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The Wrong Way—Copyright Misuse Weakens Infringement Claims

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In a short opinion destined to constrain the power of copyright holders to control the way customers and competitors can use such works as computer software, the Ninth Circuit has held that "copyright misuse" is a defense to copyright infringement claims. *Practice Management Information Corporation v. The American Medical Association*, 97 Daily Journal D.A.R. 10221 (Aug. 7, 1997). The Ninth Circuit's holding marks an important gain for the little-applied copyright misuse doctrine, previously employed only by the Fourth and Fifth Circuits.

"Misuse" of federal intellectual property rights—attempting to leverage them into greater monopoly rights than Congress intended—has long been recognized in patent law. Thus, if a patent-holder made it a condition for using a patented technology that licensees not deal with a competitor, or if the patent holder seeks royalties beyond the term of the patent, the license may be deemed unenforceable under the well-established "patent misuse" doctrine.

The principle underlying the doctrine is that Congress has set the terms of the "bargain" between patent-holders and the public: The inventor gets a limited-time monopoly in exchange for publicly disclosing the invention and allowing the public to freely use it after the patent term expires. Patent holders may not improve their side of the bargain by using the patent to extract a broader monopoly from licensees.

Traditionally, copyrights have bestowed less market power on their owners than patents, and historically there have been fewer license agreements concerning copyrights than patents. Copyright owners have therefore had fewer opportunities to attempt this kind of leveraging. Consequently, there have only been a handful of decisions based on copyright misuse. With the growing importance of computer software, however, which is commonly licensed, this has begun to change. In recently years two court of appeal decisions (both dealing with computer software) have held that "misuse" of a copyright also represents a defense to infringing that form of intellectual property. *Lasercomb America, Inc. v. Reynolds*, 911 F.2d 970 (4th Cir. 1990); *DSC Communications Corp. v. DGI Technologies, Inc.*, 81 F.3d 597 (5th Cir. 1996). Last month the Ninth Circuit joined them, squarely holding in *Practice Management* that copyright misuse is a complete defense to copyright infringement even when the defendant was not a party to the overreaching contract. This article explains how the copyright misuse defense operates and explores some of its implications.

First, what happened in *Practice Management*, and what did the Ninth Circuit decide? In 1977, Congress instructed the Health Care Financing Administration ("HCFA") to establish a uniform code for identifying physicians' services, to be used in completing Medicare and Medicaid claim forms. Instead of creating its own code, the agency contracted with the American Medical Association to adopt and use a code of medical procedures previously created by the AMA. The AMA code was embodied in a publication known as the Physician's Current Procedural Terminology ("CPT"), to which the AMA held the copyright.

INTELLECTUAL PROPERTY LAW:
If anyone signed an overreaching license, a defendant can assert that "copyright misuse" negates liability for infringement.

The HCFA's contract with the AMA gave HCFA a "non-exclusive, royalty free, and irrevocable license to use, copy, publish and distribute" the CPT. In exchange, HCFA agreed "not to use any other system of procedure nomenclature" and further agreed to require use of the AMA's code in programs administered by HCFA whenever possible.

Practice Management Information Corporation is a distributor of medical books, and purchases copies of the CPT from the AMA for resale. Unhappy with the AMA's failure to give Practice Management the volume discount it sought, the company sued for a declaration that the AMA's copyrights in the CPT were invalid. The Ninth Circuit rejected Practice Management's argument that after the government agency mandated use of the AMA's code, it became the "law," and (like judicial decisions) was therefore uncopyrightable. But the Ninth Circuit upheld Practice Management's second ground for relief: "Conditioning the license on HCFA's promise not to use competitors' products constituted a misuse of the copyright by the AMA." 97 Daily Journal D.A.R. at 10223.

> "The controlling fact is that HCFA is prohibited from using any other coding system . . . . The terms under which the AMA agreed to license use of the CPT . . . gave the AMA a substantial

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and unfair advantage over its competitors. By agreeing to license the CPT in this manner, the AMA used its copyright 'in a manner violative of the public policy embodied in the grant of a copyright.'" *Id*. (quoting *Lasercomb*).

The Ninth Circuit's opinion does not discuss the merits of the doctrine and states no reasons for adopting it. Instead, asserting that the court had "implied" in two earlier cases which ruled against the defendants that copyright misuse is a defense, and citing *Lasercomb* and *DSC Communications*, the court merely states: "We now adopt that rule."

What, more precisely, is copyright misuse? In brief, it is the use of a copyright to secure an exclusive right or limited monopoly not granted by copyright law and against public policy. Lasercomb at 977. The recent court of appeal cases hold that the use does not have to rise to the level of an antitrust violation for the copyright misuse defense to be invoked. And a defendant need not be a party to the overreaching contract to claim the benefit of the defense. If anyone signed the contract, the defendant can assert the misuse and negate liability for infringement. Importantly, copyright misuse does not invalidate the copyright, but merely precludes its enforcement during the period of misuse. *Practice Management* at 10224, n. 9; *Lasercomb* at 979 n. 22.

What constitutes an effort "to secure an exclusive right or limited monopoly not granted by the [Copyright] Office," *Lasercomb*, and what efforts are "contrary to public policy"? Because of the paucity of copyright misuse cases, these issues are not well delineated. However, the three court of appeal decisions upholding the doctrine and the small number of cases in recent times considering the defense, but finding it inapplicable, provide some guidance.

- It is copyright misuse to require licensees to use the copyrighted work to the exclusion of competitors' works. *Practice Management*.

- It is copyright misuse to require licensees and their employees to agree not to create their own works which compete with the copyrighted work. *Lasercomb*.

- It is copyright misuse to attempt to enforce a license that bars use of copyrighted software on anyone's equipment but the licensor's, when that restriction effectively prevents the development of new works. *DSC Communications*.

- It is not copyright misuse to enforce a license provision that prevents independent service organizations from using the copyrighted software to service licensor's computer systems, when the ISO is still free to develop its own, competing service software. *Triad Systems Corp. v. Southeastern Express Co.*, 64 F.3d 1330 (9th Cir. 1995).

It is worth emphasizing that a license restriction which, on its face, does not appear to extend the limited copyright monopoly can transgress the misuse doctrine if the effect of a copyright owner's attempt to enforce the provision is to secure more extensive rights than granted by the Copyright Act.

Revealingly, two of the three court of appeal cases upholding the copyright misuse defense involved computer software. This is no coincidence. Software copyrights do not literally confer patent-like protection—including monopoly power to control use of its subject—on copyrighted works. But computer programs are useful, functional works and, and software license agreements commonly include limitations on the use of the programs. The critical question posed by the copyright misuse cases is what kinds of license restrictions—and what kinds of enforcement efforts concerning facially neutral terms—will be deemed efforts "to secure an exclusive right or limited monopoly not granted by the Copyright Office" and "contrary to public policy.'" *Lasercomb* at 977 (brackets deleted).

Consider some software license terms that might come within the ambit of copyright misuse:

Reverse engineering. Software licenses commonly bar reverse engineering the program. Such prohibitions arguably represent efforts to secure an exclusive right not granted by the copyright. On the other hand, they may merely represent efforts to maintain the trade secrets in the software which copyright protection does not displace.

Platform use restrictions. A software publisher's license agreement for software development tools requires that the tools be used for the sole purpose of developing end-user application software that runs under the publisher's operating system. Is this a misuse of its copyright—seeking to obtain unfair advantage by discouraging the creation of works that help create a market for a competing operating systems—or is it simply a fair limitation: "You can create all the competing software you want, but not with our tools"?

Database licenses. A database that only embodies the "sweat of the developer's brow" is not copyrightable. If the developer requires his customers to agree not to copy it, does this secure a limited monopoly not granted by the Copyright Office? Or is it simply an agreement, altogether outside of copyright law, to make the fruits of his labor available on conditions freely accepted? (See *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447 (7th Cir. 1996) (license not preempted by copyright law).)

Whether these or other use-restricting provisions fall afoul of the copyright misuse doctrine will be determined by future cases. But drafters of software license agreements and counsel in copyright infringement actions must now carefully weigh the impact of the copyright misuse doctrine on their drafting, demand letters, pleadings and discovery.