

United States District Court, S.D. New York.

UMG RECORDINGS, INC, Plaintiffs,

v.

MP3.COM, INC., Defendant.

Sept. 6, 2000.

RAKOFF.

The purpose of today's session is to enable the Court to make those rulings that are appropriate at this time as a result of the three day trial that was conducted before the Court last week. Largely, I will be reading from a written statement that I will try to make available at the end of the session as an unofficial outline of my rulings, but I may depart from it here and there in minor respects. In addition, I will ask the Reporter to give me an expedited copy of the transcript of these rulings, and I will review that transcript, hopefully by tomorrow, and make any small corrections that are necessary to conform the transcript to my determinations. However, I do not expect that there will be any material changes from what I am about to say here in open court.

At the outset, I want to once again thank counsel for both sides for their good offices in guiding me through the brave new world of rip and burn and beam and stream. I will continue to rely on their skill and professionalism in regard to the future phase of this litigation scheduled for November.

The present phase of the trial has been devoted to all issues relating to the award of statutory damages *except* the determination of which of the copyrighted compact discs that were the subject of defendant's infringement were covered by copyrights that were validly registered by the remaining plaintiffs. Defendant also reserved the right to brief a constitutional claim that the minimum statutory damages in this case should be \$500 per CD rather than \$750 per CD: but for reasons that I will get to shortly, that issue has now become moot and need not be further pursued.

Of the issues litigated in this phase of the proceedings, the only ones that were the subject of evidentiary dispute were "willfulness" and, to a lesser extent, certain aspects of "deterrence." But in my determinations I will also refer to certain other issues that were the subject of legal argument and that are relevant to a determination of statutory damages.

In making my determinations, the standard of proof that I have applied is that at all times it has been plaintiffs' burden to establish each element of their claims of statutory damages by a preponderance of the credible evidence. Additionally, however, even though I find no persuasive support defendant's contention that plaintiffs should have to carry the higher burden of proof of "clear and convincing evidence," as a kind of independent check on my own conclusions I have

gone back and analyzed the credible evidence under that higher standard and determined that, even under that higher standard, my findings would be exactly the same. Put another way, even though some of my findings are partly premised on credibility determinations and relate to hotly disputed issues of fact, I have a high level of confidence that they reflect the real truth of these matters.

That truth leads me to conclude that defendant's infringement was indeed willful, but that there are mitigating factors that substantially reduce the level of damages that might otherwise be appropriate for such willful infringement. I will indicate approximately what that bottom-line level of damages should be in dollar terms, but only after I first review my findings of fact and conclusions of law.

Finding Number 1. In September 1999, the defendant began to develop an expanded My.MP3.Com service that was later introduced as the "Beam-It" and "Instant Listening" services in January 2000. (Let me mention parenthetically that I will not necessarily provide a citation here for every single finding I make, particularly where, as in the case of this first finding, the facts are undisputed and, indeed, are essentially stipulated in the portion of the Pretrial Consent Order that deals with the undisputed facts. The underlying record supporting my findings is, of course, publicly available.)

Finding Number 2. Even before embarking on the development of the expanded My.MP3.Com project, the defendant had expressed in no uncertain terms its recognition of the basic prohibitions of copyright law and the considerable potential for their violation in the context of MP3 downloading and streaming. Thus, for example, *The Official MP3.Com Guide to MP3* issued in 1999, which is plaintiffs' Exhibit 19 in evidence, recites at page 62: "Warning. Current U.S. and international copyright laws forbid the unauthorized copying and distribution of music files over the Internet. Don't be the example chosen by some record company or recording artist to show the rest of the world that the law really works." Again, the same book, which was written by Michael Robertson and Ron Simpson, states at page 93: "Warning. It is against U.S. and international copyright law to distribute and/or sell music or any copyright-protected intellectual property without the written permission of the copyright holder. This includes posting MP3 files of copyrighted music on the Internet or making copies. Buying a music CD does not mean that you own the content. You merely have permission (also known as a *license*) from the legal owners of the material on that CD to listen to it in a noncommercial setting." Reference may also be made to the similar comments in the same book that were referred to yesterday in counsel's summation.

Finding Number 3. Notwithstanding this knowledge, defendant decided by October 1999, if not earlier, that the design of its new service-known internally as "Da Bomb"-would involve the unauthorized copying by defendant for commercial purposes of the contents of tens of thousands of copyrighted compact discs containing the contents of hundreds of thousands of copyrighted songs. The contents of the unauthorized commercial database thereby created would then be made available, chiefly on a per-CD basis, to those My.MP3.com customers who either, in the

case of users of “Beam-It,” could indicate that they already had possession of the CD in question, or who, in the case of users of “Instant Listening,” agreed to purchase the CD for delivery shortly in the future.

Finding Number 4. From the outset, numerous employees of defendant involved in the development of the “Da Bomb” project recognized that this reliance on a database of CDs copied by defendant for a commercial purpose without the permission of the copyright owners placed the entire project in legal jeopardy. A telling example is what happened immediately after the engineers working on the project were told, on September 21, 1999, that the basic design of the proposal would include, among other things, the creation of the aforementioned database and were asked to give their comments as to any problems they might foresee. Going well beyond technical engineering comments, the engineers very quickly began to question the legality of the proposed database. Thus in an internal e-mail distributed to the defendant's engineering team at 10:14 A.M. on September 22, 1999, which is plaintiffs' Exhibit 20 in evidence, engineer James Moore stated that “[t]he legal risks seem high. Are we going to pour a lot of engineering effort into something that we're not going to be able to deploy?” Similarly, in an e-mail sent to the same group at 2:33 P.M. that same day, which is plaintiffs' Exhibit 44 in evidence, Mike Oliphant, who was described here at trial as having more familiarity with legal issues than most of the engineering staff, stated: “I'm very concerned about the legal implications of this move. We need to have this be well thought through by people who understand the ins and outs of the laws governing music distribution.” Other members of the engineering staff, in e-mails sent the same date, also expressed concerns about other copyright infringement issues implicated by the difficulty of ensuring that the user of these services was in fact the lawful owner of a copy of the CD whose sounds he was seeking to have transmitted to him from defendant's database. *See, e.g.*, plaintiffs' Exs. 21 and 22 in evidence.

Finding Number 5. This latter issue, which the defendant's employees referred to, somewhat euphemistically, as the “security” issue but which they recognized to be an issue of contributory infringement, was never fully solved, as even defendant now concedes in the stipulated facts. But defendant, proceeding with considerable speed and secrecy, launched the new system anyway on or about January 10, 2000. I accept defendant's contention that the primary motivation for speed and secrecy was to gain competitive advantage. But a concomitant result was that the defendant could not reasonably rely on anyone except its own counsel, the firm of Cooley Godward, with respect to the significant legal issues being raised, since no one else who could even pretend to expertise in the area of copyright law had access to the facts of the proposal.

Finding Number 6. The most glaring legal issue that was being raised was not the so-called “security” issue, but rather the issue of what possible legal justification there could be for the unauthorized copying for commercial purposes of tens of thousands of copyrighted CDs, the contents of which would then be streamed to thousands of users. This problem was described in the defendant's internal documents as the “fair use” issue, reflecting defendant's awareness that its copying would be clearly unlawful unless justified by some “fair use” defense. That purported defense, as articulated by Mr. Robertson, was that the expanded My.MP3.Com services were

simply facilitating a private consumer's storage of his or her privately-purchased and privately-used CDs.

Finding Number 7. Legally, as this Court subsequently found, this purported justification was and is without any merit and does not meet a single one of the legal tests for "fair use." But more importantly for present purposes, factually this purported justification was little more than a sham. Under either the "Beam It" service or the "Instant Listening" service users of My.MP3.Com did not, in fact, store their own CDs or the sounds transmitted from their own CDs with My.MP3.Com.

Finding Number 8. This factual difference between an actual storage system and what defendant was planning was fully recognized by defendant at all times relevant. Indeed, as indicated in both the exhibits and the testimony, the difference between "DaBomb" and simple storage was critical to the anticipated commercial success of the new service, since, by contrast with competitors like MyPlay, a user of My.MP3.com, after placing an order for future delivery of the CD under the "Instant Listening" service or indicating certain indicia of purported ownership of the CD under the "Beam-It" service, could arrange for defendant to instantly stream the defendant's unauthorized copy of the CD to the user. Based on both the reasonable inferences to be drawn from the exhibits and the Court's assessment of the credibility and demeanor of the witnesses, the Court finds that the defendant and its employees understood at all times that the "storage" analogy was strained at best. While they camouflaged the critical differences with broad-brush appeals to "consumer rights," they were in fact never in any doubt that this purported justification for their otherwise obvious copyright infringement rested on a doubtful factual premise.

*4 Finding Number 9. The defendant also recognized at all times that no one but its outside counsel, Cooley Godward, could provide defendant with legal advice on its copyright infringement problems that it could reasonably rely on. This brings me to what counsel and I have been referring to as the "*Bilzerian*" issue. While I think that plaintiffs have the better of this issue, I find in the end that I do not need to reach it, because even accepting into evidence all the testimony that plaintiffs sought to exclude on the grounds of the *Bilzerian* case, I find that plaintiffs have still met their burden of proving willfulness. Indeed, the record of this trial establishes overwhelmingly that everyone from mid-level management up to defendant's board of directors looked to outside counsel, Cooley Godward, as the sole source of reliable advice on the so-called "fair use" issue. Thus as early as October 12, 1999, if not earlier, Mr. Rhodes was called in to address this issue, *see* plaintiffs' exhibit 24 at p. 7, and, as the documents show and Ms. Kantor, among others, clearly testified, all legal issues in this area were more or less automatically referred to him and his colleagues at Cooley Godward.

But what was counsel's advice? We will never know, for the defendant, as is its right, has invoked attorney-client privilege and expressly disclaimed any defense of reliance on counsel. Adverting for a moment the so-called "*Nabisco*" issue, the Court is clear that it may not draw an adverse inference from the invocation of the privilege, that is, the Court may not infer from the

invocation that the advice that defendant received from its outside counsel was negative, or was premised on insufficient disclosure to counsel, or anything of the sort. But, in the absence of any defense of advice of counsel, defendant has proffered no credible evidence whatever that rebuts plaintiffs' clear and convincing proof that defendant knew at all times that its copying of plaintiffs' CDs was presumptively unlawful, that its fair use justification was factually and legally very doubtful, and that no one but its outside counsel could be relied upon to advise it as to whether there was, nonetheless, a good faith basis for proceeding. Given defendant's decision not to defend here on the basis of any reliance on such advice, there is virtually no escape from a finding that defendant willfully infringed plaintiffs' copyrights.

From the foregoing findings of fact, two conclusions of law immediately follow:

First, I conclude that defendant willfully infringed plaintiffs' copyright. As I indicated at the start of the trial, "willfulness" in the context of statutory damages for copyright infringement means that the infringer either had actual knowledge that it was infringing the plaintiffs' copyrights or else acted in reckless disregard of the high probability that it was infringing plaintiffs' copyrights. Based on the foregoing findings of fact, I find that plaintiffs have carried their burden of proving that the defendant had actual knowledge that it was infringing plaintiffs' copyright.

Second, as a result of the finding of willfulness, the Court now has the option of imposing as much as \$150,000 in statutory damages per infringed CD. Conversely, the lower end of the range is either \$750 per CD or, if defendant's constitutional argument has merit, \$500 per CD. I have considered the issue of damages under both possibilities, that is, with a possible floor of \$750 per CD or a possible floor of \$500 per CD, and find that the floor level makes absolutely no difference to my conclusion of what is the appropriate award in this case. Accordingly, the constitutional issue will not have to be briefed, as I find it is entirely moot.

But where within this enormous range of \$500 or \$750 per CD to \$150,000 per CD should the Court impose damages? In making this determination, I must consider not only willfulness but also deterrence and all the other relevant factors that counsel for the parties so eloquently argued to the Court yesterday. Unlike plaintiffs' counsel, however, I believe any attempt to reduce this determination to some kind of mathematical formula or equation is spurious. There are a great many factors to consider and the Court must weigh them as best it can, based on the evidence and on the Court's reasoned evaluation of all the relevant factors and their interplay. I will, however, single out a few of the factors that seemed to me especially important in making this determination, without, however, denigrating other factors that counsel brought to my attention and that I also considered.

First, the size and scope of defendant's copyright infringement was very large and the potential for harm was similarly large. But on the other hand, plaintiffs have made not any attempt at this trial to prove any actual damages they may have suffered. There are at least two typical ways they might have done so, either by showing the fair market value of the copyrights in question, their property value so-to-speak, or by showing the profits, if any, that defendant realized from

the infringement, such as perhaps increased advertising revenues reasonably attributable to the increased usage of the enhanced My.MP3.com. Plaintiffs did not pursue either alternative, nor any other way of showing actual damages. Of course, they are not required to: that is why, among other reasons, Congress provided statutory damages. But in determining the level of statutory damages, the Court views the absence of any proof of actual damages as a mitigating factor favorable to the defendant.

Second, while defendant obviously continued its willful infringement until the time of the Court's ruling on April 28, 2000, the Court essentially agrees with defendant's counsel that defendant's conduct since May of this year has on the whole been responsible and this is a mitigating factor in defendant's favor. I also credit that portion of Mr. Robertson's testimony in which he indicated that, even from the outset, he shunned the kind of lawless piracy seemingly characteristic of some others operating in this area. While the defendant's willful copyright infringement was a very serious transgression, defendant's otherwise responsible conduct is an appropriate mitigating factor for the Court to take into account.

Third, while the defendant's size and financial assets are highly relevant to arriving at the appropriate level of statutory damages, the Court declines to engage in speculation as to what might be the effect of any award on other litigations.

Fourth, while the difficult issue of general deterrence must always be approached with caution, there is no doubt in the Court's mind that the potential for huge profits in the rapidly expanding world of the Internet is the lure that tempted an otherwise generally responsible company like MP3.com to break the law and that will also tempt others to do so if too low a level is set for the statutory damages in this case. Some of the evidence in this case strongly suggests that some companies operating in the area of the Internet may have a misconception that, because their technology is somewhat novel, they are somehow immune from the ordinary applications of laws of the United States, including copyright law. They need to understand that the law's domain knows no such limits.

Weighing not only the foregoing factors but all the other relevant favors put before the Court, the Court concludes, and hereby determines, that the appropriate measure of damages is \$25,000 per CD. If defendant is right that there are no more than 4,700 CDs for which plaintiffs qualify for statutory damages, the total award will be approximately \$118,000,000; but, of course, it could be considerably more or less depending on the number of qualifying CDs determined at the final phase of the trial scheduled for November of this year.

That concludes the rulings of the Court.