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Entertainment Industry Loses in Web Case

By MATT RICHTEL

SAN FRANCISCO, April 25 — In a huge setback to the big record and movie companies, a federal judge in Los Angeles ruled in favor of two online services that allow people to share music, movies and other digital files freely over the Internet.

The decision puts the brakes on the momentum the entertainment industry had previously enjoyed in its legal efforts to block file-swapping services, which have made it easy for consumers to acquire copyrighted material free.

Unless the decision is reversed on appeal, entertainment industry analysts said, it heralds a new era that is likely to force Hollywood and the record business to accelerate the development of their own fee-based online distribution services. At the same time, the industry is expected to step up its efforts to go directly after individuals who it believes are violating copyright laws by distributing music, movies and other digital material without paying for them.

Judge Stephen Wilson of United States District Court ruled that Grokster and StreamCast Networks, which offers the Morpheus peer-to-peer software, are not guilty of copyright infringement. The judge said those services — unlike Napster, an earlier music-swapping software company — were essentially no different from the companies that created the videocassette recorder, which also allowed consumers to make their own copies.

"This is a watershed day," said Wayne Rosso, the president of Grokster, who said his 20-month-old service is used by 10 million people each month. "What it does is rewrite the rules."

Mr. Rosso, as well as StreamCast executives, argued that their technology was used for many legal uses, like sharing personal files, and

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noncopyrighted works, and that they should not be blamed when users illegally exchange copyrighted files.

The ruling does not directly affect KaZaA, a software distributed from outside the United States by Sharman Networks, which has also been a target of the entertainment industry.

In the media companies' battle to stop such services, this is the first ruling by a federal court that found online-sharing software does not abet copyright infringement. Two years ago, a different federal judge found, in a case upheld on appeal, that Napster, previously used by tens of millions of people to share files, was guilty of wholesale copyright infringement. The ruling essentially drove Napster out of business.

But Judge Wilson ruled that Grokster and StreamCast are fundamentally different from Napster in terms of their underlying technology. The result, the judge ruled, is that the two newer services have less ability to control what files their users download, and to prevent those users from gaining access to copyrighted material. Therefore, he said, they cannot be held accountable for their users' actions.

The services, which distribute the software free, make money by selling advertising that appears when files are opened.

"The ruling basically has recognized that technology can't be held back by archaic laws, and that's what the industry has been trying to do," Mr. Rosso said.

But the music and movie companies, pledging to appeal the decision, said the two services were overwhelmingly used by people to exchange copyrighted material. And they said the decision would force them to become more aggressive in suing individual users.

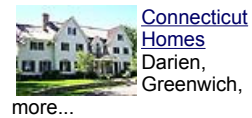
Already, the music industry has filed lawsuits against four college students it accuses of operating Web sites used by fellow students to search a computer network for copyrighted files.

In a separate matter, a judge on Thursday ordered that a large Internet service provider, [Verizon](#), must turn over to music companies the names of two customers suspected of having offered copyrighted music for download. The music companies are seeking the names as part of the new legal strategy of suing individual traders of free songs.

Andrew Lack, chief of Sony Music, said the music companies would pursue the biggest online traders in hopes of deterring other users.

"I don't think you have to go after 10 million or 5 million or 10,000 people," Mr. Lack said today. "You choose the users that make the case credible."

In recent years, the entertainment industry has characterized defeating



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In recent years, the entertainment industry has characterized defeating Napster and other such music sharing services as essential to its own success. But Mr. Lack contended that the judge's decision actually represented a victory because it supported the industry's position that individual users who freely trade copyrighted works are guilty of violating the law.

"I'm relieved on some level because the judge affirmed everything we've been saying, but for one point, which may distract people from the real meaning of the decision," Mr. Lack said, referring to today's setback for the record industry.

But Philip Leigh, a digital media analyst with Raymond James & Associates, an investment banking firm in St. Petersburg, Fla., said that the decision was a clear signal that the industry must fundamentally change, and provide inexpensive, easy-to-access music in a way that consumers have grown accustomed to on services like Napster and Morpheus.

"The music business will transform," he said. "Prices of online music will get cheaper, and consumer user rules will be liberalized."

Judge Wilson's decision focused to a large extent on the technological differences between the services and Napster.

In the case of Napster, users exchanged files that they stored on their home computers. But when Napster users wanted to find out what songs were available on other computers, they sent a search request through Napster's central computers. Those computers, in turn, searched the network to see if a media file was available.

But the networks operated by Grokster and StreamCast Networks are considered decentralized. The difference being that users searching for a song or movie file do not go through the companies' computer servers. Rather, the companies' software searches the entire network of computers for those with the most powerful systems. When the software finds a powerful computer, it turns it temporarily into a search hub, or supernode. That node then searches the network for a user's request.

As a result, Judge Wilson wrote, there was no admissible evidence "that the defendants have the ability to supervise and control the infringing conduct."

The judge said it was clear that many users employ the service to exchange copyrighted files. And he said it was also clear that the two services are profiting from their software by selling advertising. But he said that the technology was less like Napster and more analogous for legal purposes to VCR's.

In a landmark decision in 1984, the Supreme Court ruled in favor of [Sony](#), which had been sued by the television industry on the ground that

the VCR could be easily used to record copyrighted programs.

Grokster and StreamCast are not significantly different from companies that sell home video recorders or copy machines, both of which can be used to infringe copyrights, Judge Wilson wrote in his 34-page opinion.

But David Kendall, a lawyer for the Motion Picture Association of America, which represented Hollywood's interests in the case, said he believed that an appeals court would overturn the decision, finding that Grokster and StreamCast really are the same as Napster.

"It's a distinction without a legal difference," Mr. Kendall said. "We don't believe it's legally significant."

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