

# Stop Mucking up Copyright Law: A Federal Common Law of Contract as a Clean Exit Strategy

by

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## I. INTRODUCTION

The intersection of modern copyright law and state contract law has been a perilous minefield for courts and scholars. Traditionally, copyrighted content was instantiated into a book or other media and that media was sold. Purchasers bought copyrighted works more-or-less the same way they purchased other consumer goods. At the time of purchase, ownership of the embodiment containing the work was known. “I bought the book; therefore, I own the book” and customary norms established the scope of the owner’s right. Reading the book was acceptable, making copies of short excerpts was fine, but copying a substantial or significant part of the book was wrong.<sup>2</sup> Starting in the 1980s things changed for at least one class of copyrighted works, digital works (including computer software). Software is often “sold” or “downloaded” with strings attached.<sup>3</sup> The transaction may appear to the uninitiated to be the same as the sale of a book, but these strings, depending on state law, may convert the appearance of a sale of a copy into the legal reality of a mere license to use the work.<sup>4</sup> In the digital works context, “I bought the work” often only means “I purchased a license to use the work.” These strings often do not reflect accepted copyright norms.<sup>5</sup> In fact, these terms are often inimical to public values, terms that for example, prohibit public commentary on the licensed product.<sup>6</sup>

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<sup>2</sup> See generally Ann Bartow, *Electrifying Copyright Norms and Making Cyberspace More Like a Book*, 48 VILL. L. REV. 13 (2003).

<sup>3</sup> *Applied Info. Mgmt., Inc. v. Icart*, 976 F. Supp. 149, 154 (E.D.N.Y. 1997). As one court observed “[r]esolution of the issue is complicated by the fact that an agreement of this nature may convey rights and interests in two, rather than only one, form of property: the developer may transfer copyright rights in the software program (intellectual property rights) and at the same time transfer rights in the copy of the program through the material object that embodies the copyrighted work (personal property rights).” *Id.* at 150-51. As will be discussed *infra*, § 204 of the Copyright Act addresses the alienation of the copyright, but the Copyright Act is silent on the alienation of the copyright work. As one commentator observed “These ambiguities are seemingly inherent in a scheme in which, although two species of property rights are implicated, the parties themselves typically do not draw distinctions between them.” MELVILLE B. NIMMER & DAVID NIMMER, 2 NIMMER ON COPYRIGHT § 8.08 (hereinafter 2 NIMMER ON COPYRIGHT).

<sup>4</sup> Frequently, these “licenses” will use mixed terminology that may characterize the transaction in terms that are more customarily associated with a transfer of title (sale) yet coupled with terms and limitations that may suggest a license. See, e.g., *Adobe Sys, Inc. v. Stargate Software, Inc.*, 216 F. Supp. 2d 1051, 1056-57 (N.D. Cal. 2002) (“licenses” using terms such as ‘reseller,’ ‘owner,’ and ‘repurchase’); *Novell, Inc. v. CPU Distrib., Inc.*, 2000 U.S. Dist. LEXIS 9975, \*13-17 (S.D. Texas 2000) (“license” using terms such as “sell,” “reseller,” “acquire,” “resale,” and “sold”).

<sup>5</sup> LAWRENCE LESSIG, *THE FUTURE OF IDEAS: THE FATE OF THE COMMONS IN A CONNECTED WORLD* 4 (2002)(citing JESSICA LITMAN, *DIGITAL COPYRIGHT* 244-45(2001); Bartow, *supra* note 2, at \_\_\_\_.

<sup>6</sup> For example, the Microsoft EULA for Agent API prohibited “use the Character Animation Data and Image Files to disparage Microsoft, its products or services or for promotional goods.” <http://www.cni.org/Hforums/cni-copyright/199801/0048.html>. A McAfee license for VirusScan contained the following terms ““The customer shall not disclose

These strings are terms in what is commonly called a shrink-wrap license or end user agreement.<sup>7</sup> Tying these strings into a coherent body of contract law to govern copyright transactions has been a source of frustration to courts and scholars alike. This article proposes that the federal courts create a common law of contract to govern copyright disputes in order to create this coherent body of law. Alternatively, Congress may enact a body of contract law to govern copyright transactions. In either case, a uniform national body of law is required.

Federal courts currently apply state contract law to copyright disputes because as of yet, there is no federal commercial law governing copyright transactions. Because federal courts are applying state law, they are compelled to interpret the shrinkwrap license or end-user-agreement as the highest court of that state would<sup>8</sup> unless the federal court finds the term preempted under federal law.<sup>9</sup> This potentially leads to policies that depart for Congress's intention of a uniform law of copyright to fifty bodies of contract law implementing inconsistent copyright policy.<sup>10</sup> As a result, the same contract could result in different rights under the Copyright Act in different states. This conflicts with Congress's goal of a uniform national law of copyright.

Because these rights remain with the work, two copies of the same product arriving through different distribution channels potentially could have different legal statuses. One copy could have first sale rights under 17 U.S.C. § 109 and adaptation rights under § 117, and the other copy merely a license bearing only contractual rights and having no statutory rights, despite the fact that both are accompanied by identical shrinkwrap licenses. If the court finds that there has been a sale then under the first sale doctrine, once a copy of a work has been sold, each subsequent *owner* of that copy has a right to resell it.<sup>11</sup> This is an exception to the copyright owner's right to control distribution under § 106(3) of the Copyright Act. First sale rights under 17 U.S.C. § 109 are vested in the individual who has title to a *copy* of the work, but if title does not pass, then the individual is merely a licensee and does not enjoy the privileges of a first sale defense.<sup>12</sup> Title is

the results of any benchmark test to any third party without McAfee's prior written approval." And, "The customers will not publish reviews of the product without prior consent from McAfee." <http://www.badsoftware.com/nondisc.htm>. Similar terms have been enforced by software companies. See "*The Test That Wasn't*," PC MAGAZINE 29 (Aug. 1999) ("We planned to do something that has not been done in recent history: a comparison of database performance on the exact same hardware. Because a database software license prohibits publishing benchmark test results without the vendor's written permission, negotiating for permission is always a challenge. . . ." . . . "Oracle . . . formally declined to let us publish any benchmark test results.").

<sup>7</sup> Following Professor Madison nomenclature, this articles uses the terms "mass-market licenses" or "'shrinkwrap' to encompass non-negotiable restrictions on the use and consumption of works of information that do not necessarily require any action on the part of the user-reader-consumer: statements of terms and conditions for access to or use of computer systems, programs, data, and other types and forms of information . . ." Michael J. Madison, *Legal-Ware: Contract And Copyright In The Digital Age*, 67 FORDHAM L. REV. 1025, 1054-55 (1998).

<sup>8</sup> See, e.g., *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447, 1450 (7th Cir. 1996) (applying Wisconsin law); *Jacob Maxwell, Inc. v. Veeck*, 110 F.3d 749, 752 (11th Cir. 1997) (applying Florida law). **[add more examples]**

<sup>9</sup> *Veeck*, 110 F.3d at 752 n.2 ("As a general rule, state law governs the interpretation of copyright contracts, unless a particular state rule of construction would 'so alter rights granted by the copyright statutes as to invade the scope of copyright law or violate its policies.'"); MELVILLE B. NIMMER & DAVID NIMMER, 3 NIMMER ON COPYRIGHT § 12.01[A] (hereinafter 3 NIMMER ON COPYRIGHT).

<sup>10</sup> See *Goldstein v. California*, 412 U.S. 546 (1973) (objective of copyright clause in Constitution was to facilitate granting of rights "national in scope").

<sup>11</sup> 17 USC § 109. "Inasmuch as ownership of a tangible copy is wholly distinct from copyright ownership of the work embodied therein, the upshot of this provision is that when a copyright owner of a software product sells diskettes of its copyrightable work to customers, the customers may be mere licensees of the copyright, but as owners of the copy containing the computer program, they are duly vested with all rights . . ." 2 NIMMER ON COPYRIGHT, *supra* note 3, at 8:08[B][1].

<sup>12</sup> 17 U.S.C. § 109(d). The legislative history explains that "acquisition of an object embodying a copyrighted work by rental, lease, loan, or bailment carries with it no privileges" to dispose or display the work. H.R. No. 1476 at 80.

question of state law.<sup>13</sup> Depending on state law, the identical end user agreements may constitute either a sale or a license.<sup>14</sup> “I bought the software; therefore, I own the software” may depending on state contract law actually be “I bought the software, and I am a mere licensee”<sup>15</sup> to the chagrin of the putative purchaser. Or, under § 117 of the Copyright Act which provides that “owners” of computer programs may make archival copies or other copies essential to the use of the program, and make adaptations of the program.<sup>16</sup> Depending on the state, the purchaser find herself saying “I bought the software, I own the software, I may repair, adapt, or make an archival copy of the software” or “I bought the software; but, I am a mere licensee, so I may merely use the software that is no longer suited to my needs unless the license provides otherwise.”

To determine who is an owner or a licensee of a copy under the Copyright Act, a federal court must look to the relevant state law governing contracts.<sup>17</sup> The federal court must first determine the substantive contract law governing digital works. Some courts that have applied Article 2 of the Uniform Commercial Code (“UCC”) have found that software is a good under the Article 2 while other courts have applied Article 2 by analogy.<sup>18</sup> To add complexity, the state may have adopted a non-uniform version of Article 2.<sup>19</sup> Moreover, either Article 2 applies or it does not apply to the dispute; as Article 2 is part of a Code that must be interpreted consistently as an integral whole and within the large context of the entire Uniform Commercial Code.<sup>20</sup> If Article 2 does not apply then the court may look to the state common law.<sup>21</sup> There is one more possible layer of law. Some states had adopted the Uniform Computer Information Transactions Act (“UCITA”) at the same time as other states were adopting bomb shelter provisions to shield their citizens from its application.<sup>22</sup> In addition, of course, other bodies of law such as the

<sup>13</sup> *Applied Info. Mgmt., Inc. v. Icart*, 976 F. Supp. 149, 150-51 (E.D.N.Y. 1997) (“The plain meaning of the statute’s language thus indicates that ‘the owner of a copy of a computer program’ is one who has complete title to the program.”).

<sup>14</sup> *See Fantastic Fakes, Inc. v. Pickwick Int’l, Inc.*, 661 F.2d 479, 483 (5th Cir. 1981); *Bartsch v. Metro-Goldwyn-Mayer, Inc.*, 391 F.2d 150, 153 (2d Cir. 1968); *Kingsrow Enterprises, Inc. v. Metromedia, Inc.*, 397 F.Supp. 879 (S.D.N.Y. 1975); 3 NIMMER ON COPYRIGHT, *supra* note 9, at § 10.09[A].

<sup>15</sup> The term “mere” precedes licenses because under the Copyright Act, licensees enjoy fewer statutory privileges. *See, e.g.*, 17 U.S.C. § 109 (first sale right limited to owners); 17 U.S.C. § 117 (archival, essential use, and adaptation rights limited to owners).

<sup>16</sup> *See Novell, Inc. v. Network Trade Center*, 25 F. Supp. 2d 1218, 1230 (C.D. Utah 1997) (applying first sale doctrine to determine ownership under § 117). *Cf. S.O.S., Inc. v. Payday, Inc.*, 886 F.2d 1081, 1089 n. 9 (9th Cir. 1989).

<sup>17</sup> *See, e.g. Yount v. Acuff Rose-Opryland*, 103 F.3d 830, 834-35 (9th Cir. 1996) (“a contract transferring a copyright are a concern of state contract law only and are not a concern of federal law at all.”); *Gordon v. Vincent Youmans, Inc.*, 358 F.2d 261, 262-63 (2d Cir.1965) (state law applied to construction of agreement assigning rights to a song). *Cf. Rodrigue v. Rodrigue*, 218 F.3d 432 (5th Cir. 2000) (state community property law governed copyright ownership).

<sup>18</sup> *ProCD, Inc. v. Zeidenberg*, 908 F. Supp. 640 (W.D. Wisc. 1996) (citing Mark A. Lemley, *Intellectual Property and Shrinkwrap Licenses*, 68 S. CAL. L. REV. 1239, 1244 n. 23 (1995) (“citing numerous federal and state law cases”), *rev’d* on other grounds, 86 F.3d 1447 (6th Cir. 1996).

<sup>19</sup> *See, e.g., Robert E. Scott, The Uniformity Norm in Commercial Law*, in *THE JURISPRUDENTIAL FOUNDATIONS OF CORPORATE AND COMMERCIAL LAW* 149-165 (Jody S. Kraus & Steven D. Walt, eds 2000) (observing that Article 2 is substantively non-uniform producing inconsistent judicial interpretations and decreases the supply of reliable gap filling provisions).

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<sup>21</sup> RAYMOND NIMMER, *THE LAW OF COMPUTER TECHNOLOGY*, at ¶ 6:4 (collecting cases) (suggesting that the better model is for courts to interpret the contract accompanying the transaction under the common law of contracts); *Microsoft Corp. v. Harmony Computers & Elect., Inc.*, 846 F. Supp. 208 (E.D.N.Y. 1994).

<sup>22</sup> For example, while Maryland and Virginia have adopted UCITA, other states, such as Iowa, North Carolina, and West Virginia, have bomb shelter provisions to protect their citizens from UCITA and still others such as Ohio, Oregon, and New York have bomb shelter bills pending in the legislature. David A. Szwak, *Uniform Computer Information Transactions Act [U.C.I.T.A.]: The Consumer’s Perspective*, 63 LA. L. REV. 27, 51 (2002). Moreover, other states have adopted non-uniform versions with various forms of consumer protection. *Id.* If UCITA becomes widely adopted fair use rights encumbered.

Convention on the International Sale of Goods (“CISG”) may apply either directly or by analogy to the agreement.<sup>23</sup> Accordingly, there is no scarcity of possible bodies or principles of law to apply to a dispute over digital works. .

But surely major corporations with batteries of highly competent transactional counsel can draft contracts that are valid in all fifty states and protect copyrights and copyrighted works. So far, the reported cases do not support this proposition. Courts have analyzed shrinkwrap contracts under Article 2 and have split on whether it resulted in a first sale or merely a license.<sup>24</sup> There is a long line of cases involving the consumer arbitration terms in Gateway, Inc.’s mass-market consumer agreement. Courts analyzing the Gateway agreements under principles of Article 2 have again and again reached conflicting interpretations not as to the language of the terms by whether the terms formed an enforceable contract under Article 2.<sup>25</sup> So, as a working proposition, in principle shrinkwrap agreements to arbitrate are not enforceable in Kansas or Missouri but are enforceable in Wisconsin and .<sup>26</sup> A corollary of this is that if the UCC prevents in forcing the arbitration provisions then the other terms are potentially unenforceable since a court may only decline to enforce an arbitration agreement under the same general principles of contract law that permits it to decline to enforce any other provision in a contract.<sup>27</sup> Accordingly, in at least some states, purported license agreements are invalid under the UCC and a first sale exists. Thus creating two classes of the identical copies of a work. Some copies exist in the stream of commerce with § 109 and § 117 rights, and some without, seemingly identical, coexisting in a national market, but with different legal privileges. The more modern forms of contracting, such as the click-wrap agreement, may not result in increased predictability. Courts are still compelled to determine whether the contract arises under Articles 2-204, 2-207, or 2-209 depending on the applicable section or the common law of contract, the results may differ and create in different rights under the Copyright Act.<sup>28</sup> A federal body of common law could fuse these competing bodies of law, at least as to copyright and copyrightable works.

The Copyright Act has another intersection with state contract law, the federal preemption doctrine. State laws inconsistent with the 1976 Copyright Act are preempted under 17 U.S.C. § 301. The goal of § 301 is national uniformity in federal copyright policy. To further this goal,

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<sup>23</sup> United Nations Convention on Contracts for the International Sale of Goods, *opened for signature* April 11, 1980, S. Treaty Doc. No. 9, 98th Cong., 1st Sess. 22 (1983), 19 I.L.M. 671, *reprinted at*, 15 U.S.C. app. 52 (1997). (CISG applies to “to contracts of sale of goods between parties whose places of business are in different [countries].” Art. 1. The CISG does not apply to sales of goods for personal or family use. Art. 2). For example, a court in the Netherlands applied the CISG to a dispute involving the sale of computer software. *See ICT GmbH v. Princen Automatisering Oss BV*, *Gerechtshof’s Hertogenbosch # 770/95/HE* (Netherlands 1996) available at <http://www.unilex.info/case.cfm?pid=1&do=case&id=329&step=abstract> (last visited Jul 20, 2003).

<sup>24</sup>  
<sup>25</sup> Compare, e.g., *Hill v. Gateway 2000, Inc.*, 105 F.3d 1147 (7<sup>th</sup> Cir. 1997)(enforcing shrinkwrap agreement to arbitrate under Article 2-204) with *Klocek v. Gateway, Inc.*, 104 F. Supp. 2d 1332 (D. Kan. 2000)(declining to enforce arbitration agreement under Article 2-207). The language of both agreements is substantially similar as is the process resulting in the formation of the contract. Even within a single state, courts have reached difference conclusions. Compare, e.g., *Licitra v. Gateway, Inc.*, 734 N.Y.S.2d 389 (2001)(declining to enforce arbitration agreement) with *Browsers v. Gateway 2000, Inc.* 676 N.Y.S.2d 569 (1998)(finding agreement enforceable but reforming some terms).

<sup>26</sup>And in New York State, it may depend on which judge, which day, which judicial department. Compare *Licitra v. Gateway, Inc.*, 734 N.Y.S.2d 389 (2001) with *Browsers v. Gateway 2000, Inc.* 676 N.Y.S.2d 569 (1998).

<sup>27</sup>  
<sup>28</sup> See *I.Lan Sys., Inc. v. Netscout Serv. Level, Corp.*, 183 F. Supp. 2d 328, 335-339 (D. Mass. 2002)

Congress vested the federal courts with exclusive jurisdiction over most copyright claims.<sup>29</sup> Yet, there is a serious question of whether contract law as the state law enforcing the private ordering of legal relations among the parties is preempted under § 301 when the parties contract to depart from the Copyright Act's default rules.<sup>30</sup> Other scholars have suggested that these contract regimes may be preempted under the Commerce Clause of the United States Constitution.<sup>31</sup> These vexing questions of preemption become moot, if there is a federal body of contract law. The federal courts will be free to harmonize federal policies as expressed in either copyright or contract law. Contract law becomes the adjective or procedural law when necessary that permits the full and complete expression of the substantive law of copyright and its underlying policies.

This article will analyze several sections of the Copyright Act where state contract law governs the legal relations of the parties. An analysis of the "ownership" provisions of the Copyright Act will demonstrate how inconsistent state law or its application frustrates Congress's goal of a uniform law of copyright. After demonstrating that existing commercial law does not adequately address the needs of the marketplace for digital works embodied in a tangible form. As a further demonstration, this article will then compare the ownership provisions of the *copyright* (those intangible legal rights granted by the Copyright Act) with selected sections of Article 2, and concluded that some of the sections of Article 2 conflict with provisions of the Copyright Act. These conflicts make Article 2 a questionable source on which to build a body of law governing copyright transactions. This Article will then show how the existing attempts such as the Uniform Computer Information Transaction Act (UCITA) to create a uniform law governing information rights have failed because they took place at the state level and were inadequate to address the preemption question. Finally, this article will suggest a possible solution, the creation of a federal common law of contract. The preferred solution is the federal courts creating a common law of contract to govern copyright transactions.<sup>32</sup> Failing that, Congress should act and created a federal body of contract law to govern copyright. Because this new body of law would be a federal, it would not be preempted by either § 301 of the Copyright Act or the commerce clause. In any case, federal courts should be free to develop new doctrines or interpretations of contract law that further the policies underlying the Copyright Act.

## II. COPYRIGHT ACT'S "OWNER" PROVISIONS

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<sup>29</sup> 28 U.S.C. § 1338(a) (provides that "[t]he district courts shall have original jurisdiction of any civil action arising under any Act of Congress relating to ... copyrights.... Such jurisdiction shall be exclusive of the courts of the states....").

[A]n action "arises under" the Copyright Act if and only if the complaint is for a remedy expressly granted by the Act, e.g. a suit for infringement or for the statutory royalties for record reproduction, ... or asserts a claim requiring construction of the Act, ... or, at the very least, and perhaps more doubtfully, presents a case where a distinctive policy of the Act requires that federal principles control the disposition of the claim. The general interest that copyrights, like all other forms of property should be enjoyed by their true owner is not enough to meet this last test.

T.B. Harms Co. v. Eliscu, 339 F.2d 823, 828 (2<sup>d</sup> Cir. 1964).

<sup>30</sup>  
<sup>31</sup> See, e.g., Dennis S. Karjala, *Federal Preemption of Shrinkwrap and On-Line Licenses*, 22 U. DAYTON L. REV. 511, 533-34 (1997);

<sup>32</sup> Jane C. Ginsburg, *Authors as "Licensors" Of "Informational Rights" Under U.C.C. Article 2B*, 13 BERKELEY TECH. L.J. 945, 968-69 (1998) ("Arguably, any appearance of a term in the Copyright Act that the Act does not itself define calls for development of a federal common law definition, rather than an interstitial resort to state law norms.").

The ownership provisions of the 1976 Copyright Act demonstrate how inconsistent state laws result in a fragmented national law of copyright. Copyright law creates two property interests one in the copyright that is the intangible bundle of legal rights granted to the author under § 106 of the Copyright Act and the other property interest is in the tangible work in which the author's originality is expressed.<sup>33</sup> Under the Copyright Act, the creation of an ownership interest in a new copyrighted work is clear, but the provisions regarding alienating an interest in copyright, and which forms of alienation result in the transfer of an ownership interest are to some extent dependent on state law.<sup>34</sup> Moreover, the Copyright Act is silent on the legal requirements to alienate an interest in the tangible embodiment of the copyrighted work. Courts must first distinguish between the ownership of a copy and the ownership of the copyright<sup>35</sup> then courts must look to state law to determine whether an ownership interest in either the copyright or in a particular embodiment of the work (copy) has passed. Since state law is *sui generis* to each state, this may result in copyrighted works entering the stream of commerce with differing rights depending on the initial state of entry into the stream of commerce and potentially liability for infringement in one state but excused from liability either under § 109 or § 117 in another state.

#### A. Ownership of the Copyright

Section 201(a) of the Copyright Act vests ownership of the copyright right (as distinguished from the tangible medium embodying the work) in the author of the work.<sup>36</sup> Under the Constitution, the author is the person “to whom anything owes its origin; originator; maker; one who completes a work of science or literature.”<sup>37</sup> An author may be either a natural person or a juridical person under the work-for-hire provisions.<sup>38</sup> Under § 204, this initial ownership “may be transferred in whole or in part by any means of conveyance or by operation of law, and may be bequeathed by will or pass as personal property by the applicable laws of intestate succession.”<sup>39</sup> “Any of the exclusive rights comprised in a copyright, including any subdivision of any of the rights specified by section 106, may be transferred . . . and owned separately.”<sup>40</sup> “A transfer of copyright ownership, other than by operation of law, is not valid unless an instrument of conveyance, or a note or memorandum of the transfer, is in writing and signed by the owner of

<sup>33</sup> 17 U.S.C. § 202; *Effects Associates, Inc. v. Cohen*, 908 F.2d 555, 558 n.6 (9<sup>th</sup> Cir. 1990); Karjala, *supra* note 31, at 538 n. 94 (1997).

<sup>34</sup> *DSC Comm. Corp. v. Pulse Comm., Inc.*, 170 F.3d 1354, 1360 (C.A. Fed. 1999) (“ownership is an imprecise concept, and the Copyright Act does not define the term.”). The starting point of any analysis of a statute is the plain meaning. Here, ownership is a “collection of rights to use and enjoy property, including the right to transmit it to others. The complete dominion, title or proprietary right in a thing or claim. The entirety of then powers to use and disposal allowed by law.” *Applied Info. Mgmt., Inc. v. Icart*, 976 F Supp. 149, 153 (E.D. N.Y. 1997) (quoting *BLACK’S LAW DICTIONARY* 1106 (6<sup>th</sup> ed. 1990) (citations omitted in original). This definition describes the legal rights associated with ownership but is not helpful in the modern software context in which software comes with a contract (or license) that does not distinguish between the ownership in the copy and the license to use that copy in excess of that provided for under the Copyright Act.

<sup>35</sup> *Applied Info. Mgmt., Inc.*, 976 F Supp. at 153 (citing 2 *NIMMER ON COPYRIGHT*, *supra* note 3, at § 8.08[B][1] (1996)).

<sup>36</sup> 17 U.S.C. § 201(a). For example, if an artists steals marble to make a sculpture. He would own the copyright (intellectual property rights) in the work, but the actual work would belong to the person who owned the marble.

<sup>37</sup> *Burrow-Giles Lithographic Co. v. Sarony*, 111 U.S. 53, 58 (1884); *see Aalmuhammed v. Lee*, 202 F.3d 1227, 1233 (9<sup>th</sup> Cir. 2000) (“author’ involves originating, making, producing, as the inventive or master mind, the thing which is to be protected”)

<sup>38</sup> 17 U.S.C. § 201(b) (“In the case of a work made for hire, the employer or other person for whom the work was prepared is considered the author . . .”).

<sup>39</sup> 17 USC 201(d)(1).

<sup>40</sup> 17 USC 201(d)(2)

the rights conveyed or such owner's duly authorized agent."<sup>41</sup>

The federal law has displaced state law when interpreting the operative language of § 204 governing the assignment of an interest in the copyright. There is a conflict between the "writing" provisions under § 2-201 of the UCC and § 204(a) of the Copyright Act. Article 2-201, commonly called the Statute of Frauds provides that:

[e]xcept as otherwise provided . . . a contract for the sale of goods for the price of \$500 or more is not enforceable by way of action or defense unless there is some writing sufficient to indicate that a contract for sale has been made between the parties and signed by the party against whom enforcement is sought or by his authorized agent or broker.<sup>42</sup>

The three traditional exceptions are specially manufactured goods, admissions in legal proceedings, and part performance by payment or delivery.<sup>43</sup> None of these exceptions exist in copyright law nor does § 204 require a \$500 threshold. Section 204(a) provides that "[a] transfer of copyright ownership, other than by operation of law, is not valid unless an instrument of conveyance, or a note or memorandum of the transfer, is in writing and signed by the owner of the rights conveyed or such owner's duly authorized agent."<sup>44</sup> In the case of the transfer of an ownership interest in a copyright such as the granting of an exclusive license, § 204(a) preempts state law such as Article 2-201.<sup>45</sup>

While Article 2-201 and § 204(a) serve similar evidentiary purposes, §204(a) serves additional salutary purposes under the Copyright Act. The purpose of § 204(a) is to ensure that the copyright owner will not inadvertently surrender copyright rights and to compel the other party to negotiate exactly what rights are being transferred.<sup>46</sup> This requires that the writing be contemporaneous with the negotiations. In contrast, the state statute of frauds may be satisfied by admissions in a legal proceeding, sometimes years after the negotiations, and there may never have been a writing memorializing the agreement.<sup>47</sup> Accordingly, even if the writing satisfies the statute of frauds (or even if a "writing" is not needed under the statute of frauds), it can still be insufficient to meet the writing requirements of § 204(a). Moreover, if the formation of the agreement meets the other requirements of the UCC except for the writing requirement of the statute of frauds, the agreement is unenforceable but valid. For example, the party against whom enforcement is sought may admit during legal proceedings that there was a contract or the agreement was "ratified" by partial performance or payment. Thus making the agreement both

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<sup>41</sup> 17 U.S.C. § 204(a).

<sup>42</sup> UCC art. 2-201.

<sup>43</sup> UCC art. 2-201(3).

<sup>44</sup> 17 U.S.C. § 204(a).

<sup>45</sup> See Lorin Brenman, *Why Article 2 Cannot Apply to Software Transactions*, 38 DUQ. L. REV. 459, 482-83 & n. 87 (2000), (citing *Konigsberg Intern'l v. Rice*, 16 F.3d 355, 357 (9<sup>th</sup> Cir. 1994) and MELVILLE B. NIMMER & DAVID NIMMER, 1 NIMMER ON COPYRIGHT § 1:01[B][3][a] (hereinafter 1 NIMMER ON COPYRIGHT)). The weight of authority seems to be that an nonexclusive license should comply with the statute of frauds. See *Myers v. Waverly Fabrics*, 475 N.Y.S.2d 860, 862 (N.Y.A.D. 1984); *Holtzbrinck Pub. Holdings, L.P. v. Vyne Communications, Inc.*, 2000 WL 502860, at 6-8 (S.D.N.Y. 2000); but see *John G. Danielson, Inc. v. Winchester-Conant Properties, Inc.* 186 F. Supp. 2d 1, 18 (D. Mass. 2002); 3 NIMMER ON COPYRIGHT, *supra* note 9, at § 10.03[A][7] (may be granted "orally, or may even be implied from conduct.").

<sup>46</sup> *Effects Assoc., Inc. v. Cohen*, 908 F.2d 555, 557(9<sup>th</sup> Cir. 1990); *Konigsberg Intern'l*, 16 F.3d. at 356-57. Also, state courts generally interpret a contract against the drafter. Federal courts consistent with copyright policy interpret a transfer of rights against dispossessing the copyright owner of her rights, regardless of who drafted the contract.

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valid and enforceable under the U.C.C.<sup>48</sup> In comparison, under §204(a), the agreement is both unenforceable and not valid if the writing and signature are not contemporaneous with the agreement.<sup>49</sup>

## B. Ownership of a Particular Embodiment of the Copyrighted Work

In addition to the intangible copyright right, there must also be a tangible copyrighted work. A work must be fixed in a tangible medium of expression, i.e., a copy must exist as a prerequisite to federal copyright protection.<sup>50</sup> The Copyright Act is silent on the alienation of an interest in the embodiment of a work (“copy”), so courts look to state law contract principles to determine whether there was sale of a copyrighted work (as opposed to a transfer of copyright).<sup>51</sup> But once the work has been sold and title transferred, several provisions of the Copyright Act affect the legal rights that are attached to the work. One such provision is § 109, which is often called the first sale doctrine.<sup>52</sup> Section 109(a) provides that “the owner of a particular copy . . . lawfully made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy . . .”<sup>53</sup> Section 109(d) limits the privileges provided for in § 109(a) so that “[t]he privileges provid[ed] by subsections (a) and (c) do not, unless authorized by the copyright owner, extend to any person who has acquired possession of the copy . . . from the copyright owner by rental, lease, loan, or otherwise, without acquiring ownership of it.”<sup>54</sup> Ownership of a “copy” is dispositive as to first sale rights.

The elements of a first sale doctrine defense are that (1) the copy was lawfully made with the authorization of the copyright owner; (2) the particular copy was initially transferred under the copyright owner’s authority; (3) the defendant is a lawful owner of the copy in question; and (4) the defendant’s use only implicates reproduction rights under § 106.<sup>55</sup> “License agreements

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<sup>49</sup> *Konigsberg Intern’l*, 16 F.3d. at 356-57; *but see*, *Museum Boutique Intercontinental, Ltd. v. Picasso*, 880 F. Supp. 153, 162 (S.D.N.Y. 1995) (“writing which memorializes an oral license does not need to be entered into at the time when the license was initiated; a later execution of a writing confirming the oral agreement is sufficient to satisfy the statute”) citing *Eden Toys, Inc. v. Florelee Undergarment Co., Inc.*, 697 F.2d 27, 36 (2d Cir.1982).

<sup>50</sup> 17 U.S.C. § 102. A copy for the purpose of the Copyright Act includes the first instantiation of the work. What would be called in the vernacular “the original”

<sup>51</sup> *See, e.g.* *Yount v. Acuff Rose-Opryland*, 103 F.3d 830, 834-35 (9<sup>th</sup> Cir. 1996) (“a contract transferring a copyright are a concern of state contract law only and are not a concern of federal law at all.”); *Gordon v. Vincent Youmans, Inc.*, 358 F.2d 261, 262-63 (2d Cir.1965) (state law applied to construction of agreement assigning rights to a song). *Cf.* *Rodrigue v. Rodrigue*, 218 F.3d 432 (5<sup>th</sup> Cir. 2000) (state community property law governed copyright ownership). [state cases]

<sup>52</sup> *See* *Novell, Inc. v. Network Trade Center*, 25 F. Supp. 2d 1218, 1230 (C.D. Utah 1997) (applying first sale doctrine to determine ownership under § 117). *Cf.* *S.O.S., Inc. v. Payday, Inc.*, 886 F.2d 1081, 1089 n. 9 (9<sup>th</sup> Cir. 1989). The burden of proving the elements of a § 109 First Sale defense is on the defendant. *Microsoft Corp. v. Harmony Computers & Electronics*, 846 F. Supp. 208, 212 (E.D.N.Y.1994) (“In civil actions for copyright infringement, the defendant has the burden of proving that the particular pieces of copyrighted work that were sold were lawfully made or acquired.”); H.R. Rep. No. 1476 at 80 (“It is the intent of the Committee, therefore, that . . . the burden of proving whether a particular copy was lawfully made or acquired should rest of the defendant.”).

<sup>53</sup> 17 U.S.C. § 109(a); *Quality King Distributors, Inc. v. L'anza Research Intern., Inc.*, 523 U.S. 135, 141 (1998); *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339, 350 (1908) (exclusive right to “vend” under the copyright statute applied only to the first sale of the copyrighted work); HOUSE REPORT ON COPYRIGHT ACT OF 1976, H.R. Rep. No. 1476, 94<sup>th</sup> Cong., 2d Sess. 47, 79.

<sup>54</sup> 17 U.S.C. § 109(d). The legislative history explains that “acquisition of an object embodying a copyrighted work by rental, lease, loan, or bailment carries with it no privileges” to dispose or display the work. H.R. Rep. No. 1476 at 80.

<sup>55</sup> 2 NIMMER ON COPYRIGHT, *supra* note 3, at § 8.12[B][1][a]. *But see* Thomas Arno, Comment, *Use Restrictions and the Retention of Property Interests in Chattels Through Intellectual Property Rights*, 31 SAN DIEGO L. REV. 279 (1994) (suggesting

which are narrow in scope and impose substantial restrictions on the licensee's rights do not constitute first sales.<sup>56</sup> Consequently, the focus is not on whether possession has been transferred but rather was there a transfer of title.<sup>57</sup> This requires the court to analyze the state laws governing the transaction. Therefore, it would be useful to analyze the case law under the first sale doctrine to determine the circumstances under which courts have applied the concept of a first "sale" then to examine how the courts have construed the first sale doctrine in the digital works context to determine whether an ownership interest exists in a particular embodiment of the copyrighted work.<sup>58</sup>

### C. First Sale in the Old Economy Context

There is a long tradition of copyright owners attempting to frustrate the public purposes behind the Copyright Act by attempting through contract law to extend their lawful monopoly.<sup>59</sup> In response, the Courts have an equally long tradition of analyzing contracts and market transactions to determine whether title to the tangible work had passed to the customer so that it constitutes a first sale, or whether some lesser interest had passed to the customer so that the copyright owner may maintain subsequent control over the tangible work.<sup>60</sup>

The seminal United States Supreme Court case establishing the "first sale" doctrine was *Bobbs-Merrill Co. v. Strauss*.<sup>61</sup> The case involved a publisher that asserted a claim that resale of its books at a discounted price in violation of a notice on the inside leaf near the copyright notice constituted copyright infringement.<sup>62</sup> Each book contained the following notice: "The price of this book at retail is \$1 net. No dealer is licensed to sell it at a less price, and a sale at a less price will be treated as an infringement of the copyright. [s]The Bobbs-Merrill Company"<sup>63</sup> The Court analyzed the transaction. The books were sold to wholesalers and were "purchased by those who made no agreement as to the control of futures sales of the book, and took upon themselves no obligation to enforce the notice printed in the book, undertaking to restrict retail sales to a price of \$1 per copy."<sup>64</sup> Interestingly despite the discussion of the "notice", the Court found that "There is no claim in this case of contract limitation, nor license agreement controlling the subsequent sales of the book."<sup>65</sup> *Bobbs-Merrill Co.* teaches that once the owner parts with title

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that the real property paradigm of servitudes may be more economically efficient and serve the public better).

<sup>56</sup> See Sharon B. Soffer, *Criminal Copyright Infringement*, 24 AM. CRIM. L. REV. 491, 503 (1987) ("Because some copyrights are transferred through complex agreements not easily classified as sales, a court must carefully analyze a transfer to determine whether it should be considered a first sale.").

<sup>57</sup> *Id.* at 503. [title cases]

<sup>58</sup> See *Novell, Inc.*, 25 F. Supp. at 1230.

<sup>59</sup> Pamela Samuelson, *Modifying Copyrighted Software: Adjusting Copyright Doctrine to Accommodate a Technology*, 28 JURIMETRICS J. 179, 195-96 (1988); *Bobbs-Merrill Co.*, 210 U.S. at 348-51.

<sup>60</sup> Soffer, *supra* note 56, at 503.

<sup>61</sup> 210 U.S. at 348-51; *Quality King Distr., Inc.*, 523 U.S. at 140-45 (analyzing *Bobbs-Merrill* as "first case endors[ing] the first sale doctrine"). The first sale doctrine may be traced back to at least 1853. See *id.* at 140 n. 4 (citing cases). Accordingly *Bobbs-Merrill Co.* merely recognized and affirmed what was already a well-established judicial gloss on the copyright statute then enforce. Subsequent changes to the copyright act have adopted the first sale doctrine as interpreted by case law. See 2 NIMMER ON COPYRIGHT, *supra* note 3, at §8.12[B]. Accordingly, case law under the prior copyright acts is still very relevant to a sound interpretation of 17 U.S.C. § 109.

<sup>62</sup> *Bobbs-Merrill Co.*, 210 U.S. at 349-350.

<sup>63</sup> *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339, 341 (1908).

<sup>64</sup> *Id.* at 350.

<sup>65</sup> *Id.* at 351.

and “the purchaser obtains full dominion over it and has given a satisfactory price.”<sup>66</sup> The first sale has taken place.<sup>67</sup>

Subsequent cases reaffirm not only that title passes despite this embryonic form of “shrinkwrap” licensing, but also that the “first sale” granted other rights to the owner of a tangible copyrighted work. For example, in *Harrison v. Maynard*, the copyright owner sold fire damaged, unbound book sheets to a scrap dealer who resold them to a book dealer in violation of the scrap dealer's express written agreement to use the pages for scrap use only.<sup>68</sup> The book dealer bound the loose pages and resold them as a book. The Court found that there had been a first sale and that the copyright owner's rights had not been violated.<sup>69</sup> In *Independent News*, the purchaser bought comic books with their covers removed from waste paper dealers. There was an agreement between the wholesaler and distributor that title vested in the distributor and that these copies may only be sold as scrap paper. The court found that UCC § 2-403 covered the transaction and that the paper dealers were buyers in the ordinary course of business, and that there was a first sale.<sup>70</sup> This suggests that the first sale grants the owner of the copy some right to repair and to maintain their property. More recent case continues to recognize the need to determine whether there was a first sale under the UCC or did some other body of law cover the transaction.<sup>71</sup>

Once the first sale has occurred, even if a buyer disregards the copyright owner's express restrictions on the use of the copyrighted work then the buyer is not liable for copyright infringement, but the buyer may still be liable for breach of contract.<sup>72</sup> If the copyright owner licenses rather than sells the copyrighted work then the first sale doctrine does not apply, and the first and subsequent “buyers” are merely licensees who may be liable for infringing the distribution right of the copyright owner under § 106(3) should they violate the terms of the license.<sup>73</sup>

#### D. First Sale in the New Economy Context

The first sale model works well in the classic context of a software transaction. The consumer enters a store to purchase software or orders software by phone, email, web, or through the postal service.<sup>74</sup> The consumer then literally received a package containing a CD-Rom,

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<sup>66</sup> *Id.* at 349-50.

<sup>67</sup> *Platt & Munk Co. v. Republic Graphics* recognized “the just reward” justification for the first sale doctrine. 315 F.2d 847 (2d Cir. 1963). A transfer equals a first sale as long as the copyright owner has received a just reward for the use of his copyrighted work even if the transfer is involuntary. In *Lantern Press, Inc. v. American Publishers Co.*, the defendant purchased paperbound versions of plaintiff's books and rebound them in hardback for sale to schools and libraries. 419 F. Supp. 1267, \_\_\_\_ (E.D.N.Y. 1976). This practice resulted in the copyright owner receiving a lesser return than she would have earned from an original hard cover edition, but the court held that there was no violation of copyright owner's first sale rights because the copyright owner had received a just reward for the transfer. Although beyond the scope of this article, the just reward analysis may be an useful tool to deconstruct purported licenses and to permit putative licensees to exercise first sale rights.

<sup>68</sup> 61 F. 689 (2<sup>d</sup> Cir. 1894).

<sup>69</sup> 61 F. at \_\_\_\_ *Independent News Co. v. Williams*, 293 F.2d 510 (3d Cir. 1961).

<sup>70</sup> *Independent News Co., Inc.*, 293 F.2d at 510.

<sup>71</sup> CITE MA CASE

<sup>72</sup> *Microsoft Corp. v. Software Wholesale Club, Inc.*, 129 F. Supp. 2d 995, 1002 (S.D. Tex. 2000) (citing *American Int'l Pict. v. Foreman*, 576 F.2d 661, 664 (5<sup>th</sup> Cir. 1978) (citation omitted in original)).

<sup>73</sup> *Software Wholesale Club, Inc.* 129 F. Supp. 3d at 1002

<sup>74</sup> Of the four elements of the first sale exception, this article will only address the third element, the conditions under which courts have found or decline to find that the possessor of software was also an owner.

floppy disks, or other physical media containing the copyrighted software,<sup>75</sup> and payment is made at the time of purchase. This model is clearly analogous to the old economy purchase of a book with or without some writing purporting to be a limitation on subsequent distribution. Therefore, this new economy model mirrors the traditional first sale paradigm established by the courts in an era of book purchases. However, this model is already “old-new economy” and does not reflect the growing practice of downloading software. This section will explore whether the digital distribution model fits the first sale paradigm. If it does not, then this article is merely a historical critique of a passing fad of commerce the literal shrinkwrap license. If § 109 does work for digital downloads, and existing contract law cannot adequately address the need for a predictable commercial law to govern digital transactions then the continued failure of state law suggests the remedy of creating a federal common law of contract.

Section 109 is merely a limitation on the copyright owner’s § 106(3) distribution right. Subsequent transfers of pure digital content are unlikely to involve only the distribution right, but rather may raise significant questions of liability for violating both the copyright owner’s § 106(1) reproduction and § 106(3) distribution rights.<sup>76</sup> Section 109 provides an exception for the copyright owner’s distribution rights and that only following a first sale of the work.<sup>77</sup> Ordering software through web sites and then downloading the software and accompanying documentation directly onto a hard drive is fast becoming the predominate method of obtaining software for many users.<sup>78</sup> As a result, no physical, tangible, token of the work is ever conveyed to the user. Whether there can be a “first sale” absent the exchange of some tangible copy embodying the work is debatable.<sup>79</sup>

One prominent commentator suggests the following elegant solution to the digital transmission dilemma under § 109.<sup>80</sup> The paradigm of the first sale is that a lawful copy was produced by or under the authority of the copyright owner; that copy is then transferred under the authority of the copyright owner; the defendant is the lawful owner of that copy; and subsequent to ownership, the defendant distributed that copy.<sup>81</sup> In a pure digital transaction, no tangible copy is exchanged and the digital content is downloaded directly to some storage medium.

Perhaps, an example will make this point less virtual and more concrete. Entrepreneur downloads software after paying copyright owner for an authorized copy.<sup>82</sup> A few months later, Entrepreneur realizes that software no longer meets the needs of her growing business. Entrepreneur transfers a copy to another entity while simultaneously deleting the copy on her hard drive. Clearly, if Entrepreneur had bought a lawful tangible copy from her local software emporium, she would have a first sale right to transfer possession of the media on which the software was sold as long as she did not retain a copy. In the physical world example, the CD-

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<sup>75</sup> Roger E. Schechter, *The Unfairness of Click-on Software Licensing*, 46 WAYNE L. REV. 1735, 1736 (2000).

<sup>76</sup> See also Joseph P. Liu, *Owning Digital Copies: Copyright Law and the Incidents of Copy Ownership*, 42 WM & MARY L. REV. 1245, 1250 (2001); Jane C. Ginsburg, *Putting Cars on the “Information Superhighway”: Authors, Exploiters, and Copyright Infringement in Cyberspace*, 95 COLUM. L. REV. 1466, 1475 (1995).

<sup>77</sup> See STAFF OF HOUSE COMMITTEE ON THE JUDICIARY, 105<sup>TH</sup> CONG., SECTION-BY-SECTION ANALYSIS OF H.R. 2281 at 24.

<sup>78</sup> *Id.* at 1736.

<sup>79</sup> Cf. H.R. 3048, 105<sup>th</sup> Cong. 1 sess. (1997) (proposing language to make § 109 explicitly applicable to digital transmissions).

<sup>80</sup> 2 NIMMER ON COPYRIGHT, *supra* note 3, at \_\_\_\_.

<sup>81</sup> *Id.* at § 8:12. The status of the packets moving through cyberspace and the ephemeral copies made on numerous servers as part of transmission are outside the scope of this article except to assert that they are either not sufficiently fixed or are a fair use under § 107. Moreover, this article assumes that the initial transmission was by with permission of the copyright owner otherwise there never would have been a first sale.

<sup>82</sup> This hypothetical is based on the one used in the Nimmer and Nimmer on Copyright Law.

ROM or other media is merely a tangible form of the digital copy. Here in our cyberspace example, the tangible copy exists on the Entrepreneur's hard drive. In both examples, the copy was lawfully made. In one, the copyright owner authorized the fixation in the form of a CD-ROM while in the other, the copyright owner authorized the Entrepreneur to save the work at some location of her choice. The Entrepreneur owns her hard drive in the same manner as in the real world she owns a CD-ROM. In both examples, a copy was transferred with the consent of the copyright owner. Consequently, the elements of the first sale doctrine have been met in both examples, and the entrepreneur should enjoy title and the protection of the first sale doctrine either for a purchase of a CD-ROM or the download of the same program. To build further on the hypothetical, if the Entrepreneur sold the PC, this would clearly be a lawful subsequent disposition under § 109. Or, if she sold the hard drive from the PC, that too would be a lawful first sale. Therefore, as long as the Entrepreneur transfers her particular copy regardless of how it was initially instantiated, the first sale doctrine should apply to the transaction.

If the Entrepreneur transfers a copy then she deletes the copy on her hard drive, she has violated the copyright owner's § 106(1) right to make reproductions. As was discussed earlier, § 109 does not provide a defense to unlawful reproduction.<sup>83</sup> To fall within the first sale doctrine and not violate the copyright owner's § 106(1) reproduction right, the Entrepreneur must simultaneously delete the copy from her hard drive as she transfers her copy so that at any point in time there is only one copy.<sup>84</sup> In addition, § 109 will provide a defense against a claim that the transmission violated the copyright owner's § 106(3) distribution right.

The problem here is a technological one. This anomaly is not what Congress intended when it enacted the 1976 Copyright Act. Congress crafted the 1976 Copyright Act to accommodate technologies that are not yet in existence and to grant copyright protection to works created under future technologies,<sup>85</sup> and presumably to maintain the existing balance between copyright incentives and public access and fair use provisions codified in §107-§122 of the Copyright Act. The Copyright Act's fair use provisions should be interpreted when possible in a manner that assures the public that as the creation of copyright ownership is technology neutral so should fair use rights be technology neutral.<sup>86</sup> Therefore, a technology that permits simultaneous deletion and transmission should be recognized as a reasonable exercise of first sale rights.

#### E. Contracting for the First Sale

In determining whether there was a first sale, courts analyze the text of the contract or have used principles of contract law to analyze the agreement that governs the transaction.<sup>87</sup> Absent a clear statutory basis that governs transactions in computer software,<sup>88</sup> some courts have applied

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<sup>83</sup> See *infra* section XX. Whether this temporary second copy would be excused under § 107 is outside the scope of this article.

<sup>84</sup> 2 NIMMER ON COPYRIGHT, *supra* note 3, at § 8:12.

<sup>85</sup> 17 U.S.C. § 102(a) ("Copyright protection subsists, in accordance with this title, in original works of authorship fixed in any *tangible medium of expression, now known or later developed*, from which they can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device.").

<sup>86</sup> Laura N. Gasaway, *Distance Learning and Copyright: An Update*, 49 J. COPYRIGHT SOC'Y U.S.A. 195, 219 (2001) (citing U.S. COPYRIGHT OFFICE, REPORT ON COPYRIGHT AND DIGITAL DISTANCE EDUCATION, May, 1999, 161-62 (1999)).

<sup>87</sup> *Applied Info. Mgmt, Inc. v. Icart*, 976 F. F Supp. 149, 153 (E.D. N.Y. 1997) ("determination of ownership in a computer program requires interpretation of contract between the parties."); *Novell, Inc. v. Network Trade Center, Inc.*, 25 F. Supp. 2d 1218, 1230 (D. Utah 1997); *Synergist Tech., Inc. v. IDB Mobile Comm., Inc.*, 871 F. Supp. 24, 29 (D.D.C. 1994).

<sup>88</sup> Raymond T. Nimmer, *UCITA: Modern Contract Law for a Modern Information Economy*, 574 PLI/Pat 221, 224 (1999).

Article 2 of the Uniform Commercial Code.<sup>89</sup> Those courts that have declined to apply the UCC to the transaction have applied the state common law of contracts.<sup>90</sup> Under either body of law, state law determines if there was a sufficient alienation of a property right to create a transfer of ownership of a copy of the work. Frequently, courts look beyond the literal language of the contract to the underlying economic reality to determine if there was a first sale. Because the software is dominated by mass-market license or contract, it would be useful at this time to summarize the law in this area.<sup>91</sup>

Mass-market consumer contracts, better known as either standard form contracts or contracts of adhesion, have a long history in modern commercial practice and have been the subject of contentious legal scholarship.<sup>92</sup> In the physical marketplace, these contracts are often referred to as shrink-wrap licenses.<sup>93</sup> Individuals purchase the software at any business that sells computer software, then they return to their home or place of business and when they open the packaging, they will discover inside another contract, that offers terms that is often significantly different from the individual's understanding of the transaction at the point of purchase. Mass-market consumer contracts are omnipresent in e-commerce. There are two primary models for e-commerce contracting: click-wrap and browse-wrap contracts. Individuals attempting to install software as a precondition of installing the program must click on "I agree" (click-wrap contract)<sup>94</sup> or while browsing a website the visitor may see an invitation to click on a hyperlink to "legal information" or "terms of service" (browser-wrap contract).<sup>95</sup> Either model potentially binds the consumer to terms that she is unlikely to have read much less understood after payment and receipt of the software. This is well after the point that most consumers consider the transaction consummated and after which they do not expect further "dickering" or additional terms and conditions of purchase. This creates a new model. The linear sale-purchase model gives way to the sale-purchase (of good) plus additional terms (often a subsequent license). The legal affect of this new model has dominated scholarly debate for at least the past decade.

## 1. Uniform Commercial Code

In the paradigmatic software transaction, the court must first determine if the Uniform Commercial Code applies.<sup>96</sup> If the contract provides for both goods and services; the court must determine which aspect of the contract predominates.<sup>97</sup> If the purchase of goods predominates, then the court will apply Article 2. Most courts apply the Uniform Commercial

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<sup>89</sup> *Advent Systems Ltd. v. Unisys Corp.*, 925 F.2d 670, 675 (3rd Cir. 1991); James D. Hornbuckle, Note and Comment, *The Uniform Computer Information Transaction Act: State Legislatures Should Take A Critical Look Before Clicking Away Consumer Protections*, 23 WHITTIER L. REV. 839, 845-46 (2002).

<sup>90</sup> RAYMOND NIMMER, THE LAW OF COMPUTER TECHNOLOGY ¶ 6.4 (hereinafter, NIMMER ON COMPUTER TECHNOLOGY);

<sup>91</sup> See David A. Rice, *Licensing the Use of Computer Program Copies and the Copyright Act First Sale Doctrine*, 30 JURIMETRICS J. 157, 177 (1989) ("Custom software contracts ordinarily are negotiated.").

<sup>92</sup> Numerous scholars over the past sixty years have expounded on the general debate surrounding standard form contracts. See, e.g. Robert A. Hillman & Jeffrey J. Rachlinski, *Standard Form Contracting in the Electronic Age*, 77 N.Y.U. L. REV. 429, 433 n.15 & 434 n.18 (2002); Lemley, *supra* note 18, at 1264 n. 107 (collecting articles).

<sup>93</sup> "Shrinkwrap might be more accurately defined as any standard form-contract included with mass-marketed software, regardless of the manner in which the purchaser is to be made aware of the license's existence" Maureen A. O'Rourke, *Copyright Preemption After The Procd Case: A Market-Based Approach*, 12 BERKELEY TECH. L.J. 53, 57 n. 19 (1997).

<sup>94</sup> *Specht v. Netscape Comm. Corp.*, 306 F.3d 17, 21 n.3 (2d Cir. 2002).

<sup>95</sup> *Pollstar v. Gigmania, Ltd.*, 170 F. Supp. 2d 974, 981 (E.D. Cal. 2000).

<sup>96</sup> *Advent Systems Ltd.*, 925 F.2d at 676.

<sup>97</sup> 871 F. Supp. 27, n. 7; UCC § 2-102.

code, Article 2 to software transactions because there is sufficient goods nexus or by analogy.<sup>98</sup> In order to find a “goods” nexus to support the application of Article 2, courts have analogized software to music and books, finding that

music is produced by the artistry of the musicians, and in itself is not a “good,” but when transferred to a laser-readable disk becomes a readily merchantable commodity. Similarly, when a professor delivers a lecture, it is not a good, but, when transcribed as a book, it becomes a good.<sup>99</sup>

In the software context, the code is not a good; but when it is fixed in a tangible form, each fixation is a “good” and potentially falls with the scope of Article 2.

This analogy to a “book” seems stretched to some commentators,<sup>100</sup> but it is most apt for many users of mass-market software. For many consumers, the CD-Rom containing the software is the product, much the same way a book is the product. As one does not buy a book for its paper value, one does not purchase software on with a CD-ROM for its decorative value. The consumer buys both for their copyrighted content. The consumer desires to use the software on one machine and under the default terms and conditions provided for by the Copyright Act.<sup>101</sup> Just, as the consumer purchases a book to read and use under the default rules of the Copyright Act. Yet to some other consumers, the license may be is the product. These consumers desire rights in excess of those provided after a first sale under the Copyright Act. These consumers are more analogous to a consumer who purchases a copy of a stage play, and after reading it, desires to publicly perform the play. Such a consumer is interested in legal rights in excess of that which comes with the purchase of the work and must have a license for these uses. So for many consumers and small businesses, the Article 2 goods model supplemented by provisions of the Copyright Act is adequate for their needs. Alternatively, some courts unable or unwilling to stretch the Article 2 definition to include software have applied Article 2 to the software transactions in the absence of laws more directly on point. The process by which the end user consummates the transaction may effect whether the transaction is a sale or license under the Uniform Commercial Code. This section will explore some possible interpretations of Article 2 and demonstrate how these differing state laws and interpretations affect the rights of individuals, resulting in a non-uniform application of the Copyright Act.

## 2. U.C.C. § 2-401 & §2-403

*ProCd Inc. v. Zeidenberg* marked a paradigm shift in the law of shrinkwrap licenses. Before the Court of Appeals decision in *ProCd, Inc.*, a prudent consumer could approach such contracts with a healthy skepticism; now, a prudent consumer would be well advised to conform her

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<sup>98</sup> *ProCD, Inc. v. Zeidenberg*, 908 F. Supp. 640 (W.D. Wisc. 1996) (citing Lemley, *supra* note 18, at 1244 n. 23) (“citing numerous federal and state law cases”), *rev'd on other grounds*, 86 F.3d 1447 (6<sup>th</sup> Cir. 1996). But see, *NIMMER ON COMPUTER TECHNOLOGY*, *supra* note 90, at § 6:4 (collecting cases) (suggesting that the better model is for courts to interpret the contract accompanying the transaction under the common law of contracts); *Microsoft Corp. v. Harmony Computers & Elect., Inc.*, 846 F. Supp. 208 (E.D.N.Y. 1994).

<sup>99</sup> *Novell, Inc. v. Network Trade Center* 25 F. Supp. 2d 1218, 1229; *Advent Systems Ltd. v. Unisys Corporation*, 925 F.2d 670, 699-700 (3rd Cir. 1991); *Downriver Internists v. Harris Corp.*, 929 F. 2d 1147, 1150 (6<sup>th</sup> Cir. 1991).

<sup>100</sup>  
<sup>101</sup> 17 U.S.C. §117 provides all the rights the average consumer or small business needs to use software.

behavior to the terms of the shrinkwrap contract.<sup>102</sup> In January 1996, the United States District Court for the Western District of Wisconsin issued *ProCd Inc. v. Zeidenberg*, a well-reasoned opinion that carefully followed the prior law and scholarship.<sup>103</sup> On appeal, the United States Court of Appeals for the Seventh Circuit reversed<sup>104</sup> in an opinion that was long on public policy principles and shockingly lacking in citation to prior case law.<sup>105</sup> In *ProCD*, the United States Court of Appeals attempted to answer the question of whether “buyers of computer software must obey the terms of shrinkwrap licenses[.]”<sup>106</sup> The Court then concluded that “[s]hrinkwrap licenses are enforceable unless their terms are objectionable on grounds applicable to contracts in general (for example, if they violated a rule of positive law, or if they are unconscionable).”<sup>107</sup> The *ProCd, Inc.* Court treated the transaction as one governed by the Uniform Commercial Code.<sup>108</sup> The Court did not address whether there are legal differences between licenses and contracts for the first sale doctrine.<sup>109</sup> The district court had held that “placing the package on the shelf is an ‘offer,’ which the customer ‘accepts’ by paying the asking price and leaving the store.”<sup>110</sup> Under the U.C.C. “a contract includes only the terms on which the parties have agreed. One cannot agree to hidden terms . . . .”<sup>111</sup> At this level of abstraction, the district court concluded the contract was complete. The Court of Appeals interjected one additional element into the paradigm. The defendant was on notice that the shrinkwrapped software package contained additional terms. The question before the Court was whether those additional terms were somehow incorporated into the contract that apparently had been completed when money exchanged hands.<sup>112</sup>

As was demonstrated, what rights, if any, the consumer will receive is dependent on the Uniform Commercial Code and which provisions of that Code courts bring to bear on interpreting the transaction. Because the law governing the transaction is uncertain, this system lacks the consistency and predictability a uniform national system of copyright demands.

If the Court determines that Article 2 applies and the seller is a merchant then “unless otherwise explicitly agree[d] title passes to the buyer at the time and place at which the seller

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<sup>102</sup> *I.Lan Sys., Inc. v. Netscout Serv. Level Corp.*, 183 F. Supp. 2d 328, 337 (D. Mass. 2002) (“Step-Saver once was the leading case on shrinkwrap agreements. Today that distinction goes to . . . *ProCD, Inc. v. Zeidenberg*, . . . .”); *See, e.g.*, *M.A. Mortenson Co., Inc. v. Timberline Software Corp.*, 140 Wash. 2d 568, 998 P.2d 305 (license agreement supplied with software); *Rinaldi v. Iomega Corp.*, 1999 WL 1442014, Case No. 98C-09- 064-RRC (Del. Super. Sept. 3, 1999) (warranty disclaimer included inside computer Zip drive packaging); *Westendorf v. Gateway 2000, Inc.*, 2000 WL 307369, Case No. 16913 (Del. Ch. March 16, 2000) (arbitration provision shipped with computer); *Brower v. Gateway 2000, Inc.*, 246 A.D.2d 246, 676 N.Y.S.2d 569 (N.Y.App.Div.1998) (same); *Levy v. Gateway 2000, Inc.*, 1997 WL 823611, 33 UCC Rep. Serv.2d 1060 (N.Y. Sup. Oct. 31, 1997) (same).

<sup>103</sup> 907 F Supp. at 640

<sup>104</sup> *ProCD, Inc. v. Zeidenberg*, 908 F. Supp. 640, 1447 (W.D. Wisc. 1996).

<sup>105</sup> *Klocek v. Gateway, Inc.*, 104 F. Supp.2d 1332, 1339 (D. Kan., 2000). *See generally* Thomas J. McCarthy et al., *Survey: Uniform Commercial Code*, 53 BUS. LAW. 1461, 1465-66 (Seventh Circuit finding that UCC § 2-207 did not apply is inconsistent with official comment); Batya Goodman, *Honey, I Shrink-Wrapped the Consumer: the Shrinkwrap Agreement as an Adhesion Contract*, 21 CARDOZO L. REV. 319, 344-352 (Seventh Circuit failed to consider principles of adhesion contracts);

<sup>106</sup> 86 F.3d 1447, 1448 (6<sup>th</sup> Cir. 1996).

<sup>107</sup> *Id.* at 1449.

<sup>108</sup> *Id.* at 1450.

<sup>109</sup> *Id.* Although, the *ProCD, Inc.* Court left the issue of the differences between licenses and contracts for another day. Subsequent judicial opinions have relied on *ProCd, Inc.* to find licenses not valid as a sufficient transfer of rights to permit a licensee to exercise an “owners” rights under § 109.

<sup>110</sup> 86 F.3d. at 1450 citing *Peters v. State*, 142 N.W. 181 (Wis. 1913).

<sup>111</sup> *ProCD, Inc.*, 86 F.3d. at 1450 (7<sup>th</sup> Cir. 1996).

<sup>112</sup> 86 F.3d at 1450.

completes his performance with reference to the physical delivery of the goods.”<sup>113</sup> For example in *Synergistic Technology, Inc. v. IDB Mobile Communications, Inc.* the court was faced with interpreting documentation purporting to be an agreement that preceded delivery of the software. After finding that the software document in question was ambiguous, the court held that

[t]he parties not having explicitly agreed otherwise, title passed to . . . a copy of the software . . . at the time of delivery. Accordingly, [defendant] is the owner of a copy of the computer program and entitled to copy and adapt the program in the limited manner described in § 117.<sup>114</sup>

This comports with how many consumers view software. They enter into a store, select a software product, pay for the product, and assume at that point the transaction is complete and they own the software, much in the same manner as a book, VHS tape, or DVD. Nevertheless, consumer expectations may not reflect legal reality; most current consumer transactions have one element that may confound the application of U.C.C. § 2-401. Inside the packaging, some documentation purports to change the relationship, from that of purchaser with title to the copy to that of licensee, after the transaction is completed with the merchant.<sup>115</sup> Depending on the software, these terms may also be presented when the end user, who may not even be the purchaser, attempts to download the software or install it. Three common examples that create problems under contract law, parents purchase software and give it to a minor child who installs the software and “assents.” Alternatively, university purchasing office orders software, software is delivered directly to a technician(work study student) who installs it on a faculty computer and “assents” to the terms in the license. In both examples, there is a substantial question as to whether the end user is bound. A minor child cannot validly contract, and it is unlikely that any principle of agency law grants the technician either actual or apparent authority to contract on behalf of a university. A final example, user purchases an used computer with software already installed, is user bound by the agreements that the first owner agreed to as part of the installation? In all of these examples, the sale and purchase of the software are totally separate from the process and individual giving assent to the accompanying license.

In the case of such mass-market transactions that seem to create a springing contract interest post-sale, § 2-403(2) of the Uniform Commercial Code may be instructive to understand their legal validity. Section 2-402(2) provides that “[a]ny entrusting<sup>116</sup> of possession of goods to a merchant<sup>117</sup> who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in ordinary course of business<sup>118</sup>.”<sup>119</sup> Therefore, a reasonable consumer shopping at a

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<sup>113</sup> *Synergistic Tech., Inc. v. IDB Mobile Comm., Inc.*, 871 F. Supp. 24, 29 (D. D.C. 1994); UCC § 2-401

<sup>114</sup> *Synergistic Tech., Inc.*, 871 F. Supp. at 29.

<sup>115</sup> Frequently, these documents conflate the rights to transfer of the copy with the license to use the copy. In that case, the contract is ambiguous and title should pass to the purchaser under § 2-401. *See id.* at 29.

<sup>116</sup> “Entrusting’ includes any delivery and any acquiescence in retention of possession regardless of any condition expressed between the parties to the delivery or acquiescence and regardless of whether the procurement of the entrusting or the possessor’s disposition of the goods have been such as to be larcenous under the criminal law.” U.C.C. § 2-403(3).

<sup>117</sup> Merchant is defined at “(1) “Merchant” means a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction or to whom such knowledge or skill may be attributed by his employment of an agent or broker or other intermediary who by his occupation holds himself out as having such knowledge or skill.” U.C.C. § 2-104(1)

<sup>118</sup> “Buyer in ordinary course of business’ means a person who in good faith and without knowledge that the sale to him is in violation of the ownership rights or security interest of a third party in the goods buys in ordinary course from a person in the

merchant who sells software should receive the software without any strings that may bind the intermediate merchants in the distribution chain, i.e., free and clear of any purported licensing provisions.<sup>120</sup>

### 3. U.C.C. § 2-207 Battle of the Forms Cases

The *ProCD* court did not apply § 2-207 to the dispute because there was only one form.<sup>121</sup>

## F. UCC and Copyrights

So far, this article focused on the first sale of a tangible copyrighted work (such as a CD-Rom, DVD, or floppy disk). If Article 2 of the UCC, which was drafted to address the sale of goods, does not effectively provide the default rules for an exchange of a tangible copy then clearly it cannot adequately address an exchange of intangible copyrights. This section will analyze the interaction of Article 2 and the copyrights. A few of the sections of Article 2 that may conflict with statutory provisions of the Copyright Act are Assignments of Rights and Obligations (§ 2-210), Basic Obligations of the Parties (§ 2-210), Duration of Contract (§ 2-401), Sales on Approval (§ 2-326), the provisions governing title under the UCC (§ 2-403), and the buyer's right to inspect (§ 2-512).<sup>122</sup> This discussion merely illustrates some of the problems posed by any attempt to harmonize state contract law with copyright law without doing violence to either the letter or the spirit of either body of law.

### 1. Assignments of Rights and Obligations (§ 2-210)

Article 2-210(2) provides that “all rights of either seller or buyer can be assigned except where the assignment would materially change the duty of the other party, or increase materially the burden or risk imposed on him by the contract, or impair materially his chance of obtaining a return performance”<sup>123</sup> unless the parties agree otherwise. “[T]he assignability of rights is a ‘normal and permissible’ incident of the sale of goods”.<sup>124</sup> In contrast, the copyright act places limitations on the transfer of a license. An exclusive license as a transfer of an ownership interest in the copyright is assignable absent contract restrictions while a non-exclusive license is personal to the licensee and may not be assigned without permission of the copyright owner. Article 2-210 cannot be used as a gap filler in the copyright owner's silence to infer that a non-exclusive license is transferable.<sup>125</sup>

### 2. Basic Obligations of the Parties (§ 2-210)

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business of selling goods of that kind . . . ”. U.C.C. § 1-201(9).

<sup>119</sup> U.C.C. § 2-403(2).

<sup>120</sup> See *Independent News Co. v. Williams*, 293 F.2d 510, \_\_\_ (3d Cir. 1961).

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<sup>122</sup> Brenman, *supra* note 45, at 532-34 (chart comparing provisions of the Copyright Act to sections of Article 2).

<sup>123</sup> UCC art. 2-210(2).

<sup>124</sup> See Brenman, *supra* note 45, at 492.

<sup>125</sup> Sections 109, 117, among other places other limitations on the transfer of a tangible copy and which rights attend such a transfer.

Article 2-301 provides that succinctly that “The obligation of the seller is to transfer and deliver and that of the buyer is to accept and pay in accordance with the contract.”<sup>126</sup> Under the Copyright Act, the key operative language of Article 2-301 “to transfer and deliver” is a disjunctive process involving two different forms of property. The seller in the paradigmatic digital works transaction may “transfer” an interest in the copyright such as an exclusive license or may “deliver” a tangible copy of the work. Mere delivery of the goods does not transfer the copyright or even sufficient interests under the Copyright Act to effectively use the work nor does a license to use the work guarantee access to a work to be used. For example, transferring a DVD does not grant a public performance right or granting a public performance right does not assure that a copy of the work will be provided.

### 3. Duration of Contract (§ 2-401)

Article 2-309(2) provides that “Where the contract provides for successive performances but is indefinite in duration it is valid for a reasonable time but unless otherwise agreed may be terminated at any time by either party.”<sup>127</sup> “[E]xcept on the happening of an agreed event[, the termination of the contract] requires that reasonable notification be received by the other party and an agreement dispensing with notification is invalid if its operation would be unconscionable.”<sup>128</sup> In contrast, unless the parties have agreed otherwise an exclusive license is “for the full duration allowed by law” generally the copyright term.<sup>129</sup> The copyright owner does not have the right to terminate an exclusive license with reasonable notice. The duration of a non-exclusive license is less clear. Some courts have held that the duration is presumptively 30-35 years depending on the exercise of termination of transfer rights while other courts have held that it is terminable at will, if state law permits.<sup>130</sup> Consequently, in one state a possessor of a non-exclusive license has an interest that is valid for 30-35 years while in another state the possessor has an interest that is terminable at will. Of course, this also depends on the law of the circuit.

### 4. Sales on Approval (§ 2-326)

Article 2-326(1) provides that “[u]nless otherwise agreed, if delivered goods may be returned by the buyer even though they conform to the contract, the transaction is (a) a “sale on approval” if the goods are delivered primarily for use, and (b) a “sale or return” if the goods are delivered primarily for resale.”<sup>131</sup> The “sale on approval” section of the UCC may violate provisions of

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<sup>126</sup> UCC art. 2-301

<sup>127</sup> UCC art. 2-309(2).

<sup>128</sup> UCC art. 2-309(3).

<sup>129</sup> 3 NIMMER ON COPYRIGHT, *supra* note 9, at ¶ 10.10[F]; 1 PAUL GOLDSTEIN, COPYRIGHT § 4.6.3.3(a), at 4:116 (2d ed. 1999).

<sup>130</sup> Compare *Walthal v. Rusk*, 172 F.3d 481, 484-85 (7th Cir.1999) (section 203 does not create a minimum term of 35 years for licenses of indefinite duration), with *Rano v. Sipa Press, Inc.*, 987 F.2d 580, 585 (9th Cir. 1993) (section 203 does create a minimum term of 35 years for licenses of indefinite duration).

<sup>131</sup> UCC art. 2-326(1)

the Copyright Act.<sup>132</sup> In *Central Point Software, Inc. v. Global Software & Accessories, Inc.*,<sup>133</sup> the court considered the application of state law permitting sales on approval and the Computer Software Rental Amendments Act.<sup>134</sup> The court held that “Where a practice is, in substance, no different from rental, the practice is prohibited regardless of whether, under state law, the transaction may be considered a “sale on approval” between buyer and seller.”<sup>135</sup> Accordingly, at least to some copyrighted works such as computer software, there may not be a right to have a sale on approval even if permissible under the UCC.<sup>136</sup>

## 5. Title Provisions (§ 2-403)

### a. Importance of Title

Because after 1976, copyright law is uniquely a matter of federal law, state courts and legislatures have not adequately considered what impact if any changes in the U.C.C. would have on copyright law. An excellent example of this is the modern trend in the UCC of focusing on risk of loss rather than the common law fetish of title transfer.<sup>137</sup> While American Law Institute (ALI)-National Conference of Commissioners on Uniform State Laws (NCCUSL) and state legislatures consider policy implications of when risk of loss passes the Copyright Act still emphasizes the transfer of title (ownership).<sup>138</sup> This shift of focus keeps the state law of contract just a bit out of step with the federal law of copyright.

### b. Mandatory Transfer of Title

Article 2-401 provides that “[a]ny retention or reservation of by the seller of title in the goods shipped or delivered to the buyer is limited in effect to reservation of a security interest” The seller cannot prevent title passing to the buyer upon delivery. Any attempt at a reservation is immediately by law converted to a security interest. In contrast, regardless of Article 2-401 the purchase of a copyrighted digital work may transfer title to the tangible work (e.g., CD-ROM) but it does not transfer title to the copyrighted work embodied in the work. Further, the rights in the copyright are infinitely divisible. When the copyright owner transfers an exclusive right, she retains all the rights in the bundle that were not transferred within the scope of the license.

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<sup>132</sup> See Brenman, *supra* note 45, at 509.

<sup>133</sup> 880 F. Supp. 957 (E.D.N.Y. 1995).

<sup>134</sup> *Id.* at 963.

<sup>135</sup> *Id.* at 965.

<sup>136</sup> It is not clear that under the Article 2-326 that activities in *Global Software & Accessories, Inc.*, would constitute a sale on approval. The Court found that a “nearly 100% return rate; certain DBP brochures advertise only the “nonrefundable deposit,” not the purchase price; the “nonrefundable deposits” are comparable to rental fees; the relatively short DBP term is comparable to the rental term, obviously allowing Global to use the same copy of software in another DBP transaction within a short time; and the customer is not given the manufacturer’s registration card until the purchase price is paid. Even though it is the customer’s choice whether to return the software, given the nearly 100% return rate, Global should have known that its DBP operated substantially the same as its legitimate software rentals.” Perhaps, a commercially reasonable sale on approval program that was a sale on approval rather than a cover for a rental operation might pass muster under the Computer Software Rental Amendments Act.

<sup>137</sup> Linda Galler, *An Historical and Policy Analysis of the Title Passage Rule in International Sales of Personal Property*, 52 U. PITT. L. REV. 521, 524(1991) (“concept of title, which, in the modern law of sales, exists largely as an historical footnote.”).

<sup>138</sup> Brennan, *supra* note 45, at 511.

### c. When Title Passes

Article 2-401 provides that unless otherwise agreed, “title passes to the buyer at the time and place at which the seller completes his performance with reference to the physical delivery of the goods[.]”<sup>139</sup> Alternatively, “where delivery is to be made without moving the goods, (a) if the seller is to deliver a document of title, title passes at the time when and the place where he delivers such documents; or (b) if the goods are at the time of contracting already identified and no documents are to be delivered, title passes at the time and place of contracting.”<sup>140</sup> The Copyright Act uses a different nomenclature. Title is equivalent of “ownership” under the Copyright Act. A copyright owner is one who possesses any of the exclusive rights under § 106 of the Copyright Act.<sup>141</sup> A transfer of ownership under the Copyright Act is an assignment or exclusive license of a § 106 right. This transfer of ownership does not require the transfer of a physical copy of the work and occurs at the moment the documents are executed.<sup>142</sup>

### 6. Buyer’s Right to Inspect (§2-512)

Article 2-513 provides that “the buyer has a right before payment or acceptance to inspect them at any reasonable place and time and in any reasonable manner.”<sup>143</sup> In contrast, under the Copyright Act, the buyer may have a right to inspect the tangible work, for example to insure that the package contains a CD-ROM rather than floppy disks or that the disks are properly labeled. That is not much of an inspection right. Presumably, the buyer wants to insure that the CD-ROM contains the program that the label states it does or that the program runs as described in the materials. This type of inspection is subject to the Copyright Act. If inspection requires that a copy of the program be loaded into a computer then title is vitally important. As was discussed earlier in this article, § 117 of the Copyright Act permits *owners* to upload copies of software when it is essential to running to program. Licensees do not enjoy similar rights. A video store may not permit patrons to view a DVD privately in order to inspect the DVD to insure that the copyrighted work on the DVD meets their needs.<sup>144</sup> Computer stores most likely may not allow patrons to take home software to inspect it before purchase. The Copyright Act adds sever limits on Article 2-513’s buyer’s right of inspection before purchase.

### G. Common Law Contract

Another approach taken by some courts is to reject applying the Uniform Commercial Code and apply the common law of contract.<sup>145</sup> Under the common law of contract, as between seller

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<sup>139</sup> UCC art. 2-401(1)

<sup>140</sup> UCC art. 2-401(2)

<sup>141</sup> 17 U.S.C. § 106.

<sup>142</sup> Ownership of a copy of the work is a question of state law.

<sup>143</sup> UCC art. 2-513.

<sup>144</sup> Brennan, *supra* note 45, at 527.

<sup>145</sup> If a court finds that specific transaction does not concern a “good” as defined by the U.C.C., the court may then apply the common law of contract to the transaction by declining to apply the U.C.C. even by analogy.

and buyer, passing of title depends largely on intention of parties.<sup>146</sup> Under this model, the copyright owner's characterization of the transaction as embodied in the accompanying contract or license will govern the rights of the end user under the Copyright Act, and the courts will not go beyond interpreting the contract and its relevance to § 109 and § 117.

In *Novell, Inc. v. CPU Distributing, Inc.*,<sup>147</sup> the Court appeared to apply to the common law of contract to its analysis of an end user license. At issue, here was a company that purchased Novell, Inc. software from original equipment manufactures (OEMs) in violation of their agreements with Novell, Inc. The court had to decide whether Novell, Inc. OEM agreement created a license or first sale.<sup>148</sup> Under the common law, "the transfer of a product for consideration with a transfer of title and risk of loss generally constitutes as sale."<sup>149</sup> The contract has terms that were consistent with finding a sale using language such as "sale," "acquire," and "resellers," but there was also a reservations of intellectual property rights "Novell, Inc . . . owns and retains all title and ownership of all intellectual property rights in the Novell Products, including all software . . . copies of software . . . Novell does not transfer any portion of such title and ownership to OEM."<sup>150</sup> The Court held that "transfer to the OEM of tangible copies of Novell software under the OEM agreement is a sale of the particular copies, but not of Novell's intellectual property rights in the computer program itself, which is protected by Novell's copyright."<sup>151</sup>

The other paradigm is the sale-purchase model. The common law of contract should treat this as a sale since the risk of loss of the media embodying the software is shifted to the purchaser at this point in the transaction. Imagine trying to obtain a new copy of software by returning to the merchant after having to remove the software from the merchant then asserting you retained risk of loss because I did have a chance to accept the end user's license. The merchant would laugh you out of the store. The common law mirror image rule was rejected by the U.C.C. § 2-207.<sup>152</sup> If there were an exchange of forms, for example the buyer's purchase order form had terms that conflicted with the seller's invoice form enclosed with the product. Assuming that each contained sufficient terms to satisfy the common law of contract under the common law of contract "the terms of the contract are those of the party whose offer has been accepted and thus of the party who has managed to 'fire the last shot.'"<sup>153</sup> Usually this was the seller, and the buyer accepted these terms by not returning the merchandise.<sup>154</sup> In the case of software, model seems to be that the software company's shrinkwrap license is incorporated by tacit reference into the agreement with the merchant who actually provides the software to the consumer. The consumer may then counter that last offer by either writing the merchant or the software company rejecting the terms and proposing a counter-offer along with some form of acceptance by silence provision.

<sup>146</sup> *Schiavi's Mobile Homes, Inc. v. Johnson*, 244 A.2d 72, \_\_\_ (Me. 1968).

<sup>147</sup> 2000 U.S. Dist. Lexis 9975 (S.D. Tex. 2000).

<sup>148</sup> The court found that the Novell, Inc. End-User License Agreement ("EULA") or shrinkwrap license was directed at the end-user and did not interpret it as part of this dispute. 2000 U.S. Dist. Lexis 9975, at \* 8 n.4.

<sup>149</sup> 2000 U.S. Dist. Lexis 9975, at \* 11.

<sup>150</sup> In the risk and loss provision of the contract, risk passed to the OEM upon delivery except for Novell's intellectual property assets. This is consistent with a finding of a first sale.

<sup>151</sup> 2000 U.S. Dist. Lexis 9975, \* 18.

<sup>152</sup> O'Rourke, *supra* note 93, at 58 & n. 24.

<sup>153</sup> Giesela Rühl, *The Battle Of The Forms: Comparative And Economic Observations*, 24 U. PA. J. INT'L ECON. L. 189, 191 (2003).

<sup>154</sup> John E. Murray, Jr., *The Chaos Of The 'Battle Of The Forms': Solutions*, 39 VAND. L. REV. 1307, 1331 n. 93 (1986).

### III. UNIFORM COMPUTER INFORMATION TRANSACTIONS ACT (UCITA)

If the UCC is not meeting the need for a comprehensive code to address commercial or consumer transactions in digital works, there is an existing alternative to the UCC, the Uniform Computer Information Transactions Act (UCITA). UCITA is an attempt to draft a uniform law governing information transactions that would be enacted by the states.<sup>155</sup> UCITA would cover digital works.<sup>156</sup> UCITA will not succeed for at least two reasons. It may be substantively flawed as a code to govern digital transactions. In addition, UCITA is widely opposed, and there does not appear to be the political will to enact it at this time.<sup>157</sup> Further, a significant number of those jurisdictions that do not adopt UCITA must not affirmatively enact bomb shelter provisions to protect their citizens from either the rigorous or any application of UCITA.<sup>158</sup> Unlike, an act of Congress or a common law created by the federal courts, UCITA must be adopted in a substantial number of individual jurisdictions before it is effective. Consequently, between flaws or perceived flaws, lack of political will to adopt it in many states, and active opposition to the point of bomb shelter provisions in other states to exclude UCITA, UCITA is unlikely to provide an basis on which to build a uniform law of contract governing digital copyrighted works.

### IV. UNENFORCEABLE CONTRACTS

The not-so-simple choice of law question is confounded by the process leading to the contract and to the related manner in which the contract is memorialized. Until 1996, shrinkwrap licenses were topics of hot discussion in academic circles, but generated little actual litigation.<sup>159</sup> “Most commentators view[ed] shrinkwrap licenses as being of questionable validity, primarily because software users do not have an opportunity to bargain over their terms.”<sup>160</sup> In addition to fundamental principles of contract law that made shrinkwrap contracts at best a dubious proposition, the terms of many shrinkwrap contracts raised significant questions regarding the extent to which individuals may create a private law of copyright to displace or supplement the copyright regime established by Congress.<sup>161</sup> Shrinkwrap contracts often presented the courts with questions of federal preemption of state law under § 301.<sup>162</sup>

Mass-market consumer contracts tend to be drafted beyond the gray edge of the legally

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<sup>155</sup> Uniform Computer Information Transactions Act, Prefatory Note, available at [http://www.law.upenn.edu/bll/ulc/ulc\\_frame.htm](http://www.law.upenn.edu/bll/ulc/ulc_frame.htm).

<sup>156</sup> UCITA § 103(a) (“This [Act] applies to computer information transactions.”). UCITA § 102(10) defines “computer information” as “information in electronic form which is obtained from or through the use of a computer or which is in a form capable of being processed by a computer. The term includes a copy of the information and any documentation or packaging associated with the copy.” While the scope of § 103(a) is quite broad, the remaining provisions of § 103 exclude various categories of works from the scope for § 103 for example motion pictures.

<sup>157</sup> See generally <http://www.badsoftware.com/oppose.htm> (collecting sources).

<sup>158</sup> Some states, such as Iowa, North Carolina, and West Virginia, have bomb shelter provisions to protect their citizens from UCITA and still others such as Ohio, Oregon, and New York have bomb shelter bills pending in the legislature. Szwak, *supra* note 22, at 51.

<sup>159</sup> 908 F. Supp. at 650 (citing *Step-Saver Data Sys., Inc. v. Wyse Tech.*, 939 F.2d 91 (3<sup>rd</sup> Cir. 1991); *Vault Corp. v. Quaid Software Ltd.*, 847 F.2d 255 ( ); *Arizona Retail Sys., Inc. v. Software Link, Inc.*, 831 F. Supp. 759 (D. Ariz. 1993)).

<sup>160</sup> 908 F. Supp. 640, 650 (W.D. Wisc. 1996) (citing Lemley, *supra* note 18, at 1263 n. 107 (citing articles)).

<sup>161</sup> 908 F. Supp. at 650.

<sup>162</sup> 908 F. Supp. at 656-659.

permissible because these consumer contracts often remain either unread when the consumer “consents” or untested in the courts after the dispute arises.<sup>163</sup> Reading and understanding standard form contracts is difficult and time consuming. Frequently, terms are presented to the consumer in a manner designed to maximize frustration with reading the contract while encouraging the consumer click on “I agree” in order to satisfy this frustration. For example after shopping online and selecting merchandise, filling in the order blank, entering credit card data, only then are the terms presented or waiting patiently for software to download, going through innumerable registration and survey screens only then does a small box of dark gray text on lighter gray background appear and ask the consumer to click “I agree.”<sup>164</sup> Contractual terms may be intermixed with advertising text on the web in such a manner as to distract from the legally important terms in favor of content that produces additional sales.<sup>165</sup> Further, there is an economic incentive on the part of the drafters to include *in terrorem* clauses in the hopes of dissuading consumers from even contemplating litigation or arbitration.<sup>166</sup>

This leads to a policy where courts will enforce standard form contracts that provide mutually beneficial terms but “police the terms of standard form contracts to protect consumers from exploitation.”<sup>167</sup> Doctrinally, this is found in the common law unconscionability doctrine, the Restatement (Second) of Contracts § 211(3), and §2-302 of the Uniform Commercial Code.<sup>168</sup> The unconscionability doctrine permits courts to prevent “unfair surprise.”<sup>169</sup> Section

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<sup>163</sup> William T. Vukowich, *Lawyers and the Standard Form Contract System: A Model Rule That Should Have Been*, 6 GEO. J. LEGAL ETHICS 799, 827 (1993); see Hillman & Rachlinski, *supra* note 92, at 444 (“Businesses often delegate the job of drafting their terms to lawyers, who believe that they can best serve their clients by composing an arsenal of one-sided terms without regard to the business environment, or for that matter, anything else.”); Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96 HARV. L. REV. 1172, 1222, 1224 (1984). The counter argument is that business interested in their reputation or who are long term players will not supply overly exploitive contract terms because more sophisticated consumers will pressure business to change the more exploitive terms. Hillman & Rachlinski, *supra* note 92, at 441-43. In essence, the marketplace will discipline overly exploitive businesses.

<sup>164</sup> See *Pollstar v. Gigmania, Ltd.*, 170 F. Supp. 2d 974, 980-81 (E.D. Cal. 2000) (“Notice of the license agreement is provided by small gray text on a gray background.”).

<sup>165</sup> Web site design itself is instrumental in building trust. See Marie-Christine Roy, et. al., *The Impact of Interface Quality on Trust in Web Retailers*, <http://www.cirano.qc.ca/pdf/publication/2001s-32.pdf> (finding “a strong relationship between interface quality and trust.”)

<sup>166</sup> See Vukowich, *supra* note 163, at 827. An example of such a clause may be found in the Microsoft Passport Terms of Use which provides that “[b]y “inputting data ... or engaging in any other form of communication with or through the Passport Web Site” -- or any of its “associated services” -- you grant Microsoft the rights to “use, modify, copy, distribute, transmit, publicly display, publicly perform, reproduce, publish, sublicense, create derivative works from, transfer, or sell any such communication” and -- just when you were thinking it couldn't get any worse -- “exploit any proprietary rights in such communication, including but not limited to rights under copyright, trademark, service mark or patent laws.”” Jamie, *MS Passport: “All Your Bits Are Belong To Us”*, SLASHDOT, April 2, 2001, available at <http://yro.slashdot.org/article.pl?sid=01/04/03/1535244&mode=thread> (emphasis in original); Andrew Orlovski, *All Your Data (and Biz Plans) are Belong to Microsoft*, THE REGISTER, Mar. 30, 2002, available at <http://www.theregister.co.uk/content/4/18002.html> (“The current Passport Terms of Use agreement not only fails to guarantee confidentiality, but actually gives Microsoft and its business partners the right to own your information, and do pretty much what they want with it. That encompasses all your Hotmail and MSN Messenger communications today.”).

<sup>167</sup> *Id.* at 454.

<sup>168</sup> *Id.* at 459.

<sup>169</sup> The unconscionability doctrine has two elements: procedural unconscionability or substantive unconscionability. Procedural unconscionability “result[s] from improprieties in contract formation (such as oral misrepresentations or disparities in bargaining position) rather than from the terms of the contract itself.” BLACKS LAW DICTIONARY (1999). In the ecommerce context, this could occur through misleading text, colors, or graphics designed to lull the consumer into a false sense of security and to distract from the legal import of the contact formation. For example, the contact could be so integrated into the site that the consumer is unaware that she is forming a legal relationship. Substantive unconscionability “result[s] from actual contract terms that are unduly harsh, commercially unreasonable, and grossly unfair given the existing circumstances.” BLACK’S LAW DICTIONARY (1999). Substantive unconscionability would permit a court to protect a consumer against unfair surprise in the

211(3) provides that if a party has reason to know that a party manifesting assent to a standard form contract would not do so, if she were aware that it contained a particular term, that term is not part of the agreement.<sup>170</sup> Section 2-302 of the Uniform Commercial Code permits a court to reform contracts that are unconscionable. The doctrine of reasonable expectations allows a court to blue line out express contract language or refuse to enforce the language if the term frustrates the consumer's reasonable expectations.<sup>171</sup> In essence, "the law presumes the general enforceability of standard terms, while negating terms that are procured unfairly, are unreasonable or indecent, or are reasonably unexpected."<sup>172</sup> Within this context of judicial consumer protection, legislative bodies and administrative agencies have interwoven numerous statutes and regulations that provide additional consumer protection.<sup>173</sup>

Unfortunately, this merely reduces the questions of ownership under the Copyright Act to a court's willingness to interpret the agreement as either a license or a contract. If the contract is valid then the transfer will not fall under § 109 as a first sale, and absent a first sale and title passing, the recipient is not entitled to assert a §117 defense.<sup>174</sup> However, should the court decline to enforce the contract as a license, then the transaction is re-characterized as a sale; title passes; the § 109 first sale doctrine applies; and then as an owner, the defendant can assert a defense under § 117. In both cases, both § 109 and § 117 safe harbor provisions and defenses are merely a fortuitous chance of the contract law of the jurisdiction governing the dispute. This does not promote Congress' declared policy of a uniform and predictable copyright law in the

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terms of the contract.

<sup>170</sup> Restatement (Second) of Contracts § 211(3) & cmt. f (1981) ("Where the other party has reason to believe that the party manifesting such assent would not do so if he knew that the writing contained a particular term, the term is not part of the agreement.") Further, comment c states that there are further restrictions that "standard terms may be superseded by separately negotiated or added terms (§ 203), they are construed against the draftsman (§ 206), and they are subject to the overriding obligation of good faith (§ 205) and to the power of the court to refuse to enforce an unconscionable contract or term (§ 208). Moreover, various contracts and terms are against public policy and unenforceable."

<sup>171</sup> §2-302 Uniform Commercial Code ("If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.")

<sup>172</sup> See, e.g., *C & J Fertilizer, Inc. v. Allied Mut. Ins. Co.*, 227 N.W. 2d 169 (Iowa 1975) (refusing to apply narrow definition on burglary despite express language where narrow definition would defeat reasonable expectations of a purchaser of burglary insurance); Hillman & Rachlinski, *supra* note 92, at 458-61 ("The reasonable-expectations doctrine, also prominent in insurance form- contract cases, holds that "[t]he objectively reasonable expectations of applicants and intended beneficiaries regarding the terms of insurance contracts will be honored even though painstaking study of the policy provisions would have negated those expectations." As worded, the doctrine allows courts to overturn express contract language if the term contradicts the consumer's reasonable expectations. When applied, the doctrine of reasonable expectations thus creates an affirmative duty on the part of the business to point out and explain reasonably unexpected terms even if they clearly were stated in the contract. The doctrine reflects the reality that consumers fail to read their contracts and agree to be bound only to reasonable boilerplate.")

<sup>173</sup> See, e.g., 15 U.S.C. § 45(a)(1) (1982); RESTATEMENT (SECOND) OF TORTS §§ 550-51 (1977) (Concealment and Nondisclosure); HOWARD J. ALPERIN & ROLAND F. CHASE, CONSUMER LAW § 128, at 178 (1986) (Modern consumer protection statutes now exist in all states.); STUART M. SPEISER ET AL., THE AMERICAN LAW OF TORTS § 107, at 122, § 32:67, at 335 (1992).

<sup>174</sup> See *Rhone Poulenc Agro, S.A., v. DeKalb Genetics Corp.*, 284 F.3d 1323, 1331 (N.C. 2002) ("Nevertheless, UCITA (pertaining to the licensing of intangible property) provides guidance on the U.C.C.'s view of the common law. Official comment 3 to UCITA § 506(b) makes clear that the drafters of the U.C.C. concluded that the bona fide purchaser rule does not apply to the licensing of intellectual property.") I am not as sanguine as the *Rhone Poulenc Agro, S.A* Court that one can use UCITA to interpret the drafters of the U.C.C.'s intentions. UCITA was at one time to be considered as a new proposed Article 2B to the U.C.C. The U.C.C. is a joint effort of the American Law Institute (ALI) and the National Conference of Commissioners on Uniform State Laws (NCCUSL). Because of opposition within ALI, NCCUSL withdrew the proposed new Article 2B and promulgate these provisions as a separate Uniform Act, the Uniform Computer Information Transactions Act (UCITA). See Article 2B Is Withdrawn from UCC and Will Be Promulgated by NCCUSL as Separate Act (last visited May 9, 2003), [http://www.ali.org/ali/R2103\\_Art2b.htm](http://www.ali.org/ali/R2103_Art2b.htm); Szwak, *supra* note 22, at 27.

United States.<sup>175</sup>

Nevertheless, there is a significant difference between contracting for few rights and a license for fewer rights. A user who lawfully possesses software subject to a license, who then uses the copyrighted work in excess of the manner provided for in the license is a copyright infringer.<sup>176</sup> Such infringement is subject to the actual damages or statutory penalties of the Copyright Act<sup>177</sup> and its criminal provisions.<sup>178</sup> A draconian penalty is levied for engaging in behavior that Congress protects by public policy and for violating a right that the author does not even possess absent the license. In contrast, an owner of a copy of software subject to a contractual provision that limits either § 109 or § 117 rights (assuming that the contract is not void as a matter of public policy) is merely liable for actual damages because of a breach of the contract. These damages would be minimal or none existent for most of the uses that are protected by either § 109 or § 117.<sup>179</sup>

Whether a contract will be enforced is a matter of critical concern in digital context where frequently the license is the product, and licenses are used to differentiate among identical works in the market by limiting or expanding their use through contract. For example, software sold to universities is identical to software sold on the open market. Yet, university software is usually substantially less expensive. The difference between the two products is a contractual obligation imposed on education software that it be used “for educational use only.” If this condition is not enforced then the less expensive educational software will flood the market and reduce the price of the commercial product. Alternatively, a digital work may arrive on one tangible copy (CD-ROM) accompanied by permission to make additional digital copies rather than shipping additional CD-ROMs. Such a license may reduce production, shipping, and other costs to both parties and perhaps, may even have significant tax advantages.<sup>180</sup> Further, contract law may be used to protect works that are not protected by the Copyright Act. Absent such contract protection, some courts and scholars contend that there would be little motivation to develop factual databases or to maintain works in the public domain. Therefore, the commercial market place needs a predictable environment in which to develop markets for digital works and in which to extend these markets into ecommerce.

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<sup>175</sup> 17 U.S.C. § 301. In the context of an international trade in copyrighted works, this is even more problematic. Professor Lemley notes that many countries do not enforce shrink-wrap licenses or will only enforce them under specified conditions. Among the countries not enforcing shrink-wrap licenses are: Australia, Canada, Chile, Czech Republic, European Community (Belgium, Germany, Denmark, Spain, France, United Kingdom, Italy, Luxembourg, Netherlands, Greece, Ireland, and Portugal), Mexico, Norway, Philippines, Singapore, South Africa, and Taiwan. See Lemley, *supra* note 18, at 1254 & n. 53 (listing countries). This is particularly problematic in the context of gray market goods. See *Quality King Distributors, Inc. v. L'Anza Research Intern., Inc.*, 523 U.S. 135, 141-142 (1998) (first sale doctrine applies to foreign sales).

<sup>176</sup> *Gilliam v. American Broad. Cos.*, 538 F.2d 14, 20 (2d Cir.1976) (licensee infringes owner's copyright if its use exceeds the scope of the license).

<sup>177</sup> Civil remedies include injunctive relief, impounding and destroying the infringing items, actual damages and the infringers profits, or statutory damages. If the court finds that the infringement is willful, the court may impose statutory damages for up to \$150,000. See 17 U.S.C. §§ 501-505.

<sup>178</sup> The Copyright Act provides “Any person who infringes a copyright willfully (1) for purposes of commercial advantage or private financial gain, or (2) by the reproduction or distribution [in] 180 days [of] copies [with] total retail value greater than \$1,000” shall be subject to one year imprisonment and a one thousand dollar fine if the infringement involves more than nine copies with a total retain value of greater than \$2,500 then five years imprisonment. See 17 U.S.C. §506(a), 18 U.S.C. §2319.

<sup>179</sup> For example, violating the § 106(3) distribution right by transferring a licensed copy as opposed to a owned copy would result in minimal or no damages or making RAM copies in order to use a software product, archival copies, or adapting the software for person use is unlikely to result in a measurable injury to the copyright owner .

<sup>180</sup> Frequently, tax laws treat licenses and tangible copies differently. See, e.g,

## V. SECTION 301 PREEMPTION OF STATE CONTRACT LAW

The 1976 Copyright Act preempts state laws that fall within the subject matter of the copyright Act.<sup>181</sup> Generally if the work falls within the subject matter of the Copyright Act<sup>182</sup> and the state law creates rights that are the equivalent of those granted to copyright owners under § 106 then the Copyright Act preempts state law. The both the case and statutory law are undecided as to whether a state's public law governing private contract falls within the prohibition of §301 if the parties create a private law regime through contract that grants rights that are equivalent to § 106 rights in a copyrighted work.<sup>183</sup> Alternatively, the Commerce Clause of the United States Constitution provides another basis on which to find that these contracts are preempted.

### A. § 301 Preempts Private and Public Law

Section 301 preempts state laws that are the equivalent of a right granted to a copyright owner under the Copyright Act.<sup>184</sup> But if an "extra element" is "required instead of or in addition to the acts of reproduction, performance, distribution or display, in order to constitute a state-created cause of action, then the right does not lie 'within the general scope of copyright,' and there is no preemption."<sup>185</sup> Although there is language in the legislative history of § 301<sup>186</sup> and several cases stating that breach of contract claims are generally not preempted, there is also persuasive authority indicating that breach of contract claims should be preempted in certain circumstances.<sup>187</sup> The teaching of these cases is that a breach of contract claim is preempted if it is merely based on allegations that the defendant did something that the copyright laws reserve exclusively to the plaintiff (such as unauthorized reproduction, performance, distribution, or display). However, if the breach of contract claim is based on allegations that the parties' contract creates a right not existing under copyright

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<sup>181</sup> 17 U.S.C. § 301 ("all legal or equitable rights that are equivalent to any of the exclusive rights within the general scope of copyright as specified by § 106 in works of authorship that are fixed in a tangible medium of expression and come within the subject matter of copyright as specified by §§ 102 and 103. . . ., are governed exclusively by this title. Thereafter, no person is entitled to any such right or equivalent right in any such work under the common law or statutes of any State.")

<sup>182</sup> See *Wrench LLC v. Taco Bell Corp.*, 256 F.3d 446, 455 (6th Cir.2001) ("We join our sister circuits in holding that the scope of the Copyright Act's subject matter is broader than the scope of the Act's protections."); *Id.* at 454 ("[T]he scope of the Copyright Act's subject matter extends beyond the tangible expressions that can be protected under the Act to elements of expression which themselves cannot be protected."). Even uncopyrightable ideas that are part of copyrighted works come within the subject matter of copyright. See *Wrench*, at 454 (citing *United States ex rel. Berge v. Board of Trustees of the Univ. of Ala.*, 104 F.3d 1453, 1463 (4th Cir.1997)).

<sup>183</sup> *Ballas v. Tedesco*, 41 F. Supp. 2d 531, 537 n. 14 (D.N.J. 1999) (citing cases).

<sup>184</sup> *Computer Assocs. Int'l, Inc. v. Altai, Inc.*, 982 F.2d 693, 716 (2d Cir.1992).

<sup>185</sup> *Computer Assocs.*, 982 F.2d at 716 (quoting 1 NIMMER ON COPYRIGHT, *supra* note 45, at § 1.01[B][1], 1-14-15).

<sup>186</sup> See H.R.Rep. No. 1476, 94th Cong., 2d Sess. 132, *reprinted in* 1976 U.S.C.C.A.N. 5659, 5748 ("nothing in the bill derogates from the rights of parties to contract with each other and to sue for breaches of contract"); see also *Strauss v. Hearst Corp.*, No. 85 Civ. 10017 (CSH), 1988 WL 18932 (S.D.N.Y. Feb. 19, 1988), at \*9; *Ronald Litoff, Ltd. v. American Express Co.*, 621 F. Supp. 981, 986 (S.D.N.Y.1985).

<sup>187</sup> See, e.g., *Wolff v. Institute of Electrical and Electronics Eng'rs, Inc.*, 768 F. Supp. 66, 69 (S.D.N.Y.1991); *Brignoli v. Balch Hardy and Scheinman, Inc.*, 645 F. Supp. 1201, 1205 (S.D.N.Y.1986); *Smith v. Weinstein*, 578 F. Supp. 1297, 1307 (S.D.N.Y.), *aff'd*, 738 F.2d 419 (2d Cir.1984).

law--a right based upon a party's contractual promise--and the plaintiff is suing to protect that contractual right, then the claim is not preempted.<sup>188</sup>

#### B. § 301 Only Pre-empts Public Law and Does not Preempt State Enforcement of Private Contracts

As was stated earlier, § 301(a) preempts any legal or equitable rights under state law that are the equivalent to any of the exclusive rights granted under § 106 for works fixed in a tangible medium of expression and fall within § 102 and § 103 of the Copyright Act.<sup>189</sup> The crucial issue facing these courts is are rights provided by contract that are the equivalent to any of the exclusive § 106 rights or is the contract an extra-element.<sup>190</sup> These courts have held that in order for a right to be the equivalent to a § 106 right it must be a law of general applicability.<sup>191</sup> A general law is one that that applies to the entire world; one that applies to strangers to the copyright owner. In contrast, contracts are only binding on those in privity with the copyright owner. Contracts leave strangers to the author free to engage in any act that does not violate § 106. Accordingly, since statutory rights run against all the world and contract rights only against those in privity, contract rights are not the equivalent of § 106 rights and are therefore not preempted under § 301. This is a false dilemma. If we define rights that run against the entire world that bear on the subject matter of copyright as the equivalent of § 106 rights and as such preempted under § 301 then a contract regime that does not allow use without privity has in essence the same effect. If the software will not function without manifesting assent to a license agreement then that software in essence runs against all the world since no user can be a stranger to the contract.<sup>192</sup>

### VI. A FEDERAL COMMON LAW OF CONTRACT

Federal courts may create a federal common law if the rules are necessary to protect a “uniquely federal interest” that will suffer damage if state law is applied, and then it must consider the state’s interest in having its law apply and the need for a national uniform law.<sup>193</sup> Over the years, federal courts have applied several tests to determine when they will create a federal common law.<sup>194</sup> They have found that it is necessary to consider whether there is a source for the federal common law, the need for national uniformity, whether federal and state laws conflict, and whether a federal rule would displace state law in area of local concern.<sup>195</sup> However, once these factors weigh in favor of the federal common law, strong public policy supports uniformity of copyright law on a national basis requires that in the copyright context

<sup>188</sup> *National Car Rental Sys., Inc. v. Computer Assocs. Int'l, Inc.*, 991 F.2d 426, 431-433 (8th Cir.), *cert. denied*, 510 U.S. 861, (1993) (“contractual restriction [creating right not existing under Copyright Act] constitutes an extra element that makes this cause of action qualitatively different from one for copyright”).

<sup>189</sup> *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447, 1453 (7th Cir. 1996), citing 17 UCC § 301.

<sup>190</sup> *Madison*, *supra* note 93, at 1127-1132.

<sup>191</sup> *Id.* at \_\_\_\_.

<sup>192</sup> Brett L. Tolman, Note *Procd, Inc. v. Zeidenberg: The End Does Not Justify The Means In Federal Copyright Analysis*, 1998 B.Y.U. L. REV. 303, 324 (1998). Brian Covotta & Pamela Sergeeff, *Procd, Inc. v. Zeidenberg*, 13 BERKELEY TECH. L.J. 35, 48-49 (1998) (distinguishing between negotiated and mass-market contracts for federal preemption).

<sup>193</sup> *Clearfield Trust Co. v. United States*, 318 U.S. 363 (1943); Martha A. Field, *Sources of Law: The Scope of Federal Common Law*, 99 HARV. L. REV. 881 885 (1986).

<sup>194</sup> Field, *supra* note 193, at 906-946.

<sup>195</sup> *Id.* at 906-946.

federal courts exercise their inherent powers to create a federal common law of contract to govern property interests created by or related to those established under the Copyright Act.<sup>196</sup> By applying the state law of contracts, there is the anomalous proposition that depending on where the parties entered into the contract, the same contract may result in different rights under the Copyright Act. Rights under all of the fair use sections, § 107- § 122, depend on whether courts will enforce a contract that requires users to surrender their rights under the Copyright Act.<sup>197</sup> Furthermore, rights under § 109 and § 117 of the Copyright Act depend on whether under state law, the transaction resulted in title passing from the copyright owner to the owner of a particular embodiment of the work. The absence of a federal common law supports the further fragmenting copyright law by fitting it into state contract principles.

#### A. Sources For A Federal Common Law Of Contract

The general rule of *Erie R.R. Co. v. Tompkins* that “[t]here is no federal general common law”<sup>198</sup> “is inapplicable to those areas of judicial decision within which the policy of the law is so dominated by the sweep of federal statutes that legal relations which they affect must be deemed governed by federal law having its source in those statutes, rather than by local law.”<sup>199</sup> The responsibility of federal courts to define the body of federal common law that arises from the interstices of federal legislation has been established by a number of Supreme Court decisions.<sup>200</sup> Federal statutes are often a source for federal common law.<sup>201</sup> Courts discern the legislative policy underlying the statute and devise a remedy to effectuate that policy.<sup>202</sup>

In the patent context courts have noted:

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<sup>196</sup> Cf. *Clearfield Trust Co.*, 318 U.S. at 576 (creating a federal common law of commercial paper to assure uniformity concerning federal government checks).

<sup>197</sup> Contracts have been used to restrict a licensee's ability to exercise § 107 fair use rights. See, e.g., *Bowers v. Baystate Technologies, Inc.*, 320 F.3d 1317, 1325 (Fed. Cir. 2003) (contract prohibiting reverse engineering a fair use permitted by § 107 was not preempted), *petition for cert. filed*, 71 USLW 3709 (Apr. 29, 2003)(No. 02-1585). *Bowers* relied on the erroneous assumption that the fair use provision's purpose is the “protection of the property rights of individual parties ... rather than ... the protection of the general public.” *Id.* at 1325 (internal quotations and citation omitted).

<sup>198</sup> *Erie R.R. Co. v. Tompkins*, 304 U.S. 64, 78 (1938).

<sup>199</sup> *Sola Elec. Co. v. Jefferson Elec. Co.*, 317 U.S. 173, 176 (1942); *Rhone Poulenc Agro, S.A. v. DeKalb Genetics Corp.*, 284 F.3d 1323, 1327 n. 1 (Fed. Cir. 2002); *Unarco Indus., Inc. v. Kelley Co.*, 465 F.2d 1303 (7th Cir.1972), cert. denied, 410 U.S. 929, (1973); *PPG Indus., Inc. v. Guardian Indus. Corp.*, 597 F.2d 1090 (6th Cir.), cert. denied, 444 U.S. 930, (1979)

<sup>200</sup> See, e.g., *Illinois v. Milwaukee*, 406 U.S. 91, (1972) (federal common law right of nuisance recognized and applied to the pollution of interstate waters); *Textile Workers v. Lincoln Mills*, 353 U.S. 448, (1957) (federal labor law); *Texas & Pacific Railway v. Rigsby*, 241 U.S. 33 (1916) (Safety Appliance Act).

<sup>201</sup> *Quasar Co. v. Atchison, Topeka & Santa Fe Ry. Co.*, 632 F. Supp.1106, 1112 (N.D. Ill.1986).

<sup>202</sup> See, e.g., *Society of Prof'l Eng'rs v. United States*, 435 U.S. 679, 688 (1979) (federal courts may develop a common law of antitrust ‘giving shape’ to the ‘broad mandate’ of the Sherman Act); *Lincoln Mills*, 353 U.S. at 456 (Taft-Hartley Act is source of federal common law governing validity of labor arbitration awards); *Gaff v. Federal Deposit Insur. Corp.*, 919 F.2d 384, 395 (6th Cir. 1990) (looking to FIRREA and the Bankruptcy Code to formulate federal common law principle governing priority of stockholders' claims against insolvent bank after FDIC takeover); *United States of America v. Burnette-Carter Co.*, 575 F.2d 587, 590 (6th Cir.), cert. denied, 439 U.S. 996(1978) (Uniform Commercial Code and state law precedents are source for federal common law governing FHA secured transactions). *But see*, ERWIN CHEREMINSKY, FEDERAL JURISDICTION § 6.3.2, at 376 (3d ed. 1999)(“The federal judiciary will formulate a body of common law rules only pursuant to clear congressional intent for such action.”).

When an inventor or person holding patent rights desires to license or relinquish any part of the patent monopoly, such person is utilizing the monopoly of rights intended by the framers of the Constitution and the legislation of Congress to reward invention and originality. This monopoly conferred by federal statute as well as the policy perpetuating this monopoly, so affects the licensing of patents, and the policy behind such licensing is so intertwined with the sweep of federal statutes, that any question with respect thereto must be governed by federal law.<sup>203</sup>

In *Rhone Poulenc Agro, S.A.*, the United States Court of Appeals for the Federal Circuit considered the applicability of state contract law.<sup>204</sup> The Court held, “the interpretation of contact rights under patents is generally governed by state law.”<sup>205</sup> The Court found that in the context of the bona fide purchaser defense that the Court confronts

a unique situation in which federal patent statute exception explicitly governs the bona fide purchaser rule in some situations but not in all situations. It would be anomalous for federal law to govern that defense in part and for state law to govern in part. There is quite plainly a need for a uniform body of federal law on the bona fide purchaser defense.<sup>206</sup>

The Court then observed that federal courts had rejected state law governing the assignability of patent licenses. Federal courts have also rejected state commercial law for the purposes of determining whether a invention was the subject of a commercial offer for sale more than one year prior to the patent application.<sup>207</sup> A consistent federal rule was required “to avoid the possibility of a patent’s being valid in one state and invalid in another state.”<sup>208</sup>

Congressional authority to legislate patents and copyrights arise out of the same clause of the United States Constitution, and both patents and copyrights serve the same public good.<sup>209</sup> The United States Supreme Court in *Sony Corp. of America v. Universal City Studios, Inc.*, observed, “it is appropriate to refer [patent jurisprudence in a copyright case] because of the historic kinship between patent law and copyright law.”<sup>210</sup> Like patent law, Congress has a declared legislative purpose of assuring a uniform copyright law.<sup>211</sup> The policies supporting the United

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<sup>203</sup> *In re CFLC, Inc.*, 174 B.R. 119, 122 (N.D. Cal. 1994) citing *Unarco Indus., Inc.*, 465 F.2d. at \_\_\_\_ (internal citations omitted).

<sup>204</sup> 284 F.3d at 1327.

<sup>205</sup> *Id.* (citing cases).

<sup>206</sup> 284 F.3d. at 1328.

<sup>207</sup> *Id.* citing *Group One, Ltd. v. Hallmark Cards, Inc.*, 254 F.3d 1041, 1047 (Fed. Cir. 2001), cert. denied, 122 S. Ct. 1063 (2002); *Univ. of Colo. Found., Inc. v. Am. Cyanamid Co.*, 196 F.3d 1366, 1372 (Fed. Cir. 1999). Section 102(b) provides: “A person shall be entitled to a patent unless . . . the invention was . . . in public use or on sale in this country, more than one year prior to the date of the application for patent in the United States.” 35 U.S.C. § 102(b).

<sup>208</sup> 284 F.3d. at 1328 (citing cases).

<sup>209</sup> *Sony Corp. v. Universal Studios*, 464 U.S. 417, \_\_ (1984).

<sup>210</sup> *Id.* at 439 & n. 19 (citing *United States v. Paramount Pictures*, 334 U.S. 131, 158 (1948); *Fox Film Corp. v. Doyal*, 286 U.S. 123, 131,(1932); *Wheaton & Donaldson v. Peters & Grigg*, 33 U.S. (8 Pet.) 591, 657-58 (1834)).

<sup>211</sup> 17 U.S.C. § 301. See Notes of Committee on the Judiciary, House Report No. 94- 1476, U.S. Code Cong. & Admin. News 1976, 5659, 5746 (“The declaration of this principle in section 301 is intended to be stated in the clearest and most unequivocal language possible, so as to foreclose any conceivable misinterpretation of its unqualified intention that Congress shall act preemptively, and to avoid the development of any vague borderline areas between State and Federal protection.”) [emphasis added].

States Court of Appeals for the Federal Circuit's decision in *Rhone Poulenc Agro, S.A.* is equally applicable here. **[CHECK TO SEE IF ANYTHING IN LEG. HISTORY]**

## B. Need for Uniformity

Copyright law presents the same dilemma of integrating possibly conflicting state and federal policy regarding who is a bona fide purchaser as the Court faced in *Rhone Poulenc Agro, S.A.* trying to integrate state and federal bona fide purchaser rules into Patent law. The Copyright Act determines *in part* a bona fide purchaser's rights<sup>212</sup> and state law in part.<sup>213</sup> As the *Rhone Poulenc Agro, S.A.* Court held "It would be anomalous for federal law to govern [the bona fide purchaser] defense in part and for state law to govern in part. There is quite plainly a need for a uniform body of federal law on the bona fide purchaser defense."<sup>214</sup>

A strong public policy to support a uniform test to determine when ownership to a particular embodiment of a copyright righted work passes or even ownership of the intangible copyright. It would be incongruous to have the same contract language produce a sale in one state and a license in another. This is particularly significant since when titles passes determines whether the user has rights under both § 109 and § 117 of the Copyright Act. Differences in state laws will provide a perverse and unintended incentive to engage in gray market transactions.<sup>215</sup> Depending on where the transaction takes place, some works have § 109 first sale or § 117 software fair use rights and others do not—perhaps, for the first time creating an internal gray market for copyrighted products within the United States.<sup>216</sup> For example, if state A's contract law provides that the first sale takes place when the software is sold to the wholesaler then all subsequent sales to retailers and individuals consumers are all subject to § 109 First Sale defense and any attempt to impose use restrictions that purport to create a situation that violates the Copyright Act are void. Again, there may be a breach of contract issue but that will not constitute copyright infringement. This First Sale defense follows each copy wherever it may go in the stream of commerce. If a state B's law does not provide that the first sale takes place when the software is sold to the wholesaler then at what point, if any, there is a first sale is an open question. In fact, a first sale may never have taken place and all subsequent possessors are mere licensees. Accordingly, software routed through state A arrives in state C with first sale rights while the same software routed through state B arrives in state C with no first sale rights. To the consumer, the packaging is identical, but the legal ramifications are quite different. For many individual users and small businesses, the threat of statutory damages and injunctive relief is more problematic than the concerns regarding an economically efficient breach. Frequently, the economic value of a judgment on the contract claim will be insignificant compared to

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<sup>212</sup> 17 U.S.C. § 205.

<sup>213</sup> See generally UCC art. 9.

<sup>214</sup> *Rhone Poulenc Agro, S.A. v. DeKalb Genetics Corp.*, 284 F.3d 1323, \_\_\_\_ (Fed. Cir. 2002).

<sup>215</sup> For example, shrinkwrap licenses are enforceable in \_\_\_\_\_, but not in \_\_\_\_\_. Moreover, either state courts or the state legislature may change the state law of contract at anytime.

<sup>216</sup> For example, if Maryland and Virginia have adopted UCITA, other states, such as Iowa, North Carolina, and West Virginia, have bomb shelter provisions to protect their citizens from UCITA and still others such as Ohio, Oregon, and New York have bomb shelter bills pending in the legislature. Szwak, *supra* note 174, at 51. Moreover, other states have adopted non-uniform versions with various forms of consumer protection. *Id.* UCITA jurisdictions will honor the purported license and there will be no first sale. Subsequent transfers, if permitted, will not be covered by the § 101 first sale exemption. Article 2, UCC jurisdictions may or may not find that the purported license is enforceable. While common law jurisdictions are unlikely to enforce them.

statutory or actual damages under the Copyright Act. A federal body of contract law would assure that a uniform national body of law to govern copyright. Overtime, uniform rules of contract will govern distribution so that source or methods of distribution will result in a uniform body of legal rights.

Given that the federal courts have exclusive jurisdiction over disputes under the copyright law, Congress has clearly vested the federal courts with a unique authority to develop a federal law of copyright – by limiting almost to the point of exclusion any role for state courts.<sup>217</sup> Since the body of law would be binding on the states through the Supremacy Clause, any residual state court litigation would have to follow federal law. This would reduce potential conflicts from among 51 jurisdictions to the 14 federal circuits. The United States Supreme Court is quick to resolve genuine conflicts between circuits, while it will rarely grant certiorari on questions of state law. This should result in earlier authoritative pronouncements on matters of commercial copyright policy and encourage the development of a uniform national commercial law of copyright. Finally, since the United States Court of Appeals has used its plenary power over patent appeals to carve out slowly a common law to govern patent contract, creating a federal body of commercial law to govern copyright would allow the federal courts to complement each body of law. Having a consistent body of commercial law is particularly significant in the cases of many digital works that contain both patentable and copyrightable subject matter.

### C. Application of State Law Conflicts With Federal Policy

A further justification for creating a federal common law of contract is that such a body of contract law would avoid the vexing question of § 301 Preemption under the Copyright Act. Section 301 preempts state laws that conflict with federal copyright policies. There is a substantial and highly debated legal question whether state contract laws are preempted under § 301 or does § 301 only preempt public laws of general applicability and exclude contract law as a private body of law governing the relations of individuals in privity.<sup>218</sup> Because a federal body of contract law would not be preempted unless it conflicted with a federal statute or the Constitution, a federal common law of contract would render this question moot.<sup>219</sup> Further, as was discussed previously, some sections of Article 2 conflict with the Copyright Act. Article 2 is a well-textured tapestry of commercial law that is not easily deconstructed section-by-section to account for the needs of copyright law without a tidal wave of unintentional consequences surging thorough the remainder of commercial law. A federal common law of contract could alter, reinterpret, or ignore provisions of Article 2 in isolation without this *sui generis* commercial law for copyright purposes invading other aspects of commercial law. Further, a federal body of common law could harmonize all aspects of federal law and present a coherent body of law to be reviewed by Congress.

### D. Federal Law Displacing State Law on A Matter Of Traditional Local Concern

Copyrights and digital copyrighted works pose unique national concerns in an information

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<sup>218</sup> Madison, *supra* note 93, at \_\_\_\_.

<sup>219</sup> See 17 U.S.C. § 301.

economy. Under the old sales model, goods would be shipped across state lines but once they arrived, the goods would generally remain in one jurisdiction. This was particularly true of consumer goods. So, there was a nexus between the good and a physical location. This is no longer true. For example, an Ohio resident flying to California, downloads software somewhere over the Rocky Mountains for use in California. Literally, the software and the consumer are transit in interstate commerce. There are no local interests here to be displaced other than those associated with allocating the digital work as either an asset in a probate or matrimonial estate. Since allocating property rights, as a matter of probate or domestic relations does not require a uniform national application, the federal courts should look to the law of the state of residence.

The United States Supreme Court looked to state law to define the scope of the renewal right under the 1909 Copyright Act.<sup>220</sup> The issue before the Court was whether an illegitimate child was included in the term “children.” In *De Slyva v. Ballentine*, the Court teaches that the definition of “children” under the Copyright Act’s statutory heirs provision should be determined by state law unless the state defined “children” in a manner “entirely strange to those familiar with its ordinary usage,” but the Court acknowledge that some variation was permissible.<sup>221</sup> The Court then analogized the statutory heirs provision to a “compulsory bequest to the designated persons” so that the definition of “children” “is really a question of the descent of property” and most appropriately decided under state law.<sup>222</sup> Further in the balance of competing federal and state interests, “where a statute deals with a familial relationship; there is no federal law of domestic relations, which is primarily a matter of state concern.”<sup>223</sup> This factor may be the most significant in the minds of the justices. One of the factors frequently cited as a consideration in creating a federal common law is whether a uniform federal rule displacing state law would disrupt an area of local concern.<sup>224</sup> Historically, state governments exercised domestic relations law. It would be incongruous for a state probate court to process in parallel form “federal copyright property” to one set of heirs and other forms of property to another set of heirs, with both sets of heir taking as *children* of the deceased. Since estates are usually probated in only one state there is little need for a national law of probate governing the allocation of the renewal right of a copyrighted work.

#### D. Federal Common Law of Contract

“The formulation of a uniform federal rule does not require that the wisdom of the states be disregarded, and the federal rule may correspond to the rule applied in many states.”<sup>225</sup> In fact, this article suggests a hybrid approach that the federal courts adopt common well-accepted commercial law principles when possible, but remain free to develop a federal common law of

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<sup>220</sup> *De Slyva v. Ballentine*, 351 U.S. 570 (1956) (analyzing § 23 of the Copyright Act of March 4, 1909, 35 Stat. 1080, codified in 17 U.S.C. § 24 (1956) this Act was subsequently amended in 1976).

<sup>221</sup> *Id.* at 581.

<sup>222</sup> *Id.* at 582.

<sup>223</sup> *Id.* at 580. Justices Douglas and Black would have made interpreted the term solely as a matter of federal law and have the Court supply a common law definition of “children.” *Id.* at 583 (Douglas, J. dissenting).

<sup>224</sup> *See, e.g., United States v. Brosnan*, 363 U.S. 237, 242 (1960); Note, *Adopting State Law as the Federal Rule of Decision: A Proposed Test*, 42 U. CHI. L. REV. 823 (1976).

<sup>225</sup> *United States v. Carson*, 372 F.2d 429, 435 (6<sup>th</sup> Cir. 1967); 284 F.3d at 1328;

contract governing intellectual property when appropriate.<sup>226</sup> Federal courts may look to the Uniform Commercial Code as one possible source of law.<sup>227</sup> If the federal courts elect to follow the U.C.C. then the task of the federal judiciary is to

simply to apply the rules found in the Code itself and the general body of precedent developed by the Code states. If there is lack of uniformity on a particular issue, either by virtue of non-uniform changes in the UCC or differing interpretations of a uniform provision, [then the federal court] will normally follow the "weight of authority." It is essential that federal courts not follow aberrational UCC interpretations since uniformity is the *raison d'être* of applying federal and not state law. Moreover, once [the federal court] determine[s] that [it] should follow the UCC, [then it is] obliged by UCC § 1-102(1) & (2)(c) to promote uniformity.<sup>228</sup>

This would ensure the greater level of uniformity throughout the United States by preventing states with non-uniform enactments of the U.C.C. or atypical state court interpretations of the U.C.C. from distorting the law of Copyright. The federal courts could then use the common law of contracts, restatements, UCITA, or CISGA, as gap fillers to replace those provisions of the UCC that are preempted by federal law and when necessary interpret ambiguous provisions in the Copyright Act so that they are consistent with commercial practices.

Of course, federal courts could reject the UCC, in completely or in part, and look to other bodies of law. UCITA is another possible source of law. Federal courts could examine UCITA as a source on which to draw language and principles to govern transactions in information. The judiciary could selectively incorporate those UCITA principles that are sound and of especial applicability to copyright while rejecting UCITA terms that may conflict with federal copyright policy. Although proponents of UCITA assert that it is aggressively neutral as to federal intellectual property rights, and would of course be preempted if passed by a state and a UCITA term conflicted with federal copyright law, there is a substantial body of scholarship questioning the soundness of these assumptions. A federal common law would permit the courts to accrete UCITA provisions into law as necessary, if they provided the superior alternative to the existing contract law model or as gap fillers to another body of contract law.

An overlooked but significant source to draw a body of federal contract law is the Convention on the International Sales of Goods ("CISG").<sup>229</sup> Like the U.C.C., the CISG may be applied by analogy. A federal common law of contract that tracked the international obligations of the United States would insure that the same dispute would be resolved in the same manner regardless of where the dispute takes place.<sup>230</sup> In the normative a-national world of ecommerce, this would eliminate or reduce many choice-of-law questions. In a global marketplace for

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<sup>226</sup> Cf. *Henry v. Mississippi*, 379 U.S. 443 (1965) (creating a hybrid state and federal body of procedural law).

<sup>227</sup> 284 F.3d at 1328-29; *United States v. Burnette-Carter Co.*, 575 F.2d 587, 590 (6<sup>th</sup> Cir. 1978) (noting that Congress approved the U.C.C. by adopting it for DC and applying the UCC as the federal common law under FmHA).

<sup>228</sup> *Burnette-Carter Co.*, 575 F.2d at 590 (internal citations and quotation marks omitted).

<sup>229</sup> UNITED NATIONS CONVENTION ON CONTRACTS FOR THE INTERNATIONAL SALE OF GOODS (1980)[CISG], available at <http://www.cisg.law.pace.edu/cisg/text/cisg-toc.html>

<sup>230</sup> See Charles Sukurs, *Harmonizing the Battle of the Forms: A Comparison of the United States, Canada, and the United Nations Convention on the Contracts of the International Sales of Goods*, 34 VAND. J. TRANSNATIONAL L. 1481, 1484-1511 (discussing the differences between the UCC and the CISG and suggesting a need to harmonize CISG with domestic law).

copyrighted software, the harmonizing domestic contract law of fifty states (by establishing an uniform national body of contract law) with an international body of law could only promote international trade and Congress's declared goal of a uniform national law of copyright. The eclectic use of interstitial gap fillers could produce a harmonious law of contract governing copyright.

## F. Public Policy

Regardless of the source of a body of federal contract law, it should promote the core values underlying the Copyright Act. Ownership should be based on the actual character of the transaction by which the computer program possessor obtained lawful possession rather than the label placed on the transaction by contract.<sup>231</sup> Copyright holders should not be able to frustrate the rights granted by law to owners by characterizing a "sale" as a "license," "lease," or by some other nomenclature, in order to grant fewer rights to the de facto owner of the copyrighted work.<sup>232</sup> Section 109(a), § 107, and § 117 rights are independent of any rights that the copyright owner may grant in a license.<sup>233</sup> In fact, many copyright holders compel owners to surrender rights granted under the Copyright Act through the aggressive use of licenses.<sup>234</sup>

A federal common law of contract would permit federal courts to determine whether to permit copyright holders to opt-out of the copyright regime established by Congress and to create a private law of contract to displace the "social contract" inherent in the Copyright Act. Alternatively, congress could enact a positive law of contract. As with the federal courts, congress should look to state laws as models on which to build a federal body of contract law.

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<sup>231</sup> *Applied Info. Mgmt., Inc. v. Icart*, 976 F. Supp. 149, 155 (E.D.N.Y. 1997); *Softman Products Co., LLC v. Adobe Sys., Inc.*, 171 F. Supp. 2d 1075, 1086 (C.D. Cal. 2001).

<sup>232</sup> *Applied Info. Mgmt., Inc.*, 976 F. Supp. at 154.

<sup>233</sup> *Softman Products Co., LLC*, 171 F. Supp. 2d at 1083. See Julie E. Cohen, *Copyright and the Perfect Curve*, 53 VANDERBILT L. REV. 1799, 1809 (2000) ("More important, licensing decisions designed to maximize individual or private welfare may not maximize society's"). Congress enacted fair use rights such as § 107, § 109, and § 117 rights as exceptions to the owners § 106 rights to ensure that copyright owners cannot capture 100% of the consumer surplus so as to leave a guaranteed safe space in which the progress of useful arts and sciences may thrive despite the best efforts of some copyright owners.

<sup>234</sup> *Softman Products Co., LLC*, 171 F. Supp. 2d at 1083 & n. 9 (citing Lemley, *supra* note 18, at 1239) ("Software vendors are attempting en masse to 'opt out' of intellectual property law by drafting license provisions that compel their customers to adhere to more restrictive provisions than copyright law would require.").

Historically, the purpose of "licensing" computer program copy use was to employ contract terms to augment trade secret protection in order to protect against unauthorized copying at a time when, first, the existence of a copyright in computer programs was doubtful, and, later, when the extent to which copyright provided protection was uncertain. Computer program copy use "licensing" continued after federal courts interpreted the Copyright Act to provide substantial protection for computer programs as literary works. In *Step-Saver Data Systems, Inc. v. Wyse Technology*, the Third Circuit examined the historical development of the use of licensing in the software industry and concluded that subsequent changes to the Copyright Act had rendered the need to characterize the transaction as a license "largely anachronistic." 939 F.2d 91, 96 n. 7 (3d Cir. 1991).

*Softman Products Co., LLC*, 171 F. Supp. 2d at 1083. Traditional legal scholarship presumed that the software license grew out an attempt to protect software in an era when the intellectual property rights in software were uncertain. However, Professor Madison demonstrates that the origin of the software license was in an attempt by IBM to unbundle software from hardware in the mainframe market to avoid possible antitrust litigation. IBM needed to maintain control over the "copy" in order to prevent third parties from competing with it in the post-sale service market. See Michael Madison, *Reconstructing the Software License*, \_\_\_\_ LOYOLA UNV. CHICAGO L. J. \_\_\_\_ (2003) (forthcoming).

Congress has already shown some inclination to tamper with state contract laws that frustrate national uniform policies. E-Sign is a good example of this. E-Sign allows states to adopt the Uniform Electronic Transactions Act (UETA) as a safe harbor provision but preempts inconsistent state laws that hinder ecommerce. Of course, neither congress nor the courts need formally create a new body of contract law governing copyrights. This same goal could be accomplished through definition sections that provide adequate instructions on how to apply them and which clearly preempt state laws to the contrary.<sup>235</sup>

One place where federal courts should carefully scrutinize the transaction is in determining whether a transaction is a sale, a lease, or a license. Rather than looking at the language cloaking the transaction, the court must examine the economic realities of the exchange.<sup>236</sup> In the model transaction, the end user gives value in exchange for a tangible copy of the software.<sup>237</sup> The end user selects a software package. She pays for it either in person at the cash register or in the case of a distance transaction by mail or by charge card prior to the software package being delivered. The software package is delivered, and within the packing materials containing the software, there is an envelop with a warning that opening the envelop or breaking a seal constitutes consent to terms printed outside the envelop.

If one escaped the shrinkwrap then one may still be faced with a contract at installation. When the software is first installed a screen pops open with terms that must be agreed to by clicking yes or typing the end user's name before the software will install. At no point before the opening of the software packaging or before installing the software is the end user *clearly informed* of the terms of the contract. *At best* there may be an inconspicuous notice on the outside packaging that a license or important terms are enclosed, so the purchaser is unaware that this transaction purports to be unlike the purchase of a DVD, CD, book, or any other copyrighted content that consumers customarily purchase.<sup>238</sup> To distinguish ownership from a lesser interest, as in a true license, the Court should examine if the contract requires the payer (1) to make periodic payments; (2) to destroy or disable, or to return the copy; or (3) if the copyright owner retains title for the purposes of a security interest,<sup>239</sup> then the copyright holder has transferred to the payer something less than ownership.<sup>240</sup> In contrast, if the transaction involves a single

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<sup>235</sup> Cf. Field, *supra* note 193, 890 (opining that there is no operative difference "between the creation of federal common law and the ordinary interpretation of federal enactments"); George D. Brown, *Letting Statutory Tails Wag Constitutional Dogs--Have The Bivens Dissenters Prevailed?*, 64 IND. L.J. 263, 266 (1988-89) ("all forms of judicial lawmaking by federal courts--whether presented as constitutional adjudication, statutory interpretation or federal common law--are essentially the same and should be placed under the general rubric of federal common law.").

<sup>236</sup> *Microsoft Corp. v. DAK Indus.*, 66 F.3d 1091 (9th Cir. 1995); *United States v. Wise*, 550 F.2d 1180 (9th Cir. 1977); *ICART*, 976 F. Supp. at 154.

<sup>237</sup> The first sale (§109(a)) status of a copy downloaded off the Internet where the fixation takes place on the consumers premises without a corresponding transfer of any medium embodying the copyrighted work is unclear. *See, e.g.*, REPORT OF WORKING GROUP ON INTELLECTUAL PROPERTY RIGHTS OF INFORMATION INFRASTRUCTURE TASK FORCE, INTELLECTUAL PROPERTY RIGHTS AND THE NATIONAL INFORMATION INFRASTRUCTURE 90-95 (Sept. 1995); Justin Graham, *Preserving The Aftermarket In Copyrighted Works: Adapting The First Sale Doctrine To The Emerging Technological Landscape*, 2002 STAN. TECH. L. REV. 14 (2002).

<sup>238</sup> Szwak, *supra* note 174, at 33 ("consumers consider the purchase of software to be that of a product or "good," and not a license.").

<sup>239</sup> *Applied Info. Mgmt., Inc.*, 976 F. Supp. at 154 (citing NIMMER ON COMPUTER TECHNOLOGY § 1.18[1] p. 1-103 (1992); *ProCd v. Zeidenberg*, 908 F. Supp. 640, 651 (W.D. Wisc. 1996), *rev'd on other grounds*, 86 F.3d 1447 (6<sup>th</sup> Cir. 1996).

<sup>240</sup> *Softman Products Co., LLC*, 171 F. Supp. 2d at 1086 ("The pertinent issue is whether, as in a lease, the user may be required to return the copy to the vendor after the expiration of a particular period. If not, the transaction conveyed not only possession, but also transferred ownership of the copy.") (quoting RAYMOND NIMMER ON COMPUTER TECHNOLOGY § 1.18[1] p. 1-103 (1992); *see, e.g.*, Rice, *supra* note 91, at 157).

payment giving the payer possession for an unlimited period, this transaction is a sale, and the payer should be characterized as an owner under both § 109 and § 117.<sup>241</sup> Absent an obligation to return or disable a computer program after a determinable period, the reality of the transaction is that the copyright holder has transferred not only possession but also ownership of a copy.<sup>242</sup> Once the end user possesses the software, she has a perpetual royalty free right to use the software. Clearly here, the model more closely resembles a sale than a license or lease, and a federal common law of contract should reflect the reality of the transaction.

## VII. CONCLUSION

Copyright law is pervasive throughout the modern economy. As copyrighted works became more valuable and easier to copy, there was a gradual shift away from copyright law to contract law to protect the interests of copyright owners. State contract law is inadequate to do so since it may yield different results interpreting the same contract while digital content can and must flow nationally in the stream of commerce in an orderly predictable fashion. In light of 17 U.S.C. § 301 preemption and possible commerce clause preemption, state law is a shaky basis on which to build a private ordering of copyright law. The courts are unsure whether private ordering inconsistent with the default principles of copyright law are preempted or only affirmative public laws by state legislatures are preempted. In addition, federal courts must be released from any obligation to interpret an agreement in the same manner that state's highest court would interpret it and be free to impose some uniform contract law on principles copyright agreements. This new common law of copyright should evolve on a case-by-case basis as technology changes and as new business models are introduced by incorporation. It should draw on commercial experience and practices with the UCC, common law of contracts, and of course, UCITA. If Congress elects to enact a federal body of contract law, this law should be consistent with the goals of the Copyright Act. Individuals should not be permitted to contract around provisions in the laws that are designed to protect the public's interest. In either case, judges should always take care to encourage sound businesses practices while pruning those that frustrate the underlying copyright policies.

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<sup>241</sup>*Id.*

<sup>242</sup>*Softman Products Co., LLC v. Adobe Sys., Inc.*, 171 F. Supp. 2d 1075, 1086 (C.D. Cal. 2001).