

## **Wise-ing up About the First Sale Doctrine:**

### **A Look at the Ninth Circuit's Approach to *Vernor v. Autodesk***

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#### **INTRODUCTION**

*Congratulations on purchasing your new computer software! Please ignore the paragraph of legal jargon and click the "I accept" button to prevent you from ever reselling this software. Do not worry if you have not even opened the box or never intend on using the software—the button is just for show.*

In today's evolving world of computer software and software licensing, complex copyright laws often conflict with the average consumer's understanding of everyday commercial transactions. What may appear to be a simple outright sale of software might turn out to be a complicated license, subject to myriad limitations and restrictions. This tension in copyright law is at the core of the Ninth Circuit's decision in *Vernor v. Autodesk*.<sup>1</sup> From the Copyright Act itself to the interpretations by the courts in *U.S. v. Wise* and the *MAI* Trio, the protections afforded to purchasers of copyrighted property are in a state of confusion.<sup>2</sup> By analyzing the Court of Appeals' recent decision in *Vernor*, this Note will show that the Court of Appeals' attempt to combine the standards of *Wise* and the *MAI* Trio did not accord with prior precedent and caused two problems in this area of the law. First, a change of this type disrupts the ability of businesses and consumers to adjust their practices in response to the law. Without clear explanations as to how and why the law has changed, manufacturers and consumers are left stumbling in the dark. Second, this move by the court only serves to further distance the balancing tests from the subjective experience of consumers and as a result may not adequately preserve the consumer protections inherent in the first sale doctrine. Only by capturing the consumer perspective can the law reflect the bargain struck at the time of purchase. By ignoring this bargain, the law would allow hidden legal jargon to rob consumers of the value of their purchases.

This Note will explore the Ninth Circuit's approach to the first sale doctrine and the case law concerning the dividing line between licenses and sales. Section I will

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1. *Vernor v. Autodesk, Inc.*, 621 F.3d 1102, 1105–07 (9th Cir. 2010).

2. *United States v. Wise*, 550 F.2d 1180, 1183–85 (9th Cir. 1977). The *MAI* Trio is a series of three cases: *Wall Data, Inc. v. Los Angeles Cnty. Sheriff's Dep't*, 447 F.3d 769 (9th Cir. 2006); *Triad Sys. Corp. v. Se. Express Co.*, 64 F.3d 1330 (9th Cir. 1995); and *MAI Sys. Corp. v. Peak Computer, Inc.*, 991 F.2d 511 (9th Cir. 1993).

discuss the background of the *Vernor* case. Section II will discuss the core of the first sale doctrine, the precedent relied upon in *Vernor* and the debate concerning the definition of an "owner." The discussion of ownership will address whether a consumer is protected by the first sale doctrine through an outright sale, or if the purchaser is merely a licensee who is unable to resell the copyrighted item without permission from the copyright holder. Sections III and IV will compare the conclusions of the *Vernor* District Court opinion and the *Vernor* Court of Appeals opinion to assess their differing interpretations of the case law. Lastly, Section V will address the first sale doctrine's consumer protection rationale, the lack of legal guidance given to manufacturers and consumers, and the glaring absence of the consumer perspective from the Court of Appeals' test.

## I. BACKGROUND

In March 1999, Autodesk, Inc. ("Autodesk") licensed ten copies of AutoCAD Release 14 software to Cardwell/Thomas & Associates, Inc. ("CTA").<sup>3</sup> CTA subsequently upgraded to the newer version of the AutoCAD software at a discounted price under the condition that CTA destroy the copies of the old software.<sup>4</sup> Instead of destroying them, CTA sold the copies to Timothy Vernor in April 2007.<sup>5</sup>

Vernor ran a business by selling items on eBay.<sup>6</sup> He purchased used copies of software in order to resell them to his customers.<sup>7</sup> There was no evidence or assertion that Vernor ever installed the software himself.<sup>8</sup> Prior to the purchase from CTA, Vernor purchased a used copy of AutoCAD from an unspecified seller at a garage sale and attempted to sell this first copy in 2005.<sup>9</sup> His initial sales effort was interrupted however when Autodesk issued a takedown notice under the Digital Millennium Copyright Act ("DMCA") alleging copyright infringement.<sup>10</sup> Vernor contested the notice and eBay reinstated the auction after Autodesk failed to respond.<sup>11</sup> After purchasing the CTA copies of AutoCAD, Vernor listed them on eBay for sale.<sup>12</sup> Autodesk again attempted to intervene.<sup>13</sup> Due to Autodesk's repeated claims, eBay temporarily suspended Vernor's account and interrupted his

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3. *Vernor*, 621 F.3d at 1105.

4. *Id.*

5. *Id.*

6. *Id.*

7. *Id.*

8. *Vernor v. Autodesk, Inc.*, No. C07-1189RAJ, 2009 WL 3187613, at \*1 (W.D. Wash. Sept. 30, 2009).

9. *Vernor*, 621 F.3d at 1105.

10. Under the DMCA, an amendment to Title 17 of the U.S. code, a takedown notice is a message sent to a service provider by a copyright holder, directing them to infringing material that should be removed. 17 U.S.C. § 512(c)(3) (2006).

11. Under the DMCA a takedown notice may be contested via a counter notice, which shifts the burden back upon the copyright holder to respond. 17 U.S.C. § 512(g)(2)(B).

12. *Vernor*, 621 F.3d at 1106.

13. *Id.*

sale of other items.<sup>14</sup> However, when Autodesk again failed to respond to Vernor's counter notices, eBay restored Vernor's account and resumed the auctions.<sup>15</sup> Though the record is unclear, it appeared that Vernor sold two of the CTA copies of AutoCAD, but refrained from selling the other two due to the risk of Autodesk again disrupting his ability to auction items on eBay.<sup>16</sup> In August 2007, Vernor brought a declaratory action against Autodesk to establish that his sales of the used software were protected by the first sale doctrine and thus did not infringe Autodesk's copyright.<sup>17</sup> In October 2009, the District Court entered judgment for Vernor, and Autodesk appealed.<sup>18</sup>

## II. PRIOR LEGAL STANDARD

### A. THE HISTORY AND PURPOSE OF THE FIRST SALE DOCTRINE

A brief look into the history of the first sale doctrine will illuminate the tensions within the *Vernor* decision. The origin of the first sale doctrine has largely been attributed to the 1908 United States Supreme Court case *Bobbs-Merrill Co. v. Straus*.<sup>19</sup> *Bobbs-Merrill* involved a notice printed by the publisher on the inside cover of a book that purported to prevent any future sale of that book under one dollar.<sup>20</sup> When the book was subsequently sold for less than a dollar, the publisher attempted to enforce the written notice.<sup>21</sup> The Court held that the copyright statutes did not reach so far as to restrain an owner's future sales of a book when no contract limitation or license had been created.<sup>22</sup> The *Bobbs-Merrill* Court expressed a concern that copyright holders would be able to control future sales without having to bargain for that right, as would traditionally be the case in a licensing scenario.<sup>23</sup> Because there was no privity of contract between the subsequent buyer and the copyright owner, the Court found such restrictions to be beyond the bounds of the copyright statutes.<sup>24</sup> This principle, now known as the first sale doctrine, was later codified in the Copyright Act of 1909.<sup>25</sup>

The current U.S. Copyright Act secures specific exclusive rights to copyright holders. Section 106 enumerates six exclusive rights: (1) the right to reproduce one's work; (2) the right to create derivative works; (3) the right to distribute one's work publicly; (4) the right of public performance; (5) the right of public display; and (6) the digital public performance of sound recordings.<sup>26</sup> The § 106(3) right of

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14. *Id.*

15. *Id.*

16. *Id.*

17. *Id.*

18. *Id.*

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

20. *Id.* at 341.

21. *Id.* at 342.

22. *Id.* at 350-51.

23. *Id.*

24. *Id.*

25. *Vernor v. Autodesk, Inc.*, 621 F.3d 1102, 1107 (9th Cir. 2010) (citing 17 U.S.C. § 41 (1909)).

26. 17 U.S.C. § 106 (2006).

public distribution concerns the exclusive right of the copyright holder to control the transfer of ownership of copies of the protected work via "rental, lease, or lending."<sup>27</sup> This right is seen as serving a gatekeeping function, allowing the copyright owner to determine how many copies are released into commerce. However, the right of public distribution is not absolute.

The first sale doctrine, codified in § 109(a), places limits on the rights of the copyright holder once a copy has been sold: "Notwithstanding the provisions of § 106(3), the 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."<sup>28</sup> While the copyright owner may determine not to sell any more copies, under § 106(3), she may not place constraints on the future sales of a copy that has already been sold. The key language in this provision is the term "owner." As clarified in § 109(d), this first sale protection does not extend to anyone "who has acquired possession of the copy or phonorecord from the copyright owner, by rental, lease, loan, or otherwise, without acquiring ownership of it."<sup>29</sup> The definition of "owner" in this section merely looks at the objective elements of the transaction. As a result, what a consumer believes about a transaction is irrelevant.

In this manner, individual copies of a copyrighted work—if legally sold by the copyright owner—may continue to be resold without infringing the original owner's rights. The ability to resell therefore hinges on the determination that the original transfer from the copyright owner was a sale, and thus a release of the copy into the stream of commerce. *Nimmer on Copyright*, the leading copyright treatise, delves into the specifics of § 109 and what questions should be asked when assessing ownership and the first sale defense:

The appropriate lines of inquiry should be: (a) was the subject physical product (the "copy") lawfully manufactured with authorization of the copyright owner; (b) was that particular copy transferred under the copyright owner's authority; (c) does the defendant qualify as the lawful owner of that particular copy; and (d) did the defendant thereupon dispose of that particular copy (as opposed to, for example, reproducing it)?<sup>30</sup>

Nimmer highlights that many factors contribute to whether someone is deemed an owner.

Over the years, in response to new technologies and shifts in market practices, the courts have periodically revisited the issue of differentiating a sale from a license. As new forms of contracting emerge, the line between a license and a sale often becomes blurry. The most recent technological change—the transition to nonphysical (digital) media—made it difficult to define an individual "copy." In order to maintain the delineation between a license and a sale, and preserve the protection of the first sale doctrine, courts must reshape the tests that delineate

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27. *Id.* § 106(3).

28. *Id.* § 109(a).

29. *Id.* § 109(d).

30. MELVILLE B. NIMMER & DAVID NIMMER, *NIMMER ON COPYRIGHT* § 8.12 (2009).

licenses from sales.

### B. U.S. V. WISE

In *U.S. v. Wise*, the Ninth Circuit Court of Appeals examined multiple transfers of feature length motion pictures.<sup>31</sup> Appellant Woodrow Wise, Jr. operated Hollywood Film Exchange, a business that sold copyrighted feature length motion pictures to private consumers for personal use.<sup>32</sup> Many of the films sold by Wise were procured from salvage businesses that acquired the films from motion picture studios in order to recycle the film reels and sell or repurpose the blank film stock.<sup>33</sup> Wise argued that the transfers of the films from the studio to the salvage company constituted sales, while the government contended that they were merely licenses and did not allow for resale.<sup>34</sup>

The *Wise* Court assessed each of the transfers individually, as each had slightly different terms and surrounding circumstances. Many factors determined whether the transfers were sales or licenses, including the restrictions on use, reservation of title, whether it was termed a license or a sale and whether the copyright holder had the ability to reclaim the copy or mandate its destruction.<sup>35</sup> The Court relied upon the case of *Hampton v. Paramount* for the proposition that an agreement allowing a party to make copies of a motion picture, for the purpose of licensing them to others, was not an assignment or sale of the motion picture but was merely a restrictive license.<sup>36</sup> In addition to this, the Court noted that *Hampton* focused mainly on the rights conveyed by the agreement.<sup>37</sup> As the agreement in *Hampton* only conveyed limited use of the motion picture, the *Hampton* Court did not consider it to represent a sale.<sup>38</sup> The *Wise* Court emphasized that many of the film transfer contracts "reserved all rights and title in the studios."<sup>39</sup> However, *Wise* noted that "the mere failure to expressly reserve title to the films does not require a finding that the films were sold, where the general tenor of the entire agreement is inconsistent with such a conclusion."<sup>40</sup>

When considering the general tenor of the contract, the court also did not automatically exclude contracts labeled "licenses" from transactions that transferred ownership.<sup>41</sup> Some contracts did not include a reservation of title.<sup>42</sup> When analyzing these contracts, the Court looked toward the contract as a whole

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31. *United States v. Wise*, 550 F.2d 1180, 1183-85 (9th Cir. 1977).

32. *Id.* at 1183-84.

33. *Id.* at 1184.

34. *Id.*

35. *Id.*

36. *Id.* at 1189 (citing *Hampton v. Paramount Pictures Corp.*, 279 F.2d 100 (9th Cir. 1960)).

37. *Id.*

38. *Id.*

39. *Id.* at 1184.

40. *Id.* at 1191.

41. *Id.* at 1190-91.

42. "The union of all elements (as ownership, possession, and custody) constituting the legal right to control and dispose of property; the legal link between a person who owns property and the property itself." BLACK'S LAW DICTIONARY 1622 (9th ed. 2009).

and the restrictions placed upon the purchasing party. Depending on the extent of such restrictions, the Court would determine whether it was a sale with restrictions on use, or a license.<sup>43</sup> Lastly, the Court asked whether the terms allowed for the copyright owner to reclaim the copy or have it destroyed.<sup>44</sup> The *Wise* Court considered all of these factors together with the overall contract terms. Much of the language in the Court's opinion emphasized that no single factor was dispositive.<sup>45</sup> The Court analyzed each contract individually and came up with a different result based on the specific balancing of the factors in each case.<sup>46</sup>

### C. MAI TRIO

Following *Wise*, the Ninth Circuit again dealt with the distinction between an "owner" and a "licensee," this time in the context of § 117 of the Copyright Act. Section 117 of the Copyright Act provides an exception similar to the first sale doctrine called the essential step defense. Section 117(a) reads:

Notwithstanding the provisions of section 106, it is not an infringement for the owner of a copy of a computer program to make or authorize the making of another copy or adaptation of that computer program provided: (1) that such a new copy or adaptation is 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.<sup>47</sup>

This section provides an affirmative defense to copying when the owner must make a copy through use, archival or maintenance.<sup>48</sup> Much like the first sale doctrine, this exception is only afforded to owners and depends upon the determination of a sale. As "owner" is used in both §§ 109 and 117, the cases concerning § 117 provide valuable insight into the distinction between the definitions of a sale versus that of a license through the delineation of who is an "owner."

In assessing this exception to copyright, the Ninth Circuit Court of Appeals examined the definition of "owner" in three cases referred to as the *MAI* Trio.<sup>49</sup> The *MAI* Trio includes *MAI Systems Corp. v. Peak Computer, Inc.*, which dealt with the use of software by a third party computer repair business; *Triad Systems Corp. v. Service Express Co.*, also involving a third party repair business; and *Wall Data, Inc. v. Los Angeles County Sheriff's Dept.*, which concerned a customer's use of volume licenses.<sup>50</sup>

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43. *Wise*, 550 F.2d. at 1190-91.

44. *Id.* at 1191.

45. *Id.* at 1189-91.

46. *Id.* at 1193-94.

47. 17 U.S.C. § 117(a) (2006).

48. *Id.*

49. *Vernor v. Autodesk Inc.*, 621 F.3d 1102, 1109 (9th Cir. 2010).

50. *Wall Data, Inc. v. Los Angeles Cnty. Sheriff's Dep't*, 447 F.3d 769 (9th Cir. 2006); *Triad Sys. Corp v. Se. Express Co.*, 64 F.3d 1330 (9th Cir. 1995); *MAI Sys. Corp. v. Peak Computer, Inc.*, 991 F.2d 511 (9th Cir. 1993).

# 1. MAI Systems Corp. v. Peak Computer, Inc.

In 1993, the Ninth Circuit Court of Appeals returned to the issue of a sale versus a license in the case of *MAI Systems Corp. v. Peak Computer, Inc.*<sup>51</sup> The *MAI* case asked whether a computer repair company, Peak Computer, Inc. ("Peak"), violated MAI Systems Corporation's ("MAI") computer operating system copyright in the course of servicing computers owned by MAI customers.<sup>52</sup> In order to service the computers, Peak needed to activate the operating system.<sup>53</sup> This process of activation creates a working copy of the computer's operating system.<sup>54</sup> The operating system information was stored in the hard drive, or main memory bank of the computer, and needed to be copied into the random access memory (RAM) portion of the computer where active calculations were made.<sup>55</sup> There was no claim that Peak made additional copies of the software or used it in any manner inconsistent with the normal operation of the machine.<sup>56</sup> MAI asserted that this process of activation, where loading the software from the hard drive into the RAM of the computer, constituted making a "copy" under copyright law.<sup>57</sup> MAI noted that the computer software was only licensed to customers for personal use, not the use or copying by third parties.<sup>58</sup> Specific provisions in MAI's user agreement specified that the user is restricted to personal use, and that he must "keep the software . . . confidential and not make [it] available to others."<sup>59</sup>

Because the copying at issue was done within the computer as part of the activation process, the court emphasized § 117's "essential step" defense, which protects an owner from copyright infringement when the copying "is an essential step in the utilization of the computer program."<sup>60</sup> The essential step defense basically creates a safe harbor for the owners of computer software who, by the very act of using their software, create a copy within the computer, as described above.<sup>61</sup> Without this safe harbor, software owners would technically be in violation of copyright every time they used a computer program. In this instance, Peak's servicing of the computer was done at the request of the MAI customer and was thus argued to be exempt from liability under § 117.<sup>62</sup> However, the Court concluded that the customers were not eligible for protection under § 117 as they

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51. *MAI*, 991 F.2d. at 511. While MAI was partially overruled by the Computer Maintenance Competition Assurance Act, which reworded 17 U.S.C. § 117(c) and (d), the act doesn't pertain to the distinction between a license and a sale, but rather allows a carve out for maintenance and repair of computers even in a licensee situation. Digital Millennium Copyright Act, Pub. L. No. 105-304, §§ 301-02, 112 Stat. 2860 (1998).

52. *MAI*, 991 F.2d. at 513.

53. *Id.*

54. *Id.* at 518.

55. *Id.*

56. *Id.*

57. *Id.*

58. *Id.* at 513-16.

59. *Id.* at 516.

60. 17 U.S.C. § 117(a) (2006); *id.* at 519.

61. See *supra* text accompanying notes 47-48.

62. *MAI*, 991 F.2d at 518-19.

were determined to have only licensed the software and thus were not considered "owners." Although this is a fact specific inquiry (as seen in *Wise*), the Court merely stated that it was a license and did not further explain its determination.<sup>63</sup> The *MAI* Court simply stated that the contract was a license, and that the protections of § 117 do not cover licensees.<sup>64</sup>

## 2. *Triad Systems Corp. v. Service Express Co.*

In *Triad Systems Corp. v. Service Express Co.*, decided in 1995, the Ninth Circuit again approached the issue of computer servicing.<sup>65</sup> Triad Systems Corporation ("Triad") manufactured computers and software for use in the automotive industry. Southeastern Express Company ("Southeastern") was an independent company that provided servicing for Triad computers.<sup>66</sup> The core issue here was the same as in *MAI*, as Southeastern had to turn on the computers of Triad customers in order to service the machines, thus running into the same technological issue of creating an internal copy in order to operate the computers.<sup>67</sup> Again the determination concerned whether Triad Customers were owners and if the customers or Southeastern could invoke § 117 protections.<sup>68</sup> Unlike *MAI*, which only dealt with transactions deemed to be licenses, *Triad* involved three different contractual arrangements between Triad and its customers. The first form of contract, used from 1976 to 1985, was an outright sale.<sup>69</sup> The court stated that the use of these "Regime 1" sale products were noninfringing due to § 117 protections.<sup>70</sup> However, from 1985 onward, Triad began licensing its software under a restrictive policy, "Regime 2," that prevented the use by third parties.<sup>71</sup> In 1991, Triad also provided "Regime 3" contracts, in addition to the Regime 2 contracts, which included a "license transfer fee" option for licensees who wanted to sell the Triad computer systems.<sup>72</sup>

The court held that these Regime 2 and Regime 3 contracts prevented the use of the § 117 defense as they only provided a license to use the software. Following the reasoning of *MAI*, the Court determined that mere licensees could not be afforded the protections of § 117.<sup>73</sup> Again, little was mentioned about the Regime 2 and Regime 3 contracts beyond labeling them licenses.

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63. *Id.* at 517.

64. *Id.* at 519. The language considered by the *MAI* ruling has since been altered by the Computer Maintenance Competition Assurance Act to include nonowners, *see* 17 U.S.C. § 117(c)-(d) (2006); however the court's reasoning as to the definition of an "owner" has not changed. Digital Millennium Copyright Act, Pub. L. No. 105-304, § 301-302, 112 Stat. 2860 (1998).

65. *Triad Sys. Corp. v. Se. Express Co.*, 64 F.3d 1330 (9th Cir. 1995).

66. *Id.* at 1333.

67. *Id.*

68. *Id.*

69. *Id.*

70. *Id.*

71. *Id.*

72. *Id.*

73. *Id.* at 1337.



### 3. Wall Data, Inc. v. Los Angeles County Sheriff's Department

Following the trend set in *MAI* and *Triad*, in 2005 the Ninth Circuit again considered § 117 protections in *Wall Data, Inc. v. Los Angeles County Sheriff's Dep't*.<sup>74</sup> This case concerned the use of Wall Data, Inc.'s ("Wall") RUMBA software on the Los Angeles County Sheriff's Department ("the Department") computers.<sup>75</sup> The Department purchased 3,663 licenses between two versions of Wall's software. After discovering that the individual installation of each piece of software was overly time-consuming, the Department began installing a "baseline" of software onto every computer from one core copy.<sup>76</sup> This process was done by "simultaneously copying the entire contents of a single hard drive containing the baseline of software applications onto the hard drives of other computers." The Department used this process to copy the software onto 6,007 computers, well exceeding the 3,663 purchased licenses. Rather than only installing the software on 3,663 computers, the Department set up a network that was to only allow 3,663 simultaneous uses of the software.<sup>77</sup> By restricting the computers such that only the correct number of computers was using the software at one time, the Department sought to avoid copyright infringement.<sup>78</sup> The Department claimed that it was protected under a § 117 essential step defense, as this was the only feasible means to install so many copies.<sup>79</sup> Wall was not convinced by this argument and sued the Department for the 2,344 unlicensed copies.<sup>80</sup>

Utilizing the precedent of *MAI*, the Court determined that the license terms contained in Wall's software were sufficient to denote a license rather than a sale.<sup>81</sup> Again the Court focused on the retention of ownership and the restrictions contained in the "click-through" license agreement.<sup>82</sup> Specifically, the Court stated:

Generally, if the copyright owner makes it clear that she or he is granting only a license 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.<sup>83</sup>

These restrictions on use appeared to be the only rationale articulated by the *Wall* Court.

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74. *Wall Data, Inc. v. Los Angeles Cnty. Sheriff's Dep't*, 447 F.3d 769 (9th Cir. 2006).

75. *Id.* at 774.

76. *Id.*

77. *Id.*

78. *Id.* at 774-75.

79. *Id.* at 774-76.

80. *Id.* at 775.

81. *Id.* at 785.

82. A click-through agreement is the contract agreement which appears on a user's computer screen during the installation of a program and requires the user to agree to the contract before installing the software. See *Clickwrap Definition*, OXFORD DICTIONARIES ONLINE, <http://oxforddictionaries.com/definition/clickwrap> (last visited Apr. 7, 2012).

83. *Wall*, 447 F.3d at 785.

D. MINORITY VIEW: *SOFTMAN V. ADOBE*

Despite the sentiment evidenced in the *MAI* Trio, which seems to provide a low bar for determining that a transaction is a license, some courts have taken a more demanding approach. One example is found in *SoftMan v. Adobe*, a case from the Central District of California.<sup>84</sup> The *SoftMan* case involved a software distributor, SoftMan Products Co. ("SoftMan"), who distributed Adobe Systems Inc. ("Adobe") software to customers.<sup>85</sup> SoftMan would often purchase bundles (compilations of multiple pieces of software) of Adobe software from Adobe distributors at a discounted price, and resell parts of these bundles as individual pieces of software.<sup>86</sup> The *SoftMan* Court took a broad approach to the "economic realities" of the transaction. Rather than only focusing on the language used, as the *Wise* and *MAI* Trio courts did, the *SoftMan* Court highlighted a number of other cases that looked at the transaction itself to see if it qualified as a license.<sup>87</sup> *SoftMan* looked to the presence of a one-time payment and the allocation of risk should the copy be lost or damaged, to determine whether a sale had occurred.<sup>88</sup> The Court additionally cited the view that the sale of software was a transfer of goods under the Uniform Commercial Code (UCC), thus implicating notions of the economic realities of the transaction.<sup>89</sup> The UCC, a uniform law governing the law of commercial transactions, sets guidelines for the interpretation of commercial contracts and the elements necessary to create a binding contract.<sup>90</sup> The economic realities perspective looks toward the actual function of the contract rather than its title.<sup>91</sup>

One of the key aspects of the Court's reasoning was the relation of this transaction to core contractual notions of assent and the formation of a contract. Traditional conceptions of assent require a meeting of the minds where both parties understand what they are agreeing to at the time the contract is formed.<sup>92</sup> *SoftMan* denied that a customer who never installed the product, and thus never viewed or agreed to the licensing "click-through" agreement, could give proper assent to a contractual agreement.<sup>93</sup> The *SoftMan* Court briefly highlighted arguments suggesting that shrink-wrap licenses—those contained within the sealed product—are unacceptable pursuant to the Uniform Commercial Code.<sup>94</sup> Because the contract terms were unseen by the agreeing party at the time of purchase, the reasoning used by the Court was that they likely would fail the UCC's requirements

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

85. *Id.* at 1079–80.

86. *Id.* at 1080.

87. *Id.* at 1079–80.

88. *Id.* at 1085.

89. *Id.* at 1084 (citing *Microsoft Corp. v. DAK Indus.*, 66 F.3d 1091 (9th Cir. 1995)).

90. BLACK'S LAW DICTIONARY 745 (3d pocket ed. 2006).

91. *SoftMan*, 171 F. Supp. 2d at 1084.

92. RESTATEMENT (SECOND) OF CONTRACTS § 17 cmt. c (1981).

93. *SoftMan*, 171 F. Supp. 2d at 1087.

94. *Id.* at 1085.

for assent.<sup>95</sup> Ultimately, the Court declined to rule broadly on such licenses as it determined that *SoftMan* was free of the license by virtue of never having installed the software.<sup>96</sup> The *SoftMan* Court declined to adopt the reasoning of other courts that purported to extend licensing agreements to subsequent buyers on the notion that they consented to such agreements by virtue of buying from a licensed retailer.<sup>97</sup> *SoftMan* made the significant point that the licensing agreement was not presented in any manner until the software installation process.<sup>98</sup> The Court avoided a full analysis of “shrink-wrap” or “click-through” licenses, but evidenced a strong aversion to enforcing such contracts against those who did not even install the software.<sup>99</sup>

The analysis of the *SoftMan* Court is central to the issue in *Vernor*, as both issues concern the formation of a contract and how both parties come to view the transaction being made. The UCC provides guidelines for assent based on the assumption that a contract cannot be formed unless both parties understand and agree to the terms.<sup>100</sup> If the type of contract is determined, not by the intent of the parties, but rather by the words written by one party and not even seen by the other, then it seems unworkable under basic contract notions of assent. This concern was at the heart of the *SoftMan* decision. In the same vein, the criteria for determining a license versus a sale must allow for the intent of the parties. The *Wise* and *MAI* Trio cases emphasize certain factors that argue for one definition or another. The factors chosen should represent not only the realities of the written contract, but also the realities of the bargained agreement at the time it was made, which includes how both parties understood the agreement. In this manner, the selection of these factors is central to the efficacy of the first sale doctrine.

### III. LEGAL ANALYSIS IN THE *VERNOR V. AUTODESK* DECISIONS

One of the core considerations in *Vernor v. Autodesk* is whether the license versus sale distinction in the *MAI* Trio can be reconciled with the factors used in *Wise*. The *Vernor* District Court found that the decisions were irreconcilable, while the *Vernor* Court of Appeals contended that the decisions could be collapsed into a three-factor test.<sup>101</sup> Again, these tests determined if the transaction in question was a sale, which would establish ownership and grant the protection of the first sale doctrine, or if the transaction was a license, which would prevent resale without the copyright owner's permission.

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95. *Id.* at 1087.

96. *Id.*

97. *Id.* at 1088.

98. *Id.*

99. For further discussion of “shrink wrap” licensing, see David A. Costa, *Vernor v. Autodesk: An Erosion of First Sale Rights*, 38 RUTGERS L. REC. 1, 213 (2010–2011).

100. RESTATEMENT (SECOND) OF CONTRACTS § 17 cmt. c (1981).

101. *Vernor v. Autodesk, Inc.*, 621 F.3d 1102, 1111 (9th Cir. 2010); *Vernor v. Autodesk, Inc.*, No. C07-1189RAJ, 2009 WL 3187613, at \*11 (W.D. Wash. Sept. 30, 2009).

## A. VERNOR DISTRICT COURT

The District Court's analysis in the *Vernor* case began with the transfer of the AutoCAD software from Autodesk to CTA.<sup>102</sup> Taking into consideration that CTA agreed to the "click-through" agreement which accompanied the installation of the AutoCAD software, the District Court determined that the standard licensing terms contained within the "click-through" agreement defined the transfer.<sup>103</sup> These agreements prohibited "any transfer of the software without Autodesk's written permission," and directed users who upgraded the software to destroy any old copies.<sup>104</sup> The Court determined that this agreement was a license, and consequently did not transfer ownership of the software to the purchaser for the purposes of §§ 109 and 117.<sup>105</sup> However, the Court's analysis drew a distinction between the license in the *software* contained within each copy and the ownership of the *physical copies* themselves. The Court maintained that the use of the *software* could be licensed while the purchaser obtained ownership of the *physical copy*. While the purchasers were not owners of the software, they were owners of the physical copy under §§ 109 and 117.<sup>106</sup> The license was still effective for all other copyright matters pertaining to the software and would apply to the current owner of the physical copy; it simply could not restrain the right to transfer ownership of that physical copy. While the *software* is licensed to the purchaser, that purchaser still becomes the "owner" of the physical copy, thus triggering the "owner" exceptions under §§ 109 and 117 and enabling the purchaser to transfer the physical copy to someone else.<sup>107</sup>

To settle this issue, the District Court analyzed the *Wise* and *MAI* Trio opinions. Beginning with *Wise*, the District Court found that the differentiation of a license from a sale included many factors, but that no factor was independently dispositive.<sup>108</sup> The District Court listed the designation of an agreement as a license; the single, upfront payment by a transferee for a particular copy; the agreement requiring the transferee to destroy the copy; and a clause reserving title to the transferred copy in the copyright holder as important factors to consider.<sup>109</sup> Moreover, the District Court emphasized that reservation of title seemed to be the most prominent of the factors considered. While not dispositive, the Court found that "with only one likely exception, in every agreement containing an express reservation of title in the copyright holder, the panel found a mere license."<sup>110</sup> Additionally, it noted that "[i]n each instance in which the transferee could, at his

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102. Specifically, this was AutoCAD Release (version) 14. *Vernor*, 2009 WL 3187613, at \*4.

103. *Id.*

104. *Id.* While the full agreement for the new release 15 software was not included in the court record, the court assumed that the agreement contained the same destruction clause as referenced above.

*Id.*

105. *Id.* at \*5.

106. *Id.* at \*5.

107. *Id.* at \*4-5.

108. *Id.* at \*6.

109. *Id.*

110. *Id.* at \*7.

election, retain possession of the transferred copy indefinitely, and the copyright holder had no right to regain possession, the [C]ourt found an ownership transfer."<sup>111</sup> By combining the above factors, the District Court concluded that "retaining title in a copy is meaningless unless the copyright holder has some means to regain possession of the copy."<sup>112</sup> In applying the above reasoning to the *Vernor* case, the District Court emphasized that the transfer of the AutoCAD software consisted of a single, upfront payment, without any provision for the return of the copy.<sup>113</sup> Due to the weight of these factors, the District Court concluded that *Wise* would hold the transfer to be a transfer of ownership of the copy.<sup>114</sup>

Turning to the analysis of the *MAI* Trio, the Court argued that Autodesk would prevail under all three cases.<sup>115</sup> However, the Court was concerned that the *MAI* Trio gave very little discussion to the issue of ownership and seemed to decide the issue based upon whether or not the transaction was labeled a license.<sup>116</sup> The District Court was critical of *MAI*'s determination, as it neither referenced *Wise* nor gave any indication of why it was not considering the *Wise* factors in full.<sup>117</sup> In the end the Court viewed *Wall* as creating a license whenever there are "significant restrictions on the purchaser's ability to redistribute or transfer that copy."<sup>118</sup>

From the above conclusions, the District Court determined that the decisions in *Wise* and the *MAI* Trio were in opposition and that it had to choose between the two positions.<sup>119</sup> Even under the most flexible reading of *Wall*, the Court saw no way to reconcile these decisions.<sup>120</sup> The District Court argued that the factual situations of *Vernor* and one of the contracts from *Wise*—the Redgrave contract—would have different outcomes depending on the use of either the *Wise* or the *MAI* Trio analyses.<sup>121</sup> The District Court argued that because both situations involved contracts with significant use restrictions, but which nevertheless allowed for indefinite possession, *Wise* would have labeled them sales while the *MAI* Trio would have labeled them licenses.<sup>122</sup>

The District Court further maintained that the tension could not be remedied by comparing §§ 109 and 117. In comparing these two statutes, which respectively use the language "owner of a copy" and "owner of a particular copy," the court dismissed the possibility that they encompass different meanings of "owner."<sup>123</sup>

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111. *Id.*

112. *Id.* at \*8.

113. *Id.*

114. *Id.*

115. *Id.* at \*10.

116. *Id.*

117. *Id.* at \*9.

118. *Id.* at \*9 (quoting *Wall Data, Inc. v. Los Angeles Cnty. Sheriff's Dep't*, 447 F.3d 769, 785 (9th Cir. 2006)).

119. *Id.* at \*11.

120. *Id.*

121. The Redgrave contract was one of the film transfer contracts dealt with in the *Wise* case. Specifically the Redgrave contract did not account for the destruction or return of the copy.

122. *Id.*

123. *Id.* at \*12.

Though they are two distinct sections of the Copyright Act, with § 117 only applying to owners of software, the Court went on to address the history of §§ 109 and 117 in finding that the definition of owner remained constant despite many revisions and adjustments to the surrounding law and the divergence of §§ 109 and 117.<sup>124</sup>

As the Court found that the use of "owner" in §§ 109 and 117 was the same, it concluded that *Wise* and the *MAI* Trio were irreconcilable and thus it was required to "follow the oldest precedent among conflicting opinions from three-judge Ninth Circuit panels."<sup>125</sup> After considering the policy concerns, the District Court made it clear that "Congress is both constitutionally and institutionally suited to render judgments on policy; courts generally are not," and noted that other courts have joined the debate on both sides of the issue.<sup>126</sup> Emphasizing that "[p]recedent binds the [C]ourt regardless of whether it would be good policy to ignore it," the Court concluded by following *Wise* and entering judgment in favor of Vernor as the owner of the individual copies.<sup>127</sup>

### B. VERNOR COURT OF APPEALS

The *Vernor* Court of Appeals initially took a similar approach by examining the same contractual issues concerning the transfer to CTA, but came to a different conclusion regarding the application of prior case precedent.<sup>128</sup> It began its analysis with the history of §§ 109 and 117 through *Bobbs-Merrill*, asserting the same restrictions upon the §§ 109 and 117 exceptions as the lower court, namely that these sections do not apply to licensees.<sup>129</sup>

In analyzing *Wise*, the Court of Appeals highlighted five factors that were considered by the *Wise* Court: whether the agreement (a) was labeled a license, (b) provided that the copyright owner retained title to the prints, (c) required the return or destruction of the prints, (d) forbade duplication of prints, or (e) required the transferee to maintain possession of the prints for the agreement's duration.<sup>130</sup> The Court noted that once an agreement was determined to be a license, as the copyright owner retained title, it required the possessor to return the prints if a mutually agreeable price was met, and required destruction of the prints if a price could not be agreed upon.<sup>131</sup> With respect to the Redgrave contract, the Court stated that the requirement to retain possession, the restriction not to sell, license, reproduce or publicly exhibit the print, coupled with the lack of an obligation to return, constituted a sale.<sup>132</sup> The Court ended its analysis of *Wise* by stating that it "did not hold that the copyright owner's retention of title itself established the

124. *Id.* at \*12-13.

125. *Id.* at \*11 (citing *United States v. Rodriguez-Lara*, 421 F.3d 932, 943 (9th Cir. 2005)).

126. *Id.* at \*14.

127. *Id.*

128. *Vernor v. Autodesk, Inc.*, 621 F.3d 1102, 1110-11 (9th Cir. 2010).

129. *Id.* at 1107-11.

130. *Id.* at 1108 (quoting *United States v. Wise*, 550 F.2d 1180 (9th Cir. 1977)).

131. *Id.*

132. *Id.* at 1108-09.

absence of a first sale or that a transferee's right to indefinite possession itself established a first sale."<sup>133</sup> In analyzing the District Court's opinion, the Court of Appeals criticized the lower court's approach to *Wise* as overly focused on the user's ability to retain a copy of the work.<sup>134</sup>

In its examination of the *MAI* Trio, the Court of Appeals explored the § 117 essential step defense and compared it with § 109. The Court agreed with the District Court that the definitions of "owner" are the same in both sections.<sup>135</sup> Similar to the District Court's analysis, the Court of Appeals stated that *MAI* and *Triad* concerned licensees and thus persons unable to assert the essential step defense.<sup>136</sup> In looking at *Wall*, the Court of Appeals mirrored the lower court by noting the "significant restrictions" language used in the *Wall* decision.<sup>137</sup> The Court of Appeals agreed that this language required a certain type, quantity or threshold of restrictions in order to embody a license.<sup>138</sup> In contrast to the district court, the court of appeals found that *Wise* and *MAI* Trio are compatible, stating:

We read *Wise* and the *MAI* Trio to prescribe three considerations that we may use to determine whether a software user is a licensee, rather than an owner of a copy. First, we consider whether the copyright owner specifies that a user is granted a license. Second, we consider whether the copyright owner significantly restricts the user's ability to transfer the software. Finally, we consider whether the copyright owner imposes notable use restrictions.<sup>139</sup>

These three criteria were then applied to *Vernor*. The Court of Appeals held that under the three-prong test, the software was provided to CTA under a license, and thus neither CTA nor Vernor were "owners" of the software under §§ 109 or 117. Because Autodesk provided a license that retained title to the software and imposed significant transfer restrictions, such as "modifying, translating, or reverse-engineering," the Court of Appeals ruled in favor of Autodesk.<sup>140</sup>

#### IV. ANALYSIS

##### A. ARE *WISE* AND THE *MAI* TRIO RECONCILABLE?

In assessing the decision of the *Vernor* Court of Appeals, the first question is whether the *Wise* precedent was compatible with that of the *MAI* Trio. The lists of factors utilized by the courts in the future depend on how these two lines of case law are reconciled. The *Vernor* District Court spent a significant portion of its analysis arguing that they were not reconcilable, while the Court of Appeals seemed to be comfortable with using them in concert. The following sections

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133. *Id.* at 1109.

134. *Id.* at 1111.

135. *Id.* at 1110.

136. *Id.*

137. *Id.*

138. *Id.*

139. *Id.* at 1110-11.

140. *Id.* at 1111-12.

contain the lists of factors created by both courts. Part A1 outlines and compares the factors used by the *Vernor* District Court and the factors used by the *Vernor* Court of Appeals. These lists are referred to as the "District" and "Appellate" lists respectively. Part A2 discusses the conflicting perspectives on the compatibility of the *MAI* Trio decisions with the *Wise* decision. This discussion will include the *Vernor* Court of Appeals' combined three-factor test, denoted as the "Compatible" list. Lastly, Part A3 will present a "Total" list. This list will demonstrate the most comprehensive list of factors from both *Wise* and the *MAI* Trio, in order to highlight the factors left out by the *Vernor* Court of Appeals' three-factor test.

### 1. *Wise* Interpretation Comparison

As the *Vernor* Court of Appeals criticized the District Court's interpretation of the case law, it is important to compare the interpretations of both courts as to each case. Beginning with *Wise*, the *Vernor* District Court concluded that the *Wise* Court focused on six factors to determine a license versus a sale. These six factors are described in the following District list:

- D1. Designating an agreement as a license;
- D2. A clause reserving title to the transferred copy in the copyright holder;
- D3. A single, upfront payment by the transferee for a particular copy;
- D4. An agreement requiring the transferee to destroy transferred copies;
- D5. Significant restrictions on use; and
- D6. Inability of copyright holder to regain possession (indefinite possession).<sup>141</sup>

The District Court emphasized that these factors should be considered and weighed together. Though no single factor was found to be dispositive, the District Court suggested that indefinite possession, D6, weighed the most heavily, as it seemed to counteract the reservation of title, D2.

The *Vernor* Court of Appeals selected only five factors in its summary of the *Wise* Court's reasoning. These factors are described in the following Appellate list:

- A1. Labeled a license;
- A2. Provided that the copyright owner retained title to the prints;
- A3. Required the return or destruction of the prints;
- A4. Forbade duplication of prints; and
- A5. Required the transferee to maintain possession of the prints for the agreement's

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141. *Vernor v. Autodesk, Inc.*, No. C07-1189RAJ, 2009 WL 3187613, at \*6-7 (W.D. Wash. Sept. 30, 2009). The District Court mentions D5 in its discussions, but does not explicitly place it in their list. For simplicity, it is included in this list.



duration.<sup>142</sup>

It seems that both the District Court and the Court of Appeals largely viewed the *Wise* case in the same light. The most significant divergence appears to be whether on the mode of payment factored into the analysis. While the Court of Appeals did acknowledge the role of price with regard to the Redgrave agreement, it seemed to avoid this point in the overall analysis of the *Wise* reasoning.<sup>143</sup> The second divergence concerned the treatment of indefinite possession. The District Court explicitly phrased indefinite possession as an individual factor of the *Wise* analysis, while the Court of Appeals appeared to squeeze the notion into A3 under "return."<sup>144</sup> This suggests that the Court of Appeals placed less weight on the factor of indefinite possession. Despite these discrepancies, both courts seemed to insist on these factors being weighed together and neither being dispositive if treated individually.

The most glaring issue concerning the Court of Appeals' treatment of the District Court's decision is the dismissive nature of the Court of Appeals' analysis. The Court of Appeals claimed that the District Court considered the indefinite possession prong as dispositive, and thus incorrectly assumed that *Wise* favored Vernor, stating that "[t]he [D]istrict [C]ourt interpreted *Wise* to hold that a first sale occurs whenever the transferee is entitled to keep the copy of the work."<sup>145</sup> This interpretation ignored the explicit analysis given by the District Court in the following paragraph:

Autodesk expressly retains title to the "Software and accompanying materials," but it has no right to regain possession of the software or the "accompanying materials." Licensees pay a single up-front price for the software. Autodesk can require the destruction of the software, but only as consideration in the later purchase of an upgrade. The decision to upgrade, and thus the decision to accept Autodesk's destruction requirement, is entirely in the control of the licensee. Autodesk severely restricts the use and further transfer of the software. Despite these competing considerations, the court concludes that *Wise* leads to the conclusion that the transfer of AutoCAD copies via the License is a transfer of ownership.<sup>146</sup>

This excerpt shows that the District Court found that the designation of an agreement as a license, D1, the reservation of title, D3, and significant use restrictions, D5, weighed in favor of Autodesk, while it found that a single, upfront payment, D3, destruction requirements, D4, and indefinite possession, D6, weighed in favor of CTA and Vernor. The District Court noted that reservation of title, D1, is meaningless when combined with indefinite possession, D6.<sup>147</sup> In this manner, indefinite possession cancelled out reservation of title and shifted the balance in Vernor's favor. The Court of Appeals could have disagreed with the District Court

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142. Vernor v. Autodesk, Inc., 621 F.3d 1102, 1109 (9th Cir. 2010).

143. *Id.* at 1108–09.

144. *Id.* at 1108.

145. *Id.* at 1111.

146. Vernor, 2009 WL 3187613, at \*7–8 (footnote omitted).

147. *Id.* at \*8.

over the total number of factors and their relative weight, but no such argument was made. Instead, the Court of Appeals casually dismissed the District Court's analysis as treating one factor as dispositive, an action explicitly denied in the District Court's own reasoning. This dismissal of the District Court's analysis merely serves to allow the Court of Appeals to cut out the factors which conflict with the *MAI* Trio. These same factors— indefinite possession and upfront payment—are the most in tune with the consumer perspective on the transaction in question.

## 2. MAI Trio Interpretation Comparison

Both the District Court and the Court of Appeals seemed to analyze the *MAI* Trio in the same manner. The *MAI* and *Triad* cases were seen as strict licenses that do not afford owner protections to the consumers.<sup>148</sup> Both courts noted that *Wall* included the aspect of "significant restrictions."<sup>149</sup> Furthermore, the courts agreed that the *MAI* Trio lacked citation to *Wise*.<sup>150</sup> Though the Court of Appeals asserted that the two approaches were compatible, it did not attempt to clarify the glaring absence of *Wise* in the analysis of these three courts.<sup>151</sup> As *Wise* was the only precedent on the first sale doctrine, ignoring its existence only served to confuse this body of legal precedent. Aside from the further move by the Court of Appeals to reconcile these cases, both courts agreed on the general tenor of the *MAI* Trio.

In addition to the analysis above, the Court of Appeals offered three factors that it argued to be the product of reading the *Wise* and *MAI* Trio as compatible. The Court of Appeals held "that a software user is a licensee rather than an owner of a copy where the copyright owner (1) specifies that the user is granted a license; (2) significantly restricts the user's ability to transfer the software; and (3) imposes notable use restrictions."<sup>152</sup> This compatible list of factors arose from the view of the *Vernor* Court of Appeals that *Wise* and the *MAI* Trio can be reconciled. The *Vernor* Court of Appeals concluded its decision by utilizing these three factors to assess the *Vernor* case.

## 3. Discussion

By first addressing the overall compatibility of the two lines of reasoning and then considering the three common principles enumerated above, this analysis will show that even under the most favorable readings, the three principles highlighted by the Court of Appeals do not encompass all of the factors utilized by *Wise* and the *MAI* Trio.

It is apparent that the level of analysis given by the *Wise* Court is far beyond that given by courts in any of the *MAI* Trio of cases. Because none of the three cases

148. *Vernor*, 621 F.3d at 1109; *id.* at \*9.

149. *Vernor*, 621 F.3d at 1110; *Vernor*, 2009 WL 3187613, at \*9.

150. *Vernor*, 621 F.3d at 1111; *Vernor*, 2009 WL 3187613, at \*9.

151. *Vernor*, 621 F.3d at 1110–11.

152. *Vernor*, 621 F.3d at 1111.

addressed the decision in *Wise* directly, it is difficult to assume that the full *Wise* analysis was occurring in the background. All three of the *MAI* Trio opinions gave only the most cursory discussion of the agreements and seemed to designate them as licenses merely because they were styled as such—this proposition cuts strongly against the precedent in *Wise*. *MAI* relegated the discussion to a conclusory footnote, while *Triad* attaches a sentence and a footnote.<sup>153</sup> *Wall*, the most substantial of the three opinions, includes only the following: “Generally, if the copyright owner makes it clear that she or he is granting only a license 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.”<sup>154</sup> Thus it is hard to argue either that the courts ignored *Wise* or that they were implicitly applying the factors, without making large assumptions as to the reasoning not expressed in the opinions.

It must be noted at the outset that the courts appear to take a different approach when analyzing the notion of ownership in conjunction with a third party who is not claiming to be an owner, such as in *MAI* and *Triad*, as opposed to situations where the subsequent purchaser is attempting to stand in the position of an owner, as in *Wise* and *Wall*. The courts appear to concern themselves much less with the details of the license when a third party nonowner is involved. The only immediate assumption is that the courts respect the software manufacturer’s attempt to limit uses of the software by third parties as these are not as opposed to the first sale doctrine, which allows sales with restrictions on use. The *Wall* Court even acknowledged criticism of the *MAI* decision, but it failed to directly discuss the issue, as it already determined that the essential step provided no protection for the Department.<sup>155</sup> This difference in approach suggests that cases like *MAI* and *Triad* hold less precedential value over cases like *Vernor*, where the party in question is not a third party nonowner.

As the *Wall* case was the most substantial of the three, the most useful discussion will be comparing it to the analysis in *Wise*. If it is to be assumed that the *Wall* Court used the *Wise* factors, rather than ignoring them, it is unclear how the *Wall* Court reached its conclusion. The *Wall* Court simply did not discuss the contract with enough depth to engage all of the *Wise* factors.

On the other hand, *Wall* can be read as determining a license based solely on the presence of significant use restrictions. Under this reading, it would surely be in conflict with *Wise*. This seems to be the most plausible reading without assuming additional arguments beyond what is written by the *Wall* Court. Because both the District Court and the Court of Appeals continually stated that no single factor is dispositive, this interpretation of *Wall* would hold little weight.

In order to paint the Court of Appeals’ reasoning in the best light, one must assume that *Wall*’s use of the word “generally” means that the other *Wise* factors were considered in the background reasoning of the Court and not expressed in the

153. See *Triad Sys. Corp. v. Se. Express Co.*, 64 F.3d 1330, 1337 n.18 (9th Cir. 1995); *MAI Sys. Corp. v. Peak Computer, Inc.*, 991 F.2d 511, 518 n.5 (9th Cir. 1993).

154. *Wall Data Inc. v. Los Angeles Cnty. Sheriff’s Dep’t*, 447 F.3d 769, 785 (9th Cir. 2006).

155. See *id.* at 786.

opinion.<sup>156</sup> This is quite a stretch of interpretation. In addition, this interpretation appears to contribute very little to the *Wise* factors. The only substantial reasoning provided by *Wall* is the analysis of the "significant restrictions."<sup>157</sup> This is not foreign to the *Wise* Court's analysis; it is merely one of the factors that was given little weight by both the District Court and the Court of Appeals. *Wise* even occasionally phrased its analysis in the same way, as shown by the discussion of the Redgrave agreement and the "restrictions on the use of the print."<sup>158</sup> Again, these factors were not dispositive, but they were affirmatively addressed in *Wise*. In this manner, either the *MAI* Trio was rejected, as argued by the District Court, or it merely contributed the factor of "significant use restrictions." Because either interpretation seems ultimately compatible with the *Wise* factors, the concern rests with the additional factors from *Wise*, which were arguably ignored by the *MAI* Trio and the Court of Appeals' three-prong test.

While the Court of Appeals' three common factors are good starting points for an analysis in this body of law, there was little explanation as to why the list is limited to these three. The Court of Appeals itself provided a longer list in its analysis of the *Wise* Court's reasoning. Beyond the simple argument that three equal factors would provide an easier means of deciding the case, there was no explanation that appears to justify such an adjustment. Additionally, there was no discussion as to why the Court of Appeals' third factor used the term "notable" to modify "use restrictions" instead of the term "significant" that was used by *Wall*.<sup>159</sup> Ultimately, the Court of Appeals failed to adequately explain why it altered the formulation of the factors.

The Court of Appeals' three-prong test failed to encompass the key factors outlined in *Wall*, which are crucial to this analysis. Based upon all three sets of factors listed above, in addition to the explanations of the prior case law given at the beginning of this Note, the following "Total" list is the most reasonable and complete combination of factors arguing for a license:

- T1. Specifies that the user is granted a license;
- T2. Provides that the copyright owner retains title;
- T3. Imposes significant use and transfer restrictions;
- T4. Is not a single, upfront payment by the transferee for a particular copy; and
- T5. Provides for the destruction or return of the transferred copies (no indefinite possession).

The above list includes the two factors missing from the Compatible list utilized by the *Vernor* Court of Appeals: an upfront payment and indefinite possession. This list more accurately describes the nature of the transaction without oversimplifying

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156. *Wall Data*, 447 F.3d at 785.

157. *Id.* at 785.

158. *United States v. Wise*, 550 F.2d 1180, 1192 (9th Cir. 1977).

159. See *supra* note 139 and accompanying text.

the *Wise* analysis.

## V. ARGUMENT

### A. THE FACTORS

As noted in the preceding section, the Court of Appeals' treatment of the District Court was not only overly dismissive but also seemed to ignore the factors of upfront payment and indefinite possession. The Court of Appeals' actions additionally caused two problems for this area of the law. First, on a fundamental level, a change of the law without explanation or demarcation disrupts the ability of businesses and consumers to adjust their practices to parallel the law. Second, the *Vernor* Court of Appeals' excising of the two *Wise* factors further distances the balancing tests from the subjective experience of consumers. Upfront payment and indefinite possession are the most obvious characteristics to a consumer at the time of purchase. If the name of the agreement, use restrictions and other terms were contained within the box of the item, those factors would be initially hidden from the consumer. As the first sale doctrine aims to protect the economic balance of consumers, altering tests without making such changes clear and removing factors that are more immediately apparent at the time of the transaction will not adequately preserve the protections of the first sale doctrine.<sup>160</sup> Without recognition that these tests represent the assent of both parties and the agreement of both the consumer and the retailer, the tests enumerated above would have little value.

First, it must be stressed that multifactor tests such as these serve as guidelines to those who buy and sell products in the marketplace. While legal change is necessary and often beneficial, such change is only helpful when it can be adequately explained and understood. One of the tensions in this area of the law stems from the competing views of the courts. The *Vernor* Court of Appeals only exacerbates this tension by creating a new test without adequately explaining how this test fits in with the prior court decisions and how it differs. As noted above, there were a number of discrepancies even within the Court of Appeals' own reasoning, let alone among the differing lines of cases. Because this area of the law is meant to guide day-to-day transfers of goods, clarity is of the utmost importance. Without clarity, consumers will not know what they are bargaining for and retailers cannot know what measures to take in order to adequately protect their copyrighted goods.

Not only did the *Vernor* Court of Appeals create the new test with little exposition, it seemed to suggest that it was changing nothing at all.<sup>161</sup> As noted above, the Court of Appeals test both altered and deleted many of the *Wise* factors. This is not to say that any change is necessarily problematic, as change is obviously needed to cope with new technologies, but in order for these changes to properly

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160. See discussion *supra* Part II.A.

161. See discussion *supra* Part IV.A.1.

guide both courts and licensors, the changes at least need to be acknowledged by the court. By altering the precedent without acknowledgement or explanation, the *Vernor* Court of Appeals opened the door to confusion and misinterpretation by future courts.

Second, it is important to recall that the first sale doctrine was designed to protect the rights of individuals to their property against unreasonable restraints upon alienation under the guise of the copyright law. The first sale doctrine is intended to preserve the rights of owners to resell their purchased property.<sup>162</sup> There is surely a problem if consumers think they are owners but in fact they are licensees. The factors involved in the Court's test should account for the realities of the transaction from the perspective of a retailer *and* the consumer. The first sale doctrine protects the rights bargained for in a sale.<sup>163</sup> If the Court's test ignores the fact that the consumer thinks he is purchasing ownership rights, it fails to accurately define the transaction that occurred. Retailers can easily sneak licenses into any transaction without paying for those rights. In order to preserve the intention of the first sale doctrine, the law must accurately delineate a license in such a manner that the everyday consumer understands what they are purchasing. While upfront payment is not necessary for a sale, it serves an important function by incorporating the subjective viewpoint of the consumer. If a consumer pays once for an item, the consumer typically presumes he is now the owner of that item. Indefinite possession also performs this function, as someone who is able to keep the item forever is likely to presume she is the owner of that item. From the consumer perspective, a single payment for a tangible copy, which never needs to be returned, seems to have all the hallmarks of a traditional sale. If only a lawyer can determine what type of transaction is occurring, then it appears we have left the first sale doctrine far behind.

## B. POLICY CONCERNS

While the different factors are central to the application of the law, it is important to remember the real world effect of these decisions and how they interact with the concerns of creators and consumers. As the first sale doctrine operates directly in the transactions of day-to-day goods, these real world effects should be reflected in the law. Outright sales and licensing options both have value in modern media transactions. The importance is not in elevating one practice over the other, but rather in clarifying to consumers what transaction is taking place at the time of the transfer of property.

Looking first at the benefits of the first sale doctrine from the consumer perspective, the protections afforded by the first sale doctrine have provided consumers with the ability to sell their purchased items in order to recoup the value of their purchase.<sup>164</sup> This is especially important in markets where there are no

162. See discussion *supra* Part II.A.

163. See discussion *supra* Part II.A.

164. Robert H. Rotstein, Emily F. Evitt & Matthew Williams, *The First Sale Doctrine in the Digital Age*, 22 INTELL. PROP. & TECH. L.J. 23, 24 (March 2010).

license-free options. In such a market, users may be forced to pay a price that is disproportionate to their need or use of the software. If they only require a portion of the software, and are unable to access that feature in part, the license provisions may prevent them from reaping the full value of the item. Under a first sale regime, however, the user can achieve his short-term use and then sell the item to another user at a discounted price. This is especially relevant for situations similar to the *Vernor* case, which revolve around high priced specialty software. While the full software might be extremely valuable to a professional, one-time users unable to resell may not have the ability to purchase the software and recoup the difference between the cost of the software and the small value of their limited use.

In addition to the issue of recouping value from purchased goods, there are further concerns where consumers do not understand the terms of their purchase. Sophisticated consumers might recognize the differences between sales and licenses and account for the cost of the item relative to the rights they obtain, but not all consumers recognize licenses in today's marketplace of hidden contracts. As discussed above, any software licenses are "click through" licenses, contained within the software and only shown to purchasers upon installation. The restrictive agreements for users are rarely seen prior to purchase. Often these are merely windows containing extremely long text with an "I agree" button. It is doubtful that many users even see the sale restriction portion of the agreement prior to simply clicking the button to continue. There is little argument that the purchaser properly weighed the bargain of such a restrictive license when the restriction is not only hidden at the time of purchase but likely unseen thereafter. If consumers do not even know that they are purchasing a license or what a license entails, they are deprived of the benefit of the first sale doctrine without ever knowing it.

In addition to the consumer perspective, the creators themselves can enjoy the protections afforded by the first sale doctrine through the creation of a safe harbor for used item sales. Many products like novels and video games experience a renewal of interest in the used item market. If retailers know that they are free to resell these items, they are more likely to establish large businesses that cultivate this used item market. Once a mainstream item, such as a movie or video game, is no longer produced by the manufacturer, it might be too difficult or too costly for a consumer to obtain a new copy. The first sale doctrine allows for an active market of used items, priced more reasonably than rare pristine copies. In addition, the ability to purchase a used item at a discount price may entice new users to a series or brand and thus stimulate future new product sales. While the first sale doctrine is not *necessary* for used item sales, as they might also be authorized by the copyright holders, the broad protection afforded by the first sale doctrine reduces transactions costs by applying a blanket rule to all resold goods.<sup>165</sup>

On the other hand, the first sale doctrine should not impede the use of licensing regimes. Licensing enables both creators and consumers to slice and dice the uses

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165. For further discussion about the used item marketplace, see Charles Lopresto, Note, *Gamestopped: Vernor v. Autodesk and the Future of Resale*, 21 CORNELL J.L. & PUB. POL'Y 227, 243 (2011).

of an item to more appropriately fit their needs. By allowing a user to pay for a ten-day trial or a restricted use copy of the software, the needs of the consumer can be fit into the pricing scheme of the creator, rather than relying on third party transactions. One example of this system is seen in the modern versions of operating systems and office suites that are priced differently under student licenses and business licenses. These uses are tailored to the specific license given.<sup>166</sup> By utilizing licenses, content creators may avoid complicated economic scenarios where the supply outstrips the demand simply through resale.

Creators can utilize these forms of licenses to better target consumers and achieve a more significant return on their products. If creators are able to adequately price each item for each use, they might be more likely to spend time developing those specific uses. In today's digital world, few software products are sold "as is" at the time of sale. Software is often tied with ongoing online infrastructure, support mechanisms, updates, revisions and additions. Trying to price this long-term support into the initial sale—and account for resale among consumers—is a daunting task.<sup>167</sup> Take, for example, the creation of an additional three hours of content for a forty-hour video game. If that additional content can be resold among consumers, the creator might see too little return on such a small product to bother providing it. As intellectual property rights as a whole are intended to foster the creation of ideas, the economic realities of these rights must be taken into account. The ever-evolving and modular nature of software poses particular difficulties for a world in which licenses and sales are not clearly defined.

As emphasized by the many viewpoints above, it is difficult to argue that one type of transaction is better than the other. Both regimes have costs and benefits that provide the market with a more robust ability to adapt. Licensing clearly plays a larger role in today's digital economy. As increasing amounts of content are created for targeted temporary uses, content creators utilize licenses to restrict subsequent sales and guarantee the preservation of these targeted uses, as mentioned above. Rather than forcing *all* transfers of property to be open to unrestricted future sales, the first sale doctrine provides that *at least one* transfer of property is openly transferable.<sup>168</sup> Presumably a buyer who is gaining full title to property is paying for the right to sell that property in the future, while the buyer who is given notice of his limited license is only paying for that individual stick from the bundle of property rights. The court must preserve this bargained-for exchange in order to preserve the balance between licenses and sales. The goal is not to unduly push the factors to support one regime over the other but rather to ensure that the licensing regime is supported by an adequate return for the property owner.

166. See, e.g., *Office Suites*, MICROSOFT STORE ONLINE, <http://www.microsoftstore.com/store/msstore/list/parentCategoryID.37286600/categoryID.50726300> (last visited Apr. 8, 2012).

167. See generally Christian A. Nandan, *Software Licensing in the 21st Century: Are Software "Licenses" Really Sales, and how Will the Software Industry Respond?*, 32 AIPLA Q.J. 555, 581 (2004).

168. See *supra* Part II.A.



### C. LOOKING FORWARD

After considering the goals of the first sale doctrine, it is apparent that the multifactor test passed down from *Wise* has difficulty responding to modern copyright transactions. These tests do not adequately account for day-to-day consumer transactions that form the basis for these modern cases, as these commonplace transactions do not fall neatly into the categories proscribed by the courts. These tests must interact with the factors apparent to everyday consumers and take into account what agreement the consumer believes he is entering into. The Court of Appeals should have paid more attention to the specifics of *Vernor* and the developments in cases like *Softman* when it attempted to reconcile the opinions of *Wise* and the *MAI* Trio. In order to properly create a coherent doctrine, a court must incorporate more of the consumer perspective into the evaluation of these transactions. As noted above in the Total list, upfront payment and indefinite possession are examples of consumer perspective factors that may be incorporated into the tests.<sup>169</sup> *Vernor* purchased the software specifically for the purpose of resale. Much like in *Softman*, he never opened the package or installed the software, and thus was not exposed to the license. *Softman* argued that any lump-sum payment for software is a sale.<sup>170</sup> This delineation is too blunt an instrument in such a delicate area of the law; but it highlights the importance of elements like lump-sum or upfront payments. These hallmarks of a sale are essential elements in how a consumer perceives a transaction and evaluates the bargained-for exchange of property.

Despite *Softman*'s bright-line approach, the *Softman* Court made a very strong argument concerning the application of licenses to purchasers who never saw or accepted the licensing agreement. The notion of holding someone to a contract that was never even seen by the party is questionable at best. When combined with the purpose of the first sale doctrine, using this tactic to deprive purchasers of resale rights is a severe disruption of the bargain inherent in property transactions. These hidden or unaccepted license agreements were not explicitly discussed in *Wise*, the *MAI* Trio, or *Vernor*. There was no evidence that *Vernor* ever installed the software or agreed to the software licensing agreement contained therein.<sup>171</sup> These multifactor tests should account for the situation where the licensing agreement is never shown to the purchaser who refrains from opening the box.

Nevertheless, a discussion of the bargained-for exchange of property rights delves much more deeply into the realm of contracts than the scope of this Note permits. It simply must be stated that the bargained-for exchange and the clarity of such bargains are important focal points for future discussion concerning the first sale doctrine.<sup>172</sup> If a transaction appears to be a sale when money is exchanged and

169. See *supra* Part IV.A.1.

170. *SoftMan Products Co. v. Adobe Sys. Inc.*, 171 F. Supp. 2d 1075, 1086 (C.D. Cal. 2001).

171. See *Vernor v. Autodesk, Inc.*, No. C07-1189RAJ, 2009 WL 3187613, at \*1 (W.D. Wash. Sept. 30, 2009).

172. This also is a strong argument that Congress needs to step in and update the applicable copyright law. As mentioned by Adam Sikich in *Buyer Beware: The Threat to the First Sale Doctrine*

is only seen to be a license after the transaction, this initial appearance should weigh in favor of the finding of a sale overall. Rather than focusing on the title hidden within the restrictive agreement, courts may look to what the transaction initially looks like to the consumer. Clarity in the bargained for exchange is central to the protection of property rights.

It strains the prior precedent in this area to reconfigure the *Wise* factors without proposing additional concerns such as those raised by *Softman*. In this instance, the Court of Appeals has not addressed any new shifts in contract law or technology concerning these agreements. In fact, the Court overlooked many of these aspects though they seem ripe for discussion.

## VI. CONCLUSION

Upon examining the precedent from *Wise* and the *MAI* Trio, it is unclear why the Court of Appeals produced such a constrained test and eschewed the factors of indefinite possession and upfront payment. In contrast to the Court of Appeals' three-factor test, the five factors listed above seem to be the most consistent with prior precedent, though not necessarily what would be ideal in today's copyright market. But this unclear reasoning by the Court and the confusion it is likely to cause is only part of the issue. Ultimately the market will adjust to whatever factors are determined by the courts, and one would expect that Congress will further amend the Copyright Act to reflect the protections needed. The more glaring absence, as mentioned, is the notion of "click-through" licensing and resellers who do not activate software. The relevant discussion seems to side more with the forms of the licenses and the manner in which they are presented to and agreed to by purchasers. Ignoring these issues in favor of small changes in the lists of factors only delays necessary improvements in the law. Debating the labels of a "license" versus a "sale" will become much less important if the market becomes more knowledgeable and can adjust to fit with the expectations of consumers. The more confusing the law is in this area, the more difficulty the market will have in adjusting to the new rule. Future courts should more carefully explain their conclusions and ensure that their decisions are compatible with the day-to-day transactions to which the laws apply.

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*in the Digital Age*, 14 J. INTERNET L. 1, 1 (Jan. 2011), the copyright law is long overdue for an overhaul with regard to digital transactions.