NO. 12-940

In the
Supreme Court of the United States

INTERNATIONAL SECURITIES EXCHANGE, LLC,

Petitioner,

v.

CHICAGO BOARD OPTIONS EXCHANGE, INC.;
CME GROUP INDEX SERVICES, LLC;
THE MCGRAW-HILL COMPANIES, INC.,

Respondents.

On Petition for a Writ of Certiorari to the Illinois Appellate Court

REPLY BRIEF FOR PETITIONER

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REPLY BRIEF FOR PETITIONER

The decision below imposes $10,000,000,000 in deadweight losses *per year* and benefits an in-state entity based on a highly dubious construction of the scope of federal copyright preemption. Respondents cannot deny these massive inefficiencies and instead attack a series of strawmen in an effort to deny that the decision is out of step with a host of federal cases and contravenes Congress' desire for a nationally uniform copyright regime. Those efforts fail. The splits actually identified in the petition are real. What is illusory is respondents' attempt to recast their claim in an effort to distinguish between the work they put into producing the published and widely-disseminated index values, and petitioner's copying and subsequent use of those index values. The latter acts clearly fall within the broad preemptive sweep of the Copyright Act.

Respondents have little to say about the far-reaching consequences of the decision below. They steer clear of any reference to Congress' intent to create a nationally uniform copyright regime, which the decision plainly undermines. They allude to a non-existent "broad preemption savings provision," while ignoring the Act's undeniably broad preemptive force. They dismiss billions of dollars in annual deadweight losses as a mere "policy argument," but when an erroneous state-court decision construing federal law inflicts such massive costs, there is indeed a strong policy argument for this Court's review. That is particularly true when the decision eliminates federal uniformity in a way that entrenches local monopolists at the expense of efficiency in national markets. This Court has repeatedly recognized the importance of its oversight of state-court decisions addressing federal preemption, but rarely have the stakes been so high. This Court's plenary review of the decision below is imperative.

I. The Court Of Appeals' Profoundly Incorrect Decision Conflicts With Decisions Of The Federal Courts Of Appeals.

Respondents contend that the decision below presents "no conflict" with decisions of the federal courts of appeals. Opp. 2, 15, 16, 20. Respondents are mistaken.

First, the Court of Appeals concluded that only materials that qualify for copyright protection satisfy the "subject matter" requirement for preemption. Respondents repeat this assertion, thrice claiming that this case does not involve "copyrightable subject matter." Opp. 20. But as multiple circuits have held, the universe of exclusively federal copyright "subject matter" is notably broader than the subset that is actually protected or "copyrightable." *See Nat'l Basketball Ass'n v. Motorola, Inc.*, 105 F.3d 841, 849 (2d Cir. 1997) (*NBA*); *United States ex rel. Berge v. Bd. of Trustees of the Univ. of Ala.*, 104 F.3d 1453, 1463 (4th Cir. 1997); *Wrench LLC v. Taco Bell Corp.*, 256 F.3d 446, 455 (6th Cir. 2001); *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447, 1453 (7th Cir. 1996); *Montz v. Pilgrim Films & Television*, 649 F.3d 975, 979-80 (9th Cir. 2011); *Ehat v. Tanner*, 780 F.2d 876, 878 (10th Cir. 1985). As Judge Easterbrook explained in *ProCD*—a case respondents do not even acknowledge—the distinction between these two concepts (and the error in collapsing them) is critical; in enacting Section 301 Congress intended "to prevent states from giving special protection" to materials that "should be in the public domain," 86 F.3d at 1453—exactly the result of the decision below. Respondents do not deny this split in authority; they simply restate the court of appeals' erroneous view.

Second, the Court of Appeals' decision squarely conflicts with federal decisions holding that a state-law misappropriation claim premised on the unauthorized "use" of the time, effort, and goodwill associated with a creation satisfies the "general scope" requirement of copyright preemption. *See Stromback v. New Line Cinema*, 384 F.3d 283, 301 (6th Cir. 2004) (finding claim for misappropriation of "time, effort, and money" associated with producing work preempted); *Del Madera Props. v. Rhodes & Gardner, Inc.*, 820 F.2d 973, 977 (9th Cir. 1987) (finding claim for misappropriation of "time and effort expended in producing" work preempted), *abrogated in part on other grounds by Fogerty v. Fantasy, Inc.*, 510 U.S. 517 (1994). Respondents' claim "is premised on [petitioner's] unauthorized *use* of the research, expertise, reputation, and goodwill associated with [respondents'] product." Pet. App. 14a; *see also id.* at 23a; Opp. 5-7, 25-27, 33-34 (describing effort associated with creating index values). That is precisely the kind of claim that these federal courts treat as within the general scope of the Copyright Act and find preempted. The Court of Appeals, however, found the claim non-preempted based on the untenable distinction between the hard work and goodwill that went into creating the index values and the index values themselves.

Federal courts have consistently held that state-law misappropriation claims lack the necessary "extra element" to fall outside Section 301's preemptive scope. *See* Pet. 19-20. Respondents contend (at 21) that this view is not "universally held," which only underscores that there is a split in authority. Moreover, respondents' cases are distinguishable. Many involved different state-law claims that include the requisite "extra element" lacking in misappropriation claims. *See Nat'l Car Rental Sys., Inc. v. Computer Assocs. Int'l, Inc.*, 991 F.2d 426 (8th Cir. 1993) (breach of contract); *G.S. Rasmussen & Assocs., Inc. v. Kalitta Flying Serv., Inc.*, 958 F.2d 896 (9th Cir. 1992) (conversion); *Altera Corp. v. Clear Logic, Inc.*, 424 F.3d 1079 (9th Cir. 2005) (interference with contract); *see also* Pet. 20-21 n.4. Others involved right-of-publicity claims based on an individual's likeness, not misappropriation claims concerning published information. *See Toney v. L'Oreal USA, Inc.*, 406 F.3d 905, 907 (7th Cir. 2005); *Downing v. Abercrombie & Fitch*, 265 F.3d 994, 1004-05 (9th Cir. 2001); *Brown v. Ames*, 201 F.3d 654, 657 (5th Cir. 2000). Still others are unpublished or address preemption in a passing footnote. *See Stewart Title of Cal., Inc. v. Fid. Nat'l Title Co.*, 279 F. App'x 473 (9th Cir. 2008); *U.S. Trotting Ass'n v. Chi. Downs Ass'n, Inc.*, 665 F.2d 781, 785 n.6 (7th Cir. 1981). None of these cases renders illusory the Court of Appeals' divergence from the "legions" of federal decisions holding misappropriation claims preempted by the Copyright Act, and none supports nonpreemption of a claim based on "use" of intangible assets invested in creating a work. 1 M. Nimmer & D. Nimmer, Nimmer on Copyright § 1.01[B][1][f][iii].[1]

Third, the decision below conflicts with federal decisions emphasizing the exceedingly narrow scope of the purported "hot-news" exception to copyright preemption. *See Barclays Capital Inc. v. Theflyonthewall.com, Inc.*, 650 F.3d 876, 896-97 (2d Cir. 2011); *U.S. Golf Ass'n v. St. Andrews Sys.*, 749 F.2d 1028, 1037-38 (3d Cir. 1984); *see also Nash v. CBS, Inc.*, 704 F. Supp. 823, 835 (N.D. Ill. 1989), *aff'd*, 899 F.2d 1537 (7th Cir. 1990). This Court, too, has stressed the narrowness of that ruling. *See Coll. Sav. Bank v. Fla. Prepaid Postsecondary Educ. Expense Bd.*, 527 U.S. 666, 675 (1999). Indeed, as *amici* observe, since the Copyright Act's passage in 1976, *not one* federal court of appeals has held that a "hot-news" claim survives preemption. Br. of Copyright Law Professors 14. Nevertheless, the decision below heavily relied on an extremely broad reading of the exception to support its finding of no preemption. *See* Pet. App. 15a-18a, 27a. Respondents' only response is to insist that their claims are "not 'hot news' claims." Opp. 18. But if respondents' claims are different from most "'hot news' claims," it is only because they seek broader and more enduring protection, which is

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[1] Respondents also cite (at 31) *United States Golf Association v. Arroyo Software Corp.*, 81 Cal. Rptr. 2d 708 (Ct. App. 1999), a case upon which the Court of Appeals heavily relied, *see* Pet. App. 23a-24a, but that Nimmer has criticized as unconvincing and out of line with "most other cases." Nimmer § 1.01[B][1][f][iii] & n.316.

exactly petitioner's point: whatever the precise label, the Court of Appeals relied on the "hot-news" exception to create a broader preemption exception than any federal court would recognize.

The foregoing are not mere "misapplication[s]" of a "correct legal standard," Opp. 23, but divergent (and, in the case of the court below, fundamentally flawed) rules of law concerning federal copyright preemption. Unable plausibly to deny the existence of these divisions of authority, respondents instead focus on three other cases, to no avail. Respondents misleadingly argue (at 17) that petitioner "implie[d]" that *Dow Jones & Co. v. International Securities Exchange, Inc.*, 451 F.3d 295 (2d Cir. 2006), preempted similar misappropriation claims. The Court will search the petition in vain for any such implication, because *Dow Jones* held that offering and listing options on exchange-traded funds tracking the DJIA and S&P 500 does not constitute misappropriation; it was not a preemption decision and expressly reserved the question implicated here. *Id.* at 303 n.9. But while *Dow Jones* does not create a doctrinal conflict as such, it is nevertheless doubly significant. First, by opening up competition in a related market, it has allowed an accurate estimate of the staggering costs associated with the decision below. Second, it and the decision below constitute a highly anomalous practical conflict where exchanges *may* list options on ETFs tracking the indexes, but *may not* list options on the indexes themselves. This practical conflict leaves investors and exchanges in "confusion" with "inconsistent rules as to whether similar instruments can be created and traded without a license." Br. of Citadel 25. It also creates a bizarre dynamic where index-based ETF options trade competitively on a highly efficient market, while the market for index options is saddled with monopolistic rents, deadweight losses, and inefficiencies.

Respondents contend (at 19-20) that petitioner "fares no better by relying on *N.Y. Mercantile Exch., Inc. v. Intercontinental-Exchange, Inc.*, 497 F.3d 109 (2d Cir. 2007) ('*NYMEX*')." But the petition only mentions *NYMEX* while recounting the decision below. *See* Pet. 10-11, 28. Respondents also argue (at 18-19) that the *NBA* case presents no conflict with the decision below. But as noted, *NBA*—consistent with other federal decisions, including by this Court—adopted an exceedingly narrow interpretation of the "hot-news" exception, contrary to the broad reading the Court of Appeals adopted. Respondents attempt (at 19) to distinguish *NBA* on its facts, but do so on a basis—the "creativity, judgment, expertise, reputation, and goodwill" expended to create the index values—that highlights another conflict (already noted) between the decision below and the federal-court precedents.

Like its effort to distinguish *NBA*, respondents' merits-based arguments underscore that both their arguments and the decision below are out of step with the federal precedents. Respondents now assert that their misappropriation claims are directed not at petitioner's copying and distribution of the index values themselves, but at petitioner's "effort to create commercial products"—*i.e.*, the options themselves—"whose public acceptance and value would result … from [respondents'] expertise, reputation, and goodwill." Opp. 25. Thus petitioner's "proposed activities would misappropriate these purely intangible assets." *Id.*; *see also id.* at 26-27. But this characterization is inconsistent with their repeated assertions throughout this case that petitioner's conduct would "misappropriate … the underlying *Indexes*." Compl. for Declaratory & Injunctive Relief ¶ 72, *Chi. Bd. Options Exch. v. Int'l Secs. Exch.*, No. 06CH24798 (Cook County Cir. Ct. Nov. 15, 2006) (emphasis added); *see also* Pet. App. 4a (noting that respondents alleged that petitioner's "proposed use of the *indexes* would constitute misappropriation" (emphasis added)).

More important, this attempted recasting ignores that all works within the subject matter of copyright—including the index values at issue here—are a product of hard work and do not just fall from the sky. Respondents' purported distinction between the effort that goes into creating a work (which respondents suggest can support a state-law misappropriation claim) and the work itself (which is preempted) is simply untenable and underscores why the decision is wrong, in conflict with federal precedents, and profoundly dangerous. "If the language of the [Copyright Act] could be so easily circumvented, the preemption provision would be useless, and the policies behind a uniform Copyright statute would be silenced." *Daboub v. Gibbons*, 42 F.3d 285, 289-90 (5th Cir. 1995).

Respondents also contend that their misappropriation claims "do not target copying or distribution" of the indexes, which are merely "incidental" to the "acts that form that basis of the *actual* state-law claims," *viz.*, "the creation and offering of option contracts based on the indexes." Opp. 28-30. But as noted, respondents' "*actual* state-law claims" expressly allege misappropriation of the indexes. Furthermore, copying and distributing indexes is not just "incidental" but *integral* to offering and settling options on those indexes; it is what makes it possible to list options. *See* Pet. 5-6 (describing process). That some options are not settled but instead cashed out before their expiration date, or that an exchange earns revenue from trading rather than distribution of index values, does not alter the analysis. Absent the ability to settle an index option—which requires copying and distributing index values—no investor would buy or sell the option in the first place, and no exchange—CBOE or petitioner—would earn revenue. That is why respondents have continuously asserted—until now—that petitioner's conduct would misappropriate their indexes, a claim that is preempted by the Copyright Act.

II. The Court Of Appeals' Decision Undermines The Important Federal Interest Of Copyright Uniformity And Permanently Entrenches An In-State Monopolist.

Respondents have almost nothing to say about the far-reaching consequences of the decision below—its disruption of the nationally uniform copyright regime Congress intended, its permanent entrenchment of an in-state monopolist, its implicit endorsement of forum-shopping, and the extraordinary costs it inflicts upon investors, consumers, and the national economy. Remarkably, respondents do not *once* mention the important federal interest of national uniformity in the copyright laws, the driving force behind Section 301. Pet. 29-32.

Contrary to respondents' repeated suggestion (at 2, 13, 15, 21, 22, 24), Section 301(b) of the Act is not a "broad preemption savings provision." As its text reflects, Section 301(b) lacks independent force; it is simply "the mirror of the conditions found in" Section 301(a). Joseph P. Bauer, *Addressing the Incoherency of the Preemption Provision of the Copyright Act of 1976*, 10 Vand. J. Ent. & Tech. L. 1, 16 (2007). If there is anything Congress unquestionably intended to be "broad," it is Section 301(a)'s preemptive force. *See Cmty. for Creative Non-Violence v. Reid*, 490 U.S. 730, 740 (1989); H.R. Rep. No. 94-1476, at 129-30 (1976), *reprinted in* 1976 U.S.C.C.A.N. 5659, 5745; Pet. 17-18, 30.

Respondents also have no meaningful response to the serious First Amendment concerns the decision below raises. *See* Br. of Copyright Law Professors 5-9. Respondents merely contend that the indexes are not "fixed collections of pre-existing factual information that [respondents] merely compiled." Opp. 27. But of course, the idea/expression dichotomy threatened by the decision below extends well beyond the specific fact pattern of *Feist Publications, Inc. v. Rural Telephone Service Co.*, 499 U.S. 340 (1991), that respondents recite.

Most remarkably, respondents cannot deny the billions of dollars in annual deadweight losses that the decision below perpetuates, which they dismiss as "conjecture[]" and a "policy argument." Opp. 32. That estimate is not conjectural; even the Court of

Appeals acknowledged the dramatic reduction in costs that occurred following *Dow Jones*, which caused the index-based ETF options market to move from monopoly to competition. And as *amici* carefully and thoroughly explain, respondents' monopoly over options on the DJIA and S&P 500 has extraordinary and pernicious effects. *See* Br. of Citadel 8-13, 15, 20-24; Br. of Business Professors 8-16. Furthermore, when a state court's erroneous construction of federal law has these kinds of far-reaching consequences—which will become *permanent* absent review—there is indeed a powerful "policy argument" for this Court to exercise its limited resources to review this decision. Few decisions can boast economic consequences of this magnitude.

Respondents appeal to the "significant adverse social impact" of the preemption rule petitioner advocates. Opp. 33. But its supporting arguments are drawn from *Board of Trade v. Dow Jones & Co.*, 456 N.E.2d 84 (Ill. 1983), an outlier decision that has been roundly criticized. *See* Br. of Citadel 18; Pet. App. 34a. In all events, whether there is an "adverse social impact" from copying and distributing index values is ultimately a question that should be answered by reference to uniform federal copyright law, not a patchwork of state-law misappropriation torts.

This patchwork of state laws not only defeats the congressional interest in uniformity, but also raises the possibility—fully realized in this case—that state courts will erroneously employ misappropriation doctrines to protect the hard work and goodwill of entrenched local entities. Here, it is bad enough that the national economy suffers billions in costs. But the reality that the only beneficiaries of the Illinois courts' misguided decisions are an Illinois monopolist and its business partners underscores the importance of a uniform national rule. Copyright Act preemption is broad for many reasons, not least of which is the profound temptation for state courts to manipulate misappropriation law to protect local entities.

Precisely because state courts have a temptation to ignore federal preemption doctrine, and contrary to respondents' suggestion (at 14), this Court frequently reviews—and reverses—decisions from state appellate courts, especially where, as here, the court improperly rejected application of federal law. *See, e.g.*, *Dep't of Revenue of Ky. v. Davis*, 553 U.S. 328, 331-32 (2008); *Preston v. Ferrer*, 552 U.S. 346, 349-50 (2008); *Norfolk S. Ry. Co. v. Sorrell*, 549 U.S. 158, 160 (2007). Indeed, the Court recently reviewed and vacated a decision of the Illinois Appellate Court. *MeadWestvaco Corp. ex rel. Mead Corp. v. Ill. Dep't of Revenue*, 553 U.S. 16, 19 (2008). Review is even more critical because respondents' own successful procedural maneuverings to funnel this litigation into Illinois state court means that further percolation indisputably will not bring this important issue before the Court again—unlike, for example, the Fourth Amendment case respondents cite. Pet. 15-16, 34-36; Br. of Citadel 24-25. Here, the stakes are high and the need for review imperative. If this Court does not review this issue now, the decision below, and the billions in deadweight losses it perpetuates, will become permanent. This Court should intervene.

CONCLUSION

The Court should grant the petition.

Respectfully submitted,

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