

ISSUES IN SOFTWARE LICENSING AND COPYRIGHT

- I. Some Differences Between Standard Literary Works and Computer Programs
 - A. Standard works *say something*
 1. Provide information, a public good, through copies. Information is nonrival (for any given level of production, the marginal cost of providing it to an additional person is zero) and nonexclusive (additional people cannot be excluded from consuming it).
 - a. Provide entertainment through copies
 2. Initial copy provides full value to possessor. No need for additional copies in order for possessor to obtain full value.
 - a. No need for license of any of exclusive rights of copyright owner (CO)
 3. Prior to electronic age, non-negligible marginal cost for additional copy.
 4. Copy necessary to obtain full value, so number of copies some measure of value obtained
 - B. Computer programs *do something* in a machine. “Software is a machine whose medium of construction happens to be text.” (R. Davis, 1992)
 1. Not a public good. Some informational value, but not in executable form.
 2. No value obtained by possessor from initial copy unless additional copy or copies made
 - a. So need license of CO’s exclusive reproduction right unless provided by statute
 3. Product of electronic age. Easy to make additional copies and thereby get full value for others
 4. Additional copies not always necessary to obtain full value, so number of copies not necessarily a measure of value obtained
 - C. Much copyright law relating to computer software reflects this mismatch between traditional purpose of copyright law and purpose of computer software (despite software’s important role in promoting “the Progress of Science” under U.S. Const., Art. I, § 8, cl. 8)

II. Sales and Licenses of Software and Copies

A. Why are copies of software not sold but licensed?

1. To avoid first sale doctrine, control further transfer of copy
2. To specify and limit scope of use (and so of necessary copying)
3. To avoid application of law of sales
4. To permit addition of contractual terms

B. Possibilities

1. Sale of copy and no license. Owner of copy has rights under §§ 109 and 117 but no other § 106 rights.
2. Sale of copy and license of software. Owner of copy has rights under §§109(a) and 117). License may restrict or expand copying permitted under § 117.
3. License of copy and software. Licensee of copy has no rights under §§ 109(a) or 117(a). License determines rights both to copy and software.

C. License grant alternatives

1. License grant with conditions
 - a. Conditions precedent
 - i. Once conditions met, license effective
 - b. Conditions subsequent
 - i. Termination if conditions not met? Automatic or upon notice (and perhaps failure to cure)?
 - ii. *E.g.*, automatic license termination if software transferred?
2. License grant with additional covenants
 - a. Breach of covenants is not breach of condition, but material breach may permit termination of license agreement
3. Implied license
 - a. *Asset Marketing Systems, Inc. v. Gagnon*, 542 F.3d 748 (9th Cir. 2008) – provision of software under technical services agreement gave rise to implied unlimited nonexclusive license to use software

– implied license is granted when (1) someone requests creation of a work, (2) creator makes and delivers the work, and (3) creator intends that the -requestor copy and distribute work or, in the case of a computer program, use, retain and modify the work -- “relevant intent is the licensor's objective intent at the time of the creation and delivery of the software as manifested by the parties' conduct” -- license irrevocable because consideration was paid

- b. Similarly, *Intelligraphics, Inc. v. Marvell Semiconductor, Inc.*, No. 07-2499, 2009 U.S. Dist. LEXIS 9875 (N.D. Cal. Jan. 28, 2009)

III. First Sale Doctrine

A. *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339 (1908)

1. Applying pre-1909 copyright law
2. “. . . the copyright statutes . . . do not create the right to impose, by notice, such as is disclosed in this case, a limitation at which [copies of] the book shall be sold at retail by future purchasers, with whom there is no privity of contract.” (350)
3. In selling a copy, copyright owner (CO) “has exercise the right to vend.” (351)
 - a. CO owns the intangible copyright, buyer owns the tangible copy
4. Adding the right to control all future retail sales would extend a right under the statute “beyond its meaning” in light of legislative intent (351)
5. See, e.g., *Harrison v. Maynard, M. & Co.*, 61 F. 689 (2d Cir. 1894) (“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”); *Independent News Co. v. Williams*, 293 F.2d 510 (3d Cir. 1961) (first sale doctrine applies to comic books with covers removed sold to trash company that resold them)

B. Incorporated in 1909 Act and 1976 Act, 17 U.S.C. § 109(a)

1. Under § 109(a), “[n]otwithstanding the provisions of section 106(3),” (i) the “owner” of a copy (ii) “lawfully made under this title,” (iii) may “sell or otherwise dispose of the possession” of that copy
 - a. Copy may be freely transferred, but other legal restrictions remain, e.g., cannot hit someone with it, cannot make another copy from it

- b. Need not be a sale. Transfer of title so as to create ownership of copy, *e.g.*, by gift, sufficient, but must fully “dispose of” the copy, not, *e.g.*, rent it. § 117(b)
- 2. Limitation on CO’s exclusive right of distribution to the public. On first sale of copy, exclusive right of distribution is exhausted with respect to that copy.
 - a. CO benefit
 - i. Is paid for the copy
 - ii. Buyer’s or transferee’s obtaining value from the copy, by reading it, does not interfere with CO’s further exploitation of copyright
 - b. Buyer’s benefit
 - i. Obtains full value from the work by reading it, without need to copy it
 - ii. No restraint on buyer’s alienation of physical item or need for further negotiations before its transfer
 - iii. Able to obtain value by transferring copy.
 - (a) Permits more people to obtain value from work.
 - (b) To some extent, public good (nonrival) aspect of work.
 - c. Goldstein on first sale doctrine:
 - i. Contemplates that in case of lease or license, negotiation costs will be minimized because of continuing legal relationship and relatively short duration of lessee’s or licensee’s ownership, whereas in case of transfer of full ownership, absence of ongoing relationship and indeterminacy of possession of the copy will disable further agreements about transfers. II Goldstein (3d ed.) § 7.5 at 7:123.
 - (a) Emphasis on short duration of license relationship is questionable
 - ii. Assumes that copyright owner will recoup the costs of an authorized copy with its first sale. II Goldstein (3d ed.) § 7.5 at 7:124.

- iii. Rationale is that once copyright owner has transferred title to a copy, subsequent possessors should not have the trouble of negotiating with him when they contemplate a further transfer. If copyright owner wants to engage in further negotiation, he should lease or license the copy initially. II Goldstein (3d ed.) § 7.6.1 at 7:131.
- 3. Imported copies that would otherwise violate §§ 602(a) and 106(3)
 - a. § 602(a) provides that importation into U.S., without CO's authority, of copies acquired outside the U.S. is an infringement of the exclusive distribution right under § 106
 - b. *Quality King Distribs. v. L'Anza Research Int'l*, 523 U.S. 135 (1998) – § 109(a) defense applicable to copy made in the U.S., exported to authorized foreign distributor, sold abroad, imported into U.S. without authorization, sold in U.S. by unauthorized retailer – because scope of § 602(a) dependent on § 106(3), which is limited by § 109(a)
 - c. *Omega S.A. v. Costco Wholesale Corp.*, 541 F.3d 982 (9th Cir. 2008) – § 109(a) defense not applicable to copies not made in U.S., and so not “lawfully made *under this title*” (emphasis added).
 - i. *Certiorari* granted 4/19/10. Concern that decision would encourage making of copies outside U.S.
- C. Natural to say that copy is sold and software is licensed.
 - 1. But purpose of copy is only to obtain use of software, and use of software requires making additional copy(ies), so ownership of copy is worthless without right to make further copies, and issues cannot be separated.
 - 2. Need to balance (i) desire not to separate embodiment of copyrighted work from value to be obtained from it and to be fair to purchaser, (ii) statutory language crafted to deal with technical area, and (iii) risks to CO inherent in digital media.
- D. Decisions
 - 1. *Wall Data Inc. v. Los Angeles Cty. Sheriff's Dept.*, 447 F.3d 769 (9th Cir. 2006) -- two-part test for determining whether the purchaser of a copy of a software program is a licensee or an owner: generally, if CO (1) makes clear that it is granting only a license to the copy of the software, and (2) imposes significant restrictions on the redistribution or transfer of the copy, then transaction is a license, not a sale, and purchaser of the copy is a licensee, not an “owner” under § 117.

2. *UMG Recordings, Inc. v. Augusto*, 558 F. Supp. 2d 1055 (C.D. Cal. 2008) – title to promotional CDs sent to industry insiders passed to them despite label saying they were licensed for personal use only and remained the property of the record company and prohibiting sale – plaintiff did not intend to regain possession, no recurring benefit to plaintiff; only benefit of license to plaintiff would be to restrain trade; also constitute gifts under postal law, 39 U.S.C. § 3009
3. *Microsoft Corp. v. Big Boy Distrib. LLC*, 589 F. Supp. 2d 1308 (S.D. Fla. 2008) – first sale defense inapplicable to software manufactured outside U.S. since not “lawfully made under this title”

IV. Statutory Adjustments for Computer Programs

- A. As result of Computer Software Copyright Act of 1980, extra right of “owner of a copy of a computer program” to make (or authorize) another copy or adaptation provided that it is
 1. “created as an essential step in the utilization of the computer program in conjunction with a machine and that it is used in no other manner,” § 117(a)(1), or
 2. for archival purposes only, with all archival copies destroyed if continued possession of the program “should cease to be rightful,” § 117(a)(2)
 - a. Exact copies so made may be transferred, along with initial copy, only as part of transfer of all rights in program. § 117(b)
 - b. Adaptations so made may be transferred only with authorization of CO. § 117(b)
 3. Does “another” mean “one other” at a time?
 4. *Wall Data Inc. v. Los Angeles Cty. Sheriff’s Dept.*, 447 F.3d 769 (9th Cir. 2006) – department copied software by hard disk imaging (copying software from CD onto single “master” hard drive and from there onto other hard drives) onto 6007 machines while having license only for 3663, but said that configuration permitted access by only licensed number – jury rejected “essential step” defense – in challenge to jury instructions, court held that department was only licensee, not owner, of copies of software, so § 117(a) not applicable – even if it had been owner of copies, copying beyond licensed number was a matter of convenience, not “essential step” in use of software
- B. As result of Computer Software Rental Amendments Act of 1990, owner or possessor of copy of computer program may not, without authorization, for direct

or indirect commercial advantage, rent, lease or lend the copy, with narrow exceptions. § 109(b)(1)

C. As result of 1998 Computer Maintenance Competition Assurance Act (part of DMCA), right of an owner or lessee of a machine to make (or authorize) a copy of a computer program “solely by virtue of the activation of a machine that lawfully contains an authorized copy of the computer program, for purposes only of maintenance or repair of that machine,” if the copy is destroyed immediately thereafter, and no program not necessary for the activation is accessed or used other than to make the new copy by virtue of the activation. § 117(c)

1. Enacted in light of *MAI Systems Corp. v. Peak Computer, Inc.*, 991 F.2d 511 (9th Cir. 1993), so that those repairing computers could make certain temporary, limited copies while working on a computer.

2. *Storage Tech. Corp. v. Custom Hardware Eng'g & Consulting, Inc.* 421 F.3d 1307, *petition for rehearing denied*, 431 F.3d 1374 (Fed. Cir. 2005) (dubitante).

a. When Storage Tech’s tape library system is turned on, the Management Unit (MU) loads “9330” code into its RAM and the Control Unit (CU) loads “9311” code into its RAM. 9330 and 9311 code both consist of intertwined but distinct “functional code” and “maintenance code,” the latter of which diagnoses malfunctions and maintains performance of the MU and CU. Storage Tech licenses only the functional code, not the maintenance code, portion of the software to its customers. CHE repairs data libraries manufactured by Storage Tech. In order to diagnose problems, CHE intercepts and interprets error messages produced by the maintenance code. The messages are generated by the CU and sent to the MU. To ensure that the CU was configured to send the error messages, CHE had to override a password protection scheme, which (after initially using a different scheme) it did by attaching a device between the CU and MU that mimics a signal from the MU to the CU upon rebooting the CU, which causes the maintenance code on the CU to be configured to send the error messages. CHE then intercepts and interprets the error messages, on the basis of which it is able to diagnose and repair the data libraries. The maintenance code and functional code are both copied into the MU’s or CU’s RAM when the system is rebooted.

b. Crux of decision was conclusion that § 117(c) immunized copying of the maintenance code upon CHE’s rebooting of the system. First obstacle to that conclusion was that § 117(c)(1) requires that the copy be “made solely by virtue of the activation of a machine that lawfully contains an authorized copy of the computer program, for purposes only of maintenance or repair of that machine,” be “used

in no other manner and [be] destroyed immediately after the maintenance or repair is completed.” Although the maintenance code loaded into RAM after CHE rebooted the machine was not destroyed after CHE’s maintenance session but remained loaded, continuing to monitor the machine’s operation, the court found that although the “repair” was completed after CHE’s maintenance session, the “maintenance” was ongoing, including continued monitoring of the machine for problems. It was therefore sufficient, the court concluded, that CHE rebooted the machine at the end of its maintenance contract, thereby destroying the copy of the maintenance code in RAM.

- c. Second critical step was court’s conclusion that the maintenance code, as well as the functional code, was “necessary for the machine to be activated” under § 117(c)(2), because the maintenance code was inextricably intertwined with the functional code, so that both “need[ed] to be . . . loaded in order for the machine to be turned on,” H.R. Rep. No. 105-551, pt. 1, at 28. 421 F.3d at 1314. It found the fact that the maintenance code has “other functions,” such as diagnosing malfunctions, to be irrelevant, as was the possibility that Storage Tech might have written the maintenance code “as a separate, ‘freestanding’ program that would not have been needed to start the machine.”
- d. Court added, “To the extent that CHE's activities do not constitute copyright infringement or facilitate copyright infringement, StorageTek is foreclosed from maintaining an action under the DMCA. . . . That result follows because the DMCA must be read in the context of the Copyright Act, which balances the rights of the copyright owner against the public's interest in having appropriate access to the work.” 421 F.3d at 1318. It went on to state that even if there had been infringement, there would have been no violation of the DMCA, because the copying of the maintenance code into RAM upon rebooting takes place whether or not CHE’s device was used thereafter, so “there is no nexus between any possible infringement and the use of the circumvention devices.” Activation of the maintenance code may violate Storage Tech’s contractual rights, but “those rights are not the rights protected by copyright law.” 421 F.3d at 1319.
- e. Dissent opened by stating, “This court's opinion today destroys copyright protection for software that continually monitors computing machine behavior.” 421 F.3d at 1321. It noted, *inter alia*, that the maintenance code could be disabled with no effect on the operating system and was “incidental, not indispensable, to activation.” 421 F.3d at 1321. It also argued that CHE did not perform any maintenance or repair when it rebooted the system

and that CHE did not destroy the copy of the maintenance code after its service and repair session was completed. 431 F.3d at 1321-22. In response to the dissent and a petition for rehearing, the court issued another opinion denying the petition, emphasizing again that because of the way Storage Tech had written the maintenance code intertwined with the functional code, it must be loaded into RAM in order for the system to be activated. *Storage Tech. Corp. v. Custom Hardware Eng'g & Consulting, Inc.*, 431 F.3d 1374, 1376 (Fed. Cir. 2005).

V. License Conditions and Covenants

- A. *Graham v. James*, 144 F.3d 229 (2d Cir. 1998) – nonpayment of license royalties, due after software was turned over to licensee, constitutes breach of covenant, not condition, of license agreement -- presumption under New York law that contract terms are covenants, not conditions -- material breach entitles licensor to rescind license, but rescission requires affirmative step by licensor – so breach of contract but no copyright infringement
- B. *Jacobsen v. Katzer*, 535 F.3d 1373 (Fed. Cir. 2008)
1. Defendant breached terms of open source Artistic License by using parts of software (definition files) in its software without (i) including authors' names, (ii) copyright notices, (iii) references to files with terms of Artistic License, (iv) identification of original source of copied files (v) description of changes from the original
 2. Artistic License provides “The intent of this document is to state the conditions under which a Package may be copied” and notes that the rights to copy, modify, and distribute are granted “provided that” the conditions are met. Under California contract law, “provided that” typically denotes a condition.
 3. Court held that the “clear language of the Artistic License creates conditions to protect the economic rights at issue in the granting of a public license. These conditions govern the rights to modify and distribute the computer programs and files included in the downloadable software package. The attribution and modification transparency requirements directly serve to drive traffic to the open source incubation page and to inform downstream users of the project, which is a significant economic goal of the copyright holder that the law will enforce. Through this controlled spread of information, the copyright holder gains creative collaborators to the open source project; by requiring that changes made by downstream users be visible to the copyright holder and others, the copyright holder learns about the uses for his software and gains others' knowledge that can be used to advance future software releases.”

4. Thus using software while breaching conditions would constitute use outside scope of license and so copyright infringement.
- C. *MDY Indus., LLC v. Blizzard Entm't, Inc.*, 2008 U.S. Dist. LEXIS 53988, 89 U.S.P.Q.2D (BNA) 1015 (D. Ariz. 2008)
1. Blizzard's World of War software consists of "game client" software, purchased at store by user or downloaded from website, and "game server" software. After loading game client software on personal computer, user accesses the game server software through an online account for which he pays a monthly fee. Use of WoW is governed by EULA and TOU agreement, both shown when game client software is loaded and before online access. MDY's Glider software is a "bot" that plays WoW for its owner while the owner is away from his computer and thereby enables the owner to advance more quickly within WoW than would otherwise be possible.
 2. EULA grants "limited use license" to install game client software on one or more computers and use it in conjunction with online portion of game for non-commercial entertainment, says that use of game client subject to EULA and TOU. TOU § 4 titled "Limitations on Your Use of the Service." TOU § 5 titled "Rules of Conduct."
 - a. TOU § 4 prohibits, *inter alia*, users from intercepting, emulating, or redirecting the proprietary components of the game, from modifying files that are part of the game, from disrupting the game or others players' use of the game, and reserves Blizzard's exclusive right under § 106 to create derivative works.
 3. Court held that EULA, which says that users are bound by EULA and TOU, and TOU must be read together. TOU § 4 establishes limits on scope of license, and TOU § 5 contains independent contract terms
 4. Court found that users of Glider violate prohibition in § 4 against use of "bots" or any "third-party software designed to modify the [WoW] experience [.]" and that players who use Glider to mine WoW for game assets also violate § 4. "When WoW users employ Glider, therefore, they act outside the scope of the license delineated in section 4 of the TOU. Copying the game client software to RAM while engaged in this unauthorized activity constitutes copyright infringement."
 5. Court rejects reading of *Storage Technology* under which act that takes someone outside scope of license must be same act that constitutes copyright infringement. Moreover, here it is the same act: the act of using Glider, which involves copying the game client software to RAM.

6. Court rejects § 117 defense because WoW users are licenses, not owners, or their copies of the game client software, citing *MAI, Triad, Wall Data*. Applying two-part *Wall Data* test, EULA makes clear that only limited license of copies (and software) is granted, and restrictions placed on transfer of rights under EULA (transfer media, destroy all copies)
 7. Court declines to follow Vernor in following *Wise* rather than the MAI triad. Vernor applied § 109, not § 117, and *Wall Data* is binding precedent for § 117
- D. *Vernor v. Autodesk, Inc.*, 2009 U.S. Dist. LEXIS 90906, 93 U.S.P.Q.2D (BNA) 1336 (W.D. Wash. 2008) (earlier 2008 order at 555 F. Supp. 2d 1164)
1. Notes focus in *United States v. Wise*, 550 F.2d 1180 (9th Cir. 1977), dealing with first sale doctrine, on terms of license agreement, indicia of ownership vs. license of copy.
 - a. Non-dispositive indicia of license: reservation of title to CO, restrictions on transfer, requirement of return to CO after limited period, limited grant of rights of use, single up-front payment by transferee
 - b. Indicia of ownership: right to retain possession indefinitely, with no right of CO to regain possession (most important); failure to reserve title in CO
 - c. Neutral: requirement to destroy copy after use
 2. Under *Wise*, Autodesk copies were sold, not licensed
 3. Notes focus in MAI Trio, dealing with § 117, on deference to CO's characterization of transfer agreement as license: *MAI Sys. Corp. v. Peak Computer, Inc.*, 991 F.2d 511 (9th Cir. 1993); *Triad Sys. Corp. v. Southeastern Express Co.*, 64 F.3d 1330 (9th Cir. 1995); *Wall Data Inc. v. Los Angeles County Sheriff's Dep't*, 447 F.3d 769 (9th Cir. 2006).
 - a. Under MAI Trio, Autodesk copies would have been licensed.
 4. Text and legislative histories of §§ 109 and 117 lead to conclusion that "owner" has the same meaning in both.
 5. Given conflict among precedent, court held that it must follow oldest precedent, *i.e.*, *Wise*, so initial transaction was sale of copy.
 6. What about the difference between a film print and a computer program on a CD? Is that relevant to the distinction between sale and license?

VI. What difference does it make?

- A. Effect of *eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388 (2006) on ability to obtain preliminary injunction in case of copyright infringement
 - 1. *E.g., Salinger v. Colting* (2d Cir. 2010) (Docket No. 09-2878-cv, 4/30/10) -- *eBay* applies to preliminary injunctions in cases involving copyright infringement, so no presumptions of irreparable harm in case of copyright infringement
- B. *Jacobsen v. Katzer*, 609 F. Supp. 2d 925 (N.D. Cal. 2009)
 - 1. Insufficient evidence in the record to support a preliminary injunction -- no showing that Jacobsen suffered any actual harm or any continuing conduct that indicates future harm is imminent -- motion for preliminary injunction denied.
- C. Will the difference between copyright infringement and breach of contract make a difference in obtaining a preliminary injunction?