licensor of the WoW software. As the court noted, a copyright owner who grants a nonexclusive license to the copyrighted material is usually deemed to have waived the right to sue for infringement, and is only permitted to bring actions for breach of contract. Nevertheless, if such license is limited in scope and the licensee acts outside the scope of the license, a copyright infringement cause of action is still available. Thus, the court considered whether the provision in the WoW terms of use prohibiting the use of bots was a limitation on the software license, or whether it was merely a general contractual covenant.

¹ *MDY Inds., LLC v. Blizzard Entm't, Inc.*, No. CV-06-02555, 2008 WL 2757357 (D. Ariz. 2008).

The court found that, because the prohibitions on bots in the terms of use were essentially governing the gamer's ability to use exclusive rights under copyright law (copying, distribution, display, performance, and creation of derivative works), such provisions were limitations on the license, and therefore copyright infringement had occurred. The terms of use relating to bots disallowed intercepting, emulating, or redirecting proprietary components of the game, akin to restrictions on the right to copy and distribute, and prohibited the user from modifying files that are part of the game, akin to restrictions on the right to create derivative works. The court thus granted Blizzard's motion for summary judgment with respect to copyright infringement, and enjoined MDY from infringing, or contributing to the infringement of, Blizzard's copyrights in WoW software. For other reasons, MDY was also enjoined from marketing, selling, supporting, distributing, or developing Glider for use in connection with WoW.

The decision has been hailed as a victory for fair play in multiplayer videogames and is generally supported by the WoW community. However, a major critique of the decision is that,

while the outcome in this case is ostensibly fair, the ruling sets a dangerous precedent that may lead to less judicious results in the future. More specifically, one of the court's findings was that gamers employing Glider were infringing Blizzard's copyright. This implies that any player who uses a bot or other prohibited add-on is liable for statutory damages, which critics argue is excessive, but because Blizzard chose to name only MDY and not any WoW players in its suit, only MDY, the potentially negative effect of the decision was not appreciated.

The case has been appealed to the Ninth Circuit, but not yet heard. Whether the decision stands, and whether other courts around the United States follow suit, is yet to be seen. In the meantime, software licensors in litigation against their licensees should consider including copyright infringement claims in addition to those for breach of contract. Also, to increase the likelihood that copyright infringement claims will be available, drafters should address license restrictions and grants in the same clause, and couch restrictions in terms of the exclusive rights of copyright holders.

An Unanswered Question Regarding Gray Market Importations of Copyrighted Material

By Tayo Giwa (New York)

The US law governing the importation and sale of copies of copyrighted works that are lawfully manufactured abroad is currently unsettled. Costco Wholesale Corp. has petitioned the United States Supreme Court to rule on this issue, which may give the Court a chance to finally settle this increasingly contentious legal question. The disputed issue revolves around the "first-sale" doctrine, which is the legal principle that a copyright owner's exclusive right to distribute copies of its work does not encompass the right to control the terms of subsequent sales of a purchased copyrighted work.

In *Omega S.A. v. Costco Wholesale Corporation*,¹ Omega accused Costco of infringing the copyright of its watch designs because Costco bought Omega watches overseas at a cheaper price and then sold them in the United States at a discount. Omega contends that, under US Copyright Law, first-sale protection is not available to copyrighted works that are manufactured abroad and

then imported into the United States. As such, Omega argues that it has the exclusive right to distribute its copyrighted designs in the United States without having its price undercut by Costco's gray market importations.

Conversely, Costco argues that its sales of Omega watches are protected by the first-sale doctrine because it legally purchased the Omega watches overseas and its discounted sales in the United States do not constitute the first sale of the watch designs. In support of its argument, Costco cites the Supreme Court case *Quality King Distributors, Inc. v. Lanza Research International, Inc.*,² which held that the first-sale doctrine prevented a domestic manufacturer from using its copyright monopoly to stop a gray market importer from buying the copyrighted goods abroad at discounted prices and then importing them back into the United States to sell for a cheaper price.

¹ 541 F.3d 982 (9th Cir. 2008).

² 523 US 135 (1998).

In the decision now being appealed, the Ninth Circuit agreed with Omega and held that the first-sale doctrine does not apply to importers of copyrighted works manufactured abroad which are brought into the United States for sale, overruling a decision by the Central District of California. Similar to the outcome of the Costco decision, in *Pearson Education, Inc. v. Liu*,³ the US District Court for the Southern District of New York sided with a group of textbook publishers against small publishers that resell for a cheaper price in the United States imported foreign editions of the textbooks that were manufactured abroad.

To date, the only court that has sided with the gray market importers is the Central District of California; a decision that is arguably bound by Supreme Court precedent in *Quality King*. However, both the Ninth Circuit and Southern District of New York distinguished their cases from *Quality King* because Costco and Liu imported copyrighted goods that were manufactured abroad instead of importing goods that were originally manufactured in the United States like in *Quality King*.

Significantly, both the Ninth Circuit and the Southern District of New York cited Justice Ginsburg's concurring opinion in *Quality King* in which she said that *Quality King* involved a round trip journey where the copies were made in the United States then sent abroad, and then brought back into the United States. Ginsburg noted that given the facts of *Quality King*, the Court's decision did not necessarily resolve cases in which the allegedly infringing imported work was manufactured abroad. As a result, both the Ninth Circuit and Southern District of New York used Justice Ginsburg's concurring opinion as support to the argument that works manufactured abroad and then imported into the United States against a copyright holder's wishes were not covered by *Quality King's* holding.

The technical, legal question at the heart of these cases turns on the statutory interpretation of section 602(a) of the Copyright Act, which addresses the extent to which the distribution right allows a copyright owner to also control the importation of copies of his/her work, and its interplay with section 109(a) of the Copyright Act, which is where the first-sale doctrine is codified. Section 602(a) provides in part that:

Importation into the United States, without the authority of the owner of the copyright under this title, of copies or phonorecords of a work that have been acquired outside the United States is an infringement of the exclusive right to distributed copies or phonorecords under section 106, actionable under section 501.

Due to § 602(a)'s location in a different section than the exclusive rights granted in the Copyright Act and its seeming reference to all copies acquired outside the United States, the text of the statute does not clearly indicate that copyright owners have authority to restrict the importation of copies of a work without regard to the first-sale doctrine. However, *Quality King's* holding clarified that the first-sale doctrine was not limited by the place where an initial transfer of ownership occurred; according to *Quality King*, transfers of ownership of copyrighted goods that occur abroad are still protected by the first-sale doctrine when the goods are imported in the United States. Nevertheless, *Quality King* did not resolve the narrow legal question concerning whether the place where a copyrighted good was manufactured mattered for first-sale protection for imported goods.

The consequences of a Supreme Court ruling on this issue could have wide-reaching implications. For example, if the Supreme Court sides with Omega, any copyright owner of computer software or owners' manuals that are manufactured outside the United States could then regulate how retailers of the copyrighted goods in the United States sell or license those copyright goods. On the other hand, manufacturers argue that if the Supreme Court decided in favor of Costco, consumers could see a rise in the price of certain goods because they would be unable to sell goods for competitive prices abroad and thus unable to subsidize US prices with foreign sales.

Although the Central District of California is the only court to have sided with gray market importers, the existing consensus on the law is not very strong and if the Supreme Court decides to hear the case, it would give businesses much needed guidance. The lack of clarification regarding this issue is a significant problem because in our globally connected marketplace, both distributors and importers need legal certainty so that they can structure their business operations without fear that the prices of their goods will be undercut or that they are committing copyright infringement.

³ 2009 WL 3064779 (S.D.N.Y. Sept. 25, 2009).

Our Global Network

Supporting Clients Across the Globe

White & Case is a leading global law firm with lawyers in 36 offices across 25 countries.

We advise on virtually every area of law that affects cross-border business and our knowledge, like our clients' interests, transcends geographic boundaries.

Whether in established or emerging markets our commitment is substantial, with dedicated on-the-ground knowledge and presence.

Our lawyers are an integral, often long-established part of the business community, giving clients access to local, English and US law capabilities plus a unique appreciation of the political, economic and geographic environments in which they operate.

At the same time, working between offices and cross-jurisdiction is second nature and we have the experience, infrastructure and processes in place to make it happen effortlessly.

We work with some of the world's most well-established and most respected companies—including two-thirds of the *Global Fortune 100* and half of the *Fortune 500*—as well as start-up visionaries, governments and state-owned entities.

Our reviews in international legal rankings and ratings have reflected the quality and comprehensiveness of our work on behalf of our clients.

"Clients praise its 'attractive combination of technical expertise, business pragmatism and responsiveness...'"

Chambers Global 2009 USA: Intellectual Property

One of the "Top 25 IP Practices in Silicon Valley"

Silicon Valley Business Journal 2006-2009

"Clients recommend this team's 'excellent expertise and client service' in trade mark prosecution and infringement litigation on a national and international level."

Chambers Europe 2008 Germany: Intellectual Property

"Clients extol this firm's 'terrific' international capabilities in a range of trade mark, copyright and patent cases. Furthermore, its 'speed of analysis, accuracy of advice and calmness in dealing with crises' comes in for further praise."

Chambers Global 2008 USA: Intellectual Property

"This 'tremendously admired' global practice is experienced in helping a wide range of clients in IP matters, including cross-border IP issues, litigation and transactional work. It offers expertise in patents, trademarks, copyrights, privacy and data protection."

Chambers Global 2008: Intellectual Property

Americas

Los Angeles	Palo Alto
Mexico City	São Paulo
Miami	Washington, DC
New York	

Europe, Middle East and Africa

Abu Dhabi	Hamburg
Almaty	Helsinki
Ankara	Istanbul
Berlin	Johannesburg
Bratislava	London
Brussels	Moscow
Bucharest	Munich
Budapest	Paris
Doha	Prague
Düsseldorf	Riyadh
Frankfurt	Stockholm
Geneva	Warsaw

Asia

Beijing	Singapore
Hong Kong	Tokyo
Shanghai	

Offices Contributing to this Issue

Beijing

White & Case LLP
19th Floor, Tower 1 of China Central Place
81 Jianguo Lu, Chaoyang District
Beijing, 100025
China
Tel: + 86 10 5912 9600
Fax: + 86 10 5969 5760

Brussels

White & Case LLP
Avocats-Advocaten
62 rue de la Loi Wetstraat 62
1040 Brussels
Belgium
Tel: + 32 2 219 16 20
Fax: + 32 2 219 16 26

London

White & Case LLP
5 Old Broad Street
London, EC2N 1DW
United Kingdom
Tel: + 44 20 7532 1000
Fax: + 44 20 7532 1001

New York

White & Case LLP
1155 Avenue of Americas
New York, New York 10036
United States
Tel: + 1 212 819 8200
Fax: + 1 212 354 8113

Palo Alto

White & Case LLP
3000 El Camino Real
Five Palo Alto Square, 9th Floor
Palo Alto, California 94306
United States
Tel: + 1 650 213 0300
Fax: + 1 650 213 8158

Paris

White & Case LLP
19, Place Vendôme
75001 Paris
France
Tel: + 33 1 55 04 15 15
Fax: + 33 1 55 04 15 16

Shanghai

White & Case LLP
Citic Square, 39th Fl.
1168 Nanjing Road (West)
Shanghai, 200041
People's Republic of China
Tel: + 86 21 6132 5900
Fax: + 86 21 6323 9252

Washington, DC

White & Case LLP
701 Thirteenth Street, NW
Washington, D.C., 20005-3807
United States
Tel: + 1 202 626 3600
Fax: + 1 202 639 9355

www.whitecase.com

In this publication, White & Case means the international legal practice comprising White & Case LLP, a New York State registered limited liability partnership, White & Case LLP, a limited liability partnership incorporated under English law and all other affiliated partnerships, corporations and undertakings.