IDEAS ON INTELLECTUAL PROPERTY LAW

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Can licenses limit competitors' use?

Copyright ruling hits third-party software support providers

Purchasers of software know that it's not just the license that can take a bite out of their wallets — it's also the costly maintenance contracts. Smelling an opportunity, third-party providers have begun offering licensees cheaper maintenance and support alternatives. But one software company has struck back, and the favorable ruling it obtained in its copyright infringement lawsuit against a third-party provider may make it harder for such businesses to compete.

CASE DEVELOPMENTS

Oracle USA, Inc., licenses customized enterprise software and sells its licensees maintenance contracts. The maintenance includes software updates.

Updates to enterprise software must be tested and modified to fit licensees' individual customizations before being implemented. The testing process requires the creation of "development environments" that contain a copy of the software. Oracle's licenses permit its licensees to maintain their software and make development environments for themselves. Some licensees outsource the maintenance to Oracle but also to third parties, such as Rimini Street, Inc.

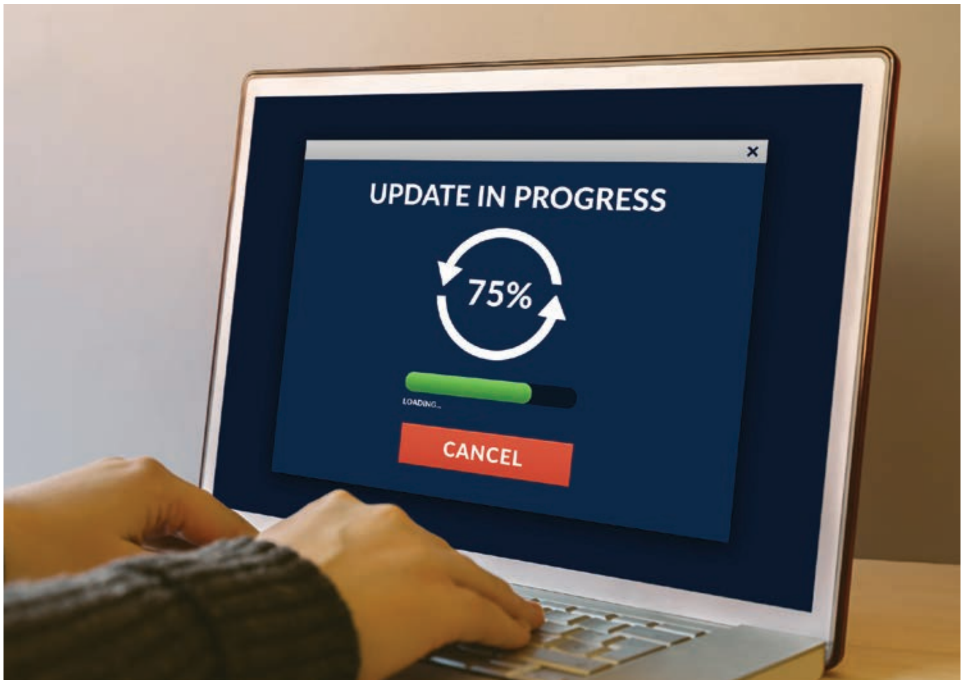
To compete effectively with Oracle's maintenance services, Rimini needed to provide software updates. This required copying the software, which, unless allowed by license, would constitute infringement.

Oracle sued Rimini for copyright infringement. The alleged infringement included copying software under the license of one Rimini customer for work for other existing customers or for unknown or future customers (so-called "cross-use infringement"). After a jury ruled in Oracle's favor, Rimini appealed to the Ninth Circuit Court of Appeals.

LICENSE LIMITATIONS

On appeal, Rimini asserted the express license defense. Under that defense, the existence of a license defeats a claim of copyright infringement. Because Rimini didn't possess a license to copy or modify Oracle's software, the success of its defense depended on whether its infringing acts fell within the scope of its customers' licenses.

Rimini contended that its cross use under the licenses for two of the three types of software at issue wasn't infringement. It claimed that it could create environments without restriction because any business that might hire it to service Oracle software would have a license to create development environments.



COPYRIGHT MISUSE DEFENSE FAILS, TOO

The defendant in the *Oracle USA, Inc. v. Rimini Street, Inc.* case also asserted the copyright misuse defense. The defense blocks copyright holders from leveraging their limited monopoly on the copyrighted material to control areas beyond that monopoly — that is, it applies when copyright holders try to impose license agreements that would prevent licensees from using any other competing product.

Rimini claimed that finding it liable for copyright infringement would limit third parties to making copies of Oracle's software only for archival and emergency backup purposes. But the Ninth Circuit Court of Appeals found that Oracle's licenses didn't preclude Rimini from developing competing software or providing competing support services. Rimini could still create development environments for a licensee for various purposes — *after* the licensee has become a Rimini customer.

The court dismissed Rimini's argument that forbidding it from creating development environments for licensees *before* they're customers gave Oracle an unfair "head start" in making copies. Just as a copyright holder has the "right of first publication," it also enjoys the right of "first copy."

Oracle responded — and the Court of Appeals agreed — that both licenses limited copying and use to support the licensee. The licenses didn't authorize Rimini to develop products it could sell for its financial gain. Work Rimini performed under one customer's license for other existing customers wasn't work in support of that particular licensee.

> Under the express license defense, the existence of a license defeats a claim of copyright infringement.

The same reasoning applied to work that Rimini performed for currently unknown or future customers. The licensees could hire a third party to maintain their software, but the licenses didn't permit them to grant a nonparty to the license a general right to copy proprietary software.

LOCATION MATTERS

The licenses for the third type of software at issue in the case were more restrictive than those for the other software types, limiting the copying of the software to the licensees' "facilities." Oracle's claim regarding this license related to Rimini's creation of development environments on Rimini computers, as opposed to the licensees' computers.

Rimini argued that a licensee's facilities could encompass Rimini's own servers. It pointed out that "sophisticated companies like Oracle's customers (and Rimini's clients)" don't keep all of their servers on their actual premises. They may own some, lease others and contract with third parties for even more capacity (for example, cloud computing providers). All of these servers, Rimini said, fell within "facilities."

The Court of Appeals, however, found that facilities under the control of a third party couldn't qualify as a licensee's facilities. It endorsed the trial court's interpretation of the definition of "a licensee's facilities" as requiring control. And the Rimini servers where the copying occurred were outside the licensee's control.

MAINTAINING THE COMPETITIVE EDGE

Among other things, this case demonstrates the importance of clear language in licenses. By tailoring its language to narrow possible uses of its software, Oracle lawfully limited other companies' ability to compete with it. □

Breaking news

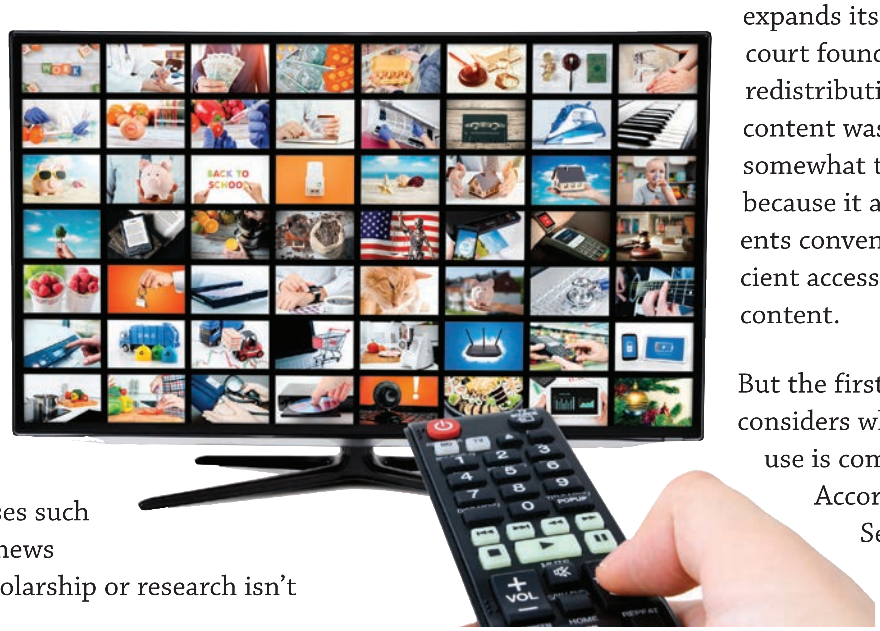
Selling access to clips of copyrighted programming isn't fair use

In an era that features hundreds of television channels and interactive, interconnected media, video clips have become a hot item. Not surprisingly, though, the sale of such clips by third parties raises copyright infringement concerns, as demonstrated by a recent case heard by the Second Circuit Court of Appeals.

NEWS CHANNEL SUES

TVEyes, Inc., continuously records the audiovisual content of more than 1,400 television and radio channels and imports that content into a text-searchable database. For a monthly fee, it offers a service allowing its "business and professional" clients to easily locate, view, archive, download and email clips of up to 10 minutes on topics of interest.

Fox News Network, LLC, sued TVEyes, alleging TVEyes infringed its copyrights by redistributing Fox's copied audiovisual content, thereby permitting TVEyes' clients to access that content without Fox's permission. The trial court found that some of the defendant's functions infringed, but it ruled that the "Watch" function that allowed for searching and viewing of clips was a permissible fair use of copyrighted material.



FAIR USE DEFENSE DEFINED

The U.S. Copyright Act provides that the "fair use" of a copyrighted work for purposes such as criticism, comment, news reporting, teaching, scholarship or research isn't infringement. The law identifies four factors that courts should consider when determining whether a use of copyrighted material is indeed fair. They are:

1. The purpose and character of the use (including whether it's of a commercial nature or for nonprofit educational purposes),
2. The nature of the copyrighted work,
3. The amount and substantiality of the portion used compared with the copyrighted work as a whole, and
4. The effect of the use on the potential market for or value of the copyrighted work.

No single factor is determinative.

SECOND CIRCUIT DECIDES

As the Second Circuit explained, the primary inquiry regarding the first factor is whether the use is transformative, meaning it communicates something new and different from the original work or otherwise expands its utility. The court found that TVEyes' redistribution of Fox content was at least somewhat transformative because it allowed its clients convenient and efficient access to a subset of content.

But the first factor also considers whether the use is commercial. According to the Second Circuit, the commercial nature of a use weighs against a finding of fair use — especially when, as in this case, the transformative character of the use is "modest." This factor, therefore, favored TVEyes only slightly.

> Fair use is less likely when the copying is extensive or encompasses the heart of the original work.

The court noted that the second factor rarely plays a significant role in the fair use evaluation and was neutral here. As for the third factor, the appellate court stressed that the relevant consideration is the amount of copyrighted material made available to the public, rather than the amount used by the alleged infringer.

TVEyes, the court pointed out, made available virtually all of the Fox programming its clients wanted to see and hear. While courts have rejected a bright-line rule proclaiming that the copying of a work's entirety can't be fair use, fair use is less likely when the copying is extensive or encompasses the heart of the original work and the transformative use of the work is thin. Given the brevity of the typical news segment on a particular topic, 10-minute clips of Fox News programming likely provided TVEyes' clients all the programming they sought and the entirety of Fox's message in the original. The third factor, the court said, strongly favored Fox.

Finally, the court weighed what it described as "undoubtedly the single most important element of fair use." Citing the success of the TVEyes business model, it concluded that, by selling access to Fox's content without a license, TVEyes deprived Fox of revenues that Fox was entitled to as the copyright holder.

PROGRAMMING CHANGE

Ultimately, the Second Circuit ruled that the balance of the factors strongly favored Fox and thus wasn't fair use. It sent the case back to the trial court with instructions for the district court to prohibit the "Watch" function via a permanent injunction. □

How the on-sale bar can threaten a patent

It's easy to understand an inventor's urge to get a new product to market. But that urge can backfire if a patent application hasn't yet been filed. Under the on-sale bar, the inventor could lose patent protection altogether. A pharmaceutical company learned this the hard way.

THE VITALS

In 2008, The Medicines Company obtained two patents covering an improved process for manufacturing an anticoagulant it had marketed for almost 20 years as Angiomax. The anticoagulant's sales represent more than 90% of the company's revenues. In February 2007, the company had entered into a distribution agreement with Integrated Commercialization Solutions, Inc. (ICS), to distribute the new formulation.

The Medicines Company sued Hospira, Inc., alleging infringement of its patents. Hospira argued that the patents were invalid. The trial court disagreed, and Hospira appealed.

THE HEART OF THE MATTER

Hospira contended that the patents were invalid under the on-sale bar. The bar applies if, before the date the patent application is filed ("the critical date"):

1. The invention is the subject of a commercial offer for sale, and
2. The invention is ready for patenting.

The Federal Court of Appeals easily found that the invention was ready for patenting and focused on the first element.

An offer for sale occurs if the other party's acceptance would make the offer a binding contract. The court found that the terms of The Medicines Company's distribution agreement with ICS made clear that the parties had entered into an agreement to sell and purchase the product. The relevant terms included:

- A statement that The Medicines Company "now desire[d] to sell the Product" to ICS and ICS "desire[d] to purchase and distribute the Product,"
- The price of the product,
- The purchase schedule, and
- The passage of title from The Medicines Company to ICS.

However, The Medicines Company asserted that the agreement didn't constitute an offer for sale because it allowed the company to reject all purchase orders submitted by ICS. The Federal Circuit dismissed this argument on two grounds.

> The on-sale bar applies if, before the date the patent application is filed, the invention is the subject of a commercial offer for sale and is ready for patenting.

First, the cases cited by The Medicines Company in support of its arguments did not have facts analogous to those here. Here, The Medicines Company agreed to sell Angiomax to ICS, and ICS agreed to buy it. Further, the parties explicitly and intentionally changed their previous distribution relationship to let ICS take title on receipt of the product at the distribution center. The passage of title, the court said, was a "helpful indicator" that Angiomax was subject to an offer for sale.

Further, the agreement required The Medicines Company to use "commercially reasonable efforts" to fill the purchase orders, contrary to the company's claim that it could reject all purchase orders. Regardless, The Medicines Company was simply unlikely to reject an order because Angiomax sales provided most of its revenues, and the agreement gave ICS the exclusive right to purchase Angiomax in the United States for its three-year period. And, under the Uniform Commercial Code, an exclusive distribution agreement imposes an obligation on the seller to use its best efforts to supply the goods, unless otherwise agreed.

NOT DEAD YET

Although the Federal Circuit found that the distribution agreement was a commercial offer for sale, it nonetheless remains to be seen whether the on-sale bar applies. The case was sent back to the trial court to determine whether the offer for sale covered the Angiomax created by the newly patented process. ◻

Giving trade dress infringement claim a shot

The hurdle for proving trade dress infringement is high. This is partly because, as the Sixth Circuit Court of Appeals recently explained, a plaintiff must produce evidence of nonfunctionality — a unique challenge since a plaintiff must prove evidence of an absence and product design often serves purposes beyond mere identification of the product's source. In the case in question, though, the court determined that the plaintiff had succeeded.

DISTRICT COURT SHOOTS DOWN CLAIM

Leapers, Inc., makes adjustable rifle scopes that are textured with "knurling." Knurling allows users to grip the products more easily and make fine-tuned adjustments. Leapers claims that it uses a unique knurling pattern that lets consumers recognize the company as the source of its products.

Leapers had an exclusive manufacturing contract with a factory in China, under which the factory agreed not to disclose any information related to Leapers' products. After the company ended the relationship, the manufacturer's factory manager formed a company that manufactured scopes for SMTS, LLC.

Leapers sued SMTS for trade dress infringement of its knurling design. The district court dismissed the case before trial, and Leapers appealed.

APPELLATE COURT TAKES ANOTHER LOOK

Trade dress generally refers to the overall appearance of a product. To succeed on a claim of trade dress infringement based on a product's design, a plaintiff must show that its design:

- Is nonfunctional,
- Has acquired a secondary meaning, and
- Is confusingly similar to the allegedly infringing design.

The trial court found that Leapers' design couldn't satisfy the nonfunctional requirement.

To establish nonfunctionality, a plaintiff must prove that its design feature isn't essential to the use or purpose of the product and that it doesn't affect the product's cost or quality. Evidence that a design is purely ornamental, incidental or arbitrary can constitute evidence of an absence of functionality.

The appellate court agreed with the trial court that knurling is "inalterably functional" because it allows a rifle scope user to "grasp or grip a thing more securely." But, it said, Leapers didn't argue that its trade dress consisted of knurling — it alleged that its trade dress consisted of a unique design printed into knurling. The Sixth Circuit concluded that a jury could reasonably find Leapers' design was ornamental and nonfunctional and therefore reversed the trial court's dismissal.

THE NEXT ROUND

The Court of Appeals declined to consider the other two requirements for trade dress infringement, sending the case back to the trial court for further consideration. So, while the company prevailed on the nonfunctionality element, the question remains as to whether it will succeed in proving infringement.

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