

UNPLUGGED:  
THE MUSIC INDUSTRY'S APPROACH TO ROLLING  
CONTRACTS ON MUSIC CDS<sup>1</sup>

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**Liner Notes**

I recently heard that Grammy Artist Alicia Keys released a live “Unplugged” (acoustic) album. Interested in quality music, I did some research and discovered that “Alicia Keys Unplugged” was released in 2005 on the J Records label, a unit of Sony BMG Music Entertainment.<sup>2</sup> I did what many music fans do: I went to Sony’s website and ordered a copy. A few days later I received the compact disc (CD) in the mail and listened to it on my Sony Discman while exercising. I actually left the CD in my car stereo for a few months and occasionally listened to it over that period of time.

Recently, I brought the CD into my house to “rip” it into my computer so that I could listen to it both throughout my house on my computer-network-based home entertainment system, and while I worked on my computer. What appeared on my computer screen next is the subject of this article.

Consumers are now accustomed to seeing End User License Agreements (EULAs) when they download material from the Internet or purchase software. Consumers are not, however, accustomed to an End User License Agreement on a music CD—a development which has consequential ramifications that call for legal exploration.

The software industry started using End User License Agreements in the form of shrinkwrap licenses as independently purchased, low-cost software for personal computers became popular.<sup>3</sup> This practice later developed into the use of “clickwrap” agreements, wherein

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**<sup>1</sup> IMPORTANT – READ CAREFULLY: THIS DOCUMENT IS COVERED BY AN END USER LICENSE AGREEMENT THAT YOU COMMITTED TO EARLIER THIS MORNING DESPITE UNAWARENESS OF SUCH. THE TERMS OF THAT LICENSE WILL BE SUPPLIED TO YOU AT A LATER DATE BUT YOU AGREE THAT THEY ARE ALL BINDING. SUFFICE IT TO SAY, THEY INCLUDE THE FACT THAT ANY REFERENCE TO THIS ARTICLE NOT PROPERLY CITED TO THIS ARTICLE WILL CAUSE YOU TO GET THE FLU. YOU ARE GIVEN AUTHORIZATION TO USE THIS ARTICLE FOR YOUR OWN ENJOYMENT BUT YOU AGREE THAT ANY PUBLIC DISSEMINATION WILL RESULT IN ADDING FIVE YEARS TO YOUR AGE. RANDOM, ARBITRARY, AND UNCLARIFIED RIGHTS ARE RESERVED TO THE AUTHOR. FINALLY, YOU ALSO CEDE YOUR FREE SPEECH RIGHTS UNLESS YOUR SPEECH IS EITHER HELPFUL OR RAVISHINGLY COMPLIMENTARY.**

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<sup>2</sup> Alicia Keys, *Unplugged* (J Records, a unit of Sony BMG Music Entertainment 2005).

<sup>3</sup> Robert W. Gomulkiewicz & Mary L. Williamson, *A Brief Defense of Mass Market Software License Agreements*, 22 Rutgers Computer & Tech. L.J. 335, 339 (1996).

customers approve of the terms and conditions of purchase when they install and use a given piece of software for the first time.<sup>4</sup> Contracts such as these, that allow acceptance of the terms after the money changes hands, are often called “rolling contracts.” The term encompasses a broad swath of agreements such as browsewrap, clickwrap and shrinkwrap contracts. Customers have long associated shrinkwrap and clickwrap agreements with software products. The model works particularly well with software because the item of value to the consumer is software affixed to a tangible medium—the medium functioning as a format for delivery. Therefore, the consumer can agree to the manufacturer’s terms before using the software, but still has the option of returning the software if the consumer objects to the terms.<sup>5</sup>

When a manufacturer includes a clickwrap agreement on a music CD, however, the situation is very different. Consumers expect that they are purchasing discs with the typical legal rights: those associated with the First Sale Doctrine—the right to use, the right to sell, and the right to gift—and those associated with the fair use defense. The consumers do not expect that their purchase will be subject to enclosed terms and conditions, and may not find them until years after purchasing the CD. I was able to listen to “Alicia Keys Unplugged” for many months, knowing that I had lost my right to return it, but before realizing that my “purchase” of the CD was part of an involved, almost 3000 word contract. This situation would provide a perplexing legal dilemma if the terms on the CD referred only to software on the disc that accompanied the music—perhaps “bonus material” that consumers are to discover after they put the CDs into their computers, where notice on the front indicated that the *bonus material* is subject to terms and conditions.

The record companies, however, are using the clickwrap agreement to affect, *ex post*, the purchaser’s rights to the *music itself*. This agreement impacts the users’ rights under the Copyright Statute, their claims to fair use, and even their right to sell the disc. The consumers cede all of these rights retroactively, upon agreeing to the terms of the clickwrap agreement. Furthermore, consumers are frequently given no notice that their rights in the music or in the disc itself are subject to a license agreement when they purchase the CD.<sup>6</sup> Apparently, under the terms of my agreement with Sony BMG Music Entertainment, listening to Alicia Keys on my car stereo for three months may have qualified as a breach of contract, and I may be subject to the laws and jurisdiction of a court 2500 miles away should Sony choose to pursue this matter.<sup>7</sup>

Clickwrap agreements on music CDs are becoming pervasive. Multiple companies compete in the market to provide technological protection measures called “Digital Rights Management” (DRM) for the CD market. Sony used DRM software called “XCP2,” made by

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<sup>4</sup> Steven A. Heath, *Contracts, Copyright, and Confusion Revisiting the Enforceability of ‘Shrinkwrap’ Licenses*, 5 Chi-Kent J. Intell. Prop. 12, 25 (2005) (“...the practice of ‘shrinkwrapping’ is rapidly giving way to ‘browsewrap’ and ‘clickwrap’ agreements”).

<sup>5</sup> Whether or not software can be returned is not always evident, though according to *ProCD Inc. v. Zeidenberg*, 86 F.3d 1447 (7th Cir. 1996) discussed *infra*, p. 281, software is inherently returnable if the consumer does not agree with the terms of the clickwrap agreement.

<sup>6</sup> As discussed *infra*, the notice typically indicates that a license agreement is included, but implies that the license agreement is related to enclosed software, not to the music itself.

<sup>7</sup> The contract on my Alicia Keys CD indicates that any disputes arising under the contract are to be settled in New York courts, though I live on the West Coast.

First 4 Internet, on fifty-two titles representing more than four million CD sales.<sup>8</sup> A competing DRM manufacturer, SunnComm, estimated that by the end of the year their MediaMax DRM software and license (used on my Alicia Keys CD)<sup>9</sup> will be on 145 million audio CDs in 2006, and used by thirty record labels.<sup>10</sup> The leading DRM software manufacturer in multiple industries, Macrovision, claims that its similar DRM is used on over 400 million CDs.<sup>11</sup> The prevalence of DRM makes a legal analysis particularly timely.

In this article I analyze rolling contracts for music compact discs through a historical analysis of both rolling contracts and music sales. In the first part of this article I address the history of rolling contract use, the current framework of the rolling contract debate, and the attempts to statutorily concretize the legitimacy of rolling contracts. In the second section, I address the history of contractual issues in music distribution, including the recent shift toward using rolling contracts on consumer music CDs. With a thorough legal background of both the contract theory and the music distribution models used in the past century, I analyze the legal enforceability of this new breed of rolling contract. I conclude that manufacturers' use of rolling contracts in the music industry leaves consumers vulnerable and highlights the problems with rolling contracts brought about by their detractors. In short, I state that these contracts are legally unenforceable. All parties should take action to allow record labels to use licenses that comport with basic contracting theory.

### **Disc 1: A Recap on Rolling Contract Theory**

In this portion of my article I briefly trace the history of rolling contract theory. I begin with a review of the cases that laid the framework for rolling contract law and provide a backdrop of the state of the law at that time and an analysis of each case's holding. With this framework in place I discuss the current state of rolling contracts by extracting the rule that emerges from the case law and applying it to music industry contracts. Next, I discuss the attempt to uniformly codify rolling contracts as they are used in electronic commerce through the Uniform Computer Information Transactions Act. Finally, I analyze the contracts used by the music delivery industry to assess their legal enforceability under both the current law and proposed legislation.

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<sup>8</sup> Andrew Edgecliffe-Johnson, *Sony BMG to compensate buys of flawed CDs MEDIA*, Financial Times UK, Dec. 31, 2005, at 9.

<sup>9</sup> CDs do not normally indicate which form of copy protection is used. Record labels further do not generally indicate which form of protection is used on their CDs until liability requires them to. Sony BMG has published a list of CDs containing MediaMax Version 5 software because of "security vulnerability that may exist with regard to" the software. SonyBMG.com, MediaMax Titles, <http://www.sonybmg.com/mediamax/titles.html> (last visited Nov. 5, 2005).

<sup>10</sup> Press Release, SunnComm International, SunnComm Forecasts that its MediaMax CD Copy Management Technology will be Applied to More than 145,000,000 Audio CDs this Year (Feb. 1, 2005) *available at* <http://www.sunncomm.com/press/pressrelease.asp?prid=200502010915>.

<sup>11</sup> Press Release, Macrovision, Macrovision Showcases Latest Music Protection and Anti-Piracy Solutions at Midem 2005 (Jan. 23, 2005) *available at* <http://www.macrovision.com/company/news/releases/newsdetail.jsp?id=Mon%20Jan%2024%2009:03:43%20PST%202005>. Note, most of these CDs are distributed in foreign markets where piracy is much greater concern.

*Track 1: History*

Any history of “rolling contracts” requires a thorough examination of Judge Easterbrook’s decision in the seminal case *ProCD, Inc. v. Zeidenberg*.<sup>12</sup> In that case, the defendant, Matthew Zeidenberg, purchased databases on compact disc (CD-ROMs) from a retail outlet in Madison, Wisconsin.<sup>13</sup> The databases, containing phone records from more than 3,000 phone directories, were compiled by ProCD, Inc. and distributed as the software product, SelectPhone™.<sup>14</sup> Because the material on the CD-ROMs was not copyrightable, ProCD resorted to a license to prevent users from copying and disseminating the material at a lower price.<sup>15</sup> The license was not printed on the outside of the box, however, but was instead “...encoded on the CD-ROM disks as well as printed in the manual, and [] appear[ed] on a user’s screen every time the software [ran]...”<sup>16</sup> Zeidenberg, despite the license, copied the information and redistributed the databases on the Internet at a lower price.<sup>17</sup> ProCD, Inc. brought suit against Zeidenberg for breach of contract.<sup>18</sup>

Zeidenberg naturally argued that his contract to purchase the software was fully integrated when he accepted the offer to purchase the software by paying for the software and leaving the store.<sup>19</sup> According to Zeidenberg, because the license agreement was not available for his review as a part of his purchase contract until after money had exchanged hands, the license agreement was a proposed *additional* contract lacking any form of consideration.<sup>20</sup>

Judge Easterbrook rejected this notion, instead recalling that “a vendor, as master of the offer, may invite acceptance by conduct, and may propose limitations on the kind of conduct that constitutes acceptance.”<sup>21</sup> He asserted that the offer provided to Zeidenberg required acceptance, not in the traditional form of accepting Zeidenberg’s money, but rather in the form of accepting the terms of the license on the screen when operating the software.<sup>22</sup> Until the license on the computer had been signed, the contract was not complete and Zeidenberg was free to unwind the incomplete contract and return the software for a refund.<sup>23</sup> This was substantiated by the UCC definition of “acceptance of goods” in which Judge Easterbrook found that “[a] buyer accepts goods ... when, after an opportunity to inspect, he fails to make an effective rejection...”<sup>24</sup>

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<sup>12</sup> *ProCD Inc.*, 86 F.3d 1447.

<sup>13</sup> *Id.* at 1450.

<sup>14</sup> *Id.* at 1449.

<sup>15</sup> *Id.* at 1450.

<sup>16</sup> *Id.*

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> *ProCD, Inc. v. Zeidenberg*, 908 F.Supp. 640, 651 (W.D.Wis. 1996) (“In defendants’ view, the contract for the sale ... was completed at the time of sale and the license represents additional terms to which they cannot be bound...”).

<sup>20</sup> *ProCD Inc.*, 86 F.3d at 1450 (Judge Easterbrook noted that there may be a difference between “contracts” and “licenses” and further noted the potential importance this difference has in cases involving copyright issues (noting *Microsoft Corp. v. Harmony Computers & Electronics, Inc.* 846 F.Supp. 208, 214 (E.D.N.Y. 1994)).

<sup>21</sup> *Id.* at 1452.

<sup>22</sup> *Id.*

<sup>23</sup> *Id.* (“Any buyer ... can prevent formation of the contract by returning the package, as can any consumer who concludes that the terms of the license make the software worth less than the purchase price.”)

<sup>24</sup> *Id.* at 1452.

Judge Easterbrook found that the UCC did not require the terms of the contract to be explicit or conspicuous.<sup>25</sup>

Perhaps the most conspicuous part of Judge Easterbrook's rationale for upholding the license as a valid contract is the pragmatic argument that if Zeidenberg's argument was taken seriously it "would drive prices through the ceiling or return transactions to the horse-and-buggy age."<sup>26</sup> In essence, he argues, the software industry had been using these license agreements for years and had developed a standard methodology for doing so. Invalidating the agreements was not practical in light of the state of software transactions in 1996. Judge Easterbrook decided *ProCD* on similar grounds as a later Massachusetts case which upheld "money now, terms later" contracts under the UCC "shall be liberally construed and applied to promote its underlying purposes and policies" which include "the continued expansion of commercial practices through customary usage and agreement of the parties."<sup>27</sup>

Lest the courts in Wisconsin run amok, the Seventh Circuit further clarified its position on rolling contracts only a year later, in *Hill v. Gateway 2000, Inc.*<sup>28</sup> In that case, the buyers of a computer claimed that the arbitration clause provided on a piece of paper inside the box containing their new computer was invalid.<sup>29</sup> The Hills purchased their computer from Gateway 2000, Inc. over the telephone and apparently received no notice from the telephone agent that additional terms such as an arbitration clause would apply.<sup>30</sup> Judge Easterbrook indicated, however, that Gateway's advertisements discussed limited warranties and lifetime support, and that therefore the Hills were on constructive notice that additional documentation detailing the terms of the warranties and support must have been available.<sup>31</sup> Once a buyer knows that additional information is available, Judge Easterbrook described three ways in which a buyer might determine what the terms of the contract are: (1) by requesting the information from the vendor before purchasing the item, (2) by obtaining the information from third parties, or (3) by reviewing the documentation in the box after receiving the item.<sup>32</sup> As such, the case fell within the bounds of the holding in *ProCD*—Gateway's offer was contingent on acceptance, which was not complete upon exchanging money, but instead was complete according to the conditions of the offer, which included the failure to reject the item purchased within an allotted timeframe.<sup>33</sup>

These two Seventh Circuit cases laid the groundwork for an area of contract law referred to interchangeably as "rolling contracts,"<sup>34</sup> "layered contracts,"<sup>35</sup> or "delayed terms" in a mass-

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<sup>25</sup> *Id.* at 1453.

<sup>26</sup> *Id.* at 1452.

<sup>27</sup> *I. Lan Sys. v. Netscout Serv. Level Corp.* 183 F.Supp. 2d 328, 338 (D. Mass 2002).

<sup>28</sup> *Hill v. Gateway, Inc.* 105 F.3d 1147 (7th Cir. 1997).

<sup>29</sup> *Id.* at 1148.

<sup>30</sup> *Id.* at 1150.

<sup>31</sup> *Id.*

<sup>32</sup> *Id.*

<sup>33</sup> *Id.* (The documentation from Gateway provided that the terms of the documentation in the box governed unless the customer returned the computer within 30 days. *Id.* at 1148).

<sup>34</sup> Stephen E. Friedman, *Improving the Rolling Contract*, 56 Am. U.L. Rev. 1, 4 n.3 (2006).

<sup>35</sup> See, e.g. *M.A. Mortenson Co. v. Timberline Software Corp.*, 998 P.3d 305, 313 (Wash. 2000) ("We conclude ... RCW 62A.2-204 ... allows the formation of "layered contracts" similar to those envisioned by *ProCD*, *Hill*, and *Brower*").

market transaction<sup>36</sup>, or, perhaps pejoratively, as “checkerboard contracts.”<sup>37</sup> With this framework we arrive at the current situation with respect to these contracts.

Many courts in multiple circuits have followed the rationale provided by the Seventh Circuit.<sup>38</sup> Not all courts, however, have come to the same conclusion.<sup>39</sup> While some exceptions still exist, the trend seems to be moving towards acceptance of rolling contracts as legally sustainable.

### *Track 2: The Current Framework*

Legal scholars frequently object to extending acceptance of contract terms beyond the financial transaction.<sup>40</sup> The rationale for these scholars’ positions is understandable; the notion that terms that are provided to the user only after consummation of the otherwise-final contract is anathema to traditional contract law theory.<sup>41</sup> Post-transaction terms also make the recipient of the terms (the consumer in traditional consumer transactions) a potential victim.<sup>42</sup> The traditional academic defense of “the little guy” logically places many scholars in opposition to the strategy of large corporations. These corporations create terms and conditions of purchase and then bury them in contracts that are not only so exhaustive that the contracts negate the possibility that users will read them,<sup>43</sup> but further fail to provide ample notice of the terms and conditions.<sup>44</sup>

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<sup>36</sup> Jean Braucher, *Amended Article 2 and the Decision to Trust the Courts: The Case Against Enforcing Delayed Mass-Market Terms, Especially for Software*, 2004 Wis. L. Rev. 753, 757 (2004) (objecting to the term “rolling contracts” as it implies that the delayed terms are a part of a legitimate contract).

<sup>37</sup> Peter A. Alces, *On Discovering Doctrine: “Justice” in Contract Agreement*, 83 Wash. U.L.Q. 471, 497 (2005) (stating that Judge Easterbrook’s concession to pragmatism leaves contract doctrine “when it suits and ‘practical considerations’ when traditional doctrine does not”).

<sup>38</sup> Gregory J. Krabacher, *Revocation of Tripartite Rolling Contracts: Finding a Remedy in the Twenty-First Century Usage of Trade*, 66 Ohio St. L. J. 397, 414-20 (2005). See, e.g., *M.A. Mortenson*, 998 P.3d at 313; *I. Lan Sys*, 183 F.Supp. 2d at 338 (holding that where a contractual dispute arose over use of business software, the clickwrap license agreement is a valid part of the contract); *Higgs v. Automotive Warranty Corp. of America*, 134 Fed.Appx. 828 (6th Cir. 2005) (citing *Hill* in holding that an arbitration clause contained in an automobile repair warranty was enforceable); *Brower v. Gateway 2000, Inc.*, 246 A.D.2d 246 (N.Y.App. Div. 1 Dept. 1998) (holding that the contract in question in *Hill* was only fully integrated once the return period had expired).

<sup>39</sup> *Arizona Retail Systems, Inc. v. Software Link, Inc.*, 831 F.Supp. 759, 766 (D.Ariz 1993) (finding that the offer to purchase software came from the buyer and the acceptance came from the seller upon commitment to ship the software. The license agreement was, therefore, a proposal to modify the agreement and required the buyer’s assent).

<sup>40</sup> Robert M. Gomulkiewicz, *Getting Serious About User-Friendly Mass-Market Licensing for Software*, 12 Geo. Mason L. Rev. 687, 687 (2004) (alleging that most of the more than one hundred law review articles written on the subject of shrink wrap licenses since 1984 have both criticized End User License Agreements and have argued that courts should not enforce them).

<sup>41</sup> Braucher, *supra* note 36 at 761 (running mass-market licensing schemes through the traditional offer-acceptance contract model and arguing that post-transaction terms fail to garner “express agreement” in accord with UCC requirements).

<sup>42</sup> Robert A. Hillman & Jeffrey J. Rachlinski, *Standard-Form Contracting in the Electronic Age*, 77 N.Y.U.L. Rev. 429, 431 (discussing the prevalence of business-to-consumer transactions that include standard-form contracts and the “increasing alacrity” with which these contracts are being used in “clickwrap” or “browsewrap” contexts).

<sup>43</sup> *Id.* at 468. Professors Hillman and Rachlinski also note the inability of users to negotiate the terms of the contract they receive after consummation of the financial transaction, as opposed to terms in boiler-plate contracts in paper form that they can presumably edit or modify at the time of acceptance. Professor Friedman further notes the

Courts, however, seem moved by an appeal to the pragmatic. Recalling the assertion that denying the legitimacy of shrinkwrap agreements would return contracts to the “horse-and-buggy age,”<sup>45</sup> other courts have noted the practical benefits of allowing post-financial transaction terms. The Seventh Circuit (Judge Easterbrook again writing for the majority) further elucidated on practical concerns in *Hill*,

If the staff at the other end of the phone for direct-sales operations such as Gateway's had to read the four-page statement of terms before taking the buyer's credit card number, the droning voice would anesthetize rather than enlighten many potential buyers. Others would hang up in a rage over the waste of their time. And oral recitation would not avoid customers' assertions (whether true or feigned) that the clerk did not read term X to them, or that they did not remember or understand it. Writing provides benefits for both sides of commercial transactions. Customers as a group are better off when vendors skip costly and ineffectual steps such as telephonic recitation, and use instead a simple approve-or-return device. Competent adults are bound by such documents, read or unread.<sup>46</sup>

Judge Easterbrook seemed to be reaching with his contractual analysis, but his conclusion is sound. Zeidenberg had no apparent notice prior to purchasing the software that additional terms would follow.<sup>47</sup> If the offeror is the master of the offer and can determine the means by which assent is manifested, should the assentor not be aware of the requirements of assent as a part of the offer? Zeidenberg's claim that he assented at the time of the financial transaction, having no indication from the offeror that a non-traditional form of acceptance was required, is certainly a reasonable position.<sup>48</sup> Yet Judge Easterbrook still found a contract existed that included licensing terms.<sup>49</sup> The heart of his rationale probably stems from his practical argument.<sup>50</sup> If *ProCD* and its progeny cases were decided, not on mechanical jurisprudence contractual analysis, but rather based on practical considerations for the modern age of commercial transactions, then logic would dictate that these contracts will be upheld in more jurisdictions in the future. Clickwrap, browsewrap, shrinkwrap, and other “money now, terms later” agreements involved in electronic commerce are becoming more prevalent than they were when Matthew Zeidenberg challenged the legitimacy of his contract with ProCD Inc. in 1996.<sup>51</sup> Repealing these agreements' validity now would yield greater cataclysmic consequences to the

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psychological disadvantage at which consumers are placed when accepting receipt of a product prior to assenting to the terms of the contract. Friedman, *supra* note 34 at 15-19.

<sup>44</sup> Jeff C. Dodd, *Time and Assent in the Formation of Information Contracts: The Mischief of Applying Article 2 to Information Contracts*, 36 Hous. L. Rev. 195, 210 (1999) (noting that the traditional contract doctrine, in which “contracts result from negotiations between parties with equal, or relatively equal, bargaining power” does not apply to licensing agreements used in software transactions).

<sup>45</sup> *ProCD, Inc.*, 86 F.3d at 1452.

<sup>46</sup> *Hill*, 105 F.3d at 1149.

<sup>47</sup> *Id.* at 1453 (explaining that certain contractual terms must be “conspicuous,” but that the terms at issue here did not require that level of notice).

<sup>48</sup> Professor Friedman suggests that Judge Easterbrook may not have required a more robust pre-sale notice requirement in *ProCD* because of the level of sophistication of the buyer and the notion that a reasonable consumer of such sophistication should reasonably expect a license agreement. Friedman, *supra* note 34 at 7.

<sup>49</sup> *ProCD, Inc.*, 86 F.3d at 1449.

<sup>50</sup> *Id.* at 1452.

<sup>51</sup> See, Hillman & Rachlinski, *supra* note 42 at 429. See also Dodd, *supra* note 44 at 219-20.

state of consumer transactions than it would have in 1996. Even scholars who object to the legitimacy of the rolling contracts model concede that mass-market license schemes are here to stay.<sup>52</sup>

The ProCD lineage of cases, however, does not presume that all rolling contracts are valid. The rule that surfaces requires that any valid contract that provides terms to the buyer after the financial transaction must provide notice to the consumer that those terms are to follow.<sup>53</sup> This notice can come either directly (where the consumer receives notice at the time of purchase<sup>54</sup>) or constructively (by means of an assumption that additional terms are required for the transaction based on either the type of goods involved in the transaction or the sophistication of the consumer<sup>55</sup>). The buyer must also have the opportunity to review the terms of the contract prior to assenting.<sup>56</sup> Further, the consumer must have the ability to return the goods and unwind the contract if the terms are not acceptable.<sup>57</sup> The timeframe in which the consumer must make a keep-or-return acceptance decision may be established by the seller.<sup>58</sup> Finally, any contract must be conscionable<sup>59</sup> and comport with the other common-law requirements of contract law.<sup>60</sup>

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<sup>52</sup> See, e.g., Dodd, *supra* note 44 at 219 (asserting that courts “know business cannot be done without” standard-form contracts); Krabacher, *supra* note 38 at 440; John A. Rothchild, *The Incredible Shrinking First-Sale Rule: Are Software Resale Limits Lawful?*, 57 Rutgers L. Rev. 1, 13 n.37 (2004) (arguing that software licenses violate the First Sale Doctrine, but suggesting that, because they are pervasive, an alternate analysis is in order).

<sup>53</sup> Professor Friedman notes that some cases have not apparently required notice, at least as discussed in the court rulings, and he cites a string of district court cases to support this: “See, e.g., *Westendorf v. Gateway, 2000 Inc.*, No. 16913, 2000 WL 307369 (Del. Ch. Mar. 16, 2000) (following rationale of Hill without mention of whether buyer had notice that additional terms would be involved in transaction); *Brower v. Gateway 2000, Inc.*, 676 N.Y.S.2d 569 (App. Div. 1998) (same); see also *O’Quin v. Verizon Wireless*, 256 F. Supp. 2d 512(M.D. La. 2003) (determining, without discussion of whether buyer had notice of additional terms before signing contract, that the arbitration agreement in a cellular telephone service plan was enforceable even though it was provided after service contract was signed); *Lozano v. AT&T Wireless*, 216 F. Supp. 2d 1071 (C.D. Cal. 2002) (similar).” Friedman, *supra* note 34 at n.63. I contend that courts may have avoided specific mention of notice requirements under an assumption that notice was provided constructively. See *infra* note 55. See also *Specht v. Netscape Communications Corp.*, 306 F.3d 17, 29 (2d Cir. 2002) (“a consumer’s clicking on a download button does not communicate assent to contractual terms if the offer did not make clear to the consumer that clicking on the download button would signify assent to those terms...”).

<sup>54</sup> See, e.g., *I.Lan Systems, Inc.* 183 F.Supp.2d at 339 (finding a clickwrap agreement valid because an earlier agreement between the two parties expressly mentioned an impending clickwrap agreement with subsequent terms).

<sup>55</sup> See *supra* note 48. See also *M.A. Mortenson*, 998 P.2d at 314 (noting that the defendant had purchased multiple pieces of software from the plaintiff, including a previous version of the software in question, and all of the software came with the same terms. Further, such license agreements are standard throughout their industry, thereby putting the defendant on constructive notice that additional terms were forthcoming); *Hill*, 105 F.3d at 1150 (holding that the customer was under notice that *some* additional terms were necessary for the sale. In that specific case the customer was notified through generic advertisements by Gateway that their products came with “limited warranties and lifetime support.” These product guarantees, according to the Court, inherently required further terms, thereby providing the Hills with notice that additional terms for the sale were inevitable. Judge Easterbrook noted three ways in which the Hills could have received the additional documentation, two of which would have provided them with the information prior to the transaction).

<sup>56</sup> *Specht*, 306 F.3d at 28-32 (holding that a license agreement that only shows up on a screen when a user voluntarily scrolled down the screen past the “download” button did not provide adequate opportunity for the purchasers to review and consent to the terms as a part of the contract).

<sup>57</sup> *ProCD Inc.*, 86 F.3d at 1453 (noting that under the UCC the “opportunity to return goods can be important” and noting the UCC’s tendency to allow buyers the opportunity to make a final decision after “a detailed review”).

<sup>58</sup> *Hill*, 105 F.3d at 1150 (accepting the end of a thirty day return period as the critical date of contract formation if the buyer failed to timely return the item). *Hill* speaks to the “failure to timely return is an acceptance” contract in



*Track 3: The Concretization of Rolling Contracts*

These guidelines should not come as a surprise. Indeed the National Conference of Commissioners on Uniform State Laws (NCCUSL) and the American Law Institute (ALI) foresaw many issues relating to the coming electronic transaction era where the existing code was weak. The groups originally attempted to augment Article 2 of the highly successful Uniform Commercial Code (UCC) with a new section entitled Article 2b.<sup>61</sup> After the code failed to gain the assent of the ALI, it was renamed the Uniform Computer Information Transactions Act (hereinafter UCITA) in 2002.<sup>62</sup> The Act has been highly controversial, drawing strong letters of opposition from States' Attorneys General<sup>63</sup> as well as private industries.<sup>64</sup> As of the writing of this article the Act has been adopted in only two states: Maryland and Virginia.<sup>65</sup>

One of the many objections to UCITA was that it was generally favorable to manufacturers' use of shrinkwrap licenses,<sup>66</sup> creating an entire legally tenable paradigm for the software licensing industry.<sup>67</sup> In light of the emerging legal trends with respect to shrinkwrap licenses, however, UCITA can be read as consumer-friendly, because it creates shrinkwrap license requirements that are even more stringent than those enforced by the courts to date.

UCITA provides the following requirements for Mass-Market Licenses:

1. Licensees must have an opportunity to review terms prior to agreeing to them<sup>68</sup>
2. Licenses must be immediately available in printable, storable,<sup>69</sup> or non-electronic forms<sup>70</sup> that licensees can keep. If the licensee cannot print or store the license, the manufacturer must provide a copy at no additional cost<sup>71</sup>

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which failure to act functions as an assent. *ProCD* speaks to an indeterminate timeframe in which the buyer can choose to return the item, so long as the buyer does not actively assent to the terms of the contract.

<sup>59</sup> *I.Lan Systems, Inc.* 183 F.Supp.2d at 338 ("To be sure, shrinkwrap and clickwrap license agreements share the defect of any standardized contract--they are susceptible to the inclusion of terms that border on the unconscionable...").

<sup>60</sup> *E.g.* must not be created under duress, yield frustration of purpose, be impracticable or impossible, etc.

<sup>61</sup> Jack M. Graves, *Party Autonomy in Choice of Commercial Law: The Failure of Revised U.C.C. § 1-301 and a Proposal for Broader Reform*, 36 Seton Hall L. Rev. 59, 70-71 (2005).

<sup>62</sup> *Id.*

<sup>63</sup> Letter from W.A. Drew Edmonson et al., State Attorneys General, to Gene Lebrun, NCCUSL (July 23, 1999), available at [http://www.jamesshuggins.com/h/tek1/ucita\\_ags\\_19990723\\_letter.htm](http://www.jamesshuggins.com/h/tek1/ucita_ags_19990723_letter.htm).

<sup>64</sup> *E.g.* Letter from Cary H. Sherman, Senior Executive Vice President and General Counsel, Recording Industry Association of America, to NCCUSL, Carlyle Ring, Jr., Chair, UCC 2B Drafting Committee, Geoffrey C. Hazard, Jr., Director, ALI (Oct. 9, 1998) available at [http://www.jamesshuggins.com/h/tek1/ucita\\_riaa\\_19981009\\_letter.htm](http://www.jamesshuggins.com/h/tek1/ucita_riaa_19981009_letter.htm). (The RIAA objected to UCITA on many of the same grounds as the MPAA. Additional copies of letters from industries can also be found linked at the bottom of the aforementioned webpage, including the letter from the MPAA.)

<sup>65</sup> *I.Lan Systems, Inc.* 183 F.Supp.2d at 332.

<sup>66</sup> Matthew J. Smith, *Comment, An Overview of the Uniform Computer Information Transactions Act: Warranties, Self-Help, and Contract Formation – Why UCITA Should Be Renamed “The Licensors’ Protection Act,”* 25 S. Ill. U. L.J. 389, 394-400 (2001).

<sup>67</sup> U.C.I.T.A. Prefatory Note (2001), available at <http://www.law.upenn.edu/bll/ulc/ucita/2002final.pdf> (introducing UCITA as a legal framework for the era of electronic transactions).

<sup>68</sup> U.C.I.T.A. § 209 (a)(3) (2002).

<sup>69</sup> U.C.I.T.A. § 209 (a)(4)(A) (2002).

<sup>70</sup> U.C.I.T.A. § 209 (a)(4)(B) (2002).

3. If terms are proposed after an initial contract, the licensee must have had reason to know that terms would be proposed later<sup>72</sup>
4. The licensee has an absolute right to return the product for a refund if the licensee refuses the terms<sup>73</sup>
5. The licensor pays any costs of return<sup>74</sup>
6. The licensor pays for any actual damages caused by installing the product for purposes of reviewing the license.<sup>75</sup>
7. Terms must not be unconscionable<sup>76</sup>
8. Terms must not conflict with terms to which the parties have expressly agreed<sup>77</sup>

These requirements are certainly no less consumer friendly than the requirements put forth by the courts; UCITA arguably takes the courts' positions as a starting point to establish more stringent, explicit, uniform rules.<sup>78</sup> At this point, however, most consumers are not protected by these provisions.

UCITA can rightly be seen in one of two ways: either it is an attempt to codify preexisting contract law as it applies to and is interpreted for a different style of contract, or it is an attempt to create a new type of contract law specific to a new type of contract. UCITA itself seems to imply that it is a little of both. The Prefatory Note speaks to the irrelevance of preexisting rules (implying the latter) and uncertainty with respect to preexisting rules (implying the former).<sup>79</sup> Indeed, UCITA borrows significantly from existing precedent, but it also oversteps existing precedent in some areas. In this way the Act leans towards creating new law based on old rules rather than simply applying old rules to unfolding situations. For example, neither common law, the U.C.C., nor the cases involving rolling contracts stand for the proposition that the offering party must pay the entire cost of unwinding a contract should the parties not agree to terms. Yet UCITA requires the offeror to pay the entire cost of unwinding a Mass-Market Transaction.<sup>80</sup> A modern application of old rules would provide no basis for such burden shifting, leading the reader to assume that NCCUSL attempted to create new law. The "return" provisions in UCITA position the Act to overstep the common law in some areas, providing more protection than common law had previously provided. The drafters of UCITA seem to provide this protection almost as if to appease the consumer to obtain support for a law that might not otherwise receive consumer support.

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<sup>71</sup> U.C.I.T.A. § 209 (a)(4)(C) (2002).

<sup>72</sup> U.C.I.T.A. § 208 (2) (2002).

<sup>73</sup> U.C.I.T.A. § 113 (c) (2002); U.C.I.T.A. § 209 (b) (2002); U.C.I.T.A. § 209 (c) (2002).

<sup>74</sup> U.C.I.T.A. § 209 (b)(1) (2002).

<sup>75</sup> U.C.I.T.A. § 209 (b)(2) (2002).

<sup>76</sup> U.C.I.T.A. § 209 (a)(1) (2002).

<sup>77</sup> U.C.I.T.A. § 209 (a)(2) (2002).

<sup>78</sup> Many of the U.C.I.T.A. sections specifically refer to the cases referred to in this paper as a framework for the proposed rules. *See, e.g.*, U.C.I.T.A § 208 comment (recalling *ProCD, Inc.* and *M.A. Mortenson* in establishing the rules for layered contracts).

<sup>79</sup> U.C.I.T.A. Prefatory Note ¶ 2 (2002).

<sup>80</sup> U.C.I.T.A. § 209 (b) (2002).

Consumers did not provide support, however,<sup>81</sup> and UCITA has languished.<sup>82</sup> Consumers are instead subjected to the courts' attempts to apply the U.C.C. or common law to electronic transactions.<sup>83</sup> Evidence suggests that the courts are creating emerging common law based on pragmatic business and marketplace concerns rather than on consumer protection. The UCITA's Mass-Market Transactions provisions can therefore rightly be seen as providing protection for consumers beyond that currently provided by emerging common law or the U.C.C..

These provisions prove critical in examining how the music industry has started to use rolling contracts on music CDs, especially in light of what the NCCUSL and the software industry (through its praise for UCITA<sup>84</sup>) thought were acceptable, appropriate consumer protections.

## Disc 2: The Music Industry

In this portion of my article I trace a history of distribution and rights models in the music industry. I posit that there are four generally classifiable distribution and rights models that have been used to date: (1) the sale of music with no legal rights protection but some degree of technological rights protection; (2) the sale of music with both legal and technological rights protection; (3) the sale of music with legal rights protection but without technological protection; and (4) the sale of music with the current model of technological, legal, and contractual rights protections. I show how technological changes ushered in legislative change to ensure the rights of the copyright holders amid expanding abilities of consumers. In the 1990s, however, copyright holders took it upon themselves, with the tacit approval of Congress as evidenced by the Digital Millennium Copyright Act, to protect their rights through the use of Digital Rights Management. Copyright holders' use of Digital Rights Management created liabilities which resulted in the music industry's desire to use contractual provisions to waive their liabilities. The legal enforceability of the resulting contracts is the source of the third portion of this article.

### *Track 1: The Traditional Music Distribution Model: The First Sale Doctrine*

For the sake of clarification, music distribution has followed two separate paths. Originally, copyright in music extended only to its printed form – sheet music.<sup>85</sup> As such, copyright law affected music in much the same way as copyright law affected books or other printed materials. Copyright protection over printed music is therefore not at issue in this article.

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<sup>81</sup> Sandy T. Wu, *Uniform Computer Information Transactions Act: Failed to Appease its Opponents in Light of the Newly Adopted Amendments*, 33 Sw. U. L. Rev. 307, 324-25 (2004).

<sup>82</sup> UCITA has only been enacted in two states and has been dropped from the ABA House of Delegates. On July 31, 2003, the NCCUSL discharged the Standby Committee for UCITA.

<sup>83</sup> See, e.g., *I.Lan Systems, Inc.* 183 F.Supp.2d at 331-32 (noting the inapplicability of either the U.C.C. or common law in software license disputes).

<sup>84</sup> Press Release, Business Software Alliance, *New Proposed Uniform Law will Establish Legal Framework for E-Commerce* (Feb. 3, 2000) available at <http://www.bsa.org/usa/press/newsreleases/New-Proposed-Uniform-Law-will-Establish-Legal-Framework-for-E-Commerce.cfm>; UCITA: Rules for the Information Highway, <http://www.ncsl.org/programs/lis/CIP/CIPCOMM/ring0301.htm>, (at Supporters of UCITA and Concerns Resolved) (last visited Oct. 22, 2006).

<sup>85</sup> Copyright protection was extended to sheet music in 1831. Copyright Act of 1831, ch. 16, 4 Stat. 436 (1831).

In the late 1800s, however, the player piano became popular. Owners of player pianos purchased pre-punched “piano rolls,” scroll-like sheets of paper that had perforations that triggered the piano to play particular notes. Piano rolls were often created by hiring a pianist to play a specially-prepared piano that perforated the paper. Publishers would then duplicate the perforated scrolls and sell them to piano roll owners. This, in effect, gave player piano owners the ability to recreate famous musicians’ performances in their living rooms. In this respect, player pianos were the bridge between the sheet music industry and the modern recording industry.

The Supreme Court, however, did not see it this way. In its famed copyright infringement case, *White-Smith Music Publ’g v. Apollo Co.*, the Court held that the copying of piano rolls were not an infringement of copyright.<sup>86</sup> The Court held that the alleged copies, “are parts of a machine which, when duly applied and properly operated in connection with the mechanism to which they are adapted, produce musical tones in harmonious combination. But we cannot think that [these perforated rolls] are copies within the meaning of the copyright act.”<sup>87</sup> (At the time, copyright law protected only “books, maps, charts, and dramatic and musical compositions.”)<sup>88</sup> The Court had similar difficulties with wax cylinders, the earliest form of phonograms, and found them more similar to the unprotected piano rolls than to books. As such, wax cylinders obtained no copyright protection.<sup>89</sup> In both cases, users were rampantly copying works of artists and selling them for profit.<sup>90</sup> It seems that in the original model of music distribution, artists sold their music in a tangible form to consumers, and most of the rights to the tangible device were included in the sale, including the right to copy the device, to sell it, or to otherwise enjoy it as the budding technology allowed.

The music industry pressured Congress to update the copyright law to protect artists. Popular composers John Philip Sousa and Victor Herbert testified before the Senate Subcommittee on the Judiciary as to the devastating effects the current copyright law would have on musicians if Congress did not modernize that law.<sup>91</sup> Congress answered their prayers by providing creators of artistic works with “the exclusive right to print, reprint, publish, copy, and vend the copyrighted work.”<sup>92</sup> Additionally, if the work was a musical composition, the holder of the copyright also had the exclusive right to “perform the copyrighted work publicly for profit.”<sup>93</sup>

By granting composers exclusive rights under copyright law, Congress also provided rights to the consumers: the rights associated with the doctrine of First Sale.

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<sup>86</sup> *White-Smith Music Publ’g Co. v. Apollo Co.*, 209 U.S. 1, 18 (1908).

<sup>87</sup> *Id.* at 18.

<sup>88</sup> *Id.* at 15.

<sup>89</sup> *Stern v. Rosey*, 17 App. D.C. 562, 566 (D.C. Cir. 1901).

<sup>90</sup> *White-Smith Music Publ’g Co.*, 209 U.S. at 8-9; *Stern*, 17 App. D.C. at 562.

<sup>91</sup> H. Henn, *The Compulsory License Provisions of the U.S. Copyright Law 3* (General Revision of the Copyright Law, Study No. 58 Senate Subcomm. on the Judiciary) (Comm. Print 1956), reprinted in 1 G. Grossman, *Omnibus Copyright Revision Legislative History*.

<sup>92</sup> Act of Mar. 4, 1909, ch. 320, 1(a), 35 Stat. 1075, 1075 (1909) (formerly codified at 17 U.S.C. 1(a)).

<sup>93</sup> *Id.* at 1(e).

On May 18, 1904, the Bobbs-Merrill Company obtained a copyright for Hallie Erminie Rives' new book, "The Castaway."<sup>94</sup> The book's copyright page included the restriction that the bookseller was "not licensed to sell it at a less price" than "one dollar net," and that "a sale at a less price will be treated as an infringement of copyright."<sup>95</sup> The Strauses sold copies for eighty nine cents per book and were promptly sued for copyright infringement by the Bobbs-Merrill Company.<sup>96</sup> This type of license provision was common at the time on patented goods, and had been upheld by many courts as a legally enforceable provision.<sup>97</sup> The Court noted, however, that "there are differences between the patent and copyright statutes in the extent of the protection granted by them."<sup>98</sup>

The Supreme Court noted the use of the phrase "the sole right of vending the same" in the existing copyright code and determined that Congress intended there to be a single right to vend copies of one's works.<sup>99</sup> This right was not divisible; one could not "part with it to another to the extent that he sees fit, and [] withhold to himself ... so much of the right as he pleases."<sup>100</sup> Justice Day concluded that the purpose of the copyright statute was to protect the right of the author to copy and sell his works.<sup>101</sup> However, to allow the copyright holder the right to control future sales of those copies that he has sold into the marketplace went beyond the legislative intent of the copyright statute.<sup>102</sup>

The resulting rule of *Bobbs-Merrill Co.* is the First Sale Doctrine—in essence, once an author has made the first sale of a copy of his work, the owner of that copy has the right to dispose of or sell the copy as the owner sees fit. The author retains no rights to the tangible copy sold to the consumer beyond the rights reserved to him under the copyright law (come 1909, the exclusive rights referred to *infra*, page 281). Congress further codified the First Sale Doctrine as a part of the Copyright Act of 1909:

...the copyright is distinct from the property in the material object copyrighted, and the sale or conveyance, by gift or otherwise, of the material object shall not of itself constitute a transfer of the copyright, ... but nothing in this Act shall be deemed to forbid, prevent, or restrict the transfer of any of a copyrighted work the possession of which has been lawfully obtained.<sup>103</sup>

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<sup>94</sup> *Bobbs-Merrill Co. v. Straus*, 139 F. 155, 157 (S.D. N.Y. 1905); *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339, 341 (1908).

<sup>95</sup> *Id.*

<sup>96</sup> *Id.* at 342.

<sup>97</sup> *Id.* at 343-45 (enumerating many such cases and distinguishing them as patent cases, licensing cases and contract cases). *But see* John A. Rothchild, *The Incredible Shrinking First-Sale Rule: Are Software Resale Limits Lawful?*, 57 Rutgers L. Rev. 1, 13 n.37 (2004) (citing cases that indicate limited reach of a patent holder to control the use of a patented item once it is sold).

<sup>98</sup> *Id.* at 345.

<sup>99</sup> *Id.* at 350-51.

<sup>100</sup> *Id.* at 349, 351.

<sup>101</sup> *Id.* at 351.

<sup>102</sup> *Id.* at 351. The copyright statute referred to in this case was the Copyright Act of 1790, which was still in effect and largely unchanged in 1905.

<sup>103</sup> Act of Mar. 4, 1909, ch. 320, 41, 35 Stat. 1075, 1084 (formerly codified at 17 U.S.C. 27).

Therefore, in 1909, not only did music composers gain the *exclusive* right to copy their music, but they also ceded any right they had to copies of their music after they had sold or gifted the copy of the music to another. The copyright holder maintained exclusive rights to the creative content, but the owner of a tangible copy held all rights to that copy of the work after the first sale.

This doctrine has been updated on a few occasions. In 1984, Congress dealt with music industry copyright issues specifically by making it an infringement of copyright for “the owner of a particular phonorecord” to dispose of that phonorecord “by rental, lease, or lending” unless authorized by the copyright owner.<sup>104</sup> The purpose was obviously to eliminate the threat posed by record stores that rented albums and tacitly encouraged customers to copy the albums at home.<sup>105</sup> In 1990, Congress extended that provision to computer software.<sup>106</sup>

*Track 2: Licensing and Fair Use*

As is the state of the law since 1984, copyright holders of sound recordings maintain the exclusive right:

1. to reproduce the copyrighted work in copies or phonorecords;
2. to prepare derivative works based upon the copyrighted work;
3. to distribute copies or phonorecords of the copyrighted work to the public by sale or other transfer of ownership, or by rental, lease, or lending; ...and
4. to perform the copyrighted work publicly by means of a digital audio transmission.<sup>107</sup>

Once the copyrighted music is sold in a tangible medium (a wax cylinder, record, reel-to-reel tape, cassette tape, compact disc, or DVD – collectively “phonorecords”<sup>108</sup>), the owner of that phonorecord is “entitled... to sell or otherwise dispose of the possession of that copy or phonorecord.”<sup>109</sup>

This still leaves two fairly large issues with which to wrestle: use and fair use. Once the author sells a copy of a phonorecord, who has the right to control its use? Can the author withhold some of the rights the phonorecord’s use through a contractual agreement, perhaps by limiting the location where one can listen to the phonorecord or the number of times one may listen to it? Can the author limit the type of equipment on which the consumer listens to the phonorecord (beyond the limitations of affixing it in a given form, such as ruling out listening to it on a cassette deck by affixing it as a compact disc)? Can the author in any way limit the

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<sup>104</sup> Record Rental Amendment of 1984, Pub. L. No. 98-450, 2, 98 Stat. 1727 (codified as amended at 17 U.S.C. 109(b)(1)(A)). An exception is given in the Act for schools and libraries.

<sup>105</sup> See S. Rep. No. 98-162, at 2 (1983) (“The Committee has no doubt that the purpose and result of record rentals is to enable and encourage customers to tape their rented albums at home.”)

<sup>106</sup> Computer Software Rental Amendments Act of 1990, Pub. L. No. 101-650, 802, 104 Stat. 5134 (codified at 17 U.S.C. 109(b)(1)(A)).

<sup>107</sup> 17 U.S.C. § 106 (2006). The scope of these exclusive rights is found at 17 U.S.C. § 114 (2006).

<sup>108</sup> 17 U.S.C. § 101 (2006) (“‘Phonorecords’ are material objects in which sounds, other than those accompanying a motion picture or other audiovisual work, are fixed by any method now known or later developed, and from which the sounds can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device. The term ‘phonorecords’ includes the material object in which the sounds are first fixed”).

<sup>109</sup> 17 U.S.C. § 109(a) (1997).

manner in which a consumer merely listens to the material on the phonorecord? The courts imply that the author may not limit use, by indicating that once the author sells the phonorecord, the author obtains all value for her sale of that copy and retains no further rights to it.<sup>110</sup> By contractually limiting the consumer's phonorecord use, the phonorecord retains some value for the consumer, thereby giving the author the ability to extract more money for an item in which the author has already exercised the "sole right of vending."<sup>111</sup> The First Sale Doctrine thus limits restrictions on use.

Courts have carved out an exception under the First Sale Doctrine for the licensing of a tangible copy, however. While licensing could be considered a form of vending,<sup>112</sup> with computer software courts have taken the approach that the owner of the copy may contract certain use rights in the disk so long as the agreement exists as a license and not as a sale. A license is distinct from a sale in that with a sale the buyer owns the good. With a license, as with a lease, the seller maintains ownership of the good and merely contracts its limited use to the buyer.<sup>113</sup> Computer software companies often license software to end users, providing lengthy terms and conditions of use. Authors relinquish a number of their exclusive rights through many of these terms and conditions<sup>114</sup> while buyers obtain certain additional rights of use through other terms and conditions.<sup>115</sup> Software provided under the license model also makes clear that the author of the software maintains ownership of the tangible copy and that it is only provided to the user so long as that user adheres to the terms of the license.<sup>116</sup>

Legal support for the exception can be found in the 1984 and 1990 Amendments to Section 109 of the Copyright Statute.<sup>117</sup> These Amendments, which accompany the text of the statutory First Sale Doctrine, provide that the owner of a tangible copy of a computer program or a phonorecord may not rent, lease, or lend, "or by any other act or practice in the nature of rental,

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<sup>110</sup> See John A. Rothchild, *The Incredible Shrinking First-Sale Rule: Are Software Resale Limits Lawful?*, 57 Rutgers L. Rev. 1, 18 (2004).

<sup>111</sup> *Id.*

<sup>112</sup> Mr. Neukom and Professor Gomulkiewicz contend that licensing is not a form of vending under the copyright statute, but rather is a precursor to vending – maintaining ownership in the physical copy while allowing others to use it. Their argument is predicated on the current version of the copyright statute and I believe is an incorrect interpretation of the word "vend" in the context in which the Court used it in *Bobbs-Merrill*, of dispersing the copy while contractually withholding rights to it. Rather, the current copyright statute avoids the term "vend" and instead speaks to the rights of the owner of the copy. See William H. Neukom & Robert W. Gomulkiewicz, *Licensing Rights to Computer Software*, 1993 Practising L. Inst. 775, 777-78, available at WL 354 PLI/Pat 775.

<sup>113</sup> Not all licensed goods have an expectation of return. In some circumstances the license requires the user to destroy the goods on completion of the license. In other situations the license provides that upon return of the goods the user receives a partial refund. Sean O'Connor, *The User of MTAs to Control Commercialization of Stem Cell Diagnostics and Therapeutics*, 21 Berkeley Tech. L.J. (forthcoming 2006).

<sup>114</sup> Gomulkiewicz, *supra* note 40 at 690. Many pieces of computer software allow limited derivative works to be made. For example, "clip art" provided in a computer processing program is licensed to the end user to be used with few limitations. Even the purpose of computer software in general is to create derivative works (word processed documents, spreadsheets, artwork, etc.) so the author must provide to the consumer, along with the software, certain abilities to create derivative works in order for the software to have value.

<sup>115</sup> Neukom & Gomulkiewicz, *supra* note 112 at 779.

<sup>116</sup> *Id.*

<sup>117</sup> Record Rental Amendment of 1984, Pub. L. No. 98-450, 2, 98 Stat. 1727 (codified as amended at 17 U.S.C. 109(b)(1)(A)) (1984); Computer Software Rental Amendments Act of 1990, Pub. L. No. 101-650, 802, 104 Stat. 5134 (codified at 17 U.S.C. §109(b)(1)(A)) (1990).

lease, or lending” said copy of the phonorecord or computer program, “*unless authorized by the owners of [the] copyright.*”<sup>118</sup> The fact that Congress withheld for the copyright owner the right to control the future leasing meant that the copyright owner could vend to a copy holder that same right. By withholding later vending control for the copyright holder of the software, Congress impliedly created an exception to the statutorily created “sole right of vending.” Congress created *two* rights of sale: the right of First Sale and, in addition, the right of rental. Since Congress provided two rights of sale it follows that the copyright owner could chose to exercise the right to rent and not the right to sell. In other words, one could argue that by providing the copyright owner with control over the ability to rent, lease, or lend a copy of a computer program, Congress thereby gave the copyright owner the ability to *control* the later right to do so, both directly and indirectly.

The changed language of the copyright statute also provides legal support for this position. No longer does the copyright owner have a “sole right of vending,” but rather the owner of a given copy has the right to dispense with the copy as he or she desires. In this vein, so long as the copyright owner never relinquishes ownership of the copy, that copy is never available for dispensation under the statutory First Sale Doctrine.<sup>119</sup>

This exception to the *Bobbs-Merrill Co.* doctrine has garnered acceptance by both courts and the Copyright Office.<sup>120</sup> While this exception has thus far only been applied to software,<sup>121</sup> the adoption of this licensing strategy by other industries is likely to gain judicial approval. The music industry in particular has an advantage in this regard, as the provisions under the Copyright Statute for phonorecords closely parallel the provisions for software; the section of the Copyright Statute that addresses the First Sale Doctrine provides parallel exceptions for phonorecords and software in light of the 1984 and 1990 amendments.<sup>122</sup> By licensing software

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<sup>118</sup> 17 U.S.C. § 109(b)(1)(A) (1997).

<sup>119</sup> Neukom & Gomulkiewicz, *supra* note 112 at 777-78.

<sup>120</sup> Rothchild *supra* note 110 at 26-27. *But see* Rothchild, *supra* note 110 at 28-37 (critiquing this strategy by the courts).

<sup>121</sup> *See, e.g., Adobe Sys. Inc. v. One Stop Micro, Inc.*, 84 F. Supp. 2d 1086, 1092 (N.D. Cal. 2000) (holding that the distribution agreement was a license and not a sale, therefore, the ‘first sale’ doctrine was inapplicable). There is a valid question of the enforceability of licenses regarding the use of ebooks, or books provided in soft form only. Ebooks.com, a large provider of ebooks requires all users to agree to certain terms of use, including terms that restrict use of the downloaded material. Copies of the works may be made for personal use only, despite the fair use defense of making copies for commentary or other applications. EBooks.com – Information – Customer license, <http://www.ebooks.com/information/customerlicense.asp> (last visited Oct. 30, 2006). Whether or not an ebook is a book or software is unclear. *See Random House, Inc. v. Rosetta Books LLC*, 150 F. Supp. 2d 613, 620-24 (S.D.N.Y. 2001).

Additionally, some test-preparation materials include copyrighted content in the form of video footage on DVDs that has been dispersed by the author under license, but the legal enforceability of such a contract has not been judicially addressed. *See, e.g., Bar/Bri Patent Bar Review*, Bar/Bri Patent Bar Review Enrollment Form at 2, <http://www.patentbarbri.com/download/pdf/enrollment01.pdf> (last visited Oct. 30, 2006). Further, the copyright statute does not place licensing (rental) provisions on video as it does for music and software, thereby legalizing video rental stores, wherein music rental stores and software rental stores are prohibited by law. 17 U.S.C. 109(b) (1997).

<sup>122</sup> 17 U.S.C. § 109(b) (1997). *See also* Record Rental Amendment of 1984, Pub. L. No. 98-450, 2, 98 Stat. 1727 (codified as amended at 17 U.S.C. 109(b)(1)(A)) (1984); Computer Software Rental Amendments Act of 1990, Pub. L. No. 101-650, 802, 104 Stat. 5134 (codified at 17 U.S.C. 109(b)(1)(A)) (1990).



or other copyrighted works, the copyright owner retains certain abilities to limit the end user's use.

The other significant "right" to address is that of fair use.<sup>123</sup> Stemming from common law,<sup>124</sup> Congress codified fair use in 1976.<sup>125</sup> To date, much of the debate in copyright law and its modernization focuses on fair use, and for that reason I find it unnecessary to address the topic at length. To summarize, Congress stipulated that, "notwithstanding [the exclusive rights retained for the copyright owner], the fair use of a copyrighted work... is not an infringement of copyright."<sup>126</sup> Acts that qualify as fair use are "criticism, comment, news reporting, teaching, scholarship and research."<sup>127</sup>

Fair use is often considered a right retained for the end users.<sup>128</sup> Legally speaking, however, it is more appropriate to view fair use as a defense.<sup>129</sup> The statute provides that violating the exclusive rights of the copyright owner in the form of fair use is "not an infringement." This formulation is substantially different from providing a "right" to fair use. A right to fair use implies that copyright owners would not be allowed retain that right; rather they may be legally required to provide it. Copyright owners would be legally restricted from providing copies to consumers that they could not fairly use. For example, if the right of fair use existed, copyright owners could not provide compact discs to the public with copy restrictions, as these restrictions would impinge on a user's right to copy the disc for educational purposes. Rather, Congress has explicitly authored this user's right by providing protection for "technological protection measures" used to thwart copying.<sup>130</sup>

As a defense, however, fair use does not require copyright owners to provide users with the ability to exercise it. Copyright owners therefore use licensing provisions to control certain forms of fair use, and courts have upheld these measures thus far. In *Davidson & Assocs.*, a company manufactured a computer game that involved use of a proprietary website for

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<sup>123</sup> Other rights, known as the statutory exceptions to the copyright holders' rights, exist in copies of music and software besides those addressed in this article. The right to copy the material for the purposes of back-up or repair of a computer is provided under statute. Rights to broadcast music are also statutorily quantified.

<sup>124</sup> L. Ray Patterson, *Free Speech, Copyright, and Fair Use*, 40 Vand. L. Rev. 1, 34 (1987) (tracing the history of fair use in the United States).

<sup>125</sup> Act of Oct. 19, 1976, Pub. L. No. 94-553, 90 Stat. 2541, 2546 (1976) (codified as amended at 17 U.S.C. 107) (1992).

<sup>126</sup> 17 U.S.C. § 107 (1992).

<sup>127</sup> *Id.*

<sup>128</sup> See, e.g. Stephen E. Blythe, *The U.S. Digital Millennium Copyright Act and the E.U. Copyright Directive: Comparative Impact on Fair Use Rights*, 8 Tul. J. Tech. & Intell. Prop. 111 (2006) (indicating through the title if nothing more the assertion that fair use is a right).

<sup>129</sup> *Chicago Bd. of Educ. v. Substance, Inc.*, 354 F.3d 624, 629 (7th Cir. 2003) ("The burden of proof is on the copier because fair use is an affirmative defense"). But see *Davidson & Assocs. v. Internet Gateway*, 334 F. Supp. 2d 1164, 1180-81 (D. Mo. 2004), *aff'd* 422 F.3d 630 (8th Cir. 2005) (using "defense" and "rights" interchangeably, as in "E. Fair Use Defense" and "defendants in this case waived their 'fair use' rights," "defendants gave up their fair use rights"). The Court's holding in this case, while confusing on this matter, implies that the defendants in this case contracted away their right to use fair use as a defense. This is entirely different from claiming that fair use itself is a right. Some scholars avoid the debate altogether by referring instead to the fair use "doctrine." See, e.g., Kate O'Neill, *Against Dicta: A Legal Method for Rescuing Fair Use From the Right of First Publication*, 89 Calif. L. Rev. 369, 369 (2001)

<sup>130</sup> 17 U.S.C. § 1201 (1999).

multiplayer gaming. The game included an End User License Agreement (EULA) to which all end users were required to agree.<sup>131</sup> The agreement restricted users from copying, photocopying, reproducing, translating, reverse engineering, deriving source code, modifying, disassembling, decompiling, or creating derivative works of the software.<sup>132</sup> When the defendants agreed to the EULA, reverse-engineered the software, and started an accompanying website for users of the game, the computer game manufacturer filed suit for breach of contract.<sup>133</sup> The court recognized that reverse-engineering as fair use was “firmly established.”<sup>134</sup> It went on, however, to hold that parties may contract away their fair use defenses, citing reasoning from a Federal Circuit Court of Appeals case<sup>135</sup> on the matter.<sup>136</sup>

The Third Circuit Court of Appeals recently extended the ability to license fair use to the ability to license Constitutional rights.<sup>137</sup> In *Video Pipeline, Inc. v. Buena Vista Home Entm't, Inc.*, Disney licensed use of movie clips to websites, but the licenses precluded the websites from being, “derogatory to or critical of the entertainment industry or of [Disney] ... or of any motion picture produced or distributed by [Disney] . . . [or] of the materials from which the Trailers were taken...”<sup>138</sup> Video Pipeline claimed the defense of Copyright Misuse: the principle that the plaintiff used its asserted rights contrary to the public interest.<sup>139</sup> The court held that these license agreements “are unlikely to interfere with creative expression to such a degree that they affect in any significant way the policy interest in increasing the public store of creative activity.”<sup>140</sup> The Court explained that critics had a variety of other venues in which to criticize or comment on Disney’s videos, and consumers likewise had a variety of venues in which to find such criticism.<sup>141</sup> Disney was therefore free to restrict derogatory comments as a part of its license agreement.

*Buena Vista* and *Davidson Assocs.* indicate the lengths to which courts are willing to go to uphold the right of contract with respect to licensing provisions of copyrightable matter. These rulings also indicate the unwillingness of courts to create an unwaivable and inalienable “right” to fair use.

Under the *Bobbs-Merrill* First Sale Doctrine analysis, an attempt to contract away fair use would fail at law—contractually withholding a right in the tangible copy would bifurcate the “sole right of vending.” Under the current Section 109 First Sale Plus Additional Rights in Vending Doctrine for computer software and phonograms, contracting away fair use is legally

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<sup>131</sup> *Davidson & Assocs.*, 334 F. Supp. 2d at 1169-70, *aff'd*, 422 F.3d 630 (8th Cir. 2005).

<sup>132</sup> *Id.* at 1170.

<sup>133</sup> *Id.* at 1173.

<sup>134</sup> *Id.* at 1180.

<sup>135</sup> *Bowers v. Baystate Techs.*, 320 F.3d 1317, 1325 (Fed. Cir. 2003) (holding that a licensing agreement that restricted reverse engineering was legally enforceable).

<sup>136</sup> *Id.* at 1181. *But see Vault Corp. v. Quaid Software, Ltd.*, 847 F.2d 255, 270 (5th Cir. 1988) (holding that a state law that prohibits fair use copying of computer software is preempted by the federal Copyright Act, though not specifically claiming that *individual contracts* may not have terms that cede fair use defenses).

<sup>137</sup> *Video Pipeline, Inc. v. Buena Vista Home Entm't, Inc.*, 342 F.3d 191, 206 (3d Cir. 2003).

<sup>138</sup> *Id.* at 203.

<sup>139</sup> *Id.* at 204 (quoting *Morton Salt Co. v. G.S. Suppiger Co.*, 314 U.S. 488, 492 (1942)).

<sup>140</sup> *Id.* at 206.

<sup>141</sup> *Id.*

sustainable. This approach is also sustainable under the owner's rights analysis, with the copyright owner maintaining ownership of the physical copy.

*Track 3: Rampant Copying Forces Authors/Labels to use Digital Rights Management*

The first two music industry distribution and rights models worked very successfully for the first hundred years of their existence. The first was short lived, and involved selling music that was then available for unabashed copying. Even this model provided copyright protection, however, as the sheer impossibility of making an audibly transparent copy was insurmountable. Further, the cost involved in duplicating vinyl records (the dominant form of music delivery from 1900-1980) was prohibitive. Copyright protection at this point came not from statute or judicial enforcement, but rather from technological obstacles. As referred to above, however, the music industry found this protection inadequate, and they lobbied for legal enforcement as well. Congress replied with the Copyright Act of 1909, providing copyright protection for musical compositions.<sup>142</sup> From 1909, the industry model involved both technological protection from copying as well as the newly enacted legal protection.

By the turn of the millennium, however, the situation drastically changed. In 1982 the compact disc (CD) was born, based on the concept of digital sampling.<sup>143</sup> This technology allowed analog, sinusoidal waveforms to be reduced to numerical data. Once music became mere binary data, the ability to render perfect copies emerged. The process was slow—in 1982 pressing a compact disc required cutting-edge equipment complete with lasers (at that time still a budding technology) and a Class 100 Clean Room.<sup>144</sup> The equipment was enormously expensive, and so the cost of producing a CD was likewise enormously expensive.<sup>145</sup> The first CD players were so expensive that they were initially available only as a boutique item.

At first the CD did not pose a threat to artists or their record labels. In fact, compact discs provided a boon; for the next fifteen years consumers re-purchased much of their music on the new format, bringing new revenue to artists for old music.<sup>146</sup> Further, copying a compact disc on anything more than the same, generation-loss inducing compact disc seemed an eternity away. The data alone was gluttonous: each minute of recording on a compact disc required over ten *megabytes* of data.<sup>147</sup> I emphasize this to illustrate the premium put on data storage in the 1980s. The then-ubiquitous 5 1/4" floppy disk stored around one hundred *kilobytes* of digital

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<sup>142</sup> Act of Mar. 4, 1909, ch. 320, 1(a), (e), 35 Stat. 1075, 1075 (1909) (formerly codified at 17 U.S.C. § 1(a), (e)) (1909).

<sup>143</sup> Steve Schoenherr, Recording Technology History at 1982 <<http://history.sandiego.edu/gen/recording/notes.html>> (last updated July 6, 2005).

<sup>144</sup> Nika Aldrich, *An Exploration of Rights Management Technologies Used in the Music Industry*, 2007 B.C. Intell. Prop. & Tech. F. (forthcoming 2007). (Working copy available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=932088](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=932088)).

<sup>145</sup> *Id.*

<sup>146</sup> John Jordan, Technology Evolution and the Music Industry's Business Model Crisis 2 (Cap Gemini Ernst & Young 2003) (noting the repurchasing trend that boosted CD sales in the 1980s and 1990s, causing a drop in the market in the 2000s).

<sup>147</sup> Compact discs operate at a sample rate of 44.1ks/s and 16 bits of depth. Stereo recordings require 10,584,000 bytes per minute of storage space not including header bits, data encryption, modulation for data integrity or table of contents data. NIKA ALDRICH, DIGITAL AUDIO EXPLAINED – FOR THE AUDIO ENGINEER 135-37 (Sweetwater Press 2nd Ed, 2005).

data—enough to store just a fraction of a second of CD-quality music.<sup>148</sup> *CD burners* (available to regular consumers) came along many years later; these burners are entirely different than the *CD pressing* systems that are still used in the industry for professional CD production.<sup>149</sup> Due to of the costs of CD duplication, the amount of data required to store music on any other digital storage device, and the generation-loss that resulted from copying to analog sources such as cassette tapes, the CD itself did not pose much threat to copyright holders.

In time, however, advances in digital audio changed this. The Digital Audio Tape (DAT) made its debut in 1986, providing user-recordable alternate digital audio storage medium.<sup>150</sup> This provided the opportunity for consumers to copy music from their CD player to their DAT recorder.<sup>151</sup> Further, digital compression technologies allowed for consumers to record music onto computer hard-drives by shrinking the size of the digital music files.<sup>152</sup> Additionally, computer-based CD burners became prevalent, allowing users to make completely accurate digital copies of their CDs.<sup>153</sup> Finally, computer storage ability increased, allowing users to store a vast number of songs on their computers. The combination of these factors led to digital audio piracy on a massive scale come the turn of the millennium.<sup>154</sup>

The music industry initially responded by creating new digital delivery media that contained Digital Rights Management (DRM) technologies. The first example came about as a result of the DAT machine. As a result of pressure from the music industry to curb potential copying,<sup>155</sup> Congress passed the Audio Home Recording Act, requiring DAT machines to incorporate a Serial Copy Management System to prevent unapproved duplication.<sup>156</sup> This Act was the music industry's first attempt at employing Digital Rights Management.<sup>157</sup> Because of lengthy delays in passing the legislation, however, the DAT machine was a commercial flop and

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<sup>148</sup> One hundred kilobytes would be enough to store 6250 samples. 44,100 Samples are required for each second of CD-quality stereo sound. NIKA ALDRICH, *DIGITAL AUDIO EXPLAINED – FOR THE AUDIO ENGINEER* 135-37 (Sweetwater Press 2nd Ed, 2005).

<sup>149</sup> “Burning” compact discs actually requires a different technology than “pressing” (replicating) discs, as is used in commercial manufacturing plants. “Burning” involves putting the pits and lands on the disc by burning holes in a layer of substrate with a laser. In a “pressed” disc the pits and lands are molded into the disc. See Sweetwater inSync, <http://www.sweetwater.com/insync/word/cdr> (last visited July 25, 2006) (explaining the difference between home made and factory manufactured CDs).

<sup>150</sup> H.R. Rep. No. 102-873 (II), at 2 (1992).

<sup>151</sup> Delton T. Horn, *DAT The Complete Guide to Digital Audio Tape* 97 (TAB Books 1991).

<sup>152</sup> U.N. Conference on Trade and Development [UNCTAD], *E-Commerce and Development Report 2004* at 72, UNCTAD/SDTE/ECB/2004/1 (2004) (“The development of compression techniques, such as mp3, that reduce music CD file sizes by 90 per cent...”).

<sup>153</sup> *Public Hearing on Technological Protection Systems for Digitized Copyrighted Works*, U.S. Patent and Trademark Office (2003) (statement of Chris Katopis, Deputy Administrator for External Affairs, U.S.P.T.O) *transcript available at* <http://www.uspto.gov/web/offices/dcom/olia/teachcomments/teachacthearing.pdf>.

<sup>154</sup> *A & M Records v. Napster, Inc.*, No. C 99-5183 MHP, 2000 WL 1009483, at \*2 (N.D. Cal. 2000) (quoting Napster.com, the famed mp3 file swapping service, in estimating that it would have 70 million users by the end of the year 2000).

<sup>155</sup> H.R. Rep. No. 102-873 (II), at 2 (1992).

<sup>156</sup> Audio Home Recording Act of 1992, Pub. L. No. 102-563, 106 Stat 4237 (1992) (codified at 17 U.S.C. §§ 1001-1010 (2000)).

<sup>157</sup> Nika Aldrich, *An Exploration of Rights Management Technologies Used in the Music Industry*, 2007 B.C. Intell. Prop. & Tech. F. (forthcoming 2007). (Working copy available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=932088](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=932088)).

the industry never adopted DAT as a music delivery medium.<sup>158</sup> A similar fate befell other attempts at creating a new delivery medium. Both the DVD-Audio format and Sony's Super Audio Compact Disc (SACD) have failed to find commercial success and are virtually dead.<sup>159</sup>

The music industry achieved success in a new delivery format as the result of efforts by Apple Computer. In 2003 Apple Computer unveiled its iTunes Music Store,<sup>160</sup> an online delivery service that provided users with a large library of downloadable songs that users could purchase for ninety-nine cents each.<sup>161</sup> The iTunes Music Store (now the iTunes Store) requires the use of iTunes software, which users can download for free (the software is included with Apple's Macintosh computers). Upon installing the iTunes software, users are required to click their approval to an End User Licensing Agreement for the iTunes Store.<sup>162</sup> (The terms of this license will be discussed in the following section of this article.) Users can then purchase songs from the iTunes Store to listen to either on their computer or on their iPod, a portable listening device made by Apple Computer.

The song files are encrypted in a proprietary format that can only be played on either Apple's software or their iPod players.<sup>163</sup> The encryption includes a technology dubbed "FairPlay" that restricts users in the following ways:<sup>164</sup>

- A user may download songs to any number of iPod portable music players
- A user may play the downloaded songs on up to five (originally three) authorized computers simultaneously<sup>165</sup>
- A user may copy the downloaded songs to an unlimited number of computers for archiving or back-up, though playback is limited to authorized computers only
- A user may copy the downloaded songs to a standard audio CD any number of times<sup>166</sup>
- A user may only copy a given "playlist" (an arrangement of songs within the iTunes software) that includes a downloaded song to a CD seven times before the playlist must be changed.
- A user may not play downloaded songs on any portable music player other than iPods.

Apple's iTunes Store and format have had great success. In its first week, Apple sold one million songs;<sup>167</sup> in July, 2006, the iTunes store distributed its 500 millionth song, only six

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<sup>158</sup> *Id.*

<sup>159</sup> See Recording Industry Association of America, RIAA 2005 Year-End Statistics (2005) available at <http://www.riaa.com/news/newsletter/pdf/2005yrEndStats.pdf> (showing that sales of DVD-A and SACD albums combined have never exceeded .2% of market share (2003), below that of even phonograph sales).

<sup>160</sup> U.N. Conference on Trade and Development [UNCTAD], E-Commerce and Development Report 2004 at 80, UNCTAD/SDTE/ECB/2004/1 (2004).

<sup>161</sup> Mark Coleman, *Playback 206* (Da Capo Press 2003) (2003).

<sup>162</sup> iTunes Store - Terms of Service, Apple Computer, Inc. available at <http://www.apple.com/legal/itunes/us/service.html> (last updated Sept. 12, 2006)

<sup>163</sup> iTunes Store - Terms of Service, Apple Computer, Inc. at Article ¶ 9(b) available at <http://www.apple.com/legal/itunes/us/service.html> (last visited Nov. 6, 2006).

<sup>164</sup> *Id.*

<sup>165</sup> Only five computers can be authorized to play a given song. De-authorizing a computer allows for another computer to be authorized.

<sup>166</sup> A CD made from a downloaded song, however, will still suffer from any audible artifacts of the audio compression used to create the downloadable song file.

months after its 250 millionth song.<sup>168</sup> The success has created a budding industry of music download distribution, and many of the usual suspects are getting involved. Pressplay was developed by Vivendi Universal and Sony; Echo was founded by several prominent music retailers in the United States; OD2 is a European-based download service co-founded by Peter Gabriel;<sup>169</sup> and URGE is a collaboration between MTV and Microsoft, which also has MSN Music Store.<sup>170</sup> Despite the recent suitors, Apple is dominant, garnering 80% of legal music downloads.<sup>171</sup> Despite Apple's success, however, most music in the United States is still purchased on compact disc.<sup>172</sup>

For record labels, distributing music on compact disc has advantages—compact discs typically contain ten songs and sell for more than ten times the price of downloaded songs.<sup>173</sup> Further, users typically purchase CDs based on their interest in only a few songs on the CD, meaning that most users pay more than ten times the price of song downloads for only a few songs. I purchased the Alicia Keys album because of my attraction to a given song, though in light of the fact that I liked one song, I anticipated or at least hoped that I would like others. The other fifteen songs on this particular CD we could say were purchased “on spec.” The record labels can therefore charge a higher price because, though they force the add-on sales, they commensurately provide more potential value to the consumer.

CDs also provide higher sound quality than the data-compressed songs available for download.<sup>174</sup> This sound quality is beneficial to record labels because discriminating listeners are attracted to the CD format over the less-expensive download options. Some users also prefer CDs for the traditional album art often included with the discs. Perhaps the most significant factor, however, is the pervasiveness of CD players. The RIAA estimates that there are between eight hundred million and one billion CD players still in use with users who intend to use them.<sup>175</sup> Until a new format accomplishes ubiquity, record labels must continue to produce their work on CD to have viability.

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<sup>167</sup> Press Release, Apple Computer, Inc., *iTunes Music Store Sells Over One Million Songs in First Week*, Apple, Inc. (May 5, 2003) available at <http://www.apple.com/pr/library/2003/may/05musicstore.html> (last visited Nov. 6, 2006).

<sup>168</sup> *iTunes downloads top 500 million mark* | CNET News.com, [http://news.com.com/iTunes+downloads+top+500+million+mark/2110-1027\\_3-5792960.html](http://news.com.com/iTunes+downloads+top+500+million+mark/2110-1027_3-5792960.html) (last visited Nov. 1, 2006).

<sup>169</sup> World Intellectual Property Organization [WIPO], Standing Comm. On Copyright and Related Rights, *Current Developments in the Field of Digital Rights Management*, at 4.2.2, U.N. Doc. SCCR/10/2 (Nov. 3-5, 2003) (prepared by Jeffrey P. Cunard).

<sup>170</sup> *MTV to Start Music Service With Microsoft*, N.Y. Times, Dec. 14, 2005 at C4.

<sup>171</sup> BBC News, *Apple wins iTunes download deal*, May 2, 2006, <http://news.bbc.co.uk/2/hi/business/4964298.stm> (last visited Nov. 6, 2006).

<sup>172</sup> Recording Industry Association of America, *RIAA 2005 Year-End Statistics (2005)* available at <http://www.riaa.com/news/newsletter/pdf/2005yrEndStats.pdf> (showing 705.4 million CD album sales in relation to 748.7 million total album sales).

<sup>173</sup> *Id.* (showing that the total revenue for downloads of songs averaged \$.99 per song, or on average \$9.90 per album, whereas the revenue for CDs indicates an average price of \$14.91 per album).

<sup>174</sup> Ken C. Pohlmann, *Principles of Digital Audio* 358-62 (McGraw-Hill 4th ed. 2000) (describing listening tests for perceptual coding algorithms).

<sup>175</sup> Cary Sherman, President, Recording Industry Association of America, Address at the Digital Rights Management Conference at The Berkeley Center for Law and Technology (Feb. 28, 2003)

The problem with the CD format for record labels is that CDs require compatibility with all CD players, and no copy provisions were built into the CD format. Therefore, releasing CDs in the market makes them just as susceptible to uncontrolled copying and dissemination by users today as it did in years past. The result is rampant copying of CDs<sup>176</sup> and likely higher proliferation of “ripping and downloading.” Record labels have tried to solve the problem by employing sophisticated Digital Rights Management technologies that stretch the intended boundaries of the CD format and use idiosyncrasies of computer-based CD players against them.<sup>177</sup> The result is generally a compact disc that either is not recognized by computers or one that, upon loading into a computer, plays separate files off of the CD.<sup>178</sup> Examples of these copy protection systems are Copy Control, Cactus Data Shield, CDS-300, MediaMax and XCP2.

*Track 4: Digital Rights Management Brings Liabilities.*

The use of DRM on CDs can bring a host of problems, including trademark infringement, warranty claims, and assertions of copyright violations stemming from use and fair use arguments.

The compact disc format was designed as a joint venture between Sony and Phillips Electronics,<sup>179</sup> and Phillips still holds the rights to the trademarked CD Digital Audio logo that can be found on most compact discs. When record labels started exploring ways to defeat compatibility with certain (computer) CD players, Phillips notified the record labels in question that doing so was a violation of their license to use the CD Digital Audio logo, and that further use would constitute trademark infringement.<sup>180</sup> Another potential issue is the trademark of the compact disc form and structure itself.<sup>181</sup> The compact disc shape and size may have developed secondary meaning<sup>182</sup> over the last twenty-five years as a device that, when sold in music stores and associated with music, is compliant with the red book standard put forth by Phillips and Sony. Phillips could argue that non-compliant discs infringe upon their trademark in the disc itself, as used for audio purposes.

Of more concern to record labels are warranty issues. Some CDs that employ copy protection technologies can cause damage to computers or speakers. Apple Computer reported that one copy protection system can harm certain Apple computers so severely that they require

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<sup>176</sup> BBC News, *Sony abandons copy-protected CDs*, Oct. 4, 2004, <http://news.bbc.co.uk/2/hi/entertainment/3712662.stm> (last visited Nov. 1, 2006) (quoting the International Federation of Phonographic Industries in estimating that 35% of all CDs sold in the world were pirate copies, up from 20% in the year 2000).

<sup>177</sup> John A. Halderman, *Evaluating New Copy-Prevention Techniques for Audio CDs* at 5-9, available at <http://www.cs.princeton.edu/~jhalderm/papers/drm2002.pdf> (last visited July 27, 2006) (explaining the results of a study done in the Princeton University Computer Science Department to ascertain how the Copy Control techniques work).

<sup>178</sup> *Id.* at Table 1 (showing a graphical representation of which devices show incompatibility with Copy Control discs).

<sup>179</sup> Kees A. Schouhamer Immink, *The Compact Disc Story\**, 46 J. Audio Eng. Soc., 458, 458 (1998) available at <http://www.exp-math.uni-essen.de/~immink/pdf/cdstory.pdf>.

<sup>180</sup> David Lieberman, *How dangerous are pirates?* USA Today, Apr. 5, 2002, at 1B.

<sup>181</sup> The trademark for “compact disc” was abandoned in 1983: Trademark Serial Number 73281719.

<sup>182</sup> “Secondary meaning” refers to a consumer’s developed mental association of a characteristic of a good (such as the product’s shape) with a particular brand of product.

service.<sup>183</sup> Another company obtained a patent on a copy protection system capable of “damaging audio output circuitry”<sup>184</sup> when any copies are made of discs employing their technology. Sony released over four million CDs in 2005<sup>185</sup> that made computers more susceptible to viruses, potentially exposing sensitive data and resulting in loss of data, and in the case of businesses, loss of revenue and loss of profits.<sup>186</sup> Without adequate warning to consumers, record labels could suffer a rash of warranty claims from damage caused by their DRM-laden CDs.

The most likely claim with respect to DRM on CDs is a warranty of merchantability claim. The UCC provides an implied warranty of merchantability for most goods.<sup>187</sup> Goods must, among other requirements:

- (a) pass without objection in the trade under the contract description; and
- (b) in the case of fungible goods, be of fair average quality within the description; and
- (c) be fit for the ordinary purposes for which such goods are used; and
- (d) run, within the variations permitted by the agreement, of even kind, quality and quantity within each unit and among all units involved; and
- (e) be adequately contained, packaged, and labeled as the agreement may require; and
- (f) conform to the promise or affirmations of fact made on the container or label if any.<sup>188</sup>

CDs that contain certain types of DRM and that, in so doing, violate the official formatting of the compact disc digital audio protocol (the “red book”) not only do not play in computer CD-ROM drives but also often do not play in other CD drives.<sup>189</sup> One CD released by the popular band Coldplay listed the various devices that it was not compatible with:

- Some CD players that have the capability of burning into an MP3 (such as portable players or car stereos)
- Some CD players that possess CD-R/RW functions (such as portable players or car stereos).
- Some car stereos with satellite "Guidance" systems
- Some CD players or car stereos with hard disk recording capacity
- Some CD-R/RW Recorders used for music
- Some portable CD players
- Some DVD players
- Some CD/LD Convertible Players
- Some Game Players
- Although you can use your PC's Windows program to listen to certain tracks, this does not mean that the CD can be played in all PCs

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<sup>183</sup> Apple Computer, Mac OS Cannot Eject Copy Protected Audio Disc, Computer Starts Up to Gray Screen AppleCare, <http://docs.info.apple.com/article.html?artnum=106882> (last visited Nov. 6, 2006).

<sup>184</sup> Anti-counterfeit compact disc. U.S. Patent 6,208,598 (filed Jan 13, 1999).

<sup>185</sup> Edgecliffe-Johnson *supra* note 8.

<sup>186</sup> Iain Thompson & Tom Sanders, Virus writers exploit Sony DRM, <http://www.vnunet.com/vnunet/news/2145874/virus-writers-exploit-sony-drm> (Nov. 10, 2005) (reporting a virus emailed to computer users in the UK exploits the Sony BMG XCP2 software and explaining how the virus works).

<sup>187</sup> U.C.C. § 2-314(1) (2003).

<sup>188</sup> U.C.C. § 2-314(2) (2003).

<sup>189</sup> Lieberman, *supra* note 180.



- The first time that this program is used (in Windows automatic starter software) it gets registered in Windows File. Thus, programs already registered do not affect Windows operations
- Windows OS also uses the latest files
- This CD does not support Macintosh PC software<sup>190</sup>

Certainly the vast majority if not all of these devices are compatible with the original compact disc format first standardized in 1980 by Sony and Phillips, and certainly most if not all of these devices contain the “Compact Disc Digital Audio” logo. In the example of Coldplay’s CD, the disc does warn on the outside that the disc is “copy-protected,” but does not in any way indicate that it is “play-protected” as well.<sup>191</sup> Comparing the CD’s purported restrictions with the requirements of merchantability under UCC § 2-314 highlights the implied warranty concerns record companies face:

- (a) A disc that does not play on a variety of the aforementioned devices would certainly not “pass without objection in the trade,”<sup>192</sup> as indicated by the objection in the trade thus far. This would be especially true under the sale model (as opposed to the license model) of analysis, wherein the buyer purchases the compact disc with certain expectations. As will be discussed in the next section of this article, a licensing model provides the opportunity for record labels to escape this constraint.
- (b) Whether or not the disc is of “fair, average quality within the description”<sup>193</sup> is unclear.
- (c) The disc is clearly not “fit for the ordinary purposes for which such goods are used”<sup>194</sup> if it cannot play on a variety of devices that purport to play compact discs, and that do play virtually all compact discs. The list of devices that Coldplay may not play on seems to limit predictable playback to the somewhat antiquated home-stereo, stand alone CD players. The “ordinary purposes” for which CDs are used clearly extends far beyond those devices.
- (d) The disc does “run...of even kind, quality and quantity within each unit and among all units involved”<sup>195</sup> if this purports to refer to a batch of the Coldplay CDs.
- (e) The discs are not, however, “adequately contained, packaged and labeled as the agreement may require”<sup>196</sup> if the agreement purports to sell the music to the

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<sup>190</sup> Ken Fisher, A CD insert to make Sony blush (Jan. 2, 2006), <http://arstechnica.com/news.ars/post/20060102-5877.html> (last visited Nov. 6, 2006) (referencing Coldplay, X&Y (EMI 2005)).

<sup>191</sup> Martin H. Bosworth, Coldplay Can’t Play (Jan. 4, 2006)

<http://www.consumeraffairs.com/news04/2006/01/coldplay.html>, (last visited Nov. 6, 2006). Note, there are many versions of this CD in the marketplace, including live versions, singles and import versions. See, e.g., *infra* notes 197, 199. The version of the CD specifically referenced in this article was released in Europe, Africa, and the Middle East, and the copy in question was discovered in India. The Big Picture, What happens when bloggers get it wrong, but the MSM gets it right?, [http://bigpicture.typepad.com/comments/2006/01/how\\_the\\_media\\_m.html](http://bigpicture.typepad.com/comments/2006/01/how_the_media_m.html) (Jan. 7, 2006). I only use this reference to indicate the potential warranty of merchantability claims labels could see, I do not mean to imply that the Coldplay CD itself, as released in the United States, is subject to such a claim.

<sup>192</sup> U.C.C. § 2-314(2)(a) (2003).

<sup>193</sup> U.C.C. § 2-314(2)(b) (2003).

<sup>194</sup> U.C.C. § 2-314(2)(c) (2003).

<sup>195</sup> U.C.C. § 2-314(2)(d) (2003).

listener for them to listen to on their compact disc players. Adequate labeling would require notification that the compact discs do not play on many devices, which is a far more accurate warning for the average consumer than the fact that the disc does is merely “copy-protected.”

Many versions and derivations of the referenced Coldplay X&Y album are available, including singles from the album and live cuts, and not all versions are equally marked. Some give notice that the discs are “subject to terms & conditions.”<sup>197</sup> Some say that they are “Compatible with CD/DVD/SACD/PC/Mac” but also say “playability on all devices cannot be guaranteed.”<sup>198</sup> Others indicate that “on some equipment, for example car CD players, playback problems may be encountered.”<sup>199</sup> Internationally, different terms and conditions and labeling and packaging may apply.<sup>200</sup> Whether or not this particular case is susceptible to a warranty of merchantability claim is a topic for another article. The point here is merely that the use of DRM posed warranty of merchantability issues for record labels.

Finally, DRM brings potential liability for use and fair use claims. Under the First Sale Doctrine and fair use analysis provided in the prior section of this article, users purchase, along with the tangible disc itself, the right to use the disc. Copyright holders are barred from withholding rights from the user as this splits the “sole right of vending” into the rights associated with the tangible media and additional rights that they can contract away later. Under the *Bobbs-Merrill Co.* First Sale Doctrine analysis, copyright holders are prevented from withholding any rights in the media that are not their exclusive rights.<sup>201</sup> Supplying a disc that prevents users from exercising their use rights in the disc could trigger the copyright misuse doctrine, as attempted in *Video Pipeline, Inc.*<sup>202</sup>

Because of the various liabilities associated with using DRM on music CDs, record labels have started to shift toward a new, fourth model of distribution.

#### *Track 5: Record Labels Shift to Licensing Distribution*

Many record labels have shifted to a licensing distribution model. The most successful and noteworthy of the licensing distribution models is the iTunes model.<sup>203</sup> Record labels are also putting license agreements on CDs, however. Inevitably, any CD that employs some form

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<sup>196</sup> U.C.C. § 2-314(2)(e) (2003).

<sup>197</sup> Coldplay, Talk (EMI 2006); Coldplay, Talk, Pt. 1 (EMI 2006); Coldplay, Talk, Pt. 2 (EMI 2006); Coldplay, Talk, Pt. 3 (EMI 2006).

<sup>198</sup> *Id.*

<sup>199</sup> Coldplay, Hardest Part (EMI 2006); Coldplay, X&Y South East Asia Tour Edition (Parlophone 2006).

<sup>200</sup> The legal enforceability of international releases of albums sold as “import CDs” in the United States must remain as the subject for later conjecture. If the labeling on the CD does not meet standards for the state in which it is sold then it may not. This also raises questions about who the licensing contract is with, noting that a record store is typically involved as a middle-man. With international CD releases sold by local stores is there any privity between the purchaser and the record label?

<sup>201</sup> See generally *supra* p. 281-281.

<sup>202</sup> See *supra* p. 281; *Video Pipeline, Inc.*, 342 F.3d at 203-06.

<sup>203</sup> BBC News, *supra* note 171 (noting the eighty percent market share of iTunes in the download market).

of software-based DRM is bound to come with a licensing agreement that, at minimum, spells out the licensing provisions for the software that comes on the CD.

The shift to a licensing paradigm has several advantages for record companies. First, it allows the record companies to use contractual measures to withhold rights. While withholding rights from the consumer would fail under the First Sale Doctrine,<sup>204</sup> record companies, like the software companies that use licensing extensively, can invoke the terms of 17 U.S.C. 109(b), which implies special treatment with regards to the withholding of rights. Second, record companies use licenses to retain ownership of all of the data on the disc, thereby granting to themselves the rights to dispense it as desired under the language of 17 U.S.C. 109(a).<sup>205</sup>

Almost all of the liabilities which record companies face due to their use of DRM can be contracted away by licensing the music to the consumers instead of selling it to them.

Licensed music comes with limited warranties, absolving the manufactures of any damage to computers or playback equipment caused by the DRM on the CD. My Alicia Keys CD came with an End User License Agreement that limits liability for damage or loss of equipment:

NO SONY BMG PARTY SHALL BE LIABLE FOR ANY LOSS OR DAMAGE, EITHER DIRECT, INDIRECT, INCIDENTAL, CONSEQUENTIAL OR OTHERWISE, ARISING OUT OF THE BREACH OF ANY EXPRESS OR IMPLIED WARRANTY, TERM OR CONDITION, BREACH OF CONTRACT, NEGLIGENCE, STRICT LIABILITY MISREPRESENTATION, FAILURE OF ANY REMEDY TO ACHIEVE ITS ESSENTIAL PURPOSE OR ANY OTHER LEGAL THEORY ARISING OUT OF, OR RELATED TO, THIS EULA OR YOUR USE OF ANY OF THE LICENSED MATERIALS (SUCH DAMAGES INCLUDE, BUT ARE NOT LIMITED TO, LOSS OF PROFITS, LOSS OF REVENUE, LOSS OF DATA, LOSS OF USE OF THE PRODUCT OR ANY ASSOCIATED EQUIPMENT, DOWN TIME AND USER'S TIME), ...<sup>206</sup>

Similar provisions are also available for other licenses, including the licenses used by older Sony and BMG discs that use previous versions of MediaMax software,<sup>207</sup> EMI discs that use copy protection,<sup>208</sup> iTunes,<sup>209</sup> and discs that used Sony's XCP software.<sup>210</sup> Because of exposure to viruses, the latter actually caused loss of data, loss of revenue, and down time for

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<sup>204</sup> See *supra* p. 281-281.

<sup>205</sup> See *e.g.*, End-User License Agreement, Sony BMG Music Entertainment at Article 9 (*provided with* Alicia Keys, Unplugged (J Records, a unit of Sony BMG Music Entertainment 2005) (on file with author) (claiming that "The DIGITAL CONTENT and the SOFTWARE contained on this CD are ... 'LICENSED MATERIALS'" and therefore ownership stays with the record label).

<sup>206</sup> *Id.* at Article 7.

<sup>207</sup> BMG Digital Content End User License Agreement, Arista Records/BMG at § 4 (*provided with* Anthony Hamilton, Comin' From Where I'm From (Arista Records/BMG 2003)).

<sup>208</sup> EMI Music, End User License Agreement at "Limitation of Liability (USA Version)," <http://www.mediaextranet.co.uk/publicsites/pdfrepository/1545179.pdf> (last visited Nov. 7, 2006).

<sup>209</sup> iTunes Store Terms of Service, Apple Computer, Inc. at § 18 (Sept. 12, 2006) *available at* <http://www.apple.com/legal/itunes/us/service.html> (last visited Nov. 7, 2006).

<sup>210</sup> End-User License Agreement, Sony BMG Music Entertainment at Article 6 (*provided with* Van Zant, Get Right with the Man (Sony 2005)).

many users.<sup>211</sup> Not all states allow users to contract complete absolution from liability for damages, but by using a licensing contract, record companies can contract the most beneficial liability clause allowed.

With their licensed music, record companies can also include clauses that allow record companies to preempt warranty of merchantability claims. While Coldplay simply did not have enough real estate on the back of their CD package to adequately list all of the devices on which their CD would not play, providing the CD under license allows them to put the limitations on the inside of the package. According to Judge Easterbrook's analysis in *Pro CD*, the contract is not fully integrated until the user agrees to the terms and conditions of the license, and those terms and conditions may come after the money changes hands.<sup>212</sup> My Alicia Keys CD provides an extensive clause waiving liability for warranty of merchantability claims:

YOU EXPRESSLY ACKNOWLEDGE AND AGREE THAT YOU ARE INSTALLING AND USING THE LICENSED MATERIALS AT YOUR OWN SOLE RISK. THE LICENSED MATERIALS ARE PROVIDED "AS IS" AND WITHOUT WARRANTY, TERM OR CONDITION OF ANY KIND, AND SONY BMG, ITS LICENSORS AND EACH OF THEIR LICENSEES, AFFILIATES AND AUTHORIZED REPRESENTATIVES (EACH, A "SONY BMG PARTY") EXPRESSLY DISCLAIM ALL WARRANTIES, TERMS OR CONDITIONS, EXPRESS OR IMPLIED, INCLUDING, BUT NOT LIMITED TO, ANY IMPLIED WARRANTIES OF MERCHANTABILITY, SATISFACTORY QUALITY, NON-INFRINGEMENT AND FITNESS FOR A GENERAL OR PARTICULAR PURPOSE...<sup>213</sup>

Similar clauses are again provided by the major players in the business.<sup>214</sup>

By licensing music on CDs, the record companies also obtain the ability to address potential copyright misuse claims posed by selling discs that withhold users' use rights. My Alicia Keys disc purports to allow me, the licensee, the apparent ability to only use the CD in conjunction with a single computer and a single "approved portable device".<sup>215</sup>

... SONY BMG grants to you a personal, non-exclusive and non-transferable license, ... to:  
(a) install one (1) copy of SOFTWARE onto the hard drive of YOUR COMPUTER,  
...

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<sup>211</sup> In that situation, Sony was generally liable because the software was installed without permission from the users, prior to acceptance of the terms of the EULA. Mark Russinovich, Mark's Sysinternals Blog: Sony, Rootkits, and Digital Rights Management Gone Too Far. <http://www.sysinternals.com/blog/2005/10/sony-rootkits-and-digital-rights.html> (Oct. 31, 2005, 11:04AM). (Revealing the presence of the Sony BMG rootkit software in question on his hard drive, discussing the difficulty in removing it and explaining the susceptibility to viruses this type of software causes).

<sup>212</sup> *ProCD, Inc.*, 86 F.3d at 1451.

<sup>213</sup> See e.g., Sony EULA *supra* note 205 at Article 6. The clause continues to again address those states that have limitations on the ability to contract away warranty of merchantability claims.

<sup>214</sup> See e.g., BMG EULA *supra* note 207 at § 3.1; EMI EULA *supra* note 208; iTunes Store EULA *supra* note 209 at § 18(b).

<sup>215</sup> Nowhere in the license is a list of the approved portable devices; the only clarification is provided in the first paragraph of the license: "certain approved, compatible portable devices owned by you." *Id.* at ¶ 1.

- (b) [install an approved media player]
- (c) use the SOFTWARE and any APPROVED MEDIA PLAYER(S) contained on this CD to access the DIGITAL CONTENT on YOUR COMPUTER or on an APPROVED PORTABLE DEVICE; in each instance, solely for your own personal and private use ...<sup>216</sup>

Apparently the license does not grant me the rights to listen to the music in any other device, such as a car stereo or my DVD player. The license also prevents me from listening to the music on my computer at the office. The license is fairly specific in the fact that the license covers both the music on the CD and the software used to control access to the music.<sup>217</sup>

Other licenses also offer the same degree of control over use. Apple's iTunes Store license, for example, limits use in accordance with what the FairPlay DRM allows.<sup>218</sup> This limitation is arguably the net result of most of the licenses used in the industry—through the provisions that prevent circumventing their DRM technologies, the licenses contractually limit the user to only what the DRM allows.

Licenses also allow record companies to limit distribution of the CDs. Under the First Sale Doctrine of 17 U.S.C. 109(a) the owner of the CD is “entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy.”<sup>219</sup> By merely licensing the music to the end user, however, the record company can limit that entitlement to the consumer. For my Alicia Keys CD, for example,<sup>220</sup> I am not allowed to “distribute, share through any information network, transfer, sell, lease or rent any of the licensed materials to any other person, *in whole* or *in part*” (emphasis added).<sup>221</sup> I am also not allowed to “export” the CD outside of the United States.<sup>222</sup>

Licenses further allow record companies to limit fair use by consumers. As discussed, under *Video Pipeline*, courts are lenient with respect to users' rights to contract away the protections they otherwise receive.<sup>223</sup> The license that came with my Alicia Keys CD is typical<sup>224</sup> in that it does not allow me to “change, alter, modify or create derivative works” of any of the music on the CD.<sup>225</sup> It also does not allow me the otherwise fair use ability to “decompile, reverse engineer or disassemble” any of the licensed materials.<sup>226</sup>

Licenses also provide record companies with the benefit of updating their contracts over time as needed. Should other threats to the record companies surface through changes in technology or legislative or judicial action, the licenses provide the record companies the right to

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<sup>216</sup> See *supra* note 206 at Article 1.

<sup>217</sup> Sony EULA *supra* note 205 at ¶ 1 (“such files and content, collectively, the “DIGITAL CONTENT”).

<sup>218</sup> iTunes Store EULA *supra* note 209 at (9)(b).

<sup>219</sup> 17 U.S.C. § 109(a) (1997).

<sup>220</sup> See also *e.g.*, BMG EULA *supra* note 207 at § 1.3; EMI EULA *supra* note 208 at “Restrictions”.

<sup>221</sup> Sony EULA *supra* note 205 at Article 3(1)(b).

<sup>222</sup> *Id.* at Article 3(1)(e).

<sup>223</sup> See *supra* p. 281.

<sup>224</sup> See *e.g.*, EMI EULA *supra* note 208 at “Restrictions”; iTunes Store EULA *supra* note 209 at § 13(a).

<sup>225</sup> Sony EULA *supra* note 205 at Article 3(1)(c).

<sup>226</sup> *Id.* at Article 3(1)(d). Presumably, this clause is included for the purposes of protecting the proprietary software used, and not for the purposes of protecting the music.

amend the contract. The most plausible of these provisions is provided in Apple's iTunes Store contract, as the contract is for a "service" that continues over time.<sup>227</sup> The contract explicitly states that the songs purchased through the iTunes Store "entail[] the ongoing involvement of Apple. Accordingly, in the event that Apple changes any part of the Service or discontinues the Service, which Apple may do at its election," users may not be able to use their purchased songs anymore.<sup>228</sup> In this respect, updated license terms are part of an ongoing relationship, and the users may elect to cancel their service at any time should they disagree with the updated terms. Similar provisions in other license agreements purport to be based on a similar contractual approach: the license of all of the contents on the CD is a temporary license and the record label may opt to revoke the license for various reasons or issue new terms at any time. My Alicia Keys CD license, for example, requires that I allow any updates to the software provided on the CD, and that if I "fail to install an update, the SONY BMG PARTIES reserve the right to terminate the term of this EULA, along with [my] rights to use the LICENSED MATERIALS, immediately, without additional notice..."<sup>229</sup>

Finally, licenses provide record companies with the typical benefits of standard form contracts: choice of law, choice of forum, waiver of venue, and waiver of trial by jury.<sup>230</sup>

In short, by licensing music record companies may use imperfect DRM technologies and avoid liability for the imperfections. Licensing also allows record companies to contractually establish narrower bounds of use with consumers than the bounds prescribed by statute. Record companies are buffered in establishing these limitations by court decisions that allow users to contract away their rights in the music they purchase.<sup>231</sup>

*Track 6: Record Labels Use Rolling Contracts to Enact the Licenses*

Record labels have borrowed the successful approach used by the computer software industry and are using rolling contracts in the form of clickwrap EULAs to create the licensing contracts with their users. Different record labels use different systems, but there are some standard themes. The Alicia Keys Unplugged CD is one of twenty-seven titles from Sony BMG using MediaMax Version 5 software from SunnComm<sup>232</sup> (one of thirty record labels using the software<sup>233</sup>), and therefore makes for good analysis. EMI, the manufacturer of the Coldplay CDs referenced herein, uses software from Macrovision called CDS-300. Macrovision's CDS series of DRM software products has been used by twenty-one other record labels including Virgin Records, Capitol Records, and Liberty Records,<sup>234</sup> on over 4000 titles and are now on

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<sup>227</sup> It should be noted that Apple's iTunes Store, being a service, does not conform to the license model of contracting. While this article has thus far only addressed sales of music and licensing of music and the legal ramifications of each, the mere contracting for a *service* for goods (cancelable at any time) may result in even fewer legally supported rights for consumers.

<sup>228</sup> iTunes Store EULA *supra* note 209 at § 9(d).

<sup>229</sup> Sony EULA *supra* note 205 at Article 8.

<sup>230</sup> See *e.g., id.* at Article 10.

<sup>231</sup> See *supra* p. 131.

<sup>232</sup> See MediaMax Titles *supra* note 9.

<sup>233</sup> Press Release, SunnComm International, SunnComm Ups CD Security Another Notch (Oct. 12, 2006) available at <http://www.sunncomm.com/press/pressrelease.asp?prid=200510120900>.

<sup>234</sup> Press Release, EFF Sues AT&T to Stop Illegal Surveillance (Jan. 31, 2006) available at [http://www.eff.org/news/archives/2006\\_01.php](http://www.eff.org/news/archives/2006_01.php).

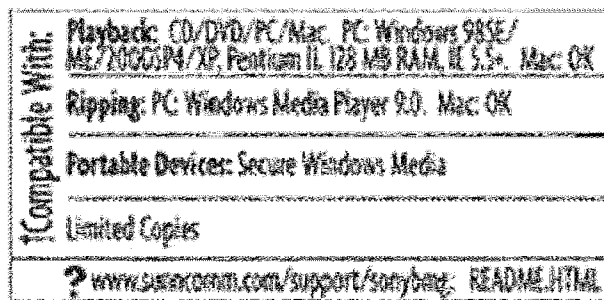
400,000,000 CDs worldwide.<sup>235</sup> These two manufacturers represent a significant quantity of the audio CD DRM market, and analysis of how they enact their rolling contracts should be sufficiently representative.<sup>236</sup>

I purchased the Alicia Keys CD directly from Sony's website; throughout the buying process, I received no notice on the website that the music was subject to an End User License Agreement. The same Sony CD, as listed on Amazon.com's website, provides notice that the CD "includes SunnComm MediaMax Version 5 content protection software..." but provides no notice of the fact that the music itself is under license.<sup>237</sup>

The CD provides notice that there is software on the disc and advises the consumer that use of the software is subject to a EULA. The CD warns on the back that:

+ CERTAIN COMPUTERS MAY NOT BE ABLE TO ACCESS THE DIGITAL FILE PORTION OF THE AUDIO DISC. USE SUBJECT TO APPLICABLE END USER LICENSE AGREEMENT<sup>238</sup>

A graphic on the back of the CD also provides some notice of limitations:



Opening the CD packaging provides no further notice. The CD itself provides no notice. The user can also play the CD in his or her computer without being confronted with the EULA. Only when the consumer attempts to "rip" the CD's contents into the computer does the EULA present itself. The bottom line on the above graphic indicates the presence of a website where consumers can go if they have questions about the license. That webpage documents Frequently Asked Questions, and the page contains an indication that a EULA exists, but the EULA itself is not available.<sup>239</sup>

<sup>235</sup> Press Release, Macrovision Increases Market Leadership with 4 Billion Protected Music Tracks; New Technology Enhancements Enable Universal Playability and Controlled CD Burning (Nov. 18, 2004) available at <http://www.macrovision.com/company/news/releases/newsdetail.jsp?id=Thu%20Nov%2018%2007:48:10%20PST%202004>.

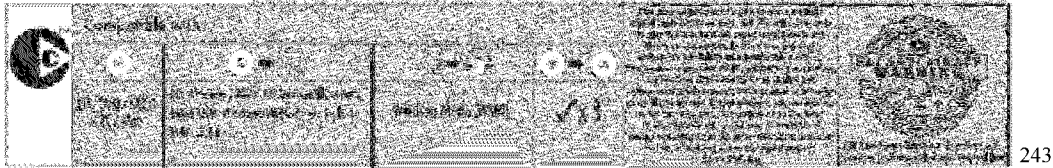
<sup>236</sup> As of September, 2006, all of Macrovision's music CD DRM products have disappeared from its website.

<sup>237</sup> Amazon.com: Unplugged: Music: Alicia Keys, <http://www.amazon.com/Unplugged-Alicia-Keys/dp/B000B5IPLK> (last visited Nov. 7, 2006).

<sup>238</sup> Alicia Keys, Unplugged (J Records, a unit of Sony BMG Music Entertainment 2005).

<sup>239</sup> Media Max Customer Care, <http://www.sunncomm.com/support/faq/> at § 3 (last visited Nov. 7, 2006).

EMI uses a different graphic than that used by Sony BMG, and the CDs provide different warnings. Like Sony BMG's graphic, EMI indicates those devices that are CD-compatible but warns that "playability on all devices cannot be guaranteed."<sup>240</sup> Some EMI discs indicate that the disc "contains Copy Control technology" and "on some equipment, for example car CD players, playback problems may be encountered."<sup>241</sup> Unlike Sony BMG, some of the EMI discs state on the back that the CD is "subject to terms & conditions."<sup>242</sup>



Like the Sony BMG discs, EMI presents a website address on the back of the discs. The EULA in question can be found on the website through the following steps: (1) click the map of North America; (2) click the map of the United States; (3) click the American flag; (4) upon reaching the Welcome page, five menu options are presented: "Music Piracy 2003," "Legal Downloads," "Copy Control," "Problem Solving," "Artists Speak." Click the "problem solving" menu at the top; (5) click the link that says "US EULA" at the bottom of the page.<sup>244</sup>

Neither Sony BMG nor EMI present the terms of the license at the time of the purchase, and therefore each are rolling contracts—in each of these situations, a rolling contract manifested through clickwrap EULAs.

### Disc 3: Conclusions

#### *Track 1: Music CDs that include EULAs are Legally Unenforceable*

The effect of these contracts is difficult to assess. Does the software license allow two contracts—one for the first *sale* of the music (assented to at the time of the sale) and one for the licensing of the accessory software (assented to upon approval of the clickwrap)? Does the software license revert the contract for the first *sale* of the music on the CD into a mere license? Does the software license indicate that the music on the CD was never purchased under first sale at all, but was rather licensed from the beginning?

The answers are elusive. The answer to the first question appears to be "no" based on the fact that the software license addresses the music on the disc as part of the "licensed

<sup>240</sup> See e.g., Coldplay, *Talk* (EMI 2006); Coldplay, *Talk*, Pt. 1 (EMI 2006); Coldplay, *Talk*, Pt. 2 (EMI 2006); Coldplay, *Talk*, Pt. 3 (EMI 2006).

<sup>241</sup> See e.g., Coldplay, *Hardest Part* (EMI 2006); Coldplay, *X&Y South East Asia Tour Edition* (Parlophone 2006).

<sup>242</sup> See e.g., Coldplay, *Talk* (EMI 2006); Coldplay, *Talk*, Pt. 1 (EMI 2006); Coldplay, *Talk*, Pt. 2 (EMI 2006); Coldplay, *Talk*, Pt. 3 (EMI 2006).

<sup>243</sup> This graphic comes from Idlewild, *Warnings/Promises* (EMI 2005).

<sup>244</sup> This file is not, by default, compatible with Apple's Macintosh computers. The file is a .pdf file, which opens by default in Apple's OSX operating system with the "Preview" application. The file can be opened with Adobe's Acrobat Reader, however. See EMI EULA *supra* note 208.



materials.”<sup>245</sup> The answer to the second question must be no; otherwise, a second contract in want of consideration would exist. Within this paradigm, the contract for the music on the CD is a fully integrated contract at the time of the sale, with all rights of use given to the consumer under the first sale doctrine—including the right to use the music in conjunction with their computer—and no licenses preventing use. The second contract relates to the software, and while the financial exchange occurs at the same time, that contract is not fully integrated until the consumer assents through clicking the “I agree” button on the EULA. That contract purports to grant the consumer the ability to use the music with his computer (which he already has) in a limited context in exchange for yielding some of the rights he obtained to the music in the first contract. The problem with this analysis is that a contract requires consideration.<sup>246</sup> In a contract in which the owner of music on a CD gives up his rights to that music in exchange for software that provides no benefit to the consumer, the record label is offering no benefit, and thus no consideration. The software provides no benefit because it merely inhibits rights of use to the music on the consumer’s computer—rights that he purchased at the time of the initial contract. This second contract is invalid for want of consideration.

The only plausible interpretation of the contract is the third—that the consumer never purchased the music on the CD at all but rather had a license from the beginning. In the first part of this article I discussed the rule that has emerged from court cases that clarifies when rolling contracts are legally enforceable:

Enforceable rolling contracts must provide notice to the consumer that such terms are to follow. This notice can be direct or constructive. The buyer must also have the opportunity to review the terms of the contract prior to assenting. Further, the consumer must have the ability to return the goods and unwind the contract if the terms are not acceptable. The seller may establish the timeframe in which the buyer must make a keep-or-return acceptance decision. Finally, any contract must be conscionable and comport with the other common-law requirements of contract law.<sup>247</sup>

EULAs contained on music CDs fail these licensing requirements in many ways. First, the contracts fail to provide the consumers with adequate notice of the impending terms. The reasonable customer purchasing one of these CDs has no constructive notice (through experience in the industry) that purchase of an audio CD is subject to terms and conditions—especially terms and conditions of the nature enclosed in the aforementioned contracts. Further, any direct notice is inadequate. Sony BMG and EMI (as representative indicators) provide no notice on the CD packaging nor do they provide direct notice at the time of purchase that the *music* on the CD is subject to terms and conditions. Both CDs contain the warning that indicates that software is included, and constructive notice can be inferred from the fact that software is present that the *software itself* may be subject to a EULA. Based on the reasoning used in *ProCD*, the presence of software on the CD should be adequate notice that the *software* on the CD is provided under license, but not the *music*.

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<sup>245</sup> Sony EULA *supra* note 205 at Article 1(2) (“The DIGITAL CONTENT and the SOFTWARE contained on this CD are sometimes referred to herein, collectively, as the ‘LICENSED MATERIALS’”).

<sup>246</sup> U.C.C. § 3-303(b) (2002).

<sup>247</sup> See *supra* notes 53-60 and accompanying text.

EMI could argue that the notice it provides that some of its discs are “subject to terms & conditions”<sup>248</sup> is sufficiently vague to cover the music itself, thereby putting the consumer on direct notice of additional terms. Further, Judge Easterbrook’s holding in *Hill* indicates that once the consumer is on notice that the goods are subject to terms and conditions, the consumer has the responsibility to make himself aware of the terms or unwind the contract.<sup>249</sup> This point could be rebuffed by the *Specht* holding, however, in that the terms were provided so remotely as to be equivalent to a “submerged screen”<sup>250</sup> The terms were not presented to the customer before the consumer was required to assent, and the path that the consumer must take to discover the terms is notably indirect.

The buyer of a music CD also does not have the opportunity to review the terms prior to assenting. A unique difference between software and music is that music compact discs generally cannot be returned after opening the seal of the package to listen to the CD. In this respect, the contract should be considered fully integrated at the time of opening the CD to listen to the music. The moment that the consumer breaks the shrinkwrap is the moment that he loses the ability to return the CD. If the consumer assents (in losing the right of return) at the time of opening the CD, and the consumer can only discover the terms upon installing the software in a computer, then the period for review of terms does not begin until *after* the consumer has already assented.

Customers do not have the benefit of an “assent-or-return” clause in this contract, as was the case in *Hill*.<sup>251</sup> In that case, the customer was given a thirty-day window to return the item; failure to do so resulted in assent.<sup>252</sup> In cases of this ilk, the timeline has been specific. For this reason, music CD EULAs are not assent-or-return contracts. Should the record companies note on the back of the CD that failure to return the CD within a reasonable timeframe results in assent to the terms on the enclosed clickwrap EULA, record companies would be more successful in arguing that their agreements are equivalent to that in *Hill*. Obviously allowing people to return CDs within a given timeframe is undesirable for record companies.

Customers do not purchase software when they buy a music CD. Customers purchase music, and the software is merely accessory. Terms that affect the software should not control the terms of the purchase of the music itself. The appropriate model for this transaction is that where the consumer purchases the music itself as a fully integrated contract at the time of purchase. The right to use the accessory software is contingent upon agreement to terms for use *of the software*, not terms *that trump the use of the music*. But even this agreement requires consideration, and these contracts fail in this regard. Finally, the contracts in question violate the basic tenants of contract law: contracts are based on agreements.<sup>253</sup> Agreement requires consent.<sup>254</sup> Consent requires awareness of the terms to which one is consenting.<sup>255</sup> The

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<sup>248</sup> See *supra* note 242 and accompanying text.

<sup>249</sup> *Hill*, 105 F.3d at 1148-50.

<sup>250</sup> *Specht* 306 F.3d at 32.

<sup>251</sup> *Hill*, 105 F.3d at 1148.

<sup>252</sup> *Id.* at 1150.

<sup>253</sup> Restatement (Second) of Contracts § 1 cmt. a. (1979) (“The word ‘contract’...is sometimes used as a synonym for ‘agreement’”).

<sup>254</sup> *Id.* at § 3 (“An agreement is a manifestation of mutual assent...”)

agreements discussed herein run contrary to the underlying purpose and character of contract law.

Because EULAs provided by record labels on music CDs do not adhere to the UCC, court decisions to date, and the values upon which contract law is based, these contracts should be found legally unenforceable.

*Track 2: Suggestions Going Forward*

Judge Easterbrook's decision in *ProCD* was not only controversial at the time,<sup>256</sup> but has continued to be controversial.<sup>257</sup> Part of the academic discomfort with his decision is based on the premise that he undermined basic principles of contract law on policy grounds,<sup>258</sup> finding contracts valid merely because they had become an integral part of our society—finding them invalid would undermine the backbone of an entire industry. The danger of allowing the music industry to continue in its current direction is that at some point, contract law may need to be turned on its head once again to accommodate a legacy form of contract used by that industry. The issue is more consequential than that, however, for if these aberrant forms of contract gain legitimacy within the music industry, other industries will soon follow suit. Many believe that the movie industry, with its incredibly data-intense content and its significantly more expensive products, is a slave to the business model and successes of the music industry.<sup>259</sup> To allow customization of the law for the music industry may have untold consequences in due time. For this reason, action should be taken with respect to EULAs used on music CDs now, while the opportunity is still available. I propose suggestions to judges, legislatures, and manufacturers of the products in question.

I suggest that judges should enforce the law that has developed to date with respect to rolling contracts. In so doing the judges will inevitably find these contracts invalid. Moreover, judges should consider adopting some of UCITA's proposed rules as policy considerations. UCITA has failed largely because consumers found the legitimization of rolling contracts objectionable.<sup>260</sup> If courts continue to uphold rolling contracts, however, then the courts should

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<sup>255</sup> For this reason, affirmative defenses are available for "contracts" wherein one party has no awareness of the terms to which they are assenting, such as mistake and misrepresentation.

<sup>256</sup> See, e.g., Christopher L. Pitet, *The Problem with "Money Now, Terms Later": ProCD, Inc. v. Zeidenberg and the Enforceability of "Shrinkwrap" Software Licenses*, 31 Loy. L.A. L. Rev. 325 (1997); Jason Kuchmay, *ProCD, Inc. v. Zeidenberg: Section 301 Copyright Preemption of Shrinkwrap Licenses—A Real Bargain for Consumers?*, 29 U. Tol. L. Rev. 117 (1997); Joseph C. Wang, *ProCD, Inc. v. Zeidenberg and Article 2B: Finally, the Validation of Shrink-Wrap Licenses*, 16 J. Marshall J. Computer & Info L. 439 (1997).

<sup>257</sup> Gomulkiewicz, *supra* note 40 at 687 note 2 and accompanying text; See also, e.g., Friedman, *supra* note 34.

<sup>258</sup> See, e.g., Kuchmay, *supra* note 256; Braucher, *supra* note 36 and accompanying text.

<sup>259</sup> Peter Burrows & Ron Grover, MSNBC, *Apple's iTunes movie muddle*, <http://www.msnbc.msn.com/id/13463631> (June 21, 2006) (discussing the video industry's "wait and see" policy with regards to online distribution with respect to the music industry).

<sup>260</sup> Consumers STILL Oppose UCITA in 2003, National Consumer Law Center, [http://www.consumerlaw.org/initiatives/e\\_commerce/ucita/index.shtml](http://www.consumerlaw.org/initiatives/e_commerce/ucita/index.shtml) (last visited Mar. 26, 2005) (explaining that consumers still did not approve of UCITA even after the amendments); Matthew D. Stein, *Rethinking UCITA: Lessons from the Open Source Movement*, 58 Me. L. Rev. 157, 178 (2006) ("With regard to UCITA, it is essentially only the software developers that have an interest in contract freedom: the rest of the world—including consumers... would prefer more of a regulatory approach").

treat those terms agreed upon in UCITA as fair in light of the legal enforceability of rolling contracts. If the music industry fails to provide the opportunity for reviewing terms prior to assent and refuses to accept returns on their products, then the consumers should not have to bear the burden of unwinding. In short, judges should find these contracts unenforceable based on the current state of contract law.

Similarly, I suggest that legislators revisit those terms of UCITA that speak specifically to requirements of rolling contracts—namely sections 113, 208, and 209. While there may be other reasons why UCITA as a whole is inappropriate, the legislature would set the law straight with regards to the requirements of this type of contract by passing some of these provisions—a contract style that, as Judge Easterbrook noted, was abundant ten years ago,<sup>261</sup> not to mention its use in the past decade.

Finally, I suggest that the music industry and other related industries explore options that would help their contracts gain legitimacy and enforceability. Under the guidance of the Recording Industry Association of America (RIAA), the music industry should work to develop a template contract that can be universally applied to music CDs that contain DRM software. The music industry can efficiently make a unified contract available through record stores or, similar to the iTunes model, provide for universal assent at the time of purchase for online orders. The industry can require all online merchants to use the template contract. Additional benefits of template contracts can be found in Professor Friedman's extensive article on the topic.<sup>262</sup> Further, the RIAA is optimally suited to draft such contracts. Professor Davis not only suggests reasons why "boilerplate" contracts have benefits, but suggests that trade associations are effective at providing such contracts.<sup>263</sup>

Second, the record industry would benefit from a visually standardized logo system that provides the consumer with some form of rudimentary notice of the terms of the purported contract. Under the current system, many of the record labels are trying to develop standard logos of their own. Further, the graphics contain too much information and are too small to qualify as anything other than an attempt at a disclaimer.<sup>264</sup> The logos do not purport to be user friendly in any way. For instance, four singles from EMI's Coldplay CD contains graphics with two entirely different layout designs and logos, four different sizes, and two different locations on the CD package.<sup>265</sup> The industry trade group IFPI created a universal mark for "Copy Control,"<sup>266</sup> but the mark only indicates that the disc employs one of many forms of copy control technologies, many of which are not at issue herein.<sup>267</sup> The recording industry would be advised

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<sup>261</sup> See *supra* p. 281.

<sup>262</sup> Friedman, *supra* note 34.

<sup>263</sup> Kevin E. Davis, *The Role of Nonprofits in the Production of Boilerplate*, 104 Mich. L. Rev. 1075 (2006).

<sup>264</sup> On Coldplay's "Talk" single, *supra* note 240, the labeling is done in the same layout and with the same content as that shown *supra* p. 281, but is less than two and a half inches wide and less than a half inch high.

<sup>265</sup> Coldplay, *The Hardest Part* (the labeling is 3 5/8" x 0.5"); SouthEast Asia Tour Edition (using the same labeling but 5 1/8" x 5/8"); Talk Live in Holland (using the graphic accompanying the note *supra* 243, sized 4 1/16" x 13/16"); and Talk (using the graphic accompanying the note *supra* 243, sized 2 7/16" x 7/16"); all referenced *supra* notes 240, 241.

<sup>266</sup> International Federation of the Phonographic Industry.

<sup>267</sup> Press Release, IFPI, IFPI announces new optional copy control symbols for CDs (Sept. 17, 2002) *available at* [http://www.ifpi.org/content/section\\_news/20020917.html](http://www.ifpi.org/content/section_news/20020917.html).

to consider a scheme resembling that employed by Creative Commons.<sup>268</sup> Their logos are user friendly, easily equated with the rights conveyed, and encompassed with a link to a single, standardized website for further information about what rights they entail.<sup>269</sup>

Finally, the recording industry should revisit its contracts to ensure equitability. Not only do these contracts fail structurally, but the contracts are manifestly inequitable with what they purport to do. The contracts as written aim to defeat both fair use and the First Sale Doctrine in ways to which, given meaningful opportunity to assent, no reasonable consumer would agree. According to these contracts, by agreeing to install rights-limiting software the consumers are ceding their rights to the music itself. No reasonable consumers see software that allows them to put a copy of the CD onto their computer for personal use as rights-enabling as DRM proponents assert they are doing. Separating the contract for the software from any rights in the music or the medium itself would substantially increase the equitability in these contracts.

With minor work it would be possible to “plug” the music industry back into currently accepted contract law. Failing to do so may create significant repercussions for contract law as we know it. I shudder to guess what Judge Easterbrook’s ruling may be on a case brought ten years from now—after the music industry, the movie industry, the ebooks industry, and four as-of-yet undeveloped industries are all dependent on the legal enforceability of contracts similar to those used by the music industry now.

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<sup>268</sup> See Creative Commons, Creative Commons Licenses, <http://creativecommons.org/licenses/> (last visited Nov. 8, 2006).

<sup>269</sup> See Creative Commons, Choosing a License, <http://creativecommons.org/about/licenses> (last visited Nov. 8, 2006).