Comments Welcome!

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This is a very early draft and so I welcome your comments. My contact information is provided below. I have not added numerous citations, shortened overly-long sections, or thought much about overall organization yet. I would be particularly interested to hear whether additional (or fewer) arguments should be made on certain points or where existing arguments are unclear or unpersuasive. It will also be apparent that the final section on further implications is barely more than an outline and so suggestions for different or additional implications to consider are particularly welcome.

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Why License Agreements Do Not Control Copy Ownership: First Sales and Essential Copies

by Brian W. Carver[1]

The so-called "license versus sale" distinction that arises with respect to copies of software or music will confront the Ninth Circuit in three upcoming cases. In *UMG Recordings, Inc. v. Augusto*, the district court found that, notwithstanding "not for resale" labels, the initial recipients of "promo CDs" owned them and were thus entitled to sell the CDs to others.[2]

In *MDY Indus. LLC v. Blizzard Entm't, Inc.*, the district court held that purchasers of Blizzard's World of Warcraft software are not owners of their copies of the software, and hence are not entitled to a Section 117 defense that would allow the owner of a copy of a computer program to make a copy of the program, provided such copy is created as an essential step in the utilization of the program.[3]

Finally, in *Vernor v. Autodesk, Inc.*, the district court found that the transfer of Autodesk's AutoCAD software[4] to a third-party was a sale, and that Vernor, having acquired AutoCAD from the third-party, could invoke the first sale doctrine in order to resell his copies of AutoCAD on eBay without liability for direct or indirect copyright infringement.[5]

These cases present the Ninth Circuit with multiple opportunities to revisit its decisions in the license versus sale context. The *Vernor* court wrote that these precedents are in irreconcilable conflict, which it could only resolve by following the earliest precedent.[6]

I will argue that the *Augusto* and *Vernor* courts reached the correct outcomes and that the *Blizzard* court erred. The *Augusto* and *Vernor* decisions, through a faithful adherence to precedent, also represent an interpretive breakthrough in an area of law fraught with misguided approaches. By recognizing what is right in these decisions and what has gone so wrong in other cases, we can see not only how to reach the correct

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2 *UMG Recordings, Inc. v. Augusto*, 558 F. Supp. 2d 1055 (C.D. Cal. 2008).
3 *MDY Indus. LLC v. Blizzard Entm't, Inc.*, 89 U.S.P.Q.2d 1015 (D. Ariz. 2008).
4 AutoCAD is a Computer Aided Design (CAD) program.
5 *Vernor v. Autodesk, Inc.*, 555 F. Supp. 2d 1164 (W.D. Wash. 2008).
6 *Vernor*, 555 F. Supp. 2d at 1172.

result in *Blizzard*, but how best to resolve the recurring question of when title to a copy passes to a transferee, giving rise to first sale and § 117 rights.

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II. When Does Title to a Copy Pass to the Transferee?
   A. The Reservation of Title Approach.
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      2. Must recognize the possibility of ownership of a copy independent from ownership of the copyright.
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      1. Must respect Supreme Court precedent and should seek to harmonize Circuit Court precedents.
      2. Should heed the warning of the Supreme Court's recent *Quanta Computer* decision.
   C. Must Respect Congressional Choices.
      1. Must recognize the limiting role played by Sections 107 through 122 and examine whether contrary contractual provisions are federally preempted.
      2. Should preserve as far as possible the national uniformity copyright law seeks.
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      2. Would, ideally, be easy for courts to apply.
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The "license versus sale" issue involves an effort to determine ownership of —or who holds "title" to—a tangible thing, e.g., a CD, CD-Rom, or DVD-Rom.[7] A copyright "license" is a grant of a permission by the holder of a copyright to another of any of the rights of copyright enumerated in 17 U.S.C. § 106, and subject to the limitations in §§ 107 through 122. One can only grant a permission if one validly holds an underlying right, so a copyright "license" must always correspond to an underlying § 106 right. When we speak of a "license to the software" or a "license to use the software" we are speaking imprecisely and, I will argue, setting ourselves up for the confusion that exists in the "license versus sale" context, where courts and litigants speak of "licensing the copy" an invented notion not found in the Copyright Act.[8] When we instead speak (or at least think) precisely and focus on determining title to a tangible CD or DVD-Rom, the right results are fairly self-evident. Common-sense determinations allow one to tell the difference between buying a DVD or renting it. There simply is no coherent third category of "licensing" a tangible thing. The only thing one could have licensed is an underlying right of copyright, and, I will argue, the contours of those permissions are a wholly separate and irrelevant issue to determining ownership of the tangible copy. This conclusion is demanded not merely by common sense, but also because to conclude otherwise ignores the limitations of sections 107 through 122 and frustrates the purposes of Congress in enacting the various limitations and exceptions to copyright. Further, it upsets copyright law's "delicate balance" between the rights of copyright owners and copyright users, and ignores

7 I will address digital files saved to hard drives below, but having handled hard drives, I have found that they are tangible things too. *See Krause v. Titleserv, Inc.*, 402 F.3d 119 (2d Cir. 2005); *Logicom Inclusive, Inc. v. W.P. Stewart & Co.*, 2004 WL 1781009 at 13-14 (S.D.N.Y. 2004); Jane C. Ginsburg, *Putting Cars on the "Information Superhighway": Authors, Exploiters, and Copyright Infringement in Cyberspace*, 95 Colum. L. Rev. 1466, 1475 (1995) ("[R]ights copyright confers will be the same whatever the format of the work, whether originally created in hard copy or in digital format...").

8 Throughout this paper, the word "copy" will be used to refer to the tangible object in which a copyrighted work is fixed. I will use "copy" to include both "copies" under 101 and "phonorecords" under 101, so as to avoid constantly referring to "copies or phonorecords" herein. Note that my concern about the use of the term "license," which I explain in greater detail in section III, *infra*, is not merely a complaint about the double use of "license" as a name for both the intangible permission and as a shorthand for "license agreement." The problem most often arises instead when the one either uses "license" to describe some category of distribution distinct from a sale, other transfer of ownership, rental, lease, or lending, and when one uses "license" in reference to a tangible thing without specifying which intangible right is being licensed, as when the *MDY* court held that Blizzard users were "licensees of the copies." *MDY Indus.*, 89 U.S.P.Q.2d 1015, pincitation.

vital Supreme Court precedent.

This paper will proceed in five parts. Part I provides brief summaries of the three cases in the Ninth Circuit that offer the Court an opportunity to clarify its jurisprudence in this area. Part II asks when title to a copy passes to a transferee, and attempts to classify the various approaches taken by courts and recommended by commentators into a few useful categories.

Part III then critiques the various approaches. I will argue that copyright holders cannot magically transform transactions into "licenses" by labeling them so in a licensing agreement, but I will also articulate an approach in which users sometimes will and sometimes will not have first sale and "essential copy" rights, depending upon easy-to-recognize features of the transactions. Courts are in desperate need of a logical approach to the question of copy ownership that respects precedent and Congressional choices, and which, in an ideal world, would simply make sense, both by being consistent with settled consumer expectations and by being straightforward for the courts to apply. I believe the approach I present, which focuses on whether the transferee has a right of perpetual possession of the copy, will satisfy those criteria. Part IV will then apply the approach I advocate to the *MDY* case to illustrate how that approach, which implements controlling Ninth Circuit precedent, would have reached a contrary result.

In the fifth and final part I will briefly address other implications of the approach I advocate, looking at whether it permits price discrimination, whether it affects the existence of a digital first sale right, whether adopting my approach would incentivize software distributors to adopt a leasing paradigm, whether the increasing use of cloud computing might impact this issue, and the implications for open source licensing schemes.

I. Three Upcoming Ninth Circuit Cases Where Determining Title to the Copy is Essential to a Correct Resolution.

A. *UMG Recordings, Inc. v. Augusto.*

Troy Augusto makes his living selling collectible merchandise on eBay, the internet auction site. UMG's copyright infringement claim against Augusto is based on his offering "promo CDs" for sale on eBay. The 26 eBay auctions at issue involved authentic CDs lawfully made and distributed by UMG.[9]

9 *Augusto*, 558 F. Supp. 2d at 1058.

Augusto purchased the CDs from retailers in the Los Angeles area or on eBay, but UMG argued that Augusto was not an "owner" of the CDs he bought, because the promo CDs contain one of the two following legends:

> Promotional Use Only—Not for Sale.

or

> This CD is the property of the record company and is licensed for the intended recipient for promotional use only. Acceptance of this CD shall constitute an agreement to comply with the terms of the license. Resale or transfer of possession is not allowed and may be punishable under federal and state laws.[10]

Promo CDs are mailed unsolicited to recipients, typically "music industry insiders who are in a position to provide publicity and exposure" for the CD. UMG has never made any efforts to retrieve promo CDs from recipients, nor does anything on the packaging of promo CDs indicate that they must ever be returned to UMG. UMG does not keep permanent records of who received any particular promo CD, and UMG does not take any steps to mark the promo CDs for later tracking. The district court considered all of these "economic realities," and concluded that "title to the CDs is transferred to the insiders."[11] An authorized disposition of the CDs having occurred, the district court held that UMG's publication right was exhausted, freeing both the recipients of the CDs as well as Augusto to sell them. UMG has appealed to the Ninth Circuit.[12]

B. *MDY Indus. LLC v. Blizzard Entm't, Inc.*

Blizzard distributes copies of World of Warcraft ("WoW"), a multiplayer online game, at most software and video game retailers for a one-time fee.[13] Players also pay a monthly fee for online access.[14] MDY sold "Glider" a

10 Appellee's Brief at 13-14.

11 *Augusto*, 558 F. Supp. 2d at 1062.

12 *UMG Recordings, Inc. v. Augusto*, No. 08-55998 (9th Cir.) (pending).

13 World of Warcraft: Wrath of the Lich King, was available from http://www.bestbuy.com for $39.99 on July 10, 2009. Note that Blizzard's "Quick Start Guide" describing a downloadable 10-day free trial says, "You may upgrade your account at any time to a full version by *purchasing* a retail copy of the game at most software and video game retailers." Blizzard Entm't Inc., *World of Warcraft :: Quick Start Guide*, *available at* https://signup.worldofwarcraft.com/trial/qs5.html (last visited Jun. 30, 2009) (emphasis added).

14 Available in most countries are a month-to-month package at $14.99 per month, a three-month plan at $13.99 per month, and a six-month plan at $12.99 per month. The subscription fees for the three-month plan and the six-month plan must be paid

software program called a "bot" that automated play of WoW. WoW is governed by a EULA and TOU that players must agree to before playing. These agreements forbid, among other things, the use of bots.[15] Blizzard alleged that users of WoW are licensees who are permitted to copy the copyrighted game client software only in conformance with the EULA and TOU, and that when users launch WoW using Glider, they exceed the license in the EULA and TOU and create infringing copies of the game client software. Thus, in Blizzard's view, its customers, not MDY, are the *direct* infringers. Blizzard alleged that MDY was liable for contributory copyright infringement because MDY materially contributed to this direct infringement by Glider users. MDY allegedly did so by developing and selling Glider with the knowledge that Glider users would create infringing copies. Blizzard also alleged that MDY was liable for vicarious copyright infringement because MDY had the ability to stop the Glider-caused infringing activity and derived a financial benefit from that activity.

MDY argued that it was not liable for contributory or vicarious copyright infringement because Glider users do not infringe Blizzard's copyright. If Glider users violate terms of the EULA and TOU, MDY argued, they are merely breaching a contract, not infringing a copyright. MDY also asserted a copyright misuse defense and an ownership defense under 17 U.S.C. § 117.

1. Are users of Glider liable for direct copyright infringement?

Nothing about Glider enables copying of the software that was not already possible. Instead Blizzard's theory is that Glider users make a copy of the software in RAM when they run WoW and that RAM copy is only permissible if the EULA and TOU are followed. But, the EULA and TOU are violated by Glider users, because those agreements forbid the use of bots. Under Blizzard's view, if the EULA/TOU are violated, then any use of WoW (that creates a RAM copy)–even by the individual that purchased it—is an unauthorized infringement.

2. The Section 117 defense.

Under 17 U.S.C. § 117, the owner of a copy of a computer program can

in full at the beginning of the period. Blizzard Entm't Inc., *WoW → Info → F.A.Q. → General, available at* http://www.worldofwarcraft.com/info/faq/general.html (last visited Jul. 10, 2009).

15 Arguably the restriction violated is one on not using unapproved third-party interfaces to the games. [more]

make a copy of that computer program provided such copy is created as an essential step in the utilization of the computer program:

> Notwithstanding the provisions of section 106, it is not infringement for the owner of a copy of a computer program to make or authorize the making of another copy or adaption of that computer program provided[] that such a new copy or adaption is created as an essential step in the utilization of the computer program[.] [16]

The district court turned to the following question: Is a purchaser of WoW an "owner" of his copy of the software?

The court applied what it named the "*Wall Data* test" to determine that purchasers of WoW are not owners of their copies of the software.[17] While the *Wall Data* court does not explicitly state a "test," the *MDY* court looked at the following factors in deciding that purchasers of WoW do not own their copies of the software: First, the EULA accompanying the software expressly states that "[a]ll title, ownership rights, and intellectual property rights in and to the Game and all copies thereof... are owned or licensed by Blizzard."[18]

Second, the *MDY* court looked to restrictions on the transfer and use of the software. According to the EULA, "The user may transfer his “rights and obligations” under the EULA only by transferring the original media containing the game client software along with all original packaging and all manuals or other documentation distributed with the software; the user must delete all copies and installations of the software from his computer; and the recipient of the software must agree to the terms of the EULA. "[19] Additionally, the court noted that the TOU places additional restrictions on the use of the software, restrictions that it felt were at least as severe as the restrictions in *Wall Data*.[20]

The Court concluded, therefore, that users of WoW, including those who use Glider, were "licensees of the copies of the game client software" and were not entitled to the section 117 defense.[21]

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16 17 U.S.C. § 117(a)(1).

17 *MDY Indus. LLC v. Blizzard Entm't, Inc.*, 89 U.S.P.Q.2d 1015, pincitation (D. Ariz. 2008).

18 *MDY Indus.*, 89 U.S.P.Q.2d 1015, pincitation.

19 *MDY Indus.*, 89 U.S.P.Q.2d 1015, pincitation.

20 *MDY Indus.*, 89 U.S.P.Q.2d 1015, pincitation.

21 *MDY Indus.*, 89 U.S.P.Q.2d 1015, pincitation. As discussed in Section III, I think the

Without a section 117 right to make essential copies, the court found that end users needed a license to make RAM copies of the software while playing it, and as Glider users were violating the EULA and TOU by using a bot, the court essentially adopted Blizzard's view, that in such circumstances, any use of WoW (that creates a RAM copy) is outside the scope of the EULA/TOU and hence is unauthorized infringement. Having established then that Glider users are *direct* infringers, the court concluded without commentary that MDY was liable for contributory copyright infringement, presumably because MDY materially contributed to the direct infringement by Glider users.

C. *Vernor v. Autodesk, Inc.*

Autodesk's software is accompanied by agreements which purport to prohibit the transfer of the software without Autodesk's written permission. Vernor acquired Autodesk products from third parties (such as "CTA") and resold them on eBay. Vernor was not a direct purchaser of Autodesk's software.

In reviewing the precedents, particularly the Ninth Circuit's decision in *United States v. Wise*,[22] the *Vernor* court found that "the critical factor is whether the transferee kept the copy acquired from the copyright holder."[23]

The *Vernor* court thus held that the transfer of AutoCAD packages from Autodesk to CTA was a sale. In the context of § 117, the court noted that *MAI*, *Triad*, and *Wall Data* involved restrictions in the respective license agreements that were sufficient to find that title to the copies remained with the transferor. However, *Wise* directly addressed § 109 and involved harsher license restrictions than those in *Wall Data* but which were insufficient to prove the absence of a first sale. The *Vernor* court found these precedents to be in irreconcilable conflict, and with *Wise* as the earlier of the conflicting precedents, it was followed. The court then held that Vernor could invoke the first sale doctrine, and his resale of the AutoCAD packages was neither direct nor indirect copyright infringement.[24] The court's decision here came on a motion to dismiss, and as of this writing, Autodesk has not appealed that ruling, but if the court

inherent ambiguity in "licensees of the copies" is likely to lead to confusion.

22 *United States v. Wise*, citation.

23 *Vernor v. Autodesk, Inc.*, 555 F. Supp. 2d 1164, pincitation (W.D. Wash. 2008).

24 The court also held that Autodesk had not established that its agreement bound Vernor or his customers. [cite]

reaches a substantially similar ruling on a pending motion for summary judgment, then, barring intervening unfavorable precedent in the Ninth Circuit, I expect Autodesk will appeal.

II. When Does Title to a Copy Pass to the Transferee?

This section describes various approaches courts and commentators have adopted to answering the question of when title to the copy passes to the transferee. This section will focus on exposition of the approaches, and I will largely hold my critiques of these approaches until the next section.

The various approaches used by courts to address this question are difficult to categorize precisely and often reflect a mixture of several identifiable approaches. However, I believe it can be useful to roughly categorize the approaches as follows:

On one extreme are courts that focus almost exclusively on whether the copyright holder purports to reserve title in the copies through an accompanying agreement. For these courts, a mere recitation by the copyright holder of a few magic words is sufficient to make virtually all other features of the transaction irrelevant. I will refer to this approach as the Reservation of Title approach.

Slightly less extreme are those courts that may look to a reservation of title first, or as one of several factors, in determining ownership of a copy, but which overall take the approach that the agreement controls and it must be examined to determine ownership of copies. I will refer to this approach as the Agreement Controls approach.

Other courts explicitly note that the mere words recited by the agreement do not govern the determination of ownership of a copy, but instead these courts look to the substance of the transaction, and consider what they often call the "economic realities" of the transaction. I will thus refer to this approach as the Economic Realities approach. The factors considered can include terms of the agreement not related to copyright permissions, but also facts about the transaction or its consequences not discussed in the agreement at all.

The Second Circuit in *Krause v. Titleserv, Inc.*[25] pushed the Economic Realities approach further than most by holding that formal title is not even

25 *Krause v. Titleserv, Inc.*, 402 F.3d 119 (2d Cir. 2005).

a necessary condition for being an "owner" under § 117, and held that courts must look holistically at the "incidents of ownership." I will include *Krause* under the Economic Realities banner.

Finally, the *Augusto* and *Vernor* courts do more to sort through this sea of confusion than most and perceptively push the Economic Realities approach a step further, until it becomes what I call the Perpetual Possession approach. These courts accomplished this not by ignoring precedent, but by following it more faithfully and by understanding what was important in earlier cases addressing this issue.

After explaining each of these approaches in this section, I will argue in the following section that the Perpetual Possession approach provides the most appropriate framework for addressing this oft-discussed, but little-understood issue.

The need for greater clarity here has already been noted by the *Vernor* court's finding that the Ninth Circuit precedent on this issue is in "irreconcilable conflict" a fact that does not even address the difficulties of reconciling the precedents on this issue across all federal courts. However, the interpretive problem is perhaps best illustrated by the three *Adobe* cases I will discuss below. Two judges, in different district courts, but both within the Ninth Circuit, addressed these three cases in 2000, 2001, and 2002. No intervening mandatory precedent occurred during this time, and the cases involved the same plaintiff attempting to enforce very similar licenses, but the court in the second case took a different approach from the first and explicitly refused to adopt the reasoning of the first. Then in the third case, which happened to be decided by the same judge as the first, the court reviewed the second *Adobe* case and refused to see the matter differently than it had before. So both courts, even when clearly cognizant of another's differing point of view, were unable to interpret the same precedent consistently with one another. When the same plaintiff, seeking to enforce essentially the same right over the same three year time period gets different results depending on whether it files its case in Northern or Central California, there is a pressing need for clarification.

A. The Reservation of Title Approach.

> "Far too often, courts merely accept plaintiff's description of the transaction as a license." William Patry.

Like the Agreement Controls approach discussed next, those courts that adopt a Reservation of Title approach are looking to the agreement between the parties for guidance, but these courts take it to an extreme by being satisfied with the slimmest of facts favoring the copyright holder. If the copyright holder simply makes the assertion that they "license their software" and do not "sell" it, then these courts are inclined to conclude that no transfer of title has occurred. This might be thought of as a sub-variety of the Reservation of Title approach, which could be dubbed the "Magic Words" approach, because for these courts it is as if merely saying the magic words "we license not sell" puts an end to the inquiry. Other courts in this category delve slightly deeper and look for specific language in the agreement reserving title in the copies to the copyright holder, and if such language is found, place all or almost all of the weight on this factor, and find no transfer of title.

1. The "Magic Words" Cases: *MAI Sys. Corp. v. Peak Computer* and *Microsoft Corp. v. Harmony Computers and Elecs.*

A cursory, unsupported footnote, consisting of a single declarative sentence, in the Ninth Circuit's *MAI Sys. Corp. v. Peak Computer* opinion has done more damage to the appropriate development of the law with respect to the question of when title to a copy passes to a transferee than perhaps anything else. The court's entire analysis of the issue of copy ownership occurs in the following sentence: "Since MAI licensed its software, the Peak customers do not qualify as "owners" of the software and are not eligible for protection under § 117. "[26] The court's conclusory pronouncement on this topic has been widely criticized by both leading commentators[27] and the Court of Appeals for the Federal Circuit,[28] a fact recognized by the Ninth Circuit itself in a subsequent opinion.[29] The main fault articulated is that *MAI's* statement fails to pay heed to 17 U.S.C. § 202, by conflating the intangible copyright with the tangible copy, and thus fails to recognize that a licensee of one of the rights of copyright might also be an owner of a particular copy.[30] Notably, the Ninth Circuit, in this footnote, cites to no statute or precedent providing for this supposed distinction between licensees and owners of a copy. The damage has been so extensive because this opinion, from 1993, represented only the second time a

26 *MAI Sys. Corp. v. Peak Computer*, 991 F.2d 511, 519 fn 5 (9th Cir. 1993).
27 2 Melville B. Nimmer, *Nimmer on Copyright* 8.08[B][1][c].
28 *DSC Commc'ns. Corp. v. Pulse Commc'ns., Inc.*, 170 F.3d 1354, 1360 (Fed. Cir. 1999).
29 *Wall Data Inc. v. L.A. County Sheriff's Dep't*, 447 F.3d 769, 786 fn 9 (9th Cir. 2006).
30 *See* Nimmer, *supra* note ## and *DSC Commc'ns*, *supra* note ##.

Circuit Court had addressed the question in the software context,[31] and thus it has been cited and followed by numerous subsequent courts.[32]

In the following year, 1994, another early opinion in *Microsoft Corp. v. Harmony Computers and Elecs., Inc.*, furthered the unfortunate trend of short statements that fail to carefully distinguish between copyrights and copies, when it wrote, "Entering a license agreement is not a "sale" for purposes of the first sale doctrine."[33] As we will see, whether there is a "sale for purposes of the first sale doctrine" involves ownership of a particular copy, something that is completely consistent with "entering a license agreement." This statement by the court is particularly unfortunate since it appears that the defendant was selling counterfeit copies[34] and since such copies are not "lawfully made"[35] the first sale doctrine would not apply for that more fundamental reason. However, the court was ruling on a preliminary injunction within the first weeks of the case and, at that time, had not had an evidentiary hearing to make a finding on the genuineness of the products sold by defendants.[36] However, even more time might not have changed this court's approach, as the court expresses in one passage the sense that it would be satisfied with mere declarations from Microsoft and its counsel that it "licenses" and does not sell its software.[37]

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31 The issue was first addressed in the software context by a Circuit Court in *S.O.S., Inc. v. Payday, Inc.*, 886 F.2d 1081, 1088 (9th Cir. 1989), discussed *infra*.

32 *Triad* (not discussing here because the court merely erroneously assumes without discussion that there is a insuperable distinction between licensees and owners of copies); [more].

33 *Microsoft Corp. v. Harmony Computers & Elecs.*, 846 F. Supp. 208, 213 (E.D.N.Y. 1994).

34 *Harmony Computers & Elecs.*, 846 F. Supp. at 212.

35 17 U.S.C. § 109(a).

36 *Harmony Computers & Elecs.*, 846 F. Supp. at 212. Microsoft made an *ex parte* application for seizure of the allegedly counterfeit product on January 12, 1994 and the court's ruling here was issued February 7, 1994, just twenty-six days later.

37 *Harmony Computers & Elecs., Inc.*, 846 F. Supp. at 213 ("Plaintiff's counsel declares that Microsoft only licenses and does not sell its Products, (Brokate Supplemental Decl. at 2). Entering a license agreement is not a "sale" for purposes of the first sale doctrine. *ISC-Bunker Ramo Corp.*, 756 F. Supp. at 1331. Moreover, the only chain of distribution that Microsoft authorizes is one in which all possessors of Microsoft Products have only a license to use, rather than actual ownership of the Products. (Brokate Second Supplemental Decl. at 5).") The court also looks to the fact that Microsoft "established a. course of conduct... consistent with an intention to retain all the rights associated with the grant of copyright" of the Microsoft Products." *Id.* By focusing here on the rights of copyright, the court conflates the intangible copyright with the tangible copy. Also, the case cited to, *ISC-Bunker Ramo Corp. v. Altech, Inc.*, 765 F. Supp. 1310 (N.D. Ill. 1990), contains no analysis of the copy ownership issue and simply concludes, "[G]iven the substantial evidence that ISC only licensed and did

2. The Honorable James Ware's *Adobe* Opinions.

Two cases in the District Court for the Northern District of California involving the same plaintiff, Adobe Systems, Inc., addressed ownership of copies and both were decided by the Honorable James Ware.[38] Adobe's case against One Stop Micro was decided in 2000 and its case against Stargate Software in 2002. In both cases, Judge Ware seeks to "give effect to the mutual intent of the parties"[39] by looking "exclusively"[40] at the language of the contract, assuming the language is 'clear and explicit'."[41] If there is ambiguity, then the court may look to custom and usage of words in the trade.[42]

In *One Stop Micro*, the contract, known as the "On Campus Reseller Agreement" or "OCRA", contained restrictions on resellers such as requirements that they not distribute outside their own country and that they take specified steps to ensure that educational purchasers were bona

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not sell its copyrighted software, the first sale doctrine has no application to Altech as a matter of law." *Id.* at 1331. Exactly what the "substantial evidence" was is unclear from that court's discussion. Another case that simply follows *Harmony* without analysis, is *Microsoft Corp. v. Software Wholesale Club, Inc.*, 129 F. Supp. 2d 995, 1002 (S.D. Tex. 2000) ("If the copyright owner licenses, rather than sells, the copyrighted work, the first-sale doctrine may not apply. (citing *Harmony*)."). *See also Davidson & Assocs. v. Internet Gateway*, 334 F. Supp. 2d 1164, 1177 (E.D. Mo. 2004) ("The Court finds the EULAs and TOU are enforceable under the UCC. First, the defendants did not purchase the Blizzard software, rather they purchased a license for the software. A sale consists in the passing of title from the seller to the buyer. Mo. Rev. Stat. § 400.2-106(1) (2000). When defendants purchased the games, they bought a license to use the software, but did not buy the software... The EULAs and TOU in this case explicitly state that title and ownership of the games and Battle.net remain with Blizzard. Defendants do not produce sufficient evidence demonstrating that title and ownership of the games passed to them."), *aff'd* 422 F.3d 630 (8th Cir. 2005). This court also conflates the intangible copyright with the tangible copy, equivocating on the use of the word "software." Reserving title to "the games" or to "Battle.net" is not the same thing as reserving title to the tangible medium in which the game is embodied.

38 *Adobe Sys., Inc. v. One Stop Micro, Inc.,* 84 F. Supp. 2d 1086 (N.D. Cal. 2000); *Adobe Sys., Inc. v. Stargate Software Inc.*, 216 F. Supp.2d 1051 (N.D. Cal. 2002).

39 *One Stop Micro*, 84 F. Supp. 2d at 1090.

40 *One Stop Micro*, 84 F. Supp. 2d at 1090.

41 *One Stop Micro*, 84 F. Supp. 2d at 1090; *Stargate Software Inc.*, 216 F. Supp.2d at 1055-56 ("The determination of ownership in turn is based primarily on an examination of the OCRA, the agreement between Adobe and its distributors. The Court looks to the language, content, and intent of the OCRA, in determining whether its terms affect a sale or license of the software.").

42 *One Stop Micro*, 84 F. Supp. 2d at 1090.

fide members of an educational institution.[43] The court wrote, "These numerous restrictions imposed by Adobe indicate a license rather than a sale because they undeniably interfere with the reseller's ability to further distribute the software."[44]

However, finding some sales terminology in the agreement, the court felt the agreement was ambiguous and consulted extrinsic evidence in the form of declarations from individuals familiar with the software industry who largely, and uncritically, reported that industry practice is for software to be "licensed" and not "sold."[45] This allowed the court to conclude "that based upon the undisputed evidence submitted by Adobe regarding the intent of the parties in entering into the agreement, trade usage, the unique nature of distributing software, as well as the express restrictive language of the contract, the OCRA is a licensing agreement. Thus, contrary to One Stop's assertions, the OCRA does not represent a first sale between the reseller and Adobe."[46]

In *Stargate Software*, Judge Ware draws repeated comparisons to his earlier decision in *One Stop Micro*, and finds that, "[s]imilar to the OCRA at issue in *One Stop*, the OCRA in this case contains multiple restrictions that limit the reseller's ability to distribute Adobe's software."[47] However, in the intervening year, the Honorable Dean D. Pregerson in the District Court for the Central District of California had decided another Adobe case, *Softman Products Co.*, and had found that the transaction there had resulted in a sale of the copy giving rise to a first sale defense.[48]

In an effort to distinguish *Stargate Software* from *Softman Products*, Judge Ware writes,[49]

43 *One Stop Micro*, 84 F. Supp. 2d at 1091 fn 2.

44 *One Stop Micro*, 84 F. Supp. 2d at 1091.

45 *One Stop Micro*, 84 F. Supp. 2d at 1091-92. Most of these declarations conflate the intangible copyright with the tangible copy and so are of no benefit.

46 *One Stop Micro*, 84 F. Supp. 2d at 1092.

47 *Stargate Software*, 216 F. Supp. 2d at 1057.

48 *Softman Products Co. v. Adobe Sys. Inc.*, 171 F. Supp.2d 1075 (C.D. Cal. 2001).

49 The two paragraphs prior to these quoted also attempt to distinguish *Softman Products*, but fail. The court first notes that *Softman Products* involved unbundling of a collection of software in apparent violation of a EULA, whereas *Stargate Software* involved the simple re-distribution of Adobe software, as is. While this is a cognizable distinction, the court fails to explain how that distinction would entail that Softman Products' transaction resulted in a sale, while Stargate Software's was not a sale. The court then notes that when "payment is made for a particular copy of software, the payment is being made for the value of the objective code that is burned on the CD-ROM," but fails to explain how this differs from the situation in *Softman Products,*

> This Court notes that software is unique from other forms of copyrighted information. Technology and software, in particular, has radically transformed the way information is created and exchanged. Software fundamentally differs from more traditional forms of medium, such as print or phonographic materials, in that software can be both, more readily and easily copied on a mass scale in an extraordinarily short amount of time and relatively inexpensively. One of the primary advantages of software, its ability to record, concentrate and convey information with unprecedented ease and speed, makes it extraordinarily vulnerable to illegal copying and piracy. This Court finds that it is important to acknowledge these special characteristics of the software industry and provide enhanced copyright protection for its inventors and developers.
>
> Lastly, as a matter of general principle, this Court finds that no colorable reason exists in this case as to why Adobe and its distributors should be barred from characterizing the transaction that has been forged between them as a license. In light of the restrictions on title that have been incorporated into the OCRA, as well as the Parties' free and willing consent to enter into and execute its terms, the Parties should be free to negotiate and/ or set a price for the product being exchanged, as well as set the terms by which the product is exchanged. (citation). Fundamental to any free society is the liberty of its members to formulate contracts in accordance with the terms that they agree and consent to mutually execute. "The right to contract freely with the expectation that the contract shall endure according to its terms is as fundamental to the society as the right to write and to speak without restraint." (citation). While exceptions are made in the case of unfair or exploitive contracts, or where an inequitable end results as a result of the agreement, commercial parties are generally free to contract as they desire. (citation).[50]

Arguably, this passage best captures the Reservation of Title approach, because across numerous cases it does appear motivated by a combination of software exceptionalism and a fervent belief in a nearly unfettered

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which also involved software burned on CD-ROMs whose true economic value was derived from that which was embodied within it.

50 *Stargate Software*, 216 F. Supp. 2d at 1059. None of the citations were to controlling precedent.

freedom to contract.[51] Adobe's efforts to control the sale of its software to educational customers was an effort to engage in price discrimination, something that this court saw no reason to obstruct. However, in interpreting the first sale doctrine, the Supreme Court of the United States has written, "[W]hether or not we think it would be wise policy to provide statutory protection for such price discrimination is not a matter that is relevant to our duty to interpret the text of the Copyright Act."[52] As will be discussed in the next section, the Reservation of Title approach over-relies on the terms of the agreement, without giving adequate consideration to controlling Supreme Court precedents that require instead a focus on other factors.[53]

3. *Wall Data Inc. v. L.A. County Sheriff's Dep't.* and *S.O.S. Inc. v. Payday, Inc.*

Two additional Ninth Circuit opinions appear to adopt this approach in an uncritical manner, *Wall Data Inc. v. L.A. County Sheriff's Dep't.*[54] and *S.O.S. Inc. v. Payday, Inc.*[55] In a passage where the *Wall Data* court had been discussing *MAI Sys. Corp. v. Peak Computer*, the court writes, "Generally, if the copyright owner makes it clear that she or he is granting only a license

51 It is, however, disconcerting that this policy argument based upon differences between software and other copyrighted works should come from the judiciary rather than the legislature. If Congress wishes to recognize a special protection for software distributors it has proven able to do so. *See* The Computer Software Rental Amendments Act of 1990, Pub.L. No. 101-650, 104 Stat. 5134, codified at 17 U.S.C.. § 109(b); *Sony Corp. of Am. v. Univ. City Studios, Inc.*, 464 U.S. 417, 430-431 (1984) ("From its beginning, the law of copyright has developed in response to significant changes in technology. Indeed, it was the invention of a new form of copying equipment – the printing press – that gave rise to the original need for copyright protection. Repeatedly, as new developments have occurred in this country, it has been the Congress that has fashioned the new rules that new technology made necessary.") (footnotes omitted). In the absence of such a Congressionally-authorized distinction, the courts should interpret the relevant copyright statutes as written.

52 *Quality King Distribs. v. L'Anza Research Int'l*, 523 U.S. 135, 153 (1998).

53 I agree with William Patry's comments on *One Stop Micro*. Patry writes, "the court misinterpreted contractual restrictions as indicating the existence of a license agreement for section 109 purposes. Restrictions on the terms of a sale do not by themselves mean a sale has not occurred. If such restrictions are violated, the contract may have been breached, but a sale took place nevertheless and thus no infringement action is available. For example, nothing in plaintiff's agreements gave it a right to call back the copies in the event of a breach. Adobe is, therefore, wrongly decided on the copyright claim. Far too often, courts merely accept plaintiff's description of the transaction as a license." [cite Patry on Copyright]

54 *Wall Data Inc. v. L.A. County Sheriff's Dep't*, 447 F.3d 769 (9th Cir. 2006).

55 *S.O.S. Inc. v. Payday, Inc.*, 886 F.2d 1081 (9th Cir. 1989).

to the copy of software and imposes significant restrictions on the purchaser's ability to redistribute or transfer that copy, the purchaser is considered a licensee, not an owner, of the software."[56] To the extent *Wall Data* was relying on *MAI*, it has already been noted that the Ninth Circuit in *MAI* cited to no statute or precedent to support its single footnote that addressed ownership of copies and the *Wall Data* court here adds no such citations.[57] Thus, the approach just articulated has no obvious precedential basis.

However, the chief importance of *Wall Data* in a discussion of when title to a copy transfers is in understanding that the *Wall Data* court went out of its way to indicate that "a more fundamental reason" for its § 117 decision there lay in the fact that the Sheriff's Department's actions would not constitute an "essential step" as required by § 117,[58] so whether the Department owned its copies or not was not the fundamental basis of the Court's decision.[59] For that reason, *Wall Data* should not be treated as a controlling precedent on the issue of when title to a copy passes to a transferee, and should not guide district courts squarely facing that question.[60]

Perhaps more importantly, I will explain later in this section that the controlling precedent in the Ninth Circuit on this issue was to be found in two opinions never cited in the *Wall Data* opinion.[61] Other Circuits have

56 *Wall Data Inc. v. L.A. County Sheriff's Dep't*, 447 F.3d 769, pincitation (9th Cir. 2006).

57 *Wall Data* does cite, in a footnote, to *One Stop Micro* in order to quote some of the declarations of members of the software industry, but this is neither statute, nor controlling precedent.

58 17 U.S.C. § 117.

59 *Wall Data Inc. v. L.A. County Sheriff's Dep't*, 447 F.3d 769, 786 fn 9 (9th Cir. 2006).

60 The result might be different if the two rationales in *Wall Data* were "alternate" holdings both equally supporting its decision, but the Court itself chose to describe the "essential step" holding as "more fundamental." The limitation of § 117(a)(1) applies to i) owners of a copy that make another copy ii) created as an essential step, iii) that is used in no other manner. Since the statute treats all these requirements equally, the court should be interpreted to have rested its ruling solely on the "essential step" issue because there is nothing inherently or statutorily "more fundamental" about that requirement. Thus, for the court to use such language should be taken to indicate its determination of the basis of its ruling. Further, as already indicated, on the "owner" issue the *Wall Data* court merely cites to *MAI*, which provided a single footnote which cited to nothing, and so deserves less deference than the earlier *DAK Indus.* or *Wise* decisions which provided far more guidance on how to make the ownership determination. It is unfortunate that the *Wall Data* court failed to cite or discuss those two cases, as then it could have helped to clarify this troublesome area of law.

61 *United States v. Wise*, 550 F.2d 1180 (9th Cir. 1977) and *Microsoft Corp. v. DAK Indus.*,

adopted a "rule of orderliness" that when two panel opinions are like "ships passing in the night" and a subsequent panel reaches a contrary result "the later opinion is a nullity; any other rule would invite judicial chaos."[62] Therefore, *Wall Data* should be treated as a nullity with respect to interpreting when title to a copy passes to a transferee.

In *S.O.S. Inc. v. Payday, Inc.*, the Ninth Circuit appeared to be satisfied with any statement that might reserve title in the copy. In this case, the transferee merely rented the computer on which the disputed copy of software resided and the Ninth Circuit wrote,

> The literal language of the parties' contract provides that S.O.S. retains "*all* rights of ownership." (Emphasis added.) This language plainly encompasses not only copyright ownership, but also ownership of any copies of the software. Payday has not demonstrated that it acquired any more than the right to possess a copy of the software for the purpose of producing "product" for its customers.[63]

However, the court here also repeatedly notes that Payday was to lease the computers on which the software at issue ran, and that these computers would even reside in a third-party accountant's office, and thus the parties initially may not have even contemplated that Payday would ever possess a copy of the software.[64] Thus, while the language used by the court here appears to be a strong statement of a Reservation of Title approach, the rationale behind the court's decision here may be more nuanced. When evaluating the contract, as a whole, the court saw a leasing arrangement that applied not only to the computer hardware, but to the individual copies of the software as well.

The approach I will advocate for here does not seek to disturb the fact that a true lease should be treated as a lease that does not give rise to § 109 or

66 F.3d 1091 (9th Cir. 1995).

62 "[O]ur rule of orderliness comes into play when two panels become "ships passing in the night." A subsequent panel may be unaware of an earlier holding and, consequently, may reach a contrary result. No interpretation is involved, as the later panel makes no mention of the earlier case. In such an instance, we can easily say that the later opinion is a nullity; any other rule would invite judicial chaos." *Grabowski v. Jackson County Pub. Defenders Office*, 47 F.3d 1386, 1400 (5th Cir. 1995) (Smith, J, concurring in part and dissenting in part); *Recursion Software, Inc. v. Interactive Intelligence, Inc.*, 425 F. Supp. 2d 756, 777 (N.D. Tex. 2006).

63 *S.O.S. Inc. v. Payday, Inc.*, 886 F.2d 1081, 1087 (9th Cir. 1989).

64 *Payday, Inc.*, 886 F.2d 1081, pincitation.

§ 117 rights. I believe that is what we find in this case, and so while the court reaches the correct result, its rationale when faced with these facts, and especially the way it chose to phrase that rationale, make this case less useful in guiding courts trying to determine whether an agreement denominated a "license" actually provides for the sale of copies.[65]

In summary, the Reservation of Title approach largely looks to the agreement accompanying the copy, focusing especially on whether the copyright holder makes any claim to reserve title in the copies delivered to the transferee. Too often courts adopting this approach rely solely on the word "license" as if the mere incantation of that word puts an end to the inquiry. Other courts rightly dig deeper.

B. The Agreement Controls Approach.

"The terms of the contract control." Raymond T. Nimmer (2006).

Some courts and commentators have explicitly or impliedly adopted a view that the agreement that accompanies a copy of a copyrighted work completely controls whether title to the tangible thing passes to the recipient or remains with the copyright holder. On this view, one looks to the four corners of the agreement and nowhere else to determine if the possessor of a copy of a copyrighted work is also the owner of that copy.

For example, Raymond T. Nimmer has written, "[S]ince Section 117 does not delineate when a person becomes an owner of a copy of a computer program, whether ownership is transferred will be determined in light of and controlled by the agreement of the parties. The terms of the contract control."[66] He buttresses this view, with the further proviso that where an agreement is silent on copy ownership, "courts should look to the context of the transaction, including any established industry practice of licensing rather than selling copies."[67]

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65 That the *S.O.S.* court failed to cite to *Wise* also weakened its discussion of the sorts of factors one should consider when determining title to a copy.

66 Raymond T. Nimmer, The Law of Computer Technology 1:115 (2006).

67 *Id.*; Raymond T. Nimmer's view has developed over the years, as several courts quote earlier versions of his text for different views. For instance, we find, "Ownership of a copy should be determined based on the actual character, rather than the label, of the transaction by which the user obtained possession. Merely labeling a transaction as a lease or license does not control. If a transaction involves a single payment giving the buyer an unlimited period in which it has a right to possession, the transaction is a sale. In this situation, the buyer owns the copy regardless of the label the parties use for the contract. Course of dealing and trade usage may be relevant, since they

When courts adopt this view, it often takes the form of evaluating the terms of the agreement to determine what restrictions are placed on the copyright license granted to the recipient. I will explain in the next section why such an approach is misguided. First, I review some examples of this approach in particular cases.

1. *DSC Commc'ns Corp. v. Pulse Commc'ns, Inc.*

In *DSC Commc'ns Corp. v. Pulse Commc'ns, Inc.*,[68] the Federal Circuit wrote,

> Plainly, a party who purchases copies of software from the copyright owner can hold a license under a copyright while still being an "owner" of a copy of the copyrighted software for purposes of section 117. We therefore do not adopt the Ninth Circuit's characterization of all licensees as non-owners. Nonetheless, the *MAI* case is instructive, because the agreement between MAI and Peak, like the agreements at issue in this case, imposed more severe restrictions on Peak's rights with respect to the software than would be imposed on a party who owned copies of software subject only to the rights of the copyright holder under the Copyright Act. And for that reason, it was proper to hold that Peak was not an "owner" of copies of the

establish the expectations and intent of the parties. 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. Raymond Nimmer, The Law of Computer Technology § 1.18[1] p. 1-103 (1992)." *Applied Info. Mgmt. v. Icart*, 976 F. Supp. 149, 154 (E.D.N.Y. 1997); *DSC Commc'ns Corp. v. Pulse Commc'ns, Inc.*, 170 F.3d 1354, 1362 (Fed. Cir. 1999) ("One commentator has argued that when a copy of a software program is transferred for a single payment and for an unlimited term, the transferee should be considered an "owner" of the copy of the software program regardless of other restrictions on his use of the software. See Raymond T. Nimmer, The Law of Computer Technology P 1.24[1], at 1-143 to 1-144 (3d ed. 1997)."). I have been unable to find such language in the 2006 edition, and as a "looseleaf" treatise whose pages are updated and often discarded, it is difficult to trace the development of Prof. Raymond T. Nimmer's evolving view, but the 2006 edition contains numerous statements that suggest a Reservation of Title approach that is implied from an Agreement Controls approach. *See* Law of Computer Technology 1:115 at 1-302 (2006) ("[I]f the terms of a license provide that ownership of the copy and the copyright remain in the copyright owner, the provisions preclude transfer of title to the copy of the licensee."). Prof. Raymond T. Nimmer has been retained as Autodesk's expert in the *Vernor* case. *See Vernor v. Autodesk, Inc.*, No. 07-01189, Docket Nos. 52 and 60 (W.D. Wash.).

68 *DSC Commc'ns Corp. v. Pulse Commc'ns, Inc.*, 170 F.3d 1354 (Fed. Cir. 1999).

copyrighted software for purposes of section 117.[69]

Here, the Federal Circuit has avoided conflating the intangible copyright with the tangible copy and appears focused on the correct issue. However, the court missteps when it allows consideration of a restriction on a permission related to a right of copyright to guide its determination of ownership of title to a copy. The court writes that "the DSC-Ameritech agreement provides that Ameritech shall "not provide, disclose or make the Software or any portions or aspects thereof available to any person except its employees on a 'need to know' basis without the prior written consent of [DSC]..." Such a restriction is plainly at odds with the section 109 right to transfer owned copies of software to third parties."[70]

As will be detailed in the next section, if such reasoning is accepted, then section 106 rights are not truly "subject to" sections 107 through 122, as the careful balance Congress tried to strike in drafting those sections may be contracted away with a few carefully-crafted sentences. Here, Ameritech purportedly is not the owner of its copy of the software, and hence cannot transfer its copy to others, solely *because* the agreement says Ameritech cannot transfer the software. If this is how to determine title to the copy, then agreements just need to exclude each of the limitations in §§ 107 through 122 and no one but the copyright holder will ever hold title to any copy, and no one will ever have a fair use right, we can put an end to libraries, there will be no first sale right, there will be no classroom uses, § 117 rights, or any of the others. Enforcing such terms stands as an obstacle to the accomplishment of the full purposes and objectives of

69 *DSC Commc'ns Corp. v. Pulse Commc'ns, Inc.*, 170 F.3d 1354, pincitation (Fed. Cir. 1999) (bound to apply 4th Cir. law but finding none); *see also Adobe Sys. v. One Stop Micro, Inc.*, 84 F. Supp. 2d 1086, 1091 (N.D. Cal. 2000) ("These numerous restrictions imposed by Adobe indicate a license rather than a sale because they undeniably interfere with the reseller's ability to further distribute the software.") and at 1092 ("[T]he Court holds that based upon the undisputed evidence submitted by Adobe regarding the intent of the parties in entering into the agreement, trade usage, the unique nature of distributing software, as well as the express restrictive language of the contract, the OCRA is a licensing agreement. Thus, contrary to One Stop's assertions, the OCRA does not represent a first sale between the reseller and Adobe."). Note that Raymond T. Nimmer was Adobe's expert in the *One Stop Micro* case. *Id.* at 1091; *Applied Info. Mgmt. v. Icart*, 976 F. Supp. 149, 155 (E.D.N.Y. 1997) (where no terms defined the transfer of a copy and where payment was divided into three different payment periods, ownership of a copy was an issue of fact precluding summary judgment); *Adobe Sys. v. Stargate Software, Inc.*, 216 F. Supp. 2d 1051, 1055 (N.D. Cal. 2002) ("The determination of ownership in turn is based primarily on an examination of the OCRA, the agreement between Adobe and its distributors.").

70 *DSC Commc'ns. Corp. v. Pulse Commc'ns., Inc.*, 170 F.3d 1354, 1361 (Fed. Cir. 1999).

Congress in enacting §§ 107 through 122, and permits an unconstitutional copyright land-grab by rights holders.

The Federal Circuit also considered the fact that the agreement purported to prohibit the end users of the software "from using the software on hardware other than that provided by DSC."[71] Given that restraint of trade and efforts to extend the copyright (or patent) monopoly beyond the covered work to unrelated goods have been of chief concern to the Supreme Court and other courts to consider the issue, it is baffling why the Federal Circuit failed to consider that problem here, especially in light of the fact that the court was bound to apply Fourth Circuit law, where the leading copyright misuse case, *Lasercomb*, was decided.[72] Had the court been confronted by a Microsoft Windows license agreement that purported to require that the software only be used on computers provided by Microsoft, the court would have apparently happily enforced the agreement and prevented the entire computer industry from functioning as we know it.[73]

2. *Novell, Inc. v. CPU Distrib., Inc.* and *Novell, Inc. v. Unicom Sales, Inc.*

Novell, Inc. v. CPU Distrib., Inc.[74] provides another example of the Agreement Controls approach to determining copy ownership. The court writes, "To determine whether the transfer of copies of Novell software from Novell to its OEMs is a sale, the Court must construe the OEM Agreement between Novell and each of the OEMs. The OEM Agreement provides that it will be "construed in accordance with the laws of the State

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71 *DSC Commc'ns. Corp. v. Pulse Commc'ns., Inc.*, 170 F.3d 1354, 1361 (Fed. Cir. 1999).

72 *See Bobbs-Merrill Co. v. Straus*, 210 U.S. 339 (1908); *Bauer & Cie v. O'Donnell*, 229 U.S. 1 (1913); *Motion Picture Patents Co. v. Universal Film Mfg. Co.*, 243 U.S. 502 (1917); [more]; *Sony Corp. of Am. v. Univ. City Studios, Inc.*, 464 U.S. 417, 441 (1984) (finding it "extraordinary to suggest that the Copyright Act confers upon all copyright owners collectively, much less the two respondents in this case, the exclusive right to distribute VTRs simply because they may be used to infringe copyrights" and finding that to construe copyright law as Universal urged "would enlarge the scope of [Universal's] statutory monopolies to encompass control over an article of commerce that is not the subject of copyright protection." [more]; *Lasercomb Am., Inc. v. Reynolds*, 911 F.2d 970 (4th Cir. 1990); [more].

73 As of this writing one is still free to purchase computer hardware capable of running Microsoft operating systems from Hewlett-Packard, Dell, Acer, Lenovo, Toshiba, Apple, and from numerous components manufacturers.

74 *Novell, Inc. v. CPU Distrib.*, No. H-97-2326, 2000 U.S. Dist. LEXIS 9975 (S.D. Tex. May 4, 2000).

of Utah...""[75] Here the court provides an example of one of the deficiencies of the Agreement Controls approach by illustrating that such an approach will require resort to the varying laws of the states. In this case, the court looked to Utah law, but since the choice depends on the choice made in the agreement, in other cases courts have looked to the canons of contract construction from other states.[76]

Here, however, the particular choice of law does not appear to have been determinative of the result, for once the court determined to look to the agreement, the court found "unambiguous sales language" throughout the agreement, citing nearly two dozen examples.[77] This feature of this case makes it a somewhat atypical example, but to the extent the court was swayed by the fact that all risk of loss passed to defendants upon delivery of the copies[78] and nothing in the contract suggested that Novell was merely providing possession of the copies to defendants temporarily and expected the copies to be returned if not sold, then this approach could look more like the Economic Realities approach discussed next. But given the court's overall focus on allowing the terms of the agreement to control, I categorize it here.

It is certainly a merit of this particular opinion that it actively avoided looking to restrictions on the rights of copyright to determine title ownership. The court considered the term of the agreement that provided that "OEM agrees not to provide Novell Products or any part or copies thereof to any third party without the prior written consent of Novell." This sort of term restricting transfers has been viewed by other courts as nearly decisive and leads those courts to a finding that the transferees are not owners of the copies.[79] But the court recognized the lesson of Supreme Court precedent and wrote, "As was true in the *Bobbs-Merrill* case, this provision may contractually obligate the OEM not to transfer the copies except under the circumstances set forth in the OEM Agreement, but it does not preclude the application of the "first sale doctrine" as codified in § 109(a)."[80]

75 *CPU Distrib.*, 2000 U.S. Dist. LEXIS 9975 at *11.

76 *Applied Info. Mgmt. v. Icart*, 976 F. Supp. 149 (E.D.N.Y. 1997) (applying New York law); *Novell, Inc. v. Network Trade Center, Inc.*, 25 F.Supp.2d 1218 (D. Utah 1997) (applying the U.C.C.);morecitations.

77 *CPU Distrib.*, 2000 U.S. Dist. LEXIS 9975 at *13-*17.

78 *CPU Distrib.*, 2000 U.S. Dist. LEXIS 9975 at *16.

79 MDY is one; othercitations.

80 *CPU Distrib.*, 2000 U.S. Dist. LEXIS 9975 at *16. *See also Applied Info. Mgmt. v. Icart*, 976 F. Supp. 149 (E.D.N.Y. 1997). The *Icart* court is also careful not to fall into some of the over-simplifications and logical errors of earlier decisions, and while largely relying

In *Novell, Inc. v. Unicom Sales, Inc.*,[81] however, the Agreement Controls approach was applied even where the court gave the impression it was looking at something more. The court, citing *Wise*, wrote, "In determining whether a transaction is a sale or a license, the Court reviews the substance of the transaction, rather than simply relying on the plaintiff's characterization of the transaction."[82]

The case involved Novell software acquired under two different agreements. The defendants acquired some copies from Frederick County Public Schools ("FCPS"), who in turn had received the software from Novell under an agreement titled the "School License Agreement" ("SLA"). In examining the substance of that initial transaction, the court wrote that the license agreement, "granted FCPS a license to copy the software for use only by its students and employees. The license was for a specific term of one year, and required payment of an annual license fee. When the SLA expired, FCPS was required to return the software to Novell. All of these terms are consistent with a license, rather than a sale."[83]

The court thus held that the first sale doctrine did not apply to defendants' distribution of such software.[84] The focus here on an annual fee for software that had to be returned at the end of the term, while not overly emphasizing restrictions on the right to copy, reflects an approach focused solely on the terms of the agreement.[85]

The defendants had also acquired Novell software from parties who were termed "Qualified Educational Institutions" under Novell's Direct Education Order program ("DEO program").[86] Unlike the SLA software which involved FCPS itself signing an agreement with Novell, the Qualified Educational Institutions were not required to enter into a separate written

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on the agreement in an effort to determine copy ownership, the court does manage to avoid reading too much into terms that govern the rights of copyright. Ultimately the court decides that there is genuine issue of material fact as to whether the copy is owned and this precludes summary judgment.

81 *Novell, Inc. v. Unicom Sales, Inc.*, No. 03-2785, 2004 U.S. Dist. LEXIS 16861 (N.D. Cal. Aug. 17, 2004).

82 *Unicom Sales*, 2004 U.S. Dist. LEXIS 16861 at *28-*29.

83 *Unicom Sales*, 2004 U.S. Dist. LEXIS 16861 at *30.

84 *Unicom Sales*, 2004 U.S. Dist. LEXIS 16861 at *31.

85 To the extent the court looked at the one-year term , the annual license fee, and the requirement of return, the Perpetual Possession approach, described below, would also have no quarrel with such considerations.

86 *Unicom Sales*, 2004 U.S. Dist. LEXIS 16861 at pincitations.

license agreement, although a printed "software license" was included in the box in which the software was packaged.[87]

At this point in the opinion the court displays its narrower focus on the agreement more clearly: "the Court will proceed to examine *the terms of Novell 's Software License* to determine whether it describes a sale or a license."[88] (emphasis added).

The court then considers the following, "The agreement grants the right to use the software, for an unlimited period of time, but only within the customer's organization. If the customer breaches any of the terms, the license is automatically terminated, and the customer must either destroy the software or return it to Novell. The agreement expressly states that any rights not expressly granted are reserved to Novell."[89] The court notes that *Softman* had found the perpetual possession factor to be key, but attempted to distinguish *Softman* by emphasizing that "Here, although the Software License is not for a specific time period, it expressly requires return or destruction of the software if the license is terminated."[90] The court concluded that "The limited rights in the software, as set forth in the Software License, describe a license in the software, rather than a sale."[91]

This analysis of the DEO software agreement applies an Agreement Controls approach, emphasizing the term of the agreement that required return in event of breach.

3. *Stuart Weitzman, LLC v. MicroComputer Res., Inc.*

In *Stuart Weitzman, LLC v. MicroComputer Res., Inc.*,[92] the Southern District of Florida reviewed the holdings in the Federal Circuit's *DSC Commc'ns* and the Second Circuit's *Krause*, and wrote, "A discussion of the facts and legal conclusions in these cases reveals that *Krause* is the controlling case, and therefore guides the Court's application of Section

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87 *Unicom Sales*, 2004 U.S. Dist. LEXIS 16861 at *31.

88 *Unicom Sales*, 2004 U.S. Dist. LEXIS 16861 at *35. The court later reiterates the need to look to substance, but does so only in order to dismiss the label on the agreement and not in order to focus on the realities of the transaction beyond the agreement's terms. *Id.* at *37.

89 *Unicom Sales*, 2004 U.S. Dist. LEXIS 16861 at *35.

90 *Unicom Sales*, 2004 U.S. Dist. LEXIS 16861 at *36 fn10.

91 *Unicom Sales*, 2004 U.S. Dist. LEXIS 16861 at *35.

92 *Stuart Weitzman, LLC v. Microcomputer Res., Inc.*, 510 F. Supp. 2d 1098 (S.D. Fla. 2007), *vacated by, remanded by* 542 F.3d 859 (11th Cir. 2008) (dismissing for lack of subject matter jurisdiction).

117."[93] The court writes that, "Both *Krause* and *DSC Communications* stand for the proposition that a court must look to the nature of a party's rights in a piece of software to ascertain whether it is an "owner" under Section 117(a). "[94] As will be explained below, I see these two cases differently. The *Stuart Weitzmann* court appeared willing to look to the agreement, specifically at the restrictions on Stuart Weitzman's permissions with respect to rights of copyright, in order to determine title to the copies in Stuart Weitzman's possession.[95] However, in this case there was no signed agreement between the parties, and so the court turned instead to the factors identified in *Krause*.[96]

The court found the following factors ultimately weighed in favor of Weitzman's ownership of its copy:

> Weitzman paid MCR a substantial sum to develop the programs for its benefit. The Custom Software was specifically designed to serve Weitzman and was stored on Weitzman's servers. MCR did not formally reserve a right to repossess the copy of the Custom Software Weitzman used or to limit Weitzman's freedom to discard or destroy its copies of the software anytime it wished.[97]

That Weitzman paid a substantial sum for custom software seems as though it need not to be a dispositive factor in other cases, as one could easily pay a substantial sum for custom software that one fully intends to only lease from its author for a specified period of time, with full knowledge that title to one's copy remains with its author. While it is not clear from the court's opinion, the highly customized nature of the software suggests that Weitzman not only possessed his copy of the software, but the *only* copy of the software. If that was so, it might lend further support to the finding that Weitzman owned that copy, as it would suggest MRI had no interest in its return or safe-keeping and thus that Weitzman was entitled to perpetual possession of the copy.

C. The Economic Realities Approach.

"Ownership of a copy should be determined based on the actual

93 *Stuart Weitzman,* 510 F. Supp. 2d at 1103. It is unclear what the court means by "controlling" as neither decision was mandatory precedent for this court.
94 *Stuart Weitzman,* 510 F. Supp. 2d at 1106.
95 *Stuart Weitzman,* 510 F. Supp. 2d at 1106.
96 *Stuart Weitzman,* 510 F. Supp. 2d at 1106.
97 *Stuart Weitzman,* 510 F. Supp. 2d at 1107.

> character, rather than the label, of the transaction by which the user obtained possession. Merely labeling a transaction as a lease or license does not control." Raymond T. Nimmer (1992).

While the Reservation of Title and the Agreement Controls approaches elevate form over substance, a slight majority of courts have been willing to look beyond the four corners of the agreement and look instead to "the economic realities" of the transaction. The factors considered can include terms of the agreement not related to copyright permissions, but also facts about the transaction not discussed in the agreement at all.

The leading articulations of the approach come from two Ninth Circuit cases and an expansion of the approach in which the Second Circuit was willing to look beyond even formal "title" to determine who is an "owner" under § 117.

1. *United States v. Wise*

Without using the phrase "economic realities" the Ninth Circuit in *United States v. Wise*,[98] nonetheless gave birth to an approach to determining ownership of a copy that looks to such realities of the transaction. The case involved feature-length motion picture prints, which were occasionally provided, under various agreements, to "V.I.P."s described as "prominent member(s) of the motion picture industry or community" and to others such as television studios.[99]

The court looked beyond the failure of some of the agreements considered to expressly reserve title in the copyright owner and nonetheless found with respect to one of the transactions that "the general tenor of the entire agreement" was inconsistent with the concept of a sale.[100] The *Wise* court also wrote, "And, since "copyright proprietors frequently transfer rights in their works by complicated agreements which cannot simply be called 'sales[,]' in each case, the court must *analyze the arrangement at issue* and decide whether it should be considered a first sale.""[101]

This analyzing of "the arrangement at issue" and looking to "the general tenor of the agreement" led the *Wise* court to find some transactions

98 *United States v. Wise*, 550 F.2d 1180 (9th Cir. 1977).
99 *Wise*, 550 F.2d at 1184,
100 *Wise*, 550 F.2d at 1191.
101 *Wise*, 550 F.2d at 1188-89 (emphasis added) (*citing United States v. Bily*, 406 F. Supp. 726 (E.D.Pa.1975).).

involved sales and others did not. One contract the *Wise* court considered allowed the actress, Vanessa Redgrave, to keep possession of the film print "at all times" for her "personal use and enjoyment," but prevented her from transferring the print to anyone else.[102] The court determined that this contract was a sale despite the purported restrictions on transfer, illustrating that such a term was clearly not dispositive in the *Wise* court's view.

It is striking in reviewing the cases that those courts that carefully consider and attempt to apply the *Wise* court's approach tend to make the fewest logical errors and reach sensible results more than those courts that do not cite *Wise* and take some other approach.[103]

2. *Microsoft Corp. v. DAK Indus.*

One of the best examples of the Economic Realities approach is *Microsoft Corp. v. DAK Indus.*[104] Here the Ninth Circuit directly addresses the question of whether a transaction was "a lump sum sale of software units to DAK " or merely "a grant of permission to use an intellectual property."[105] The court writes that, "we must look through [this transaction's] form to the "economic realities of the particular arrangement." and "Because we look to the economic realities of the agreement, the fact that the agreement labels itself a "license" and calls the payments "royalties," both terms that arguably imply periodic payment for the use rather than sale of technology, does not control our analysis."[106]

This case, decided in 1995, has been too often ignored by courts, even within the Ninth Circuit that were addressing the very same question: how to determine if a transaction has resulted in a "sale" of software despite it bearing a "license" label.[107] These oversights by subsequent courts were probably the result of the different context. Here the Ninth Circuit needed to determine the answer to this question not to go on to apply the first sale doctrine or to evaluate § 117 rights, but instead to make a finding under

102 *Wise*, 550 F.2d at 1192.

103 [Long footnote goes here.]

104 *Microsoft Corp. v. DAK Indus.*, 66 F.3d 1091 (9th Cir. 1995); *Datalex Ltd. v. PSA, Inc.*, No. 01-06482, 2003 U.S. Dist. LEXIS 27563, *6 (C.D. Cal. Jan. 30, 2003) (""Economic realities" of an exchange determine whether a transaction is a sale, a lease, or a license. (*citing DAK Indus.*)").

105 *DAK Indus.*, 66 F.3d at 1095.

106 *DAK Indus.*, 66 F.3d at 1095.

107 Cite most cases in the Ninth Circuit since 1995 here.

the bankruptcy code regarding whether the debt related to this transaction arose prepetition or postpetition.[108] This is a shame, because the court here provides marvelous guidance on determining when a sale has occurred that looks to salient factors about the transaction.

The court notes the following about the transaction:

- DAK's entire debt to Microsoft arose at once at the outset. It was not incurred in installments over time.
- The amount of DAK's payment was calculated based upon quantity of units, not upon duration of use.
- DAK received all of its rights when the term of the agreement commenced, even though payments were made on an installment plan over time, as in the purchase of goods on unsecured credit.
- The timing of the payments was not correlated to DAK's sales of the copies.
- The agreement granted DAK a "right to sell" not "permission to use" the copies.
- Microsoft did not provide anything at its expense to DAK after the commencement of the agreement.

The court concludes, "For these reasons, the economic realities of this agreement indicate that it was basically a sale, not a license to use."[109]

3. *Softman Prods. Co., LLC v. Adobe Sys., Inc.*

The earlier-mentioned *Softman Prods. Co., LLC v. Adobe Sys., Inc.*[110] opinion applied the Economic Realities approach to find a sale. The court wrote, "It is well-settled that in determining whether a transaction is a sale, a lease, or a license, courts look to the economic realities of the exchange."[111] The court cited to *DAK Indus.* and indicated that the mere "license" label did not control its analysis. The court, citing § 202, also recognized that the question before it was not one of ownership of the copyright, but of "ownership of individual pieces of Adobe software."[112]

When examining the transaction's economic realities, the court highlighted the following: "the purchaser commonly obtains a single copy of the

108 *DAK Indus.*, 66 F.3d at 1095.
109 *DAK Indus.*, 66 F.3d at 1096.
110 *Softman Prods. Co., LLC v. Adobe Sys., Inc.*, 171 F. Supp. 2d 1075 (C.D. Cal. 2001).
111 *Softman Prods. Co., LLC*, 171 F. Supp. 2d at 1084.
112 *Softman Prods. Co., LLC*, 171 F. Supp. 2d at 1084.

software, with documentation, for a single price, which the purchaser pays at the time of the transaction, and which constitutes the entire payment for the "license." The license runs for an indefinite term without provisions for renewal. In light of these indicia, many courts and commentators conclude that a "shrinkwrap license" transaction is a sale of goods rather than a license."[113]

The court also looked to whether risk of loss transferred as an indicator that title had passed. The court writes,

> The reality of the business environment also suggests that Adobe sells its software to distributors. Adobe transfers large amounts of merchandise to distributors. The distributors pay full value for the merchandise and accept the risk that the software may be damaged or lost. The distributors also accept the risk that they will be unable to resell the product. The distributors then resell the product to other distributors in the secondary market. The secondary market and the ultimate consumer also pay full value for the product, and accept the risk that the product may be lost or damaged. This evidence suggests a transfer of title in the good.[114]

Ultimately the court distinguishes *Harmony* and explicitly declines to adopt the analysis of *One Stop Micro*, finding that "a single payment for a perpetual transfer of possession is, in reality, a sale of personal property and therefore transfers ownership of that property, the copy of the software."[115]

4. *Krause v. Titleserv, Inc.*: The "Incidents of Ownership"

In *Krause v. Titleserv, Inc.*,[116] the Second Circuit pushed the Economic Realities approach a step further than any other court had by rejecting the idea that "formal title" was even necessary for purposes of being an "owner" under § 117.[117] The court wrote in an oft-quoted passage,

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113 *Softman Prods. Co., LLC*, 171 F. Supp. 2d at 1085.

114 *Softman Prods. Co., LLC*, 171 F. Supp. 2d at 1085 (footnotes omitted).

115 *Softman Prods. Co., LLC*, 171 F. Supp. 2d at 1086. Note the use of the word "perpetual" here which is a intimation of the Perpetual Possession approach. The court also rejects the holdings of *Harmony* and *One Stop Micro* with respect to the applicability of agreements never assented to, because here, Softman, as a reseller, never installed the software and thus never assented to any Adobe EULA or other licensing agreement. *Id.* at 1087-88.

116 *Krause v. Titleserv, Inc.*, 402 F.3d 119 (2d Cir. 2005).

117 Many courts considering § 117 discuss the legislative history in which the CONTU report had recommended language for the statute that applied to the "rightful

> [I]t seems anomalous for a user whose degree of ownership of a copy is so complete that he may lawfully use it and keep it forever, or if so disposed, throw it in the trash, to be nonetheless unauthorized to fix it when it develops a bug, or to make an archival copy as backup security. We conclude for these reasons that formal title in a program copy is not an absolute prerequisite to qualifying for § 117(a)'s affirmative defense. Instead, courts should inquire into whether the party exercises sufficient incidents of ownership over a copy of the program to be sensibly considered the owner of the copy for purposes of § 117(a). The presence or absence of formal title may of course be a factor in this inquiry, but the absence of formal title may be outweighed by evidence that the possessor of the copy enjoys sufficiently broad rights over it to be sensibly considered its owner.[118]

In looking at these "incidents of ownership," the court focused on the following:

> Titleserv paid Krause substantial consideration to develop the programs for its sole benefit. Krause customized the software to serve Titleserv's operations. The copies were stored on a server owned by Titleserv. Krause never reserved the right to repossess the copies used by Titleserv and agreed that Titleserv had the right to continue to possess and use the programs forever, regardless whether its relationship with Krause terminated. Titleserv was similarly free to discard or destroy the copies any time it wished.[119]

In another sentence that one wishes other courts had before them when addressing this issue, the *Krause* court writes, "Krause's ownership of the

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possessor of a copy of a computer program" and Congress changed the term "rightful possessor" to "owner" but did not explain its reason. Some courts have thought this change signified an intent on Congress' part to restrict the application of § 117 to those with full "title" to the copy. The *Krause* court rightly points out that, "The term "rightful possessor" is quite broad. Had that term been used, the authority granted by the statute would benefit a messenger delivering a program, a bailee, or countless others temporarily in lawful possession of a copy. Congress easily could have intended to reject so broad a category of beneficiaries without intending a narrow, formalistic definition of ownership dependent on title." *Krause*, 402 F.3d at 123. I concur and believe courts have only caused mischief by seeking to divine Congressional intent in a situation where nothing definitive is available.

118 *Krause*, 402 F.3d at 123-24.

119 *Krause*, 402 F.3d at 124.

copyright in the programs is not disputed, but is *irrelevant* to Titleserv's rights under § 117(a), which depend on ownership of a copy of the copyrighted material." (Emphasis added).[120] I will argue in the next section that the irrelevance identified by the court here is only half of the irrelevance to be identified. That is, a key failing of the Agreement Controls approach is in thinking that permissions related to the rights of copyright are relevant to ownership of the copy, but they are not, and hence not just Krause's ownership of the copyright is irrelevant, but any permissions of copyright granted to a licensee are also irrelevant to the determination of copy ownership.

The court concluded, "Titleserv's right, for which it paid substantial sums, to possess and use a copy indefinitely without material restriction, as well as to discard or destroy it at will, gave it sufficient incidents of ownership to make it the owner of the copy for purposes of applying § 117(a). "[121]

D. The Perpetual Possession Approach.

> "If a transaction involves a single payment giving the buyer an unlimited period in which it has a right to possession, the transaction is a sale." Raymond T. Nimmer (1992, 1997).

In several of the opinions which I contend applied an Economic Realities approach, one can see hints of an approach that lies at the heart of this methodology and that is arguably driving its results. The two decisions in *Augusto* and *Vernor* have, intentionally or not, teased this interpretative focus out of the Economic Realities approach to state what I call the Perpetual Possession approach. After explaining this understanding of, or variation on, the Economic Realities approach, I will argue that this is an excellent development that the courts faced with this question should embrace. As the preceding survey of the cases has revealed, courts are in desperate need of a logical approach that respects precedent and Congressional choices, and which, in an ideal world, would simply make sense, both by being consistent with settled consumer expectations and by being straightforward for the courts to apply. After providing examples of the Perpetual Possession approach here, in the next section I will argue that the Perpetual Possession approach is such an approach.

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120 *Krause*, 402 F.3d at 124.
121 *Krause*, 402 F.3d at 124-25.

1. *UMG Recordings, Inc. v. Augusto*

The *Augusto* court wrote, "In determining whether a transaction is a sale or a license, courts must analyze the "economic realities" of the transaction. [T]he fact that the agreement labels itself a 'license'... does not control our analysis." (*citing DAK Indus.*)."[122]

The court then singles out one factor for special consideration, as it wrote, "The right to perpetual possession is a critical incident of ownership. (*citing Krause*) (describing a person's "degree of ownership of a copy" as "complete" when "he may lawfully use it and keep it forever, or if so disposed, throw it in the trash"). Accordingly, the distributor of a copyrighted product's intent to regain possession is strong evidence that the product was licensed, not sold, to the recipient. The absence of this intent is strong evidence that the product was sold."[123]

The *Augusto* court also found this factor of "perpetual possession" to have been critical to the Ninth Circuit's decision in *Wise*. The court wrote,

> The Ninth Circuit's decision in *United States v. Wise* demonstrates the importance of regaining possession of the licensed product. In *Wise*, the court evaluated several contracts under which movie studios transferred movie prints. Most of the contracts required that the recipients return the movie prints after a fixed term. ("The license agreements with respect to the films involved in this case generally... required their return at the expiration of the license period."). The Ninth Circuit determined that these contracts were licenses.
>
> However, some of the contracts permitted the recipient to keep the film print. In particular, one contract allowed an actress to keep possession of the film print "at all times" for her "personal use and enjoyment," but prevented her from transferring the print to anyone else. The Ninth Circuit determined that this contract was a sale, not a license. (citations omitted).[124]

In applying this key factor to these facts, the court found that,

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122 *UMG Recordings, Inc. v. Augusto*, 558 F. Supp. 2d 1055, 1060 (C.D. Cal. 2008).
123 *Augusto*, 558 F. Supp. 2d at 1060 (footnote omitted).
124 *Augusto*, 558 F. Supp. 2d at 1061.

> Here, UMG gives the Promo CDs to music industry insiders, never to be returned. The recipients are free to keep the Promo CDs forever. Nothing on the packaging of the Promo CDs or in the licensing label requires that the recipient return the Promo CDs to UMG. There are no consequences for the recipient should she lose or destroy the Promo CDs – which UMG allegedly considers its property. UMG does not request that any recipients return the Promo CDs and does not otherwise make any affirmative effort to recover possession of the Promo CDs. Further, it appears that UMG could not take these actions; UMG does not keep permanent records identifying who received which Promo CDs. Accordingly, the music industry insiders' ability to indefinitely possess the Promo CDs is a strong incident of ownership through a gift or sale.[125]

The *Augusto* court also relied on *DAK Indus.* to identify another important factor: the absence of a recurring benefit to the transferor. The court wrote,

> Generally, licenses provide recurring benefits for the copyright owner. (*citing DAK Indus.*) (determining that Microsoft sold its software to DAK in part because Microsoft received a set payment independent of DAK's length of use of the software); (*citing SoftMan Prods. Co.*) ...Here, UMG receives no recurring benefit from the recipients' continued possession.[126]

Finally, the *Augusto* court noted that the only apparent benefit to UMG to claim that it retains title to the copies is as part of an effort to restrain trade by preventing the transfer of its music. However, the court explains that, "This purpose was rejected 100 years ago by the Supreme Court. *See Bobbs-Merrill Co. v. Straus*, 210 U.S. 339 (1908) (rejecting a book publisher's attempt to restrict resale of a book through a label that prohibited sales for less than one dollar)..."[127]

In applying the Economic Realities approach dictated by Ninth Circuit precedent, the *Augusto* court found the heart of that approach in two factors: possession and payment. If the possession is permanent and the payment[128] is not correlated to the period of time possessed, then these

125 *Augusto*, 558 F. Supp. 2d at 1061 (citations and footnote omitted).
126 *Augusto*, 558 F. Supp. 2d at 1061 (citations and parenthetical omitted).
127 *Augusto*, 558 F. Supp. 2d at 1061 (parallel citations omitted).
128 The *DAK Indus.* court also already noted that nothing should prevent the court from finding that title to the copy has passed to the transferee where multiple payments are

are strong indicia that title to the copy has passed to the transferee, whereas if the possession is expected to be temporary or the payments are correlated to the period of time possessed, then these are strong indicia that title to the copy remains in the transferor.

The importance of these factors lurked in the background of the Ninth Circuit's key precedents on ownership of copies for decades,[129] but the *Augusto* court's opinion placed these critical indicia of ownership in sharper relief and thereby has shown a way forward for future courts.[130]

The *Augusto* court also did something that is too infrequent in these cases by considering the relevance of Supreme Court first sale precedents. The courts who have looked to restrictive terms in agreements to reach a result on the question of copy ownership have often made no effort to reconcile enforcement of such provisions with the Supreme Court's refusal to enforce such a restrictive provision in *Bobbs-Merrill.* Even if there are cases where a relevant distinction can be made, courts should pause to explicitly make such a distinction.

2. *Vernor v. Autodesk, Inc.*

The *Vernor* court began its analysis, as it should, with a review of the controlling precedent of *Wise,* and noted the admonition found there that the court "must analyze the "arrangement at issue and decide whether it

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not correlated with period of possession, but instead are more akin to a single fee paid on an installment plan. *Augusto* itself also illustrates that there need not be payment at all, as in the case of a gift. Instead, the crucial factor is that the copyright holder has voluntarily and permanently parted with its possession of the copy. *Cf.* 17 U.S.C. § 115(c)(2) (defining "distributed" in the context of compulsory licenses). An exception to "voluntarily" can even be found in the case of a forced judicial sale. *See, infra,* note ##.

129 And in the more recent Second Circuit opinion in *Krause*.

130 There are, however, certain phrasings in the *Augusto* opinion that are not ideal, particularly the use of the word "license" which has invited so many past courts to conflate the intangible copyright with the tangible copy. This court avoids that pitfall, but preferably would have written more precisely about title to the copies. Subsequent courts have already begun to apply the *Augusto* court's formulation. *See F.B.T. Prods., LLC v. Aftermath Records*, No. 07-3314, 2009 U.S. Dist. LEXIS 5981, at *13-*14 (C.D. Cal. Jan. 20, 2009); *but cf. F.B.T. Prods., LLC v. Aftermath Records*, No. 07-3314 (C.D. Cal. May 12, 2009) (unreported) (declining to provide a jury instruction based on the *Augusto* factors where issue "was not what a license is as a matter of copyright law, but rather what the parties intended when they agreed to the "records sold" and "masters licensed" provisions in the Eminem agreements.") (on appeal as No. 09-55817).

should be considered a first sale."[131] After a careful review of the facts, rationale, and holdings in *Wise*, the court wrote,

> In comparing the transactions found to be sales in Wise with those that were not, the critical factor is whether the transferee kept the copy acquired from the copyright holder. When the film studios required that prints be returned; the court found no sale. When the studios did not require the transferee to return the prints, the court found a sale. Even a complete prohibition on further transfer of the print (as in the Redgrave Contract), or a requirement that the print be salvaged or destroyed, was insufficient to negate a sale where the transferee was not required to return the print.[132]

Applying this guidance from *Wise*, the *Vernor* court wrote,

> Taking direction solely from *Wise*, the court concludes that the transfer of AutoCAD packages from Autodesk to CTA was a sale. Like the Redgrave Contract, the Settlement Agreement and License allowed CTA to retain possession of the software copies in exchange for a single up-front payment. Like the Redgrave Contract, the Settlement Agreement and License imposed onerous restrictions on transfer of the AutoCAD copies. Similar to the salvage transactions in *Wise*, the License required CTA to destroy the software in the event that it purchased a software upgrade. Under *Wise*, however, this is a "sale with restrictions on use," and is a sufficient basis to invoke the first sale doctrine.[133]

The *Vernor* court then looked beyond the first sale context to those cases that have addressed the copy ownership issue in relation to § 117, and considers *MAI*, *Triad*,[134] and *Wall Data*. Without giving it a name, as I have here, the *Vernor* court recognized that these courts were, without citing *Wise*, looking to restrictive terms in the agreements accompanying a transferred copy to determine whether title to the copy passed. The court interpreted these cases to reflect an approach that would counsel that the more restrictions found or the more draconian the restrictions are, the less likely it is that title to the copy rests with the transferee. And the *Vernor* court acknowledged, that in a comparison of restrictive terms, the Autodesk agreement would fall on the very restrictive end of the comparison. This

131 *Vernor v. Autodesk, Inc.*, 555 F. Supp. 2d 1164, 1169 (W.D. Wash. 2008) (citing *Wise*).
132 *Vernor*, 555 F. Supp. 2d at 1170 (footnote omitted).
133 *Vernor*, 555 F. Supp. 2d at 1170-71 (footnote omitted).
134 *Triad Sys. Corp. v. Southeastern Express Co.*, 64 F.3d 1330 (9th Cir. 1995).

placed the district court in the uncomfortable position of having two approaches to addressing the same question, both articulated by the Ninth Circuit at different times, and which, in the present case, lead to opposite results. The court tried valiantly to find a means to escape the conflict by considering whether any difference between § 109 and its predecessor statute, § 27 considered in *Wise* could be used to distinguish the cases. The court also looked to the fact that *Wise* was a criminal case, and the difference between motion picture film prints and software, and the differences between § 109 and § 117, to see if any of these could provide a basis for resolving the conflict and place this case more in line with one or the other Ninth Circuit precedents. However, the court persuasively argued that none of these provides an adequate basis for distinguishing the cases and thus the court is guided by the principle that a subsequent panel of the Ninth Circuit cannot overrule an earlier panel absent intervening Supreme Court precedent or *en banc* authority. With no such intervening authority, the court was bound to follow *Wise*.

The *Vernor* court's opinion is a carefully-reasoned and thorough opinion that reached the correct result. It did it in part through a close reading of *Wise* which uncovered the same critical factor that the *Augusto* court had emphasized: perpetual possession.[135] However, it also worked through the irreconcilable conflict caused by the disparate approaches to copy ownership that have built up over the years. The Ninth Circuit, however, will through the cases described in Section I, have at least three opportunities to follow *Vernor's* lead in returning to its *Wise* precedent. If one of these three cases were to be heard *en banc* on this issue it could provide the most clarity, but even the three-judge panels can do much to clarify the law by simply affirming the insights found in *Augusto* and *Vernor* and by following *Wise*.

It is useful to reflect on the features we should expect from an interpretative approach to the question of copy ownership, as it will help to confirm the wisdom of the Perpetual Possession approach adopted in *Wise* and followed in *Augusto* and *Vernor*. Thus, in the next section, I argue for the essential and desirable features of such an approach.

III. The Correct Approach to Determining Copy Ownership:

Courts are in desperate need of a logical approach to the question of copy

135 *Vernor*, 555 F. Supp. 2d at 1170 ("the critical factor is whether the transferee kept the copy acquired from the copyright holder.").

ownership that respects precedent and Congressional choices, and which, in an ideal world, would simply make sense, both by being consistent with settled consumer expectations and by being straightforward for the courts to apply. I will argue that the Perpetual Possession approach is such an approach.

A. Must be Logically Correct.

Two logical errors run rampant in the "license versus sale" jurisprudence, but arise from the same source: a failure to distinguish between the intangible copyright and the tangible copy. First, the word "license" is used in at least two distinct ways, which makes courts susceptible to inadvertent equivocation. Second, one's mere status as the licensee of a right of copyright is erroneously presumed to be incompatible with also being the owner of a copy. Any approach to determining ownership of a copy must avoid these logical errors.

1. Must not equivocate with respect to the word "license."

When "license" is used as a noun in the copyright context, it means something like, "a grant by the holder of a copyright to another of any of the rights embodied in the copyright short of an assignment of all rights" as in "The agreement contained a license to reproduce 20 copies of the photograph."

When "license" is used as a verb it typically means "to give permission or consent" as in "The author licensed her publication right to the nation's largest distributor."

These uses of the word relate only to the intangible copyright.

The word "license" is also, unfortunately, used in conjunction with tangible things. First, as a noun it is often used synonymously with the terms "agreement" or "contract" when that underlying agreement contains grants of copyright permissions, as in "Did she sign the license?" This usage seems to lead to confusion less often and I will not address it further here.

However, particularly in the software context, the word "license" is used as a verb in yet another way that I wish to focus on. Software distributors often say, "We only license our software. We do not sell it." This is a difficult sentence to parse because of the layers of ambiguity involved, but particularly from reading the cases, one comes to understand that the intended definition is not just that described above of "to give permission or consent" with respect to some right of copyright, but instead is used in a way that means something more like:

> to transfer to another possession of a tangible object in which a copyrighted work is embodied, for a specified period of time or perpetually, without transferring title to the tangible object, and providing at least some copyright permission.

It would be useful to have a different term to indicate this unique use of "license." Something like "no title to the copy license" would perhaps convey the intended meaning, but would be exceedingly cumbersome. For purposes of clarity in this section, when I talk about this sense of "license" I will place the word in italics, like so: *license*.[136]

It is useful at this point to note that in § 106(3), Congress has given copyright holders the following exclusive right:

> to distribute copies or phonorecords of the copyrighted work to the public by
> - sale or
> - other transfer of ownership, or
> - by rental,
> - lease, or
> - lending.[137]

Upon looking carefully, the first thing one should notice is that an exclusive right to distribute by *license* is nowhere to be found. Take each enumerated form of distribution in turn. First we have "sale" which is most certainly not what copyright holders mean by *license*. Then there is "other transfer of ownership" but the key feature of *licensing* was supposed to be that ownership of the copy was not transferred. The next two, "rental" and "lease" are synonymous in most contexts, though some distinguish the two on the basis of whether the period of possession is auto-renewing. In either case, they both fundamentally involve a limited period of possession in exchange for consideration.[138] It is that feature, consideration, that distinguishes the fifth and final recognized method of distribution

136 If a quote a court using the term in this sense, I will not use italics.
137 17 U.S.C. § 106(3).
138 That consideration is something less than the full value of permanent possession of the thing rented or leased.

"lending." Lending is what libraries and neighbors do and it is done without payment. But all three of rental, lease, and lending fundamentally involve a limited period of possession. For that reason, none of those three can be what is meant by *license* because copyright holders who use the term routinely do so in transactions where the copy is provided to the transferee for an unlimited period of possession.

The Copyright Act never granted to copyright holders the exclusive right to distribute by means of *license*.[139] So, copyright holders made it up. But what are the consequences of that fact?

One might argue that copyright holders only have the exclusive right to distribute in the five ways specified in the statute. Any other form of distribution is simply not a form of distribution recognized by the Copyright Act or granted exclusively to copyright holders.[140] Even on this view the consequences are not immediately clear. Does this mean it is forbidden to distribute by *license* or simply that copyright holders can do so, but when doing so they will not be exercising one of their exclusive rights under copyright? If the latter, it would seem to be a consequence of that fact that copyright holders would also not be able to make use of the remedies of copyright to prevent such non-copyright based distributions. That is, if distribution by *license* is not one of the exclusive rights granted to copyright holders, then anyone can do it without infringement of any right of the copyright holder! This would be a puzzling transaction because, assuming a first distribution by *license*, the *licensee* would, perhaps while acknowledging that he holds no title to the copy, offer to *license* the copy to another, which, since he could pass no greater right than he held, would amount to a mere transfer of possession and nothing more. Arguably this might violate some contractual provision of the first exchange, but *ex hypothesi* it could not violate any right of copyright.[141]

One problem with this scenario is that nothing about the transaction would appear any different from a § 106(3) distribution. If the *licensee* offered it

139 That is a statement that sounds strange only if one fails to keep the specific definition of *license* that is under consideration in mind.

140 This argument could rely in part on the choice made by Congress to narrow the publication right which had previously used the phrases "publish" and "vend" and had forced courts to attempt to interpret the scope of "vend" in particular. [citations] In the 1976 Act, Congress clarified by enumerating the methods of distribution it intended to grant exclusively to copyright holders.

141 I also assume, for the sake of this bizarre scenario, that the *licensee* does not purport to grant any of the actual rights of copyright of the copyright holder, such as the right to reproduce or prepare derivative works.

on a perpetual basis, it would *look* in every respect like a sale or other transfer of ownership, and if the *licensee* offered it for a limited period of time, it would look either like a rental/lease or lending, depending on whether consideration was received. This is, of course, precisely the problem with distribution by *license* in the first instance by the copyright holder. The copyright holder wishes to insist that it is not an exercise of the publication right that gives rise to the first sale doctrine, but, in those cases were there is a right of perpetual possession, the transaction looks in every relevant respect like a sale or other transfer of ownership.

Approaching the problem from another angle, we should agree that either distribution by *license* is an exercise of the publication right or it is not. If it is not, then we have the problems described above: anyone can do it without infringing. This is clearly unacceptable, at least to copyright holders. However, if distribution by *license* is an exercise of the publication right, then the first sale doctrine should apply. That is the overriding purpose of the first sale doctrine: Congress gives the copyright holder one exercise of the publication right and after that, the right is exhausted and the first sale doctrine takes over. Thus advocates of the *licensing* paradigm face a dilemma, either it fails in its purpose because the first sale doctrine still applies or it fails in its purpose because the recipient is free to pass the copy along to another without infringing an exclusive right of the copyright holder.

If this sounds absurd, then recall how we got here. We were faced with two options: either distribution by *license* is forbidden or it is not. If it is forbidden, then all the questions of copy ownership are solved. If it is not forbidden, then given that it is not among the enumerated rights of copyright holders, what are its consequences? And we found the consequences are certainly not what copyright holders would hope and are borderline absurd. The only thing defenders of distribution by *license* could say is that not only are copyright holders entitled to distribute by means not enumerated in the Copyright Act, but also they are entitled to exclude others from doing the same. That is, they have an exclusive right that is not enumerated. If this is the argument defenders of distribution by *license* are forced into, then things have not gone well for them at all, because such unenumerated exclusive rights would pose serious due process problems.[142]

142 *Baggett v. Bullitt*, 377 U.S. 360, 367 (1964) ("a law forbidding or requiring conduct in terms so vague that men of common intelligence must necessarily guess at its meaning and differ as to its application violates due process of law.").

While it is not my primary purpose here to fully develop the above argument, it would appear that the better view is that distribution by *license*, since it is not among the methods of distribution enumerated in § 106(3), is not recognized and not available. That is, there is simply no such thing as distribution of a copy by means of *license*. Instead, every transaction falls into one of two categories: those that provide perpetual possession are sales or other transfers of ownership (e.g., gifts) and those that provide a limited period of possession are a rental/lease or a lending, depending on whether consideration is required. In the case of copies of software and music, those transactions that fall into the sale or gift category provide first sale rights and those transactions that fall into the lease or lending category do not. As a peripheral benefit, such a view provides enormous administrative simplicity, because the only fact about a transaction that matters is whether it allows for a right of perpetual possession or not.

Such a result would be a breath of fresh air because of the rampant confusion that usage of the term *license* has caused. Before considering some examples of this confusion, it is worthwhile to provide some historical context on the development of this usage of the term *license*. The Third Circuit explained, in an opinion from 1991, that:

> When these form licenses were first developed for software, it was, in large part, to avoid the federal copyright law first sale doctrine... [Court describes software rental companies.] The first sale doctrine, though, stood as a substantial barrier to successful suit against these software rental companies, even under a theory of contributory infringement. By characterizing the original transaction between the software producer and the software rental company as a license, rather than a sale, and by making the license personal and non-transferable, software producers hoped to avoid the reach of the first sale doctrine and to establish a basis in state contract law for suing the software rental companies directly. Questions remained, however, as to whether the use of state contract law to avoid the first sale doctrine would be preempted either by the federal copyright statute (statutory preemption) or by the exclusive constitutional grant of authority over copyright issues to the federal government (constitutional preemption). (citations). Congress recognized the problem, and, in 1990, amended the first sale doctrine as it applies to computer programs and phonorecords... This amendment

> renders the need to characterize the original transaction as a license largely anachronistic.[143]

But the usage, even if anachronistic, has persisted, in part because software distributors wanted more than to defeat the first sale doctrine in the case of software rental companies. Even after Congress responded to that concern, software distributors were unwilling to give up the *licensing* fiction because it appeared to provide a means to other desirable ends such as price discrimination, controlling ancillary markets, and preventing competition in related goods.[144]

The merits of permitting copyright owners these additional benefits are not my focus. I am concerned with how the ambiguous use of the word "license" has created a land mine for courts who end up speaking imprecisely or in the worst case scenarios, reaching erroneous conclusions.

The *Microsoft Corp. v. Software Wholesale Club, Inc.* opinion provides one example. The court wrote,

> "However, a party that licenses its products rather than selling them may avoid the application of the first-sale doctrine. *See, e.g., Harmony Computers & Elecs.*, (the fact that Microsoft licenses rather than sells its products likely precludes application of the first-sale doctrine); *Novell, Inc.*, 2000 U.S. Dist. LEXIS 9975, at *7-18 (the first-sale defense applied, but only because Novell sold, rather than licensed, its software product)."[145]

What does the phrase "licenses its products" mean here? Both "license" and "products" could have two meanings.[146] If it just means that a license, as in a

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143 *Step-Saver Data Sys. v. Wyse Tech.*, 939 F.2d 91, 96 (3d Cir. 1991).

144 As an example of price discrimination, most of the Novell and Adobe cases are about educational versions of the software offered at a price discounted from the regular retail price. For anti-competitive examples, Blizzard's terms are designed to prevent third parties from offering competing match-making services for online play and attempt to prevent third-parties from developing independent software that interoperates with Blizzard's software, giving Blizzard sole control of those lucrative markets.

145 *Microsoft Corp. v. Software Wholesale Club, Inc.*, 129 F. Supp. 2d 995, 1007 (S.D. Tex. 2000) (citation omitted).

146 Particularly in the software context, we sometimes think of the intangible copyrighted work as the "product" and other times by "product" we might mean the tangible copy on which the work is embodied. The same ambiguity arises with the word "software" making a "license to use the software" equally, if not more, ambiguous.

grant of permission, is provided with respect to some right of copyright, then it has fallen into the error of ignoring 17 U.S.C. § 202, by failing to recognize the possibility of ownership of a copy independent from ownership of the copyright, to be discussed more fully next. But, if it instead means *license*, that is, a transfer of possession without a transfer of title to the copy, then one has the problems already described in this section with such a notion and one has presumed the answer to the question being asked, that is, in trying to determine whether someone is an owner of a copy, it is not much use to say that those who are not owners of a copy do not have the rights of owners of a copy. We knew this at the outset. What was wanted was a feature of the transaction that would distinguish the owners from the non-owners, other than the label applied by the copyright holder.[147]

2. Must recognize the possibility of ownership of a copy independent from ownership of the copyright.

17 U.S.C. § 202 provides that,

> Ownership of a copyright, or of any of the exclusive rights under a copyright, is distinct from ownership of any material object in which the work is embodied. Transfer of ownership of any material object, including the copy or phonorecord in which the work is first fixed, does not of itself convey any rights in the copyrighted work embodied in the object; nor, in the absence of an agreement, does transfer of ownership of a copyright or of any exclusive rights under a copyright convey property rights in any material object.[148]

147 It might be a logically coherent position to accept that the copyright holder simply can declare that title to the copy is not passing and no other feature of the transaction matters, but it would remain unclear where the authority to make such declarations came from, it would be a view with surprising consequences, as there would be some non-owners whose bundle of substantive rights would be identical to an owner, and only the handful of courts that embraced the Reservation of Title approach would possibly accept such an argument.

148 17 U.S.C. § 202. The predecessor statute, 17 U.S.C. § 27, read similarly: "The copyright is distinct from the property in the material object copyrighted, and the sale or conveyance, by gift or otherwise, of the material object shall not of itself constitute a transfer of the copyright, nor shall the assignment of the copyright constitute a transfer of the title to the material object; but nothing in this title shall be deemed to forbid, prevent or restrict the transfer of any copy of a copyrighted work the possession of which has been lawfully obtained.'" Section 41 of the 1909 Act was identical, with the substitution of "this Act" for "this title."

That ownership of the tangible thing is a separate issue from what rights under copyright one might have with respect to that tangible thing is also a centuries-old principle in U.S. law. The Supreme Court wrote in 1882,

> In *Stephens v. Cady*, 55 U.S. 528 (1853), and again in *Stevens v. Gladding*, 58 U.S. 447 (1855), the point decided was that, by a sale of the copperplate engraving of a map on execution from a State court against the owner of the copyright, the purchaser acquired no right to strike off and sell copies of the map.
>
> Mr. Justice Nelson, in delivering judgment in *Stephens v. Cady*, said: "The copperplate engraving, like any other tangible personal property, is the subject of seizure and sale on execution, and the title passes to the purchaser the same as if made at a private sale. But the incorporeal right, secured by the statute to the author, to multiply copies of the map by the use of the plate, being intangible, and resting altogether in grant, is not the subject of seizure or sale by means of this process..."[149]

149 *Ager v. Murray*, 105 U.S. 126, 129-130 (1882) (modernizing internal citations); *Werckmeister v. Springer Lithographing Co.*, 63 F. 808, 812 (C.C.D.N.Y. 1894) (author of painting may sell his painting and retain the right to its copyright); *Patterson v. J. S. Ogilvie Pub. Co.*, 119 F. 451, 453 (C.C.D.N.Y. 1902) (plates sold by sheriff became the property of the purchaser, but gave him no right to publish the copyrighted work which could be printed from them); *Werckmeister v. American Lithographic Co.*, 142 F. 827, 830 (C.C.D.N.Y. 1905) ("The author of a painting, when it is finished, before publication, owns a material piece of personal property, consisting of the canvas and the paint upon it. He also owns an incorporeal right connected with it; that is, the right to make a copy of it. These two kinds of property, although growing out of the same intellectual production, are in their nature essentially and inherently distinct. The law has always recognized that they are distinct. The defendants' counsel admitted on the argument that, after a copyright has been once taken out, the two kinds of property are distinct, and that the owner of a painting may then sell the painting to one person, and the copyright to another. The claim is that that cannot be done before the statutory copyright is taken out. But the law has always recognized that a common-law copyright, before a general publication, is a distinct property from the thing to which the copyright applies. One man may be the owner of the thing, and another of the copyright in the thing. For instance, a person who has received a letter, voluntarily sent him by the writer, owns the piece of paper upon which the letter is written; but the writer of the letter continues to be the owner of the copyright, and can, by injunction, prevent the person who has received the letter from publishing it. (citations omitted). A teacher delivering lectures orally to students remains the owner of the copyright, although he has permitted the particular persons hearing the lectures for their own instruction to take copies of them. (citations omitted). A person who has transferred the ownership of a copy of a book to another, under an agreement that it shall be transferred only for a particular and restricted purpose, does not thereby part with the copyright. (citations omitted). A public representation of a

If both the Federal Copyright Statute and the Supreme Court have recognized that one could own a tangible thing that embodies a copyrighted work, yet might have no right under copyright to copy, modify, or distribute that copyrighted work, then the Agreement Controls approach, which looks to restrictions on the rights of copyright in an effort to determine title to a copy must be erroneous. Like Cady and Gladding, one could have permission with respect to *none* of the rights of copyright and still be an owner of a copy.

This shows a key error of the Federal Circuit's decision in *DSC Commc'ns. Corp. v. Pulse Commc'ns., Inc.* because one could say that Cady and Gladding suffered from rights that were severely limited "in ways that are inconsistent with the rights normally enjoyed by owners"[150] but that had no bearing on whether each held title to the tangible embodiment of the copyrighted work.[151]

B. Must Respect Precedent.

The cases to consider ownership of copies seem particularly prone to ignoring relevant precedents. It is not typically an explicit refusal to follow an earlier case's approach, but often it involves ignoring that precedent through a failure to cite or discuss it. This may be explained by the wide

play does not authorize a person who hears it to make a copy of it. (citations omitted.).); *Harms v. Cohen*, 279 F. 276, 281 (D. Pa. 1922) ("[A] copyright is an intangible thing, and it is separate and distinct from the material object copyrighted..."); *Local Trademarks, Inc. v. Price*, 170 F.2d 715, 718 (5th Cir. 1948) ("A copyright is an intangible, incorporeal right in the nature of a privilege or franchise and is independent of any material substance such as the manuscript or plate used for printing. It is entirely disconnected therefrom."); *Hughes Tool Co. v. Fawcett Pubs., Inc.*, 315 A.2d 577, 579-80 (Del. 1974) ("17 U.S.C. § 27 indicates that a statutory copyright "is distinct from the property in the material object copyrighted."...A common-law copyright, like its statutory successor, is distinct from that which is copyrighted. It is not a material substance, but is an incorporeal right in the nature of a franchise or privilege of publication."); *United States v. Wise*, 550 F.2d 1180, 1187 (9th Cir. 1977) ([T]he copyright is distinct from the property which is copyrighted, and the sale of one does not constitute a transfer of the other.").

150 *DSC Commc'ns. Corp. v. Pulse Commc'ns., Inc.*, 170 F.3d 1354 (Fed. Cir. 1999).

151 I believe an effort to distinguish these cases solely because they involved copperplates from which one would make copies, rather than copies themselves would fail, because the cases following these, cited above, often do involve the very embodiment of the work, such as the painting in *Springer Lithographing Co.*, and because the nature of engravings is such that the copperplates are not treated differently than the copies they produce. For example, one could not create duplicate copperplates without permission and avoid liability for infringement of the reproduction right.

range of cases in which ownership of a copy can be relevant, such as first sale cases, § 117 cases, and even a too-often ignored case primarily addressing a question of bankruptcy law.[152] If the courts search only for those precedents addressing the statute they seek to interpret, they may miss those cases decided under other statutes that address the same underlying issue of ownership of a copy. As the *Vernor* court held, however, there is no reason to believe that "owner of a particular copy" means one thing in § 109 and "owner of a copy" means something different in § 117.[153] Thus, whatever the reason for earlier failings, it should at least be the objective of any interpretive approach to follow controlling precedents.

In particular, the courts frequently fail to ensure that their holdings are consistent with the existing Supreme Court precedents on this issue, particularly the case widely regarded as establishing the first sale doctrine, *Bobbs-Merrill Co. v. Strauss*.

1. **Must respect Supreme Court precedent and should seek to harmonize Circuit Court precedents.**

In *Bobbs-Merrill Co. v. Strauss*, the Supreme Court held that while the Copyright Act, then in effect, provided copyright holders with a reproduction and publication right,

> one who has sold a copyrighted article, without restriction, has parted with all right to control the sale of it. The purchaser of a book, once sold by authority of the owner of the copyright, may sell it again, although he could not publish a new edition of it.[154]

The Bobbs-Merrill Company had printed a notice in a book it published which read,

> The price of this book at retail is one dollar 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.[155]

This notice shares many characteristics of the terms found in software licensing agreements that courts are asked to interpret over 100 years later. This fact did not escape the district court in *Novell, Inc. v. CPU*

152 *DAK Indus.*
153 *Vernor*.
154 *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339, 350 (1908).
155 *Bobbs-Merrill Co.*, 210 U.S. at 341.

Distrib., who wrote,

> The Court concludes that whether the EULA is otherwise enforceable or not, it is similar to the notice included in the books published by Bobbs-Merrill and, as such, does not preclude a finding that a first sale occurs when Novell delivers the copies of its software to the OEMs.[156]

This is the proper analysis. Given that the Supreme Court has held that Bobbs-Merrill's restrictions were unenforceable, there should at least be an investigation of whether software licensing terms that seek to evade the first sale doctrine are suspect as well, and certainly such terms should not be deferred to as key evidence for the proposition that title to the copy has not passed to the transferee.

Additionally, the courts considering transfers of title should, where possible, not create Circuit conflicts. There are a series of older "waste paper" and salvage cases that held that even where a copyright holder sold copies of his work to another solely for purposes of destruction, that such transactions were nonetheless first sales that could not give rise to copyright infringement when the salvage company sold the copies in breach of the agreement.[157] Again, if the courts were willing to ignore breach of such a central term of these agreements and nonetheless find a first sale, present day courts that allow litigants to defeat the first sale doctrine through restrictive terms in licensing agreements appear to have the analysis completely backwards. The courts should instead seek to harmonize their

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156 *Novell, Inc. v. CPU Distrib.*, 2000 U.S. Dist. LEXIS 9975 at *8 (S.D. Tex. May 4, 2000).

157 *United States v. Wise*, 550 F.2d 1180, 1193 (9th Cir. 1977) ("[T]here would of course be a "first sale" of any film sold for salvage.");*United States v. Atherton*, 561 F.2d 747, 751 (9th Cir. 1977) ("In a criminal prosecution, a sale for salvage purposes can be a first sale."); *United States v. Drebin*, 557 F.2d 1316, 1327 (9th Cir. 1977); *Independent News Co. v. Williams*, 293 F.2d 510, 516 (3d Cir. Pa. 1961); *Harrison v. Maynard, M. & Co.*, 61 F. 689, 691 (2d Cir. 1894) ("[T]he right to restrain the sale of a particular copy of the book by virtue of the copyright statutes has gone when the owner of the copyright and of that copy has parted with all his title to it, and has conferred an absolute title to the copy upon a purchaser, although with an agreement for a restricted use. The exclusive right to vend the particular copy no longer remains in the owner of the copyright by the copyright statutes. The new purchaser cannot reprint the copy. He cannot print or publish a new edition of the book; but, the copy having been absolutely sold to him, the ordinary incidents of ownership in personal property, among which is the right of alienation, attach to it. If he has agreed that he will not sell it for certain purposes or to certain persons, and violates his agreement, and sells to an innocent purchaser, he can be punished for a violation of his agreement; but neither is guilty, under the copyright statutes, of an infringement."

decisions with these cases or at least address the cases to explain why they are distinguishable in a given instance.

2. Should heed the warning of the Supreme Court's recent *Quanta Computer* decision.

In *Quanta Computer, Inc. v. LG Elecs., Inc.*,[158] the Supreme Court reaffirmed the long-standing doctrine of patent exhaustion, and in so doing, included a discussion of how the Supreme Court came to reject its holding in *Henry v. A. B. Dick Co.*,[159] which had permitted, in 1912, post-sale restrictions on the use of a patented article.

A.B. Dick Co. sold its patented Rotary Mimeograph machine with a notice attached that read, "LICENSE RESTRICTION. This machine is sold by the A.B. Dick Co. with the license restriction that it may be used only with the stencil paper, ink and other supplies made by A.B. Dick Company, Chicago, U.S.A."[160]

While the Court upheld this restriction, it did so against vigorous dissent which predicted an uncontrolled multiplication of such license restrictions that would permit contract law to cause the expansion of patent law beyond its intended limits.[161]

The following year, 1913, the Court found an opportunity to limit the *A.B. Dick Co.* holding in *Bauer & Cie v. O'Donnell.*[162] James O'Donnell was a proprietor of a drug store who refused to honor a restriction placed by Bauer Chemical on packages of its patented "Sanatogen," a water-soluble albumenoid,[163] which purported to require all such packages to retail for no

158 *Quanta Computer, Inc. v. LG Elecs., Inc.*, 128 S. Ct. 2109 (2008).

159 *Henry v. A. B. Dick Co.*, 224 U.S. 1 (1912).

160 *A. B. Dick Co.*, 224 U.S. at 11. A.B. Dick was an early innovator of the "Give away the razors and charge for the razor blades" model. The Court writes, "the patentee sold its machines at cost, or less, and depended upon the profit realized from the sale of other non-patented articles adapted to be used with the machine, and that it had put out many thousands of such machines under the same license restriction." *Id.* at 26.

161 *A. B. Dick Co.*, 224 U.S. at 51-55 (White, C.J., *dissenting*). This was an unusual 4-3 opinion because the case was argued after the death of Justice Harlan and during the absence of Justice Day, who took no part in the decision of the case. The majority opinion was written by Justice Lurton, and joined by Justices McKenna, Holmes and Van Devante. Justices Hughes and Lamar joined the dissent.

162 *Bauer & Cie v. O'Donnell*, 229 U.S. 1 (1913).

163 Albumen is the white of an egg which contains (among other things) several dozen types of albumin (with an 'i'), mostly ovalbumin, the main protein found in egg white. It can also refer to the non-germ bulk of certain grains which serve the same structural

less than one dollar. O'Donnell purchased the packages first from Bauer and, after they severed relations with him, from jobbers[164] and sold them for less than a dollar. O'Donnell indicated that he intended to keep doing so.[165]

There, despite a license "for sale and use at a price not less than one dollar" and terms which purported to state that purchase was an acceptance of the conditions[166] and that any violation of the restrictions caused all rights to revert to the patentee, the Court rejected the characterization of the license as "a license to use the invention"[167] and noting that "the patentee had no interest in the proceeds of subsequent sales, no right to any royalty thereon or to participation in the profits thereof"[168] the Court concluded that the

> packages were sold with as full and complete title as any article could have when sold in the open market, excepting only the attempt to limit the sale or use when sold for not less than one dollar... There was no transfer of a limited right to use this invention, and to call the sale a license to use is a mere play upon words... The right to vend conferred by the patent law has been exercised, and the added restriction is beyond the protection and purpose of the act. This being so, the case is brought within that line of cases in which this court from the beginning has held that a patentee who has parted with a patented machine by passing title to a purchaser has placed the article beyond the limits of the monopoly secured by the patent act.[169]

Not content to merely distinguish *A.B. Dick Co.*, the Court took the opportunity four years later to explicitly overrule it.[170] The case was overruled in *Motion Picture Patents Co. v. Univ. Film Mfg. Co.*[171] The *Quanta Computer* Court's summary of the case will suffice here:

> [A] patent holder attempted to limit purchasers' use of its film

and metabolic purposes.

164 "Jobbers" are wholesalers who operate on a small scale or who sell only to retailers and institutions, often "by the job."

165 *O'Donnell*, 229 U.S. at 9.

166 Compare to today's shrinkwrap and click-wrap agreements.

167 *O'Donnell*, 229 U.S. at 17.

168 *O'Donnell*, 229 U.S. at 17.

169 *O'Donnell*, 229 U.S. at 17.

170 In the interim, on October 15, 1914, Congress also enacted the Clayton Antitrust Act, 38 Stat. 730.

171 *Motion Picture Patents Co. v. Universal Film Mfg. Co.*, 243 U.S. 502 (1917).

> projectors to show only film made under a patent held by the same company. The Court noted the "increasing frequency" with which patent holders were using *A.B. Dick*-style licenses to limit the use of their products and thereby using the patents to secure market control of related, unpatented items. Observing that "the primary purpose of our patent laws is not the creation of private fortunes for the owners of patents but is 'to promote the progress of science and useful arts,'" (quoting U.S. Const., Art. I, § 8, cl. 8), the Court held that "the scope of the grant which may be made to an inventor in a patent, pursuant to the [patent] statute, must be limited to the invention described in the claims of his patent." Accordingly, it reiterated the rule that "the right to vend is exhausted by a single, unconditional sale, the article sold being thereby carried outside the monopoly of the patent law and rendered free of every restriction which the vendor may attempt to put upon it.[172]

The importance of this line of patent exhaustion cases is that in 2008, the Supreme Court affirmed their vitality in a unanimous opinion. So, while the Supreme Court has found all manner of contractual restrictions on the sale and use of a tangible thing embodying a copyrighted or patented invention invalid, some software and music CD distributors believe that they have found a magical restriction that can avoid this problem. By adding a contractual restriction that claims to reserve title in the tangible object itself, while allowing every other feature of the transaction to look like a sale (or vending) they believe they have avoided over a century of Supreme Court precedent and Congressional policy. The only thing more surprising than the fact of this hubris is the success they have had in persuading courts to fall for it.

C. Must Respect Congressional Choices.

Software manufacturers have invented a new form of publishing software that they have named "licensing" and because of alleged essential differences between software and other forms of copyrighted works, seek a special dispensation from the courts to treat the transactions they engage in as immune from the first sale doctrine. Even if software is uniquely situated with respect to its methods of distribution, this is not a determination for the courts to make. As the Supreme Court has written, "Sound policy, as well as history, supports our consistent deference to Congress when major technological innovations alter the market for copyrighted materials.

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172 *Quanta Computer, Inc. v. LG Elecs., Inc.*, 128 S. Ct. 2109, 2116 (2008).

Congress has the constitutional authority and the institutional ability to accommodate fully the varied permutations of competing interests that are inevitably implicated by such new technology."[173] This judicial deference to Congressional policy choices should be reflected in at least two ways that are often neglected in discussions of copy ownership: whether contractual provisions that seek to subvert the limitations and exceptions articulated in §§ 107 through 122 are federally preempted and whether an approach to determining copy ownership could be used that would preserve the national uniformity copyright law seeks.

1. **Must recognize the limiting role played by Sections 107 through 122 and examine whether contrary contractual provisions are federally preempted.**

The rights of copyright enumerated in 17 U.S.C. § 106 are "Subject to sections 107 through 122..."[174] This language sets up a structure through which a list of the rights of copyright will be enumerated in § 106, but the precise scope of those rights can only be determined by reading § 106 in conjunction with the limitations and exceptions in §§ 107 through 122.

When one of these limitations is found to apply, it does not represent an "excused" infringement of a § 106 right, but rather indicates that the § 106 right at issue never extended that far to begin with. Congress has carefully chosen the contours of these rights and courts should raise doubts about the ability of one party to a typically un-negotiated contract of adhesion between parties of unequal bargaining power to re-draw these lines that Congress has chosen. At a minimum, it seems an erroneous approach to look at whether an agreement purports to limit the permissions given with respect to these rights of copyright in an effort to determine whether the licensee has rights Congress put beyond the control of the copyright holder to begin with.

The point may be best expressed by way of an example from another context. Imagine if we tried to determine whether individuals could make a fair use of a work under § 107 by looking to any agreements accompanying the copyrighted work to see if there were terms in the agreement that restricted the recipient's fair use rights or permissions with respect to copying, modifying, or distributing the work generally. It would be a bizarre methodology that would entitle every copyright holder to simply do away

173 *Sony Corp. of Am. v. Univ. City Studios, Inc.*, 464 U.S. 417, 431 (1984).
174 17 U.S.C. § 106.

with the fair uses of his work by fiat. We would never accept that Congress could have intended that result.[175] Nonetheless, courts routinely accept a similar methodology when trying to determine if individuals have first sale rights under § 109 or "essential copy" rights under § 117. We might get better results if we thought of § 109 and § 117 as specific fair uses that Congress felt so important that it decided to articulate them separately, rather than simply relying on § 107 to cover these cases. Seen through that lens, the approaches taken by many courts on this issue leave much to be desired.

A full discussion of whether such contractual arrangements are federally preempted is beyond the scope of this article. I would just say briefly that when the *Step-Saver Data* court provided its useful history of how the software industry came to "license" but not sell copies of its works in an effort to avoid the reach of the first sale doctrine, it noted that, "Questions remained, however, as to whether the use of state contract law to avoid the first sale doctrine would be preempted either by the federal copyright statute (statutory preemption) or by the exclusive constitutional grant of authority over copyright issues to the federal government (constitutional preemption). (citations)"[176]

But while the rental of software that concerned the industry was addressed by Congress, the courts have not seriously taken up the other questions posed by the *Step-Saver Data* court, as none of the courts to address this issue have a substantive discussion of federal preemption and only a handful mention it at all.[177]

Courts have, in the past, found the scope of federal preemption to be quite broad in the copyright context. The Supreme Court wrote,

> These [patent and copyright] laws, like other laws of the United States enacted pursuant to constitutional authority, are the supreme law of the land. When state law touches upon the area of these federal statutes, it is "familiar doctrine" that the federal policy "may

175 It would also raise constitutional issues under the First Amendment, but those are not my focus here. [cite to literature discussing ability or lack thereof to contract away one's fair use right]

176 *Step-Saver Data Sys. v. Wyse Tech.*, 939 F.2d 91, 96 (3d Cir. 1991).

177 *SoftMan Prods. Co. v. Adobe Sys.*, 171 F. Supp. 2d 1075, 1083 fn 10 (C.D. Cal. 2001) (citing *Step-Saver*); *Foresight Resources Corp. v. Pfortmiller*, 719 F. Supp. 1006, 1010 (D. Kan. 1989) (citing *Vault*); *Vault Corp. v. Quaid Software, Ltd.*, 847 F.2d 255, 269-270 (5th Cir. 1988).

> not be set at naught, or its benefits denied" by the state law.[178]

and other courts have noted that,

> [E]ven apart from Section 301, the general proposition pertains in copyright law, as elsewhere, that a state law is invalid that "stands as an obstacle to the accomplishment of the full purposes and objectives of Congress."[179]

The precise contours of this preemption can only begin to be determined if a court takes up the question of whether the license agreement it typically would take at face value "stands as an obstacle to the accomplishment of the full purposes and objectives of Congress" or "sets at naught" a federal policy embodied in the Copyright Act.[180]

2. Should preserve as far as possible the national uniformity copyright law seeks.

The Second Circuit in *Krause* provided an argument that it put forward as a reason against interpreting § 117(a) to require formal title, but which is also an argument against using an Agreement Controls approach to determining copy ownership. The court wrote,

> Several considerations militate against interpreting § 117(a) to require formal title in a program copy. First, whether a party possesses formal title will frequently be a matter of state law. See 2 Melville B. Nimmer & David Nimmer, Nimmer on Copyright § 8.08[B][1] (stating that copy ownership "arises presumably under state law"). The result would be to undermine some of the uniformity achieved by the Copyright Act. The same transaction might be deemed a sale under one state's law and a lease under another's. If § 117(a) required formal title, two software users,

178 *Sears, Roebuck & Co. v. Stiffel Co.*, 376 U.S. 225, 229 (1964); *but cf. Bonito Boats v. Thunder Craft Boats*, 489 U.S. 141, 165 (1989) ("[W]here "Congress determines that neither federal protection nor freedom from restraint is required by the national interest," (citing *Goldstein*) the States remain free to promote originality and creativity in their own domains."). The question courts should address is whether Congress, in enacting §§ 107 through 122 has determined that these limitations are among those within the national interest that cannot be set at naught. Unfortunately, courts have done too little to develop this line of inquiry. [cite Nimmer, Contract into Expand?]

179 *Facenda v. N.F.L. Films, Inc.*, 542 F.3d 1007, 1028 (3d Cir. 2008) (citing Nimmer on Copyright § 1.01[B][3][a].).

180 cite Nimmer.

> engaged in substantively identical transactions might find that one is liable for copyright infringement while the other is protected by § 117(a), depending solely on the state in which the conduct occurred. Such a result would contradict the Copyright Act's "express objective of creating national, uniform copyright law by broadly preempting state statutory and common-law copyright regulation."[181]

If we must look to the agreement to determine ownership of title, then we must invariably interpret that agreement. Courts that believe they must interpret an agreement, after looking to its governing law clause, are prone to adopt the interpretative canons of construction of the state found in the governing law clause and such a practice leads us directly into the inconsistencies the *Krause* court feared.[182] Other courts have complained that the U.C.C. provides no better guidance.[183] And since this is not merely an inconvenience but a means of subverting one of the goals of Congress in enacting the Copyright Act, we should have a strong preference for any interpretative approach that would avoid this problem. The Perpetual Possession approach, by focusing almost exclusively on the term of possession, provides an approach that does not pose such conflicts with the Congressional will.

D. Would Hopefully Make Sense.

As I have argued above, the law in the area of copy ownership is currently in disarray and it often appears that courts are uncertain what approach to take to the question and what precedents to follow. Additionally, the courts can produce results in these cases that are at odds with consumer expectations, especially if the rationales applied in some cases were applied across all categories of copyrighted works. As counsel for MDY asserted during oral argument, "a person who purchases a copy of the WoW game client software from a commercial retailer and walks out of the store with the copy in hand certainly would not view himself as a mere licensee of what he just purchased. The person could dispose of the software copy as he chose, throwing it in the trash, giving it to a friend, or installing it on his computer – all consistent with ownership. "[184]

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181 *Krause*, 402 F.3d at 123 (citing *Community for Creative Non-Violence v. Reid*, 490 U.S. 730, 740 (1989) and 17 U.S.C. § 301(a).).

182 In the *CPU Distrib.* case, the court looked to Utah law. Other courts have looked to the canons of contract construction from other states. *See supra*, note ##.

183 *Applied Info. Mgmt. v. Icart*, 976 F. Supp. 149, 154 fn 2 (E.D.N.Y. 1997).

184 *MDY Indus.*, 89 U.S.P.Q.2d 1015, pincitation.

The Perpetual Possession approach avoids these problems by providing an approach that is easy for courts to apply and produces results that align with consumer expectations.

1. **Should, as far as possible, be consistent with settled consumer expectations.**

The general public would never stand for the terms found in "licensing agreements" if they were routinely applied to books, but the courts considering copy ownership issues routinely use approaches that would appear to apply to all copyrighted works equally, and which often enforce the most draconian of terms. If a different approach would reach results across all types of copyrighted works that did not upset settled consumer expectations, then that would be a strong reason to consider using that approach instead.

While courts are right to respect the freedom to contract, they fail in their duty if they do not also recognize its limits, especially in the context of copyright law, where Congress has crafted a "delicate balance" between the rights of copyright owners and copyright users.

2. **Would, ideally, be easy for courts to apply.**

The *Vernor* court's discussion of *MAI*, *Triad*, and *Wall Data*, illustrate that looking at restrictive terms in the agreements accompanying a copy has become a strange exercise in comparing restrictive terms in various agreements in which the following process occurs: if the agreement before the court seems more restrictive than one that another court held did not result in a transfer of title to the copy, then the court should hold likewise. For this approach to work, we have to believe that no prior court got it wrong and that we will be able to independently sort out any cases that arise where the restrictiveness of the provisions presented falls somewhere in between the restrictions in previous cases that were the most restrictive but that still constituted a sale and the least restrictive that still did not constitute a sale. It seems Pollyannaish to believe things will work out so neatly when in reality agreements will vary across multiple variables and with respect to each issue will have terms that are more or less restrictive than were found in any prior agreements considered. If courts follow such an approach much longer there will be enough conflicting opinions out there that no court faced with the question that believes it must rely on the agreement alone will have any useful guidance on how to proceed.

The Perpetual Possession approach, however, is easy for courts to apply. The only economic reality that a court need learn about a transaction is whether the recipient has a right to perpetual possession of the copy. The court could ask, "Is there any expectation that the possessor must return the copy after a period of time agreed upon in advance?"[185] The answer to this question should be dispositive in most cases. If not, one could ask, "If there was a payment, was it correlated to periods of use?" as such periodic payments can be indicative of a rental or leasing arrangement.

IV. How to Address *MDY Indus. LLC v. Blizzard Entm't, Inc.*

Purchasers of WoW pay a single amount up front for the client software and nothing in Blizzard's EULA or TOU reflect a requirement that WoW purchasers return the software to Blizzard after any specified period. It is theirs to keep, destroy, or give away for as long as they like. Under the Perpetual Possession approach, this leads to the conclusion that WoW purchasers are owners of their copies. As owners of copies, they are entitled, under § 117(a)(1), to make another copy of WoW, provided that such a new copy is created as an essential step in the utilization of WoW in conjunction with a machine and that it is used in no other manner.[186] When an owner of a copy of WoW runs WoW in conjunction with Glider, a RAM copy of WoW is created as an essential step in the utilization of WoW in conjunction with their computer and that RAM copy is used in no other manner. The creation of the RAM copy is an essential step in the utilization of WoW in conjunction with their computer, because the creation of RAM copies is an automated process that necessarily occurs in the utilization of any program. WoW simply could not be utilized at all in conjunction with a computer without the creation of a RAM copy, thus the creation of RAM copies are an "essential step" in the utilization of WoW in conjunction with a computer. The RAM copy is used in "no other manner" because using the RAM copy is the only way to use WoW in any manner in conjunction with a computer. The "no other manner" requirement seems motivated by an interest in preventing the creation of infringing copies and Glider is not a cracking or copying tool that enables infringement.[187]

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185 A term requiring return or destruction upon breach of the agreement would not be considered, because the aim is to understand the possessor's present rights, not the mere possible consequences that might be imposed if the agreement were breached.

186 17 U.S.C. § 117(a)(1).

187 The interpretation of each of the elements of § 117 are adeptly addressed at length in *Krause*, 402 F.3d at 125-130.

Thus, if WoW users were entitled to make RAM copies of WoW under § 117, then even if such users breached their agreement with Blizzard with respect to using bots, they were not direct infringers of Blizzard's copyright, and hence MDY Indus. is not liable for secondary infringement. This result is reasonable because it is profoundly odd that assisting someone to break the rules of a game would constitute secondary copyright infringement.

No one likes cheaters, but Blizzard has alternative methods of dealing with bots, and could adopt both a "carrot and a stick" approach. It could offer the carrot of creating alternative Battle.net server networks where bots are allowed and utilize the stick of continuing to terminate users who utilize bots on servers where they are not allowed. Blizzard also has the ability to terminate the Battle.net account of a user violating the terms of that service, forcing them to sacrifice the remainder of the month's service already paid for, and could also cancel the authorization code that came with client software, forcing the user to purchase another copy of WoW in order to play again. The cost to users of new Battle.net accounts and new authentication codes would be a strong deterrent to repeat botting, especially where alternative networks existed where it was allowed.

V. Further Implications of the Perpetual Possession Approach.

[Intro]

A. Effects on Price Discrimination?

[Price discrimination is still possible where the transaction is a genuine rental or lease because § 109 does not apply to anyone who has acquired possession of the copy by rental or lease.[188] Thus, for any group, such as students, who one would like to offer a discount, but would not want them to be able to resell the copy to those outside the group, one simply has to structure the discounted transactions as genuine rentals or leases that require a periodic payment for possession and where any copies must be returned at the end of the rental or lease period.[189]]

188 17 U.S.C. § 109(d).

189 This approach could even be more lucrative for software distributors. For example. Microsoft Office "Home and Student 2007" for Windows is offered by Best Buy for $149.99 (compared to Microsoft Office Professional 2007 at $499.99) as of Jul. 16, 2009. If, instead of structuring the transaction so that the student purchaser has perpetual possession of the copy, Microsoft instead charged $60 per year to lease the software, with a requirement of returning the copy if the lease was not renewed, then a

B. Implications for a Digital First Sale Right?

[Adopting a perpetual possession approach to title determinations need not impact one's pre-existing views on a "digital" first sale doctrine, because such a doctrine will inevitably involve copies. Except in the circumstances where the tangible hard drive or iPod is itself sold along with all its contents, transferring a digitally-stored work will involve making a copy for the transferee. Section 109 only acts as a limitation on the publication right in § 106(3) and thus if a digital first sale right requires reproductions governed by § 106(1), then whether those are permissible can be settled independent of any method of determining title to copies for purposes of § 109.]

C. Changing Incentives for Software Distributors?

[Software distributors may be encouraged to engage in more leasing and hence may employ more DRM, kill-switches, phone-home features, or similar technical measures to attempt to enforce the lease period. At least some of these approaches are legal and some are in use presently, so this is not an insuperable obstacle for the industry. It is unlikely to be worse for users who, under a "licensing" regime already allegedly lack § 109 and § 117 rights. Under a leasing model they should at least expect lower upfront prices.]

D. Applicability to Cloud Computing?

[Cloud computing services are becoming ubiquitous. To the extent the end user never possesses a copy of the underlying software used to operate such services, the approach argued for here with respect to determining title to copies has no bearing. Many cloud services are currently offered at no cost, but even those where one pays a fee the expectation from the outset is that one is paying for a service for a specified time period and there is no expectation that one will be able to transfer the underlying software to another when you are done with it. Instead, when you have no further use for the service you simply stop making the periodic payments. No settled consumer expectations are thwarted here.]

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student who used the software through four years of high school or college would end up paying $240, an increase of 60% over the current approach. Software distributors also already have the technical capacity to use authorization codes and other methods to prevent continued usage beyond the lease period.

E. Effects on Open Source Licensing Schemes?

[Recipients of open source software are owners of their copies, because they have a right to perpetual possession. However, no open source licensor has ever suggested otherwise, and in fact, most open source licenses expressly disclaim any restrictions on the recipients use of the software, and expressly permit the recipient to modify it and distribute both the original and any modified versions to others. There is nothing about the proposed approach for determining title to copies that frustrates any of these licensing schemes.]

VI. Conclusion

To determine whether title to a copy has been transferred, courts should look to whether the transferee has a right of perpetual possession of the copy. This is the key factor that distinguishes sales and gifts on the one hand and leases and lending on the other. The invented notion of "licensing" software, where that means transferring perpetual possession of a copy but retaining title to the copy, is both incoherent and not found in the Copyright Act. Courts that look to the agreement accompanying a copy are focusing on the wrong factors for determining ownership of the copy, unless they stay focused on the right of perpetual possession, as the controlling precedents in both the Ninth and Second Circuits have done. Where other courts have gone astray, the *Augusto* and *Vernor* courts have found the correct path and demonstrated an approach that is logical, that respects controlling precedent and Congressional choices, and that is easy to apply yielding results that square with settled consumer expectations. Thus the *Augusto* and *Vernor* opinions show us not only how to resolve *MDY Indus.*, but the question of copy ownership in all future cases.