

Sega Enterprises, Ltd. v. Accolade, Inc., 1993 U.S.
App. Lexis 78 (9th Cir. January 3, 1993)

Kathleen Love

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Sega Enterprises, Ltd. v. Accolade, Inc.,

1993 U.S. APP. LEXIS 78 (9TH CIR. JANUARY 3, 1993).

Introduction

Sega Enterprises, Ltd. (“Sega”), a manufacturer of video entertainment systems, sued Accolade, Inc. (“Accolade”), a manufacturer of video entertainment software compatible with Sega’s systems, for copyright and trademark infringement. The United States District Court for the Northern District of California granted Sega’s motion for a preliminary injunction precluding Accolade’s use, manufacture and sales of its Genesis III-compatible video games. On appeal, the United States Court of Appeals for the Ninth Circuit reversed, finding Accolade’s copying fair use and Sega responsible for any trademark confusion.

Facts

Plaintiff-appellee, Sega, develops and manufactures video entertainment systems, including the Genesis console and video game cartridges. Defendant-appellant, Accolade, is a developer and manufacturer of computer software including video game cartridges, some of which are compatible with the Genesis console. Sega markets its products in a number of Southeast Asian countries, including Taiwan. Taiwan does not recognize foreign copyrights and a number of counterfeiters have managed to exclude the Sega trademark from game programs in order to manufacture counterfeit cartridges. In order to protect its trademark rights in the Genesis console and Genesis-compatible games, Sega developed a trademark security system (“TMSS”). Upon insertion of a game cartridge, the Sega Genesis III searches for a security code. If the code is correctly located, the console grants compatibility and displays a Sega trademark. If the code is not located, access will be denied.

Accolade identified the code through a two-step process and created four games which were compatible with the Genesis III and displayed the Sega trademark. First, in order to learn the requirements for compatibility, Accolade employed a “reverse engineering” process. Part of that process involved disassembly, or transformation of the machine-readable “object code” into human-readable “source code.” From Sega game cartridges, Accolade generated printouts of the source code. From this source code, Accolade engineers discovered the requirements for compatibility with the Genesis console and documented the functional descriptions of those requirements. Second, Accolade created games for the Genesis. It maintained that it did not copy Sega’s game programs. It only used the information regarding the Genesis interface specifications.

Sega filed suit for trademark infringement and false designation of origin

under sections 32(1) and 43(a) of the Lanham Act.¹ It also alleged copyright infringement under the Copyright Act. Accolade counterclaimed for false designation of origin under section 43(a) of the Lanham Act.² The district court granted Sega's motion for a preliminary injunction after finding that the TMSS code was not functional, thus Accolade had no functionality defense to the trademark infringement claim. Regarding the copyright claim, the district court found that intermediate copying of the code constitutes infringement and rejected the fair use defense because Accolade disassembled the code for a commercial purpose, Sega lost sales and there were alternatives to copying in order to discover the functional aspects of the program. On appeal, the judgment was reversed, but the appellate court declined to issue an injunction *pendente lite* precluding Sega's further use of its security system.

Legal Analysis

The court of appeals examined the issue whether the Copyright Act precludes the disassembly of a copyrighted computer program for purposes of gaining access to functional, unprotected elements of the program. It found disassembly permissible under the Copyright Act when there is a legitimate reason for disassembling the program and when there are no other means of accessing the unprotected elements.

Accolade argued that disassembly of the object code does not constitute copyright infringement. It claimed that intermediate copying is permissible as long as the end product is not substantially similar to the copyrighted work. The court rejected this argument citing *Walker v. University Books*³ which held that use of only a portion or smaller version of a copyrighted work does not shield the user from liability. The court observed that on its face, the language of section 106 of the Copyright Act proscribes intermediate copying as it grants the copyright owner exclusive rights "to reproduce the work in copies."⁴

Accolade also claimed that disassembly in order to gain an understanding of functional ideas constitutes fair use under section 107 of the Copyright Act which establishes the fair use defense to an otherwise valid copyright infringement claim.⁵ The appellate court agreed that disassembly constitutes fair use when it is the only means of gaining access to unprotected aspects of a program and there is a legitimate interest in gaining access. Four factors are to be considered in determining whether a particular use is fair: the purpose and character of the use; the nature of the copyrighted work; the amount and substantiality of the portion used in relation to the copyrighted work as a whole; and the effect of the use upon the potential market.⁶

1. 15 U.S.C. § 1114 (a)(1), 1125(a)(1988).

2. 15 U.S.C. § 1125(a)(1988).

3. 602 F.2d 859, 864 (9th Cir. 1979).

4. 17 U.S.C. §106 (1988).

5. 17 U.S.C. §107(1988).

The court's analysis of the purpose and character of the use weighed in favor of a finding of fair use. Accolade copied Sega's software to discover functional aspects of the program. Any commercial purpose was indirect since the copying was merely intermediary in developing Accolade's own products. Accolade had no intention of bypassing its own creativity. Also, despite Accolade's commercial gain, the court found competition between video game manufacturers and the dissemination of numerous creative works serves the public interest. The presumption of unfairness was overcome given the purpose and character of the use.

The court found that the second factor, the nature of the copyrighted work, also weighed in favor of fair use. It said that many aspects of computer programs are utilitarian and not protected under the Copyright Act. Adopting the Second Circuit's approach in *Computer Assoc. Int'l, Inc. v. Altai, Inc.*,⁷ it found that when the computer program is broken down into its core functional elements, many aspects of the program are not protectible. Accolade had a valid fair use defense in that functional elements cannot be discovered without translating the code which in turn cannot be done without making copies of the code. In addition, there was no indication of a viable alternative to copying the code in order to find the functional elements. Disassembly was necessary to understand the functional requirements for Genesis compatibility. If disassembly was per se an unfair use, the owner of copyrighted material would have a monopoly over the unprotected functional aspects of the material. This was contrary to the express intent of Congress under the Copyright Act. Thus, the court found the nature of the copyrighted work was such that copying in order to access functional elements may constitute fair use.

The third statutory factor, the amount and substantiality of the portion used in relation to the copyrighted work as a whole, weighed against fair use. Accolade disassembled the entire copyrighted work. However, the court held that this factor was not conclusive or dispositive. It found that where the ultimate use is limited, the fact that the whole design was copied is of little importance.

Finally, the court found the effect of the use upon the potential market was indicative of fair use. Accolade did not attempt to usurp the market for Genesis-compatible video games. It wanted to become a legitimate competitor in the field. The court said Accolade undoubtedly affected the market by releasing its video games in the market. However, most consumers of video games purchase more than one game especially if the games are substantially different. Sega's attempt to limit competition in the market was clearly contrary to the express purpose of the Copyright Act of promoting creativity and competition. The effect of Accolade's copying on the market was minor and weighed in favor of fair use.

The court held that Sega had not shown a likelihood of success on the merits since three of the four factors weighed in favor of a finding of fair use. The third factor, substantiality of the portion used compared to the whole copyrighted

work, only weighed slightly in Sega's favor and was not dispositive. In light of the important public interest in stimulating artistic creativity, the court found disassembly of a copyrighted computer program for the purpose of seeking access to functional concepts fair use and dissolved the preliminary injunction.

The court then considered the issue of whether, on grounds of false display of trademark, a computer manufacturer may enjoin competing cartridge manufacturers from obtaining access to its computers through the use of an initialization code which causes the manufacturer's trademark to appear when access is gained. Use of the initialization code in Accolade's game cartridges caused the Sega trademark to appear upon access to the Genesis III. Section 32(1)(a) of the Lanham Act proscribes the reproduction of a registered mark which is likely to cause confusion among consumers.⁸ Section 43(a) prohibits false designation of the origin of goods where such use is likely to cause confusion among consumers.⁹ The court found that when there is no other readily available means of access to an unpatented system, use of the code is permissible regardless of the display of the misleading trademark.

Sega and Accolade agreed that use of the initialization code constituted a misuse of trademark and unlawful mislabeling from which confusion could result. The disagreement arose as to who was at fault for the confusion. Sega claimed that use of the code constituted trademark infringement and Accolade claimed that Sega's use of the TMSS constituted false designation of origin.

The court found Sega liable because the TMSS regulated access to an unpatented system of functional concepts and there was no indication of an alternate means of discovering those functional concepts. It said that Sega knew the code would limit competition in that competitors would learn how to use the code and their video games would end up falsely labeled. Sega should have foreseen that the code would discourage competitors who wanted to avoid false labeling.

Sega argued it should not be liable for false labeling because competitors were not precluded from developing games which did not display the Sega trademark. It contended that Accolade's engineers could have used an alternative method that did not employ the TMSS. Accolade argued that the TMSS is a functional feature which is necessary in order for a video game cartridge to operate on the Genesis III console. The court agreed with Accolade and held that the initialization was a functional feature and Accolade may lawfully use it. Factors which aid in determining whether a feature is functional include the availability of alternative designs, whether the feature is essential to the purpose of the design and whether the feature affects the cost or quality of the article. Because there was no evidence of a reasonable alternative means of gaining access to the Genesis III and because the TMSS code was essential to gaining access, the court held that Sega failed to establish nonfunctionality and was not entitled to injunctive relief under the Lanham Act.

8. 15 U.S.C. §1114(1)(a)(1988).

9. 15 U.S.C. §1125(a)(1988).

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Conclusion

Reversing the district court's grant of preliminary injunction, the court considered four factors as an indication of fair use under the Copyright Act. It examined the purpose and character of the use, including whether there was a commercial purpose, the nature of the copyrighted work, the amount and substantiality of the portion used and the effect of the use upon the potential market. The court found that Accolade's copying of Sega's copyrighted material was protected fair use because there was a legitimate reason for disassembling the program and no other means of accessing the unprotected elements.

As to the trademark claim, the court found that the trademark was misused where it served to limit competition and that Sega should have been aware of a likely false labeling effect on its video game competitors. The court also stated that Sega did not prove nonfunctionality where there was no evidence of a readily available alternative means of access to an unpatented system. Use of the code was therefore permissible regardless of the display of a misleading trademark.

Kathleen Love

