SECOND CIRCUIT REVERSES "HOT NEWS" JUDGMENT AGAINST THEFLYONTHEWALL.COM FOR PUBLISHING BROKER BUY-SELL RECOMMENDATIONS

On June 20, 2011, the Second Circuit Court of Appeals issued its opinion in *Barclays Capital Inc., et al. v. Theflyonthewall.com, Inc.*[1] *("Fly II")*, holding that the plaintiff brokerage firms cannot restrict the publication of their trading recommendations by an online news aggregator. While the Second Circuit did not abolish the "hot news" doctrine, which allows news purveyors to prevent free-riding by competitors, it found the doctrine preempted by federal copyright law where the news aggregator expends its own resources to discover and disseminate recommendations of numerous brokers.

Background

Plaintiffs (the "Firms") are a group of major financial institutions that provide securities brokerage services to the public. The Firms engage in extensive research regarding publicly traded companies and each produces recommendations to buy, sell or hold securities based on its own research. Each morning the Firms circulate their proprietary research and recommendations to select clients and potential clients in return for what they hope will be trading fees from clients acting on their recommendations.

Defendant, Theflyonthewall.com ("Fly"), is an internet-based news service that aggregates recommendations from 65 investment firms' analysts and publishes them to subscribers for a fee. The value of a Fly subscription is that it supplies subscribers with recommendations before they are made public. In other words, Fly's dissemination puts subscribers almost on par with the select group to which the Firms restrict timely delivery of their recommendations.

At issue on appeal was whether the district court erred in finding that Fly's publication of the Firms' recommendations constitutes "hot news" misappropriation under New York State law, and specifically whether federal copyright law preempts (and thus precludes) the state law "hot news" claim.

District Court Decision

In 2006, the Firms sued Fly in the Southern District of New York for federal copyright infringement (for excerpting large portions of research reports) and for "hot news" misappropriation under New York State law for Fly's publication of the Firms' recommendations. At a bench trial before Judge Cote, Fly conceded the copyright claim and the court entered a preliminary injunction that "restrain[ed] Fly from further infringement of 'any portion of the copyrighted elements of any research reports generated by Barclays Capital or Morgan Stanley.'"

[1] Docket No. 10-1372-cv, June 20, 2011.

The district court relied on a multi-factor test articulated in *National Basketball Assoc. v. Motorola, Inc.* ("NBA")[2] in concluding that the New York State "hot news" misappropriation claim survived federal preemption because: 1) the Firms generate or gather information at a cost; 2) the information is time-sensitive; 3) Fly's use of the information constitutes free-riding on the Firms' efforts; 4) Fly directly competes with a product or service offered by the Firms; and 5) the ability of other parties to free-ride on the Firms' efforts would reduce the incentive to produce the product or service, the existence of which would thus be substantially threatened. The district court specifically rejected Fly's argument that its efforts at collection, aggregation and dissemination of information meant that it was not free-riding on the Firms' efforts.

As a result, the court entered a permanent injunction enjoining Fly from reporting the Firms' recommendations for a period ranging from 30 minutes to several hours after such recommendations were released by the Firms. Fly appealed and sought a stay of the injunction, and the Second Circuit granted an expedited appeal.

Second Circuit Review and Holding

The Second Circuit reversed the district court, holding that the Firms' "hot news" claim was preempted by federal copyright law. The Second Circuit chided the district court for failing to consider the preemption issue, and instead "adopt[ing] as determinative *NBA*'s ruling that a narrow form of the 'hot news' misappropriation tort survives preemption." Importantly, however, the Second Circuit acknowledged that, pursuant to the *NBA* holding, the "hot news" tort survives.[3]

The Second Circuit observed that amendments to the 1976 Copyright Act reflected Congressional attempts to provide for legal uniformity in copyright law. The amendments articulate a two-part test that identifies state law claims as preempted by the Copyright Act: 1) if they seek to vindicate "legal or equitable rights that are equivalent" to one of the bundle of exclusive rights protected by copyright law; and 2) if the works are of the type protected by the "subject matter requirement" of the Copyright Act.

One theory advanced against preemption is that "hot news" involves a distinct moral dimension not captured by copyright law. The Second Circuit disavowed this notion: "[n]o matter how 'unfair' Motorola's use of NBA facts and statistics may have been to the NBA - or Fly's use of the fact of the Firms' Recommendations may be to the [Firms] - then, such unfairness alone is immaterial to a determination whether a cause of action for misappropriation has been preempted by the Copyright Act."

The Second Circuit found preemption in *Fly II* because the Firms' recommendations are subject matter covered by copyright law, the Firms' rights in their reports and recommendations are provided by the copyright law, and Fly is not free-riding because it collects, collates and

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2 105 F.3d 841 (2d Cir. 1997).

3 *Fly II* at 33.

disseminates factual information. In short, the Second Circuit observed, "The Firms are making the news; Fly, despite the Firms' understandable desire to protect their business model, is breaking it."

Further, the Second Circuit explained that a "hot news" claimant must have acquired the material through the use of labor, skill and money, and the defendant must have appropriated and sold this material as the defendant's own. In contrast, rather than acquiring recommendations through efforts akin to reporting, the Firms *create* them. A Firms' issuance of a recommendation *is itself a fact* that is news that may move the markets. The Second Circuit also noted that Fly always attributed the recommendations to the respective Firms because it is precisely Fly's attribution to Firms that gives the news its value. Indeed, there was "no meaningful difference" between Fly's behavior and that of members of the traditional news media reporting on "winners of the Tony Awards or, indeed, scores of NBA games with proper attribution of the material to its creator."

The Second Circuit was careful to limit its holding to the specific facts of the case. It warned that, had a Firm published a survey of its own and other entities' recommendations, and Fly copied the publication, this would have been a different case and then Fly might have been liable under a "hot news" misappropriation tort that would survive Copyright Act preemption.

Implications

While *Fly II* acknowledged an important right to disseminate news freely, the holding does not provide *carte blanche* for news aggregators to repurpose others' works. The court did not repudiate New York State's "hot news" misappropriation tort, and was careful to acknowledge Fly's independent and "substantial organizational effort" to report the financial news, which prevented a determination that Fly was free-riding on the Firms' efforts.

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If you have any questions concerning this memorandum, please contact William M. Ried (212-728-8729, bried@willkie.com), Amir R. Ghavi (212-728-8726, aghavi@willkie.com) or the Willkie attorney with whom you regularly work.

Willkie Farr & Gallagher LLP is headquartered at 787 Seventh Avenue, New York, NY 10019-6099. Our telephone number is (212) 728-8000 and our facsimile number is (212) 728-8111. Our website is located at www.willkie.com.

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