

BUYER BEWARE: THE THREAT TO THE FIRST SALE DOCTRINE IN THE DIGITAL AGE

By Adam W. Sikich

The rise of digitally transmitted content such as eBooks, mp3s, and digital movies has threatened traditional notions about whether consumers actually own what they buy, and whether they will be entitled to resell or otherwise dispose of their downloaded purchases as they please. Buyers' rights derive from the First Sale Doctrine of copyright law, which is a statutory principle that states that a copyright owner's exclusive right to distribution of a copy of a work ends with the lawful initial transfer of that copy. Under this doctrine, any "owner of a particular copy" of a copyrighted work may freely sell or transfer that copy regardless of whether the copyright owner approves. While the doctrine has been a fixture in society for nearly a century and has helped foster everything from second-hand bookstores to eBay and is well-established with respect to tangible works, the law has not been updated to account for the rise of digitally transmitted intangible works.

BACKGROUND ON THE FIRST SALE DOCTRINE

The doctrine was first articulated in 1908, in the US Supreme Court decision *Bobbs-Merrill Co.*

v. Straus,¹ a case that concerned the scope of rights accorded owners of copyright. Specifically, the issue was whether copyright law permits an owner to control a purchaser's subsequent sale of a copyrighted work. In this case, the publisher, in an attempt to circumvent the statutory requirement of a "sale," placed a notice in the cover of the book stating that any sale for less than one dollar would amount to copyright infringement.² While the publisher

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attempted to create a license with the purchaser and control the resale of the book, the court held that the publisher's note did not constitute a license agreement and the exclusive right to "vend" applies only to the initial sale.³ In other words, the statutory right to sell did not also create a right to limit resale.

Congress codified this principle in the 1909 Copyright Act and subsequently broadened the doctrine in the 1976 Copyright Act to include any "owner" of a lawfully made copy or phonorecord (recorded music) regardless of whether it was first sold to that subsequent owner:

[T]he owner of a particular copy or phonorecord lawfully made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord.⁴

The law also states, however, that the doctrine does not apply when possession of the copy occurs through "rental, lease, loan, or otherwise, without acquiring ownership of it," unless the copyright owner authorizes it.⁵ Taken together, Sections 109(a) and 109(d) establish that the determining factor applicable to the doctrine is whether the recipient rightfully owns a copy of the work. The statute further defines the word "copy" as follows:

[M]aterial objects, other than phonorecords, in which a work is fixed by any method now known or later developed, and from which the work can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device. The term "copies" includes the material object, other than a phonorecord, in which the work is first fixed.⁶

It should be noted that the 1976 revision applies not only to subsequent sales by the owner of the copy, but also to lending, such as with libraries. As reflected in the legislative history of the 1976 Act, "[a] library that has acquired ownership of a copy is entitled to lend it under any conditions it chooses to impose."⁷ While the doctrine limits the distribution right guaranteed to copyright owners by law by

acting as a defense to copyright infringement, it does not limit the other guaranteed rights of reproduction, public display, public performance, and the creation of derivative works.

This statutory framework traditionally has worked well where copies appear in a material object such as a printed book, a movie DVD, or a music CD, but it does not work as well when the works are digitally transmitted, because of the legal uncertainty as to whether the doctrine applies to transactions that lack a material copy changing hands.

THE CURRENT MARKET REALITY

Digitally transmitted content delivery has risen in popularity within the last 10 years as copyright owners explore economical means by which to generate revenue and consumers look for increased convenience and choices. One need look no further than Apple's iTunes® music store, which this year surpassed 10 billion music downloads over its seven year history, to see how popular the digitally downloaded format has become.⁸

Given the lack of clarity as to whether the doctrine applies to digitally transmitted works and the doctrine's inapplicability to situations where possession but not ownership of a copy of the work occurs, copyright owners have increasingly implemented license agreements in order to impose restrictions on the use and transferability of digital works. In some cases, the owner attempts to retain full dominion over distribution rights,⁹ by crafting a license that explicitly states that the licensee (consumer) obtains no ownership interest in the copy of the work. By way of example, three of the most popular online providers of eBooks, digital music, and other digital content—Amazon.com, BarnesandNoble.com, and Walmart.com—have terms of use that explicitly prohibit the transfer of digital content purchased through their respective Web site to another user.¹⁰

In some situations, the control retained by the copyright owner or authorized distributor far exceeded restrictions on future use by deleting the work from the consumer's possession when circumstances warranted it. The most famous example of this occurred in 2009 when Amazon.com remotely removed digital copies of the classic George Orwell novels *1984* and *Animal Farm* from Kindle users' devices after Amazon.

com learned that it did not have sufficient rights to offer digital versions of those novels.¹¹ Amazon.com acted in accordance with its terms of use in effect at the time and took the extreme step of deletion to avoid litigation with Orwell's publisher.

THE NINTH CIRCUIT THROWS A CURVEBALL

Understandably, confusion has resulted from the licensing practices of copyright owners who appear to use contract law to circumvent the doctrine. As a result, the law is in flux and buyers are frustrated. These tensions are exemplified by the recent US Court of Appeals for the Ninth Circuit decision of *Vernor v. Autodesk*.¹² Although this case involved material copies of CD-ROM software rather than digital delivery, the *Vernor* court importantly held that extensive restrictions contractually imposed on the use of a material copy of software trumps the First Sale Doctrine. This decision is significant because it broke from the tradition of courts dating back to *Bobbs-Merrill* that upheld the applicability of the doctrine to the transfer of a material copy of a work even when the copyright owner attempted to couch the transaction as a license rather than a sale.¹³

In *Vernor*, Autodesk, Inc. distributed software pursuant to a limited software license agreement (SLA) whereby Autodesk retained title to the software copies and imposed use and transfer restrictions on its customers (e.g., prohibiting the renting, leasing, or transferring of the software without Autodesk's prior consent).¹⁴ Autodesk also called for termination of the license if the SLA restrictions were violated.¹⁵ The SLA had to be accepted prior to installing the software,¹⁶ and Autodesk assigned serial numbers and activation codes to copies of the software and tracked registered licensees.¹⁷

Vernor bought used copies of Autodesk's software from a customer of Autodesk, and then put the copies up for sale on eBay.¹⁸ Vernor was aware of the SLA, but, importantly, he never agreed to its terms nor installed the software.¹⁹ After Autodesk notified eBay that those sales were not permitted, Vernor filed a declaratory judgment action requesting that the court rule that his actions were non-infringing due to the First Sale Doctrine. Autodesk moved to dismiss and sought summary judgment.

The district court deemed Vernor's acquisition of the software as a transfer of possession rather than a license; therefore, the doctrine applied and Vernor was not liable for infringement. Citing the prior Ninth Circuit decision *United States v. Wise*,²⁰ a case which dealt with the transfer of movie prints pursuant to distribution agreements, the district court held that labeling something a license is not determinative because *Wise* dictated that all of the circumstances of the transaction must be analyzed, and in this case, the fact that Vernor made a one-time payment for the software rather than paying recurring royalties and acquired an implied right of perpetual possession favored the finding of a sale/transfer.²¹

On appeal, however, the Ninth Circuit viewed the case differently. Downplaying the district court's focus on Vernor's one-time payment for the software and the fact that Vernor was not required to relinquish possession, the Ninth Circuit vacated and remanded and held that the high level of specificity on the license restrictions made Vernor a licensee rather than an owner of the software copies. In addition to a discussion of *Wise*, the Ninth Circuit looked at three of its prior software cases, the "MAI trio," that also addressed the issue of owner versus licensee.²² Based on *Wise* and the MAI trio, the Ninth Circuit developed a three-factor test to determine whether a software user is a licensee rather than an owner, and therefore, whether the user was entitled to invoke the doctrine:

1. Has the copyright owner specified that the user is granted a license;
2. Has the copyright owner significantly restricted the user's ability to transfer the software; and
3. Has the copyright owner imposed notable use restrictions?²³

Because Autodesk's SLA specifically reserved title to the copies of the software and imposed substantial transfer and use restrictions, the Ninth Circuit determined that Autodesk's customers, including Vernor even as a subsequent purchaser and reseller, were licensees rather than owners.²⁴ Accordingly, the sale of the software to Vernor by the original licensee, which was prohibited by the SLA, was invalid. Thus, Vernor and Vernor's customers were not owners of their copies of the software.

The Ninth Circuit remanded the matter for further proceedings. Notably, the court acknowledged the policy considerations and the potential impact that its decision may have on the distribution of works. On the one hand, a customer's ability to possess a copyrighted work indefinitely should not in itself compel a finding of a first sale, because often there is no way for a consumer to return the copy to the copyright owner. However, on the other hand, judicial enforcement of software license agreements, which often are contracts of adhesion, could eliminate the software resale market. Moreover, these practices could be adopted by other copyright owners such as book publishers, record labels, and movie studios.²⁵ Ultimately, the Ninth Circuit decided to leave the policy considerations to Congress to sort out.²⁶

The release of the *Vernor* decision sent shockwaves throughout the blogosphere and within the software, publishing, and entertainment industries because of the apparent shift from established case law. If the *Vernor* decision stands,²⁷ the movie, music, and publishing industries, among others, will have more incentive to expand on license-based content delivery, because *Vernor's* three-pronged test to determine whether or not the doctrine applies creates a low threshold that copyright owners would need to meet in order to preclude the application of the doctrine.²⁸

Further clarity on the future of the doctrine may come in the form of another case that also happens to be before the Ninth Circuit: *UMG Recordings, Inc. v. Augusto*.²⁹ This case involves Augusto's sale of promotional CDs that UMG provided to music industry insiders.³⁰ The CDs at issue contained a label that included language stating that the CD was for promotional use only and not for sale, with some labels containing more detailed usage restrictions.³¹ Augusto purchased these CDs from music stores and online auctions, and then resold them on eBay.³² UMG sued for copyright infringement and Augusto asserted the doctrine as a defense, arguing that UMG's distribution of the promotional CDs to industry insiders amounted to a gift, not a license.³³ Looking at the "economic realities of the transaction," the district court held that the doctrine applied because UMG made no attempt to regain possession or derive any continued benefit.³⁴ But given that UMG is also in the Ninth Circuit, it will be very interesting to see

how the case fares on appeal in light of the Ninth Circuit's new *Vernor* test.

POST-VERNOR REALITY

Post-*Vernor*, some groups have real concerns about the application of the First Sale Doctrine to their industry. Despite the legal support that the *Vernor* decision gives to expand the licensing culture in copyright transactions, copyright owners will have to weigh those arguments against practical and financial considerations. Libraries have relied on the doctrine as the basis by which they lend books, magazines, CDs, movies, and other copyrighted material, so there is concern among library associations that the widespread adoption of restriction-heavy licenses could hinder the dissemination of knowledge if those licenses are allowed to dictate the conditions upon which libraries can lend works, including but not limited to controlling the library's circulation window of a work.³⁵

The fear of adverse change also is present in commercial resale sectors where companies like eBay have flourished by facilitating the buying and selling of secondhand goods, many of which are copyrighted works.³⁶ Copyright owners likely would be more willing to implement restrictions on resale in a commercial context rather than with libraries because of the commercial interest in increasing profits by retaining ownership and restricting third party sales that would not benefit the original owner.

Change also may come in the home video market where the entire business model of purchasing large quantities of DVDs from movie distributors and then renting them to consumers relies on the First Sale Doctrine. If movie distributors are able to contractually restrict what consumers and would-be resellers do with their copies of movies, then they could conceivably put companies such as Netflix® and Redbox® (the DVD kiosk rental company) out of business and target the consumer home market directly via video-on-demand or streaming via Internet portals such as Hulu.com.

Even within the software industry, where courts such as *Vernor* have shown a proclivity to support restrictive licensing, consumers are increasingly accessing software via Internet download or cloud computing rather than via a CD-ROM or floppy disk, so it is even less likely that the doctrine would remain viable for those types of works.

It is difficult to predict whether the fear of wide-scale restrictive licensing in the delivery of copyrighted content will be realized. In fact, it is possible that a business model may be created that would support the resale of digitally transmitted works to the delight of copyright owners and consumers alike. However, whether or not any of these scenarios occur does not change the questions that remain about the viability of the doctrine for digitally transmitted works.

HOW TO MODERNIZE THE DOCTRINE

The US Copyright Office and Congress are long overdue in addressing the modernization of the doctrine. The US Copyright Office has not taken a serious look at the doctrine since the year 2000 when it requested public comment on various issues relating to digital works and the doctrine. Some of its questions included:

- Should the First Sale Doctrine be expanded in some way to apply to digital transmissions? Why or why not?
- Does the absence of a digital First Sale Doctrine under present law have any measurable effect (positive or negative) on the marketplace for works in digital form?
- To what extent, if any, is the First Sale Doctrine related to, or premised on, particular media or methods of distribution?
- To what extent, if any, does the emergence of new technologies alter the technological premises (if any) upon which the First Sale Doctrine is established?³⁷

After a few rounds of comments, the US Copyright Office issued its resulting Report to Congress Pursuant to Section 104 of the Digital Millennium Copyright Act DMCA Section 104 Report (DMCA Report), in August 2001.³⁸ In its report, the US Copyright Office decided that no change to the doctrine was needed at that time. Despite its unfortunate conclusion, the public comment process led to many interesting proposals as to how to fix the doctrine. One proposal, by the “Library Associations” (which was a coalition made up of the American Library Association, American Association of Law Libraries, Association

of Research Libraries, Medical Library Association, and Special Libraries Association), tackled how to address works that are only accessible in digital form. Their proposal would have amended 17 U.S.C. § 109(a) as follows:

[N]otwithstanding the provisions of section 106(3), the owner of a particular copy or phonorecord lawfully made under this title, *or the owner of any right of access to the copyrighted work*, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy, phonorecord, *or right of access*.

The DMCA Report also referenced the feasibility of what is known as “forward-and-delete” technology. Under forward-and-delete technology, a work would not be simultaneously accessible on both the sender and the recipient’s computer or media device, so the transaction would not invoke the copyright owner’s exclusive rights of reproduction.³⁹ Because the file would no longer be within the sender’s possession following the transmission, proponents of implementing forward and delete argue that this is the legal equivalent of giving, lending, or selling a material copy in a fixed form. The US Copyright Office refused to embrace the forward-and-delete approach because it concluded that the technology was not readily available at the time.⁴⁰

Congress has been nearly as inactive on the issue of the First Sale Doctrine. Surprisingly, there have been no Congressional bills introduced on the First Sale Doctrine since 2003. At that time, Senator Sam Brownback introduced legislation that embraced the forward-and-delete approach.⁴¹ Years earlier, Congressman Rick Boucher introduced a slightly different attempt to modernize the doctrine, but his version broadened the scope of the doctrine by invoking not only the rights of distribution and reproduction, but also the rights of performance and display. Also, Boucher’s version used the less definitive language “erases or destroys his or her copy or phonorecord at substantially the same time” instead of the more precise “forward-and-delete” language.⁴²

In this author’s opinion, a combination of the proposals from the Library Associations and Senator Brownback will best serve the doctrine in today’s

society because the combination addresses both the “particular copy” issue and the reproduction right dilemma. Accordingly, I propose the following amended 17 U.S.C. § 109(a):

[N]otwithstanding the provisions of section 106(3), the owner of a particular copy or phonorecord lawfully made under this title, or the owner of any lawful right of access to the copy-righted work, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy, phonorecord, or right of access so long as the technology used by that person to transmit the copy, phonorecord or right of access automatically deletes the work contemporaneously when transmitting the copy.

This proposal is the closest to addressing the current market realities while respecting the intent of the doctrine as it has existed for nearly a century. The technology that is available today is more advanced than the technology available 10 years ago, and if forward-and-delete becomes law then the legislative mandate should create an overnight market demand for such technology. In fact, forward-and-delete technology could even foster a new wave of digital rights management (DRM) technology,⁴³ but instead of the restrictive controls in existing DRM technology that frustrates consumers, this new wave could actually be *pro-consumer* by facilitating the resale of digitally transmitted works.

CONCLUSION

Modifying a longstanding bedrock of copyright law such as the First Sale Doctrine is not likely to come easy. Nevertheless, unless changes are made, the tension between copyright owners and consumers is likely to grow as copyright owners continue to push the limits of restrictive access to content. Ensuring proper protections for copyrighted works developed and distributed through exciting new platforms must not come at the expense of a valued century-old doctrine that has allowed people to freely resell works in commerce, maintain the viability of our library system, and allow consumers to otherwise dispose of copies of works as they see fit.

NOTES

1. *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339 (1908).
2. *Id.* at 341.
3. *Id.* at 350.
4. 17 U.S.C. § 109(a). The “lawfully made under this title” language is at the heart of the recently decided US Supreme Court case *Costco v. Omega* whereby the Court split 4-4 and upheld the Ninth Circuit’s decision that the First Sale Doctrine does not apply to imported goods manufactured abroad. That issue is beyond the scope of this article.
5. 17 U.S.C. § 109(d).
6. 17 U.S.C. § 101.
7. H.R. Rep. No. 94-1476, § 109, at 79 (1976), as reprinted in 1976 U.S.C.C.A.N. 5659, 5693.
8. Paczkowski, John. “iTunes: 10 Billion Songs Sold in Less Than Seven Years.” *All Things Digital*, Feb. 24, 2010, accessed at <http://digitaldaily.allthingsd.com/20100224/apples-itunes-thanks-10-billion/> on October 13, 2010.
9. These licenses take the form of End User License Agreements (EULAs), click-through agreements (e.g., “by clicking here, I agree and understand to all of the foregoing terms”), or, in some instances, shrink-wrap agreements whereby the consumer “agrees” to the terms simply by breaking the package on the software.
10. See <http://www.amazon.com/gp/help/customer/display.html?nodeId=200144530&#content>, <http://www.barnesandnoble.com/nook/legal/index.asp>, and <http://mp3.walmart.com/store/eula.gsp>. Barnesandnoble.com does offer a “LendMe” feature that allows eBooks to be lent to another for 14 days before reverting back to the lender’s account. While the eBook is lent, it is not available to the lender. See http://www.barnesandnoble.com/include/terms_of_use.asp for more details.
11. Pogue, David. “Some e-books are more equal than others,” *New York Times*, July 17, 2009, accessed at <http://pogue.blogs.nytimes.com/2009/07/17/some-e-books-are-more-equal-than-others/> on October 11, 2010. The parties eventually settled.
12. *Vernor v. Autodesk*, No. 09-35969 (9th Cir. 2010).
13. See *Krause v. Titleserv, Inc.* 402 F.3d 119 (2d Cir. 2005) (defendant, former employer of plaintiff software developer, was deemed the owner of software program because defendant paid substantial consideration for development of the software, software resided on defendant’s computers, and plaintiff allowed defendant to permanently use the software); *DSC Commc’ns Corp. v. Pulse Commc’ns, Inc.*, 170 F.3d 1354 (Fed. Cir. 1999) (“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”); *Softman Products Co. v. Adobe Systems Inc.*, 171 F.Supp.2d 1075 (“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”); *Novell, Inc. v. CPU Distrib., Inc.*, 2000 U.S. Dist. Lexis 9975 (S.D.Tex.2000) (transaction involving software was a sale despite copyright owner’s attempts to label it as a license).
14. *Vernor* at 13866.
15. *Id.* at 13867.
16. *Id.* at 13866.
17. *Id.*
18. *Id.* at 13865.
19. *Id.* at 13868.
20. *United States v. Wise*, 550 F.2d 1180 (9th Cir. 1077).
21. *Id.* at 13879.
22. The MAI trio consists of *MAI Sys. Corp. v. Peak Computer, Inc.*, 991 F.2d 511 (9th Cir. 1993); *Triad Sys. Corp. v. Se. Express*

- Co., 64 F.3d 1330 (9th Cir. 1995); and *Wall Data, Inc. v. Los Angeles County Sheriff's Dep't*, 447 F.3d 769 (9th Cir. 2006). Each case involved the essential step defense codified in 17 U.S.C. § 117(a)(1), which requires a similar analysis to Doctrine cases because both defenses require the possessor to own the copy of the work rather than license it.
23. *Id.* at 13878.
 24. *Id.* at 13880.
 25. *Id.* at 13885–13886.
 26. *Id.* at 13886.
 27. Vernor's attorneys filed a petition for *en banc* review to bring the case before the entire panel of Ninth Circuit judges.
 28. This could be true at least within the jurisdiction of the Ninth Circuit (Alaska, Arizona, California, Guam, Hawaii, Idaho, Montana, Nevada, Northern Mariana Islands, and Oregon); nevertheless, other Circuits may decide to adopt its holding.
 29. *UMG Recordings, Inc. v. Augusto*, 558 F. Supp. 2d 1055 (C.D. Cal. 2008). Other circuits have not been as active on the First Sale Doctrine as the Ninth Circuit.
 30. *Id.* at 1058.
 31. *Id.*
 32. *Id.*
 33. *Id.* at 1060.
 34. *Id.* at 1062.
 35. See, generally, Brief of Amici Curiae, American Library Association *et al.* at 7-9, *Vernor v. Autodesk, Inc.*, No. 09-35969 (9th Cir. 2010).
 36. eBay touts that in 2009 the total worth of goods sold on eBay was \$60 billion. "Who We Are," eBay Web site, <http://www.ebayinc.com/who>, accessed Sept. 21, 2010.
 37. Report to Congress Pursuant to Section 104 of the Digital Millennium Copyright Act, Request for public comment, 65 Fed. Reg. 35673 (June 5, 2000).
 38. Report to Congress Pursuant to Section 104 of the Digital Millennium Copyright Act DMCA Section 104 Report (U.S. Copyright Office, August 2001). Available at <http://www.copyright.gov/reports/studies/dmca/sec-104-report-vol-1.pdf>.
 39. Recall that the first sale Doctrine explicitly refers only to Section 106(3) of the Copyright Act, which is the provision concerning the exclusive right of distribution.
 40. DMCA Section 104 Report, P. 98 (U.S. Copyright Office, August 2001). Available at <http://www.copyright.gov/reports/studies/dmca/sec-104-report-vol-1.pdf>.
 41. Consumer, Schools, and Libraries Digital Rights Management Awareness Act of 2003, S.1621 (108th Congress). Accessed via THOMAS at <http://thomas.loc.gov/cgi-bin/query/z?c108:S.1621>.
 42. Digital Era Copyright Enhancement Act, H.R. 3048 (105th Congress).
 43. DRM refers to access control technologies that rights holders and computer and electronics manufacturers use to limit how digital works and devices are used.