

Collateral Damages:

Why Congress Needs To Fix Copyright Law's Civil Penalties



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Introduction

Imagine that you run a business, and one day you ask your lawyer whether selling one of your products could lead to a lawsuit. She tells you that the product is well-designed and responsibly marketed, but there's still a chance that someone might get injured, and sue you. But then your lawyer says something crazy: she has no idea what you might have to pay if you lose. It could be \$100, and it could be \$10 million. And crazier still, the damages could have no relationship to the harm you caused; a person whose injuries cost \$100 to fix could still get \$10 million.

What are the consequences of this scenario? Any lawsuit becomes a game of chance, and losing could mean the end of your business. You might well decide you can't risk selling your product at all. When the penalties are harsh and unpredictable, a legal threat becomes a powerful weapon. Rational people will avoid even lawful, important activities for fear of massive penalties if they've miscalculated and a court rules against them.

In most areas of the law, we try to avoid this kind of unfairness and uncertainty by making sure that we tie penalties to the harm caused, with additional penalties where someone seems to have caused harm deliberately. But that's not what we do when it comes to copyright infringement. The U.S. allows copyright holders to ask for "statutory damages" of \$750 to \$150,000 per copyrighted work, with no guidelines and few controls over where in that huge range a given case will fall. The result is capricious, unpredictable, and often excessive penalties.

This whitepaper explains U.S. copyright law's civil penalty regime. It describes the two major problems with this regime: excessive penalties and unpredictability. It discusses the harms that flow from this broken law. Finally, it suggests some measured changes Congress can make to fix these problems.

The Law

U.S. law lets copyright holders ask for "statutory damages" in an infringement lawsuit. If a copyright holder proves its case, and asks for statutory damages, a jury decides how much the defendant must pay—anywhere from \$750 to \$30,000 per copyrighted work.¹ If the court finds that the infringement was "willful," the maximum per work jumps to \$150,000.² In order to get statutory damages, the copyright holder has to register their work with the Copyright Office before the infringement happens, or within three months of the work's first publication.³

A copyright holder who asks for statutory damages *doesn't have to show any evidence of harm, or that the defendant made any profit from the infringement*. A copyright holder can, if she chooses, simply ask the jury to come up with a number.

¹ 17 U.S.C. § 504(c)(1).

² § 504(c)(2).

³ § 412.

Copyright holders can choose between statutory damages and actual damages right up until the court issues a final judgment.⁴ That means a plaintiff can try to convince a jury that it suffered *more* than \$150,000 in actual harm per work, and still choose the automatic award behind “door number 2” if the jury doesn’t buy it.

The Copyright Act doesn’t give judges and juries any guidance on how to choose a number within the \$750-\$150,000 range. It only says that the amount should be “as the court considers just.”⁵

And it’s not only people who copy or use creative works that can be hit with these penalties: copyright cases are often brought against distributors, owners of technology platforms, builders of digital tools and devices, and even investors. People only indirectly involved in any actual copyright infringement can be made to pay statutory damages, often multiplied by the hundreds or thousands when their products touch many different copyrighted works.

The penalties in a copyright suit are very different from almost all other kinds of civil lawsuits. In most personal injury, breach of contract, and patent or trademark infringement cases, a plaintiff can only recover enough money to compensate her for the actual harm, and no more. In egregious personal injury cases, a jury can award “punitive damages” over and above the cost of the injury, but punitive damages are normally limited to about ten times the actual injury, at most. Even in complex federal civil suits like antitrust and racketeering, damages are limited to three times the actual injury. In all of these cases, the injury must be proved with evidence. Copyright has none of these limitations.

U.S. copyright law’s massive civil penalties are also out of line with all other countries, including countries with thriving film, music, TV, and literary industries. Worldwide, only 28 countries have statutory damages for copyright. Of those, 19 are emerging or developing economies and only 4, besides the U.S., are advanced economies.⁶ Only two European Union members, Bulgaria and Lithuania, have statutory damages.⁷ And of the countries that have statutory damages, *every one except the U.S.* imposes limits or safeguards that avoid some of the problems described below.⁸

Supporters of the current system usually offer three justifications for it. One is that statutory damages give courts a way to compensate copyright holders in cases where it is hard to prove the harm from infringement. The second is that they can be used to punish copyright infringers who acted deliberately or maliciously. And the third is that they deter people from infringing copyrights. Let’s see if these purported benefits outweigh the costs.

⁴ § 504(c)(1).

⁵ *Id.*

⁶ Pamela Samuelson, Phil Hill, and Tara Wheatland, “Statutory Damages: A Rarity in Copyright Laws Internationally, But For How Long?” 5-6, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2240569.

⁷ *Id.*

⁸ *Id.* at 13-26.

I. Excessive Penalties

Because statutory damages can be awarded in such a broad range, without firm guidelines or evidence requirements, penalties can be shockingly large. The pioneering digital music company MP3.com was ordered to pay over \$118 million in statutory damages for creating a database of music in order to give online access for those who already owned the songs on CD. The company was forced to shut down.⁹ Free Republic, a nonprofit conservative commentary website, was penalized \$1 million for posting copies of several *Washington Post* and *Los Angeles Times* articles in an effort to illustrate bias in the media.¹⁰ And a firm sued for making copies of 240 financial news articles for internal use was ordered to pay \$19.7 million, or \$82,000 per infringed article.¹¹ The actual harm suffered by the news service in that case was probably about \$60,000 *in total*.¹²

Individuals who infringe can also be on the hook, even if they have no commercial purpose. Most famously, Jammie Thomas-Rasset, a home Internet subscriber and mother of four, was assessed \$222,000 in statutory damages for sharing 24 copyrighted songs using the peer-to-peer software Kazaa—\$9,250 per song.¹³ And a jury found Boston University undergraduate Joel Tenenbaum liable for \$675,000 for sharing 30 songs.¹⁴ Several commentators observed that whatever one's views on peer-to-peer file-sharing and infringement, these awards against noncommercial users seemed excessive. Indeed, judges in both cases found the awards excessive and unfair, and tried to reduce them.¹⁵ One even implored Congress to reconsider copyright's penalties.¹⁶

Businesses connected to products or services that enable customers to interact with digital content are especially at risk of massive penalties that bear no connection to reality, because statutory damages are multiplied by the number of copyrighted works involved. For example, four major record labels sued XM Satellite Radio in 2006 over the design of a portable radio receiver with recording functions. They asked for maximum statutory damages. Given that XM broadcasted about 160,000 songs per month, a conservative estimate of the number of alleged infringements yielded a potential penalty of \$37 billion, nearly three times the revenues of the entire recording industry.¹⁷ The case was settled in 2007, with the threat of bankrupting damages undoubtedly playing a role.

⁹ *UMG Recordings, Inc. v. MP3.com, Inc.*, No. 00 Civ. 472 (JSR), 2000 WL 1262568, at *1, *6 (S.D.N.Y. Sept. 6, 2000).

¹⁰ *Los Angeles Times, Inc. v. Free Republic*, 99 No. CV 98-7840 MMM (AJWx), 2000 WL 565200, at *1 (C.D. Cal. Apr. 4, 2000).

¹¹ *Lowry's Reports, Inc. v. Legg Mason, Inc.*, 302 F. Supp. 2d 455 (D. Md. 2004).

¹² Blaine Evanson, *Due Process in Statutory Damages*, 3 Geo. J.L. & Pub. Pol'y 601, 632 n.203 (2005).

¹³ *Capitol Records, Inc. v. Thomas-Rasset*, 692 F.3d 899, 907 (8th Cir. 2012).

¹⁴ *Sony BMG Music Entm't v. Tenenbaum*, 660 F.3d 487, 490, 515 (2011).

¹⁵ *Sony BMG Music Entm't v. Tenenbaum*, 721 F. Supp. 2d 85, 117 (D. Mass. 2010) *vacated in part*, 660 F.3d 487 (1st Cir. 2011); *Capitol Records, Inc. v. Thomas-Rasset*, 799 F. Supp. 2d 999, 1011 (D. Minn. 2011) *vacated*, 692 F.3d 899 (8th Cir. 2012).

¹⁶ *Capitol Records, Inc. v. Thomas*, 579 F. Supp. 2d 1210, 1227 (D. Minn. 2008)

("The Court would be remiss if it did not take this opportunity to implore Congress to amend the Copyright Act to address liability and damages in peer-to-peer network cases . . . it would be a farce to say that a single mother's acts of using Kazaa are the equivalent, for example, to the acts of global financial firms illegally infringing on copyrights in order to profit in the securities market.").

¹⁷ See <https://www.eff.org/deeplinks/2006/05/record-labels-sue-xm-radio>.

In these and many other cases, statutory damages can reach jaw-dropping amounts that are out of proportion to any actual harm caused by infringement, and far beyond the multipliers commonly used in other areas of the law to punish and deter wrongdoing.

Notably, statutory damages are paid not to the government (as with a criminal fine) but to the copyright holder who brought the lawsuit. When statutory damages are many times the cost of the harm that the copyright holder actually suffered, the copyright holder comes out far ahead at the end of the lawsuit.

And while it's true that higher penalties will deter more people from infringing copyright—to a certain point—it's hard to see how the possibility of a \$675,000 penalty will deter an individual more than a \$50,000 one if either amount will cause bankruptcy. Increasing penalties beyond all reason doesn't increase deterrence.

II. Penalties Are Unpredictable

Damage awards vary widely from one copyright case to the next. With no guidelines in the Copyright Act and no requirement for plaintiffs to prove actual harm, each case becomes a roll of the dice. Anyone whose business and daily activities touch creative works—an entrepreneur, investor, artist, or technology user—faces incredible uncertainty.

For example, a record label challenging three companies that used its recordings under similar circumstances received \$10,000 per work in one case, \$30,000 per work in another, and \$50,000 per work in a third.¹⁸ One photocopying service that reproduced book chapters and articles for use in student coursepacks was ordered to pay \$5,000 per infringed work, while another was assessed \$50,000 per work for the same conduct.¹⁹

It's also hard to predict when a court will label an infringement “willful,” and eligible for the enhanced damages range of \$30,000 to \$150,000 per work. Sometimes, even a person or business that uses their best efforts *not* to infringe or encourage infringement, relying on fair use and other limitations on copyright law, is still declared a “willful infringer” and hit with massive penalties. This happened in the MP3.com case, even though MP3.com made online digital music available only to people who could prove they already owned the music on CD.

For a person who uses ten copyrighted works, being found liable for \$7,500 in damages is very different from being penalized at \$1,000,000. Yet both are possible—and there's little or no way to tell beforehand what a court will do. Sometimes courts hand down a massive penalty regardless of the user's motivations or attempts to comply with the law in good faith.²⁰

¹⁸ *Peer Int'l Corp. v. Luna Records, Inc.*, 887 F. Supp. 560 (S.D.N.Y. 1995); *Peer Int'l Corp. v. Max Music & Entm't, Inc.*, No. 03 Civ. 0996KMWDF, 2004 WL 1542253 (S.D.N.Y. July 9, 2004); *Peer Int'l Corp. v. Pausa Records, Inc.*, 909 F.2d 1332 (9th Cir. 1990).

¹⁹ Compare *Basic Books, Inc. v. Kinko's Graphics Corp.*, 758 F. Supp. 1522, 1543-45 (S.D.N.Y. 1991) with *Princeton Univ. Press v. Mich. Document Servs.*, 855 F. Supp. 905, 913 (E.D. Mich. 1994) (*Rev'd*, *Princeton Univ. Press v. Mich. Document Servs.*, 99 F.3d 1381, 1392 (6th Cir. 1996)).

²⁰ *Los Angeles Times, Inc. v. Free Republic*, *supra* note 10.

III. Excessive and Unpredictable Penalties Undermine Copyright's Purpose

A. Copyright's Penalties Are a Roadblock for Entrepreneurship

Legal risk is often a normal part of doing business. The way most companies manage that risk is by trying to abide by the law.

But if your technology could touch copyrighted works (as many do these days), it's not always clear how the law applies. And that means companies can't figure out where and how to invest. Because massive statutory damages can be awarded even if your product has little or no impact on the market for the copyrighted works, and a good faith attempt to comply with the law (such as by adhering to copyright's fair use doctrine) might not prevent a business-killing award, innovators who don't start out in a favored relationship with major copyright holders effectively have no way to mitigate their risk at the outset—except to direct their creative energies away from many forms of information technology. And with no way to mitigate the risk of crippling damages in a lawsuit, innovators struggle to attract early investment.

The result is that today's copyright system unnecessarily restricts innovation in digital technology. In many cases, it gives major entertainment conglomerates who control thousands of copyrights a veto power over independently developed technologies that might challenge established players and create new markets for creative work.

Although there's no way to know what products and services were never brought to market because of the potential for massive statutory damages, the risks to innovation are not speculative. Innovators in digital audiotape,²¹ the VCR,²² the portable music player,²³ and digital video distribution²⁴ were all threatened with statutory damages. Discussing the demise of the original Napster service after a copyright suit in 2000, venture capitalists explained that investment in digital music “became a wasteland” for a decade, in part because of lawsuit risks.²⁵

Rational, predictable civil damages in copyright cases would allow entrepreneurs and investors to evaluate and manage their risks up front so that innovation can flow.

²¹ Jube Shriver, Jr., *Battle Over Digital Audiotape: Lawsuit: Songwriter Sammy Cahn and Four Others File a Class-Action Suit Seeking to Block U.S. Sales of the Machines. They Claim Sony is Infringing On Copyrights*, L.A. Times (Jul. 10, 1990), available at http://articles.latimes.com/1990-07-10/business/fi-172_1_songwriter-sammy-cahn; see also *CBS Songs v. Amstrad Consumer Electronics Plc*, [1987] 2 WLR 1191 (House of Lords 1988) (similar suit against maker of analog audiotape recorders).

²² *Sony Corp. of Am. v. Universal City Studios, Inc.*, 464 U.S. 417 (1984).

²³ *Recording Indus. Ass'n of Am. v. Diamond Multimedia Sys., Inc.*, 180 F.3d 1072 (9th Cir. 1999).

²⁴ *Viacom Int'l, Inc. v. YouTube, Inc.*, 676 F.3d 19 (2d Cir. 2012).

²⁵ Michael Carrier, “Copyright and Innovation: The Untold Story” 22, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2099876.

B. Copyright's Penalties Chill Free Speech

Building upon the work of others is an indispensable part of art and culture. Quotation and satire are tools of political participation as well as cultural life. These activities are protected by copyright's built-in limitations, including the fair use doctrine and the ban on copyright in ideas. The Supreme Court has said that these limitations are what keep copyright law from violating the freedom of speech guaranteed by the First Amendment to the Constitution.²⁶ But the boundaries of fair use, and the distinction between ideas and expression, are sometimes unclear. When the consequence of crossing these sometimes fuzzy boundaries is thousands or millions of dollars in automatic damages, many people will stay away entirely.

Fair use allows a production like Comedy Central's Daily Show to compile clips of cable news broadcasts into biting commentaries on politics and the media without asking permission to use each clip. The Daily Show can rely on the vast resources and commercial relationships of a large corporate parent to mitigate the risk of statutory damages. An independent satirist lacking those resources must face the possibility of ruinous lawsuits and bankruptcy to create and share Daily Show-style video commentaries.

The same risk impedes documentary filmmakers, amateur video creators, musicians, and writers. By discouraging artists from exercising the rights that copyright reserves to them, the broken civil penalty regime chills free speech.

C. Copyright's Penalties Fuel Lawsuit Abuse

The potential for six-figure recoveries with no proof of harm attracts those who would use the legal system itself as a money-making scheme. Lawyers representing pornography producers, filmmakers, and photo agencies have filed thousands of lawsuits against Internet users across the U.S. These cases are rarely if ever tested in court. Instead, lawyers use the courts' subpoena power to identify home Internet subscribers and website owners. Then they threaten and harass their targets into paying cash "settlements" of \$2,000 to \$10,000.²⁷

The threat of six-figure statutory damages is one of the most effective clubs wielded by these "copyright trolls" to coerce settlements. For a typical Internet user, a threat of ruinous damages such as those awarded in the *Tenenbaum* and *Thomas-Rasset* cases is reason enough to settle a case for several thousand dollars, even when he or she did not infringe any copyrights. In these cases, statutory damages effectively nullify the procedural safeguards for defendants that Congress and the courts have created. By providing hefty,

²⁶ *Eldred v. Ashcroft*, 537 U.S. 186, 219-221 (2003).

²⁷ See, e.g., *Nu Image, Inc. v. Does 1-23,322*, 799 F. Supp. 2d 34 (D.D.C. 2011); *On The Cheap, LLC v. Does 1-5,011*, 280 F.R.D. 500, 502 (N.D. Cal. 2011); *Mick Haig Prods. E.K. v. Does 1-670*, 687 F.3d 649 (5th Cir. 2012); *Ingenuity 13 LLC v. John Doe, No. 2:12-cv-8333-ODW*, 107 U.S.P.Q.2d 1241, 2013 WL 1898633 (C.D. Cal. May 6, 2013); *Malibu Media, LLC v. John Does 1, 6, 13, 14, and Bryan White*, No. 12-2078, 2013 WL 3038025 (E.D. Pa. Jun. 18, 2013); *reFX Audio Software Inc. v. Does 1-97*, No. 13-cv-0409, 2013 WL 3766571 (E.D. Mo. Jul. 16, 2013); *Purzel Video GMBH v. Does 1-67*, No. 4:13-CV-450 SNLJ, 2013 WL 3941383 (E.D. Mo. July 31, 2013); Sean B. Karunaratne, *The Case Against Combating BitTorrent Piracy through Mass John Doe Copyright Infringement Lawsuits*, 111 Mich. L. Rev. 283, 293 (2012); Shyamkrishna Balganeshe, *The Uneasy Case Against Copyright Trolls*, 86 S. Cal. L. Rev. 723 (2013).

automatic monetary awards even where there is little or no financial harm, they allow unscrupulous lawyers to reap windfall profits from campaigns of lawsuit threats.

Copyright trolling is a widespread problem. Although one notorious outfit known as Prenda Law ceased its lawsuit campaign in January 2013 and was later sanctioned for fraud, copyright troll suits (identified in one study as copyright suits against multiple John Doe defendants) were nearly one-third of *all* the copyright suits filed in the U.S. in 2013. In Illinois, Indiana, and Wisconsin, these suits were over *half* of the copyright suits filed in that year.²⁸

D. Copyright's Penalties Stop the Courts From Doing Their Job

Copyright's irrational and unpredictable civil penalties mean that close cases that could benefit from a court's thoughtful consideration are often settled without creating a lasting precedent. With statutory damages raising the stakes of litigation to an impossible level, the courts cannot do their job of interpreting and clarifying the law.

This is especially harmful in fair use cases. Fair use is a vitally important part of copyright. By allowing some uses of copyrighted work without permission for purposes like scholarship, criticism, commentary, journalism, and the creation of new works, fair use promotes creativity and keeps copyright in line with the First Amendment's guarantee of free speech. But fair use is a flexible doctrine developed through court cases. When the threat of statutory damages keeps potential fair users from risking a court challenge, courts are unable to develop a body of decisions to guide other would-be fair users.

Because they keep even close cases from going to court, out-of-control statutory damages also make it much harder for the courts to help fix other problems in copyright law, including the "orphan works" problem (works for which an owner can't be located to give permission) and refining fair use for the digital age. Cases that could help resolve these issues through precedent often don't get brought.

IV. Rational Remedies: What A Fix Might Look Like

One or more small changes to copyright law could go a long way towards fixing these problems.

First, Congress could remove the threat of statutory damages for people who believe, and have reasonable grounds for believing, that their use of copyrighted works is legal. This would allow artists and journalists who rely on fair use, and digital entrepreneurs who take care not to encourage infringement by their users, to create and do business while keeping their risk manageable.

Second, Congress could require that copyright holders who bring lawsuits must present evidence of harm whenever possible. In most cases, subpoenas and other "discovery" tools of modern litigation give copyright holders the ability to gather evidence of their actual

²⁸ Matthew Sag, "Copyright Trolling: An Empirical Study" 24, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2404950.

harm. In the rare cases where it's actually very difficult or impossible to prove harm, the courts could waive this requirement.

Third, Congress could reduce the maximum and minimum amounts for statutory damages in cases that involve personal, noncommercial uses of copyrighted works. A lower limit for damages in these cases could deter infringement while removing the profit motive for abusive copyright trolling.

Finally, Congress can also amend the Copyright Act to add some guidelines for judges and juries in awarding statutory damages. These guidelines would reduce uncertainty and keep penalties more predictable. For example, Israel's copyright act tells judges to look at the duration of the infringement, the severity of the infringement, the actual harm, and the infringer's good faith, among other factors.