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**IS THIS MINE OR YOURS? THE EFFECT OF THE RULINGS IN
VERNOR V. AUTODESK AND THE LIBRARY OF CONGRESS ON THE
DETERMINATION OF WHO OWNS SOFTWARE COPIES**

*Cody Gillians**

In July of 2010, the Copyright Office issued a ruling that allowed owners of iPhones and other cell phones to reprogram their devices to allow the use of lawfully-obtained programs not approved by their phone manufacturers. Despite the ruling, however, the Copyright Office was unable to determine whether the copies of the programs loaded onto the phones were licensed to the users or owned by the users. In September of that year, the Ninth Circuit decided Vernor v. Autodesk, allowing copyright owners to simply add language to the license agreements in order to give users a license instead of ownership of the software copies. This recent development discusses that decision's impact on licensing agreements in light of the Copyright Office's iPhone ruling and why the test in the Vernor decision may be completely unnecessary in the future.

I. INTRODUCTION

In 1990, my parents bought me a video game system along with a few games. Over the next few months, I defeated all of the "bosses,"¹ collected all of the rewards, and completed all of the

* J.D. Candidate, University of North Carolina School of Law, 2012. First, I would like to thank the University of North Carolina Journal of Law and Technology editors for all of their valuable assistance during the publication of this Recent Development. I would also like to thank Professor Laura N. Gasaway and Professor Deborah R. Gerhardt for their professional insight and critical reviews during this process. Finally, I would like to thank Professor Ruth Ann McKinney for her support, guidance and encouragement in helping me to become a better writer.

¹ "Bosses" are characters at the end of levels in video games, which are themselves software. See Clive Thompson, *Who's The Boss*, WIRED.COM (May

games. Once finished with a particular game, I traded it to one of my friends in exchange for one of their games. This routine allowed us to keep playing new games while reducing the need for our parents to buy new games. In our opinion, we owned each game our parents bought for us. Consequently, we believed that we could trade it for another game, lend it to a friend for a few days, or do anything else we chose with it. Over the next twenty years, many new avenues to trade and even resell software became popular. Stores such as GameStop² and websites such as eBay³ and Craigslist⁴ allowed owners of video games and other software to sell their copies of games and programs once they no longer wanted them. This process seemed to work harmoniously for a number of years. Two recent court decisions, however, are forcing consumers to re-evaluate what they actually own.

In 2010, two independent rulings addressed the issue of ownership of a computer program restricted by a license agreement. The first ruling came from the Copyright Office division of the Library of Congress. Every three years, the Librarian of Congress has the authority to determine whether there are uses of copyrighted works that should be exempted from the Digital Millennium Copyright Act's prohibition on the circumvention of technological protection measures.⁵ On July 26,

8, 2006), <http://www.wired.com/gaming/gamingreviews/commentary/games/2006/05/70832>.

² GameStop is a retailer that allows customers to trade in used video games for store credit toward the purchase of another video game. GAMESTOP, <http://www.gamestop.com/gs/specialty/tradeins/> (last visited Nov. 7, 2010).

³ eBay is an online website that allows registered users to sell merchandise and create online stores. See Sue Ann Mota, *eBay v. MercExchange: Traditional Four-Factor Test for Injunctive Relief Applies to Patent Cases, According to the Supreme Court*, 40 AKRON L. REV. 529, 535 (2007) (discussing the purpose of eBay).

⁴ Craigslist is an "electronic meeting place for those who want to buy, sell, or rent" goods and services. See Chi. Lawyers' Comm. for Civ. Rights Under Law, Inc. v. Craigslist, Inc., 519 F.3d 666, 668 (7th Cir. 2008) (describing the nature of Craigslist, primarily as an online venue for buying, selling, or renting housing).

⁵ 17 U.S.C. § 1201(a) (2006); See also "Copyright Office/DMCA: Cellphone 'Jailbreaking' Allowable Under New DMCA Anticircumvention Exemptions,"

2010, the Librarian of Congress followed the recommendation of Marybeth Peters, the Register of Copyrights, and issued a ruling allowing users of iPhones and other cell phones to utilize lawfully-obtained third-party applications on their phones by circumventing access controls surrounding the phone's software.⁶ In the Register's recommendation to the Library of Congress regarding allowing this new class of uses, she noted that "the law relating to who is the owner of a copy of a computer program under Section 117 is in flux."⁷ Consequently, the Register concluded that when the law is unclear, the regulatory process should not be the preferred method to address uncertainties.⁸ Instead, the Register recommended that cell phone users be allowed to circumvent copyright protections to use legally obtained software under a fair use argument.⁹

In the Register's analysis of whether an iPhone user owned the copy of the iPhone software programmed into his phone, she noted that there is a conflict in the Ninth Circuit on the question of what criteria should be used to determine whether an iPhone owner is a licensee or an owner of the copy of the Apple operating system loaded onto the iPhone.¹⁰ This conflict was later resolved by the Ninth Circuit's ruling on an appeal from the Western District of Washington's decision in *Vernor v. Autodesk, Inc.*¹¹ There, the Ninth Circuit evaluated precedent within its jurisdiction to create a new test to determine whether the transfer of a copy of a computer

80 PAT. TRADEMARK & COPYRIGHT J. (BNA) No. 417, at 1 (summarizing the Library of Congress's procedure for determining exemptions).

⁶ Copyright Office/DMCA: Cellphone 'Jailbreaking' Allowable Under New DMCA Anticircumvention Exemptions, *supra* note 5, at 1.

⁷ E-mail from Marybeth Peters, Register of Copyrights, to James H. Billington, The Librarian of Congress (June 11, 2010), at 90, <http://www.copyright.gov/1201/2010/initialed-registers-recommendation-june-11-2010.pdf>.

⁸ *Id.*

⁹ *Id.* at 91.

¹⁰ *Id.* at 91-94.

¹¹ No. 09-35969, 2010 U.S. App. LEXIS 18957 (9th Cir. Sept. 10, 2010); *see also Vernor v. Autodesk, Inc.*, 555 F. Supp. 2d 1164 (W.D. Wash. 2008).

program to a purchaser is a sale of the copy of the program or simply a license to use the copy.¹²

This Recent Development will first, in Parts II and III, discuss both the Librarian of Congress's initial inquiry into who owns the copy of a computer program followed by a brief discussion of the Ninth Circuit's ruling in *Vernor v. Autodesk*. In Part IV, the Ninth Circuit's new test will be applied to the recently released Apple iPhone 4 licensing agreement to show the ease with which a company can create licensing agreements that give users a license to use the copy of software instead of full ownership of the copy of the software. This recent development will propose that even though Apple has only licensed to the iPhone 4 user a copy of the software loaded on the phone under the test proposed by the Ninth Circuit, the court should consider adding an additional inquiry into whether the copyright owner has taken sufficient steps to enforce its software licensing. Finally, Part V discusses why the *Vernor* test may become obsolete given the current trends of software ownership.

II. THE LIBRARIAN OF CONGRESS'S RECOMMENDATION

The Digital Millennium Copyright Act ("DMCA") was enacted in 1998, in part, to shelter authors that employ protective measures to prevent their works from being unlawfully copied in the digital realm.¹³ Title I of the DMCA created two new prohibitions to protect owners of digital copyrighted materials: a prohibition on circumventing technological measures used by copyright owners to protect their works and a prohibition on tampering with copyright management information.¹⁴ Additionally, the DMCA allows the

¹² *Vernor*, 2010 U.S. App. LEXIS 18957.

¹³ See *United States v. Elcom Ltd.*, 203 F. Supp. 2d 1111, 1119 (N.D. Cal. 2002) (explaining the need to balance fair use and copyright protection).

¹⁴ UNITED STATES COPYRIGHT OFFICE, *The Digital Millennium Copyright Act of 1998*, U.S. Copyright Office Summary (Dec. 1998), <http://www.copyright.gov/legislation/dmca.pdf>. Circumventing a technological measure "means to descramble a scrambled work, to decrypt an encrypted work, or otherwise to avoid, bypass, remove, deactivate, or impair a technological measure, without the authority of the copyright owner." 17 U.S.C. § 1201(a)(3)(A) (2006). Copyright management information is specified

Copyright Office to perform a triennial review to exempt certain classes of users of copyrighted works from the prohibition on circumvention if the prohibition is likely to adversely affect users in their ability to make non-infringing uses of those particular classes of works.¹⁵ In October 2008, the Copyright Office began another inquiry to determine whether there were new classes of users that should be exempted from the prohibition described above.¹⁶ After this inquiry, the Copyright Office published proposed exemptions suggested by the public and held hearings to listen to arguments by proponents and opponents of these proposed exemptions.¹⁷ On June 11, the Register of Copyrights, Marybeth Peters, submitted her recommendation of the classes of users that should be exempted to the Librarian of Congress, James Billington.¹⁸ Subsequently, on July 26, 2010, he exempted six new classes of works from the prohibition on circumvention.¹⁹ One of the new exempted classes include users that use “computer programs that enable wireless telephone handsets to execute software applications, where circumvention is accomplished for the sole purpose of enabling interoperability of such applications, when they have been lawfully obtained, with computer programs

“information conveyed in connection with copies or phonorecords of a work or performances or displays of a work, including in digital form, except that such term does not include any personally identifying information about a user of a work or of a copy, phonorecord, performance, or display of a work.” § 1202(c).

¹⁵ § 1201(a)(1)(B) (2006); *see also* Copyright Office/DMCA: Cellphone ‘Jailbreaking’ Allowable Under New DMCA Anticircumvention Exemptions, *supra* note 5, at 1 (discussing exemption procedure for certain class of copyrighted works).

¹⁶ Copyright Office/DMCA: Cellphone ‘Jailbreaking’ Allowable Under New DMCA Anticircumvention Exemptions, *supra* note 5, at 1.

¹⁷ *Id.*

¹⁸ E-mail from Marybeth Peters, *supra* note 7, at 1.

¹⁹ The Register recommended that five classes of works be exempted and that one class be denied exemption but the Librarian chose to exempt six classes of works. *Id.*; *see also* Exemption to Prohibition on Circumvention of Copyright Protection Systems for Access Control Technologies, 75 Fed. Reg. 43,825, 43,829 (July 27, 2010) (to be codified at 37 C.F.R. pt. 201) (describing the exemption process in more detail).

on the telephone handset.”²⁰ In short, the Library of Congress exempted from the prohibition on circumvention cellular phone users that re-program their phone to use legally-obtained applications and programs not approved by their cellular service provider. The process to re-program cell phones is commonly called “jailbreaking” in the cell phone community.²¹ Cell phone users desire to jailbreak their phones primarily to install applications or perform tasks not approved by their cell phone designer.²² One downfall to jailbreaking is its potential to disrupt the normal functions of the phone and to cause instability in the phone’s operation, which cell phone designers might find undesirable because it can result in greater maintenance costs.²³ Also, phone manufactures desire to be the sole provider of software for their phones.

In ruling whether jailbreakers should be allowed to circumvent copyright protections on cell phone operating systems, the Register attempted to determine whether the various versions of the iPhone contracts constituted a sale or a license of a copy of the iPhone software.²⁴ The Register concluded that she could not determine “whether the various versions of the iPhone contracts with consumers constituted a sale or license of a copy of the computer programs contained on the iPhone.”²⁵ In her attempt to resolve this question, the Copyright Office asked proponents and opponents of this exemption to provide responses to this question.²⁶ The

²⁰ Copyright Office/DMCA: Cellphone ‘Jailbreaking’ Allowable Under New DMCA Anticircumvention Exemptions, *supra* note 5, at 1.

²¹ See generally Mark Milian, ‘Jailbreaking’ iPhones and unlocking carrier restrictions legal, government says, LOS ANGELES TIMES (July 26, 2010, 2:18 PM), <http://latimesblogs.latimes.com/technology/2010/07/iphone-jailbreak-legal.html>; Thomas Ricker, *iPhone Hackers: “we have owned the filesystem,”* ENGADGET (July 10, 2007), <http://www.engadget.com/2007/07/10/iphone-hackers-we-have-owned-the-filesystem/>.

²² Advantages and Disadvantages of Jailbreaking iPhone or iPod Touch, IPHONESPIES (Dec. 11, 2008), <http://www.iphonespies.com/iphone-news/why-jailbreak-your-iphone-or-ipod-touch/>.

²³ *Id.*

²⁴ E-mail from Marybeth Peters, *supra* note 7, at 90.

²⁵ 75 Fed. Reg. 43,825, 43,829 (July 27, 2010) (to be codified at 37 C.F.R. pt. 201).

²⁶ E-mail from Marybeth Peters, *supra* note 7, at 86.

proponents of this exemption, led by the Electronic Frontier Foundation (“EFF”), first noted that under Section 117 of Title 17 of the United States Code, the “owner of a copy of a computer program” is authorized to prepare “a new copy or adaptation . . . as an essential step in the utilization of the computer program in conjunction with a machine.”²⁷ EFF then argued that the Section 117 adaptation privilege extends to jailbreaking but noted that the Librarian will have to determine whether an iPhone owner is the “owner of a copy” of the Apple firmware loaded onto iPhones in order for Section 117 to apply.²⁸ EFF believes that the owner of the iPhone is the owner of the copy of the iPhone software loaded onto the phone. EFF came to this conclusion by using the Second Circuit’s test of “whether the party exercises sufficient incidents of ownership over a copy of the program to be sensibly considered the owner of the copy for purposes of Section 117.”²⁹ Applying this test, EFF concluded that:

iPhone purchasers satisfy this test because they purchase a single copy for a single price, they have the right to possess the copy for an unlimited time, they have the right to discard or destroy copies as they wish, and there are no substantial restrictions on transfer of the copy along with the hardware.³⁰

Opponents of this exemption, led by Apple Inc., argued that Section 117 does not apply simply because the licensee is not the “owner” of the copy of the iPhone Software.³¹ Apple first evaluated the legislative history of Section 117 by examining the Final Report of the National Commission on New Technological Uses of Copyrighted Works (“CONTU”). The CONTU report noted that if “proprietors feel strongly that they do not want

²⁷ *Id.*; see 17 U.S.C. § 117 (2006).

²⁸ Letter from Fred von Lohmann, Senior Staff Attorney, Electronic Frontier Foundation, to Robert Kasunic, Principal Legal Advisor, U.S. Copyright Office 2 (July 13, 2010), *available at* http://www.copyright.gov/1201/2008/answers/7_13_responses/eff-supplemental-answers-jailbreak.pdf

²⁹ *Id.* (quoting *Krause v. Titleserv*, 402 F.3d 119, 125 (2nd Cir. 2005)).

³⁰ *Id.* at 2.

³¹ David L. Hayes, *Response of Apple Inc. to Questions Submitted by the Copyright Office Concerning Exemptions 5A and 11A*, U.S. COPYRIGHT OFFICE (June. 23, 2009), http://www.copyright.gov/1201/2008/answers/7_13_responses/apple's-response-to-copyright-office-questions-of-6-23-09.pdf.

rightful possessors of copies of their programs to prepare such adaptations, they could, of course, make such desires a contractual matter.”³² Next, Apple emphasized three Ninth Circuit opinions.³³ Most notably among the three was a 2006 decision, *Wall Data Inc. v. Los Angeles County Sheriff's Dept.*³⁴ In *Wall Data*, the Ninth Circuit created a two-part test for determining whether the acquirer of a copy of a software program is a licensee or an owner.³⁵ First, if the copyright holder expresses that he intends to give the user purely a license to use the copy of the software and, second, the copyright holder imposes significant restrictions on how the customer is permitted to use the copy of the software, then the sale of the software is considered sale of a license to use the copy of the software.³⁶ Using this test with the Apple iPhone Software License Agreement (“SLA”), Apple concluded that the iPhone owner is a licensee of the copy of the iPhone software and not the owner of the copy of the iPhone software.³⁷ Apple also used the “sufficient incidents of ownership” test used by the Second and Federal circuits.³⁸ The Federal Circuit concluded that Section 117 is inapplicable in situations where the licensor retains ownership of the program copy by drafting a license agreement with provisions that provide that the licensor retains title in the software copy, limits the licensee’s right to transfer copies of the software, and limits the hardware on which the software could run.³⁹ In Apple’s case, the Apple SLA provides that the licensee does not own title to the copy of the iPhone software and imposes restrictions on transfer.⁴⁰ Apple also applied the Second Circuit’s ownership test and concluded that because the iPhone user has not paid Apple to develop the iPhone software, the iPhone software is not customized to serve a particular iPhone user’s needs and the Apple

³² *Id.* at 3; see also *Krause*, 402 F.3d at 128.

³³ Hayes, *supra* note 31, at 3.

³⁴ *Id.*; see also *Wall Data Inc. v. Los Angeles County Sheriff's Dept.*, 447 F.3d 769, 785 (9th Cir. 2006).

³⁵ Hayes, *supra* note 31, at 3.

³⁶ *Id.*

³⁷ *Id.*

³⁸ *Id.* at 4.

³⁹ *Id.*

⁴⁰ *Id.*

SLA reserves the right to terminate the license. Therefore, Apple concludes that the iPhone user is a licensee and not an owner of the copy of the iPhone software.⁴¹

The Register evaluated these arguments by Apple and EFF and felt that it was impossible to determine how a court would resolve this situation given these facts.⁴² Though the Register ultimately concluded to allow this class by concurring with EFF's fair use argument, a determination by the Register that iPhone users owns the software on his phone could have provided a better reason to allow this new class of users.⁴³

III. A NEW TEST OF OWNERSHIP IN *VERNOR V. AUTODESK*

As stated in Part II, the Register noted there was a conflict in the Ninth Circuit as to what criteria should be used to determine if an owner of a copy of a computer program is a licensee or an owner of that program.⁴⁴ The Ninth Circuit resolved that conflict in September of 2010 in *Vernor v. Autodesk*.⁴⁵

A. Facts

Autodesk is the developer of a computer program, AutoCAD, which assists architects and other designers in creating plans for their projects⁴⁶ Autodesk holds registered copyrights in all versions of their software including the Release 14 version at issue in this case.⁴⁷ Since 1986, Autodesk has sold their AutoCAD software with an SLA.⁴⁸ Customers are required to accept the SLA before they are permitted to use the program.⁴⁹ A customer who

⁴¹ *Id.*

⁴² E-mail from Marybeth Peters, *supra* note 7, at 90.

⁴³ *Id.* at 91.

⁴⁴ See *supra* Part I, II.

⁴⁵ No. 09-35969, 2010 U.S. App. LEXIS 18957, at *26 (9th Cir. Sept. 10, 2010) (holding that "a software user is a licensee rather than an owner of a copy where the copyright owner (1) specifies that the user is granted a license; (2) significantly restricts the user's ability to transfer the software; and (3) imposes notable use restrictions.").

⁴⁶ *Id.* at *3.

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ *Id.*

does not accept the SLA has the opportunity to return the software for a full refund.⁵⁰ The SLA contains separate terms and conditions for different types of users.⁵¹ The SLA states that “Autodesk retains title to all copies”⁵² and that “the customer has a nonexclusive and nontransferable license to use Release 14.”⁵³ Additionally, the SLA imposes transfer restrictions including a prohibition on transferring the software outside of the Western Hemisphere.⁵⁴ Finally, the SLA contains important use restrictions and license termination conditions.⁵⁵ Autodesk also takes significant measures to enforce these agreements, including assigning unique serial numbers and requiring the customer to “input ‘activation codes’ within one month of installation to continue using the software.”⁵⁶ The activation code is only issued after the serial number is authenticated by Autodesk.⁵⁷

In March of 1999, Autodesk settled with Cardwell/Thomas & Associates, Inc (“CTA”) for their illegal and unauthorized use of its software.⁵⁸ The settlement agreement included a provision where Autodesk licensed ten copies of their software to CTA, and CTA agreed to the terms of the SLA packaged with the software.⁵⁹ The Autodesk SLA was located on the packaging of the software, in the settlement agreement, and onscreen during the installation of the program.⁶⁰ Soon after, CTA upgraded from Release 14 to AutoCAD 2000 for a lower price⁶¹ and should have destroyed the copies of Release 14 as instructed by the SLA.⁶² Instead, CTA sold

⁵⁰ *Id.*

⁵¹ *See id.* (“The commercial license, which is the most expensive, imposes the fewest restrictions on users and allows them software upgrades at discounted prices.”)

⁵² *Id.* at *4.

⁵³ *Id.*

⁵⁴ *Id.*

⁵⁵ *Id.*

⁵⁶ *Id.* at *5.

⁵⁷ *Id.*

⁵⁸ *Id.* at *6.

⁵⁹ *Id.*

⁶⁰ *Id.*

⁶¹ *Id.* (noting that CTA paid \$495 for an upgrade license to AutoCAD 2000 versus \$3,750 for a new license for AutoCAD 2000).

⁶² *Id.*

four copies of Release 14 to plaintiff Vernor along with the activation codes needed to use the software.⁶³ Vernor later listed the four copies of the software for sale on eBay.⁶⁴ Autodesk issued a DMCA take-down notice⁶⁵ to eBay claiming copyright infringement.⁶⁶ Vernor then filed a counter-notice challenging the validity of Autodesk's claim.⁶⁷ Finally, Vernor brought an action against Autodesk to establish that his resales of used software did not infringe on Autodesk's copyright.⁶⁸ The district court granted summary judgment in favor of Vernor declaring that Vernor did not infringe Autodesk's copyright.⁶⁹ Autodesk appealed this decision to the Ninth Circuit.⁷⁰

B. The Court's Analysis

The Supreme Court articulated that the first-sale doctrine⁷¹ "is exhausted after the owner's first sale of a particular copy of the copyrighted work."⁷² The first-sale doctrine is not applicable to one who possesses a reproduction of the copyrighted work but does not own it, however.⁷³ Interpreting *United States v. Wise*,⁷⁴

⁶³ *Id.* at *8.

⁶⁴ *Id.* at *9.

⁶⁵ "The take-down provision of Section 512 permits copyright owners to notify [Online Service Providers ("OSP")] . . . that an infringing work is available on the copyright owner's Web site. Upon receipt of a complaint notice, the OSP must 'respond expeditiously' and remove, or disable access to, the infringing material." Greg Jansen, *Whose Burden is it Anyway? Addressing the Needs of Content Owners in DMCA Safe Harbors*, 62 FED. COMM. L.J. 153, 163 (2010) (discussing what a DMCA take-down notice is); *see also* 17 U.S.C. § 512(c) (2006).

⁶⁶ *Vernor*, 2010 U.S. App. LEXIS 18957, at *8–9.

⁶⁷ *Id.* at *8.

⁶⁸ *Id.* at *10.

⁶⁹ *Id.*; *see Vernor v. Autodesk, Inc.*, 555 F. Supp. 2d 1164, 1170–71, 1175 (W.D. Wash. 2008).

⁷⁰ *Vernor*, 2010 U.S. App. LEXIS 18957, at *10.

⁷¹ The first-sale doctrine allows the purchaser of a copyrighted work to transfer a lawfully made copy of a copyrighted work without permission from the copyright holder. *See Bobbs-Merrill Co. v. Straus*, 210 U.S. 339, 350–51 (1908); *see also* 17 U.S.C. § 109 (2006).

⁷² *Vernor*, 2010 U.S. App. LEXIS 18957, at *12–13.

⁷³ *Id.* at *14.

⁷⁴ 550 F.2d 1180 (9th Cir. 1977).

the district court concluded that the Ninth Circuit held that a person is an owner of a copy of computer software “whenever the transferee is entitled to keep the copy of the work.” The district court found that because Autodesk did not necessitate customers to return copies of Release 14, Autodesk had *sold* Release 14 to CTA, and, therefore, CTA became an owner of the copy of that software.⁷⁵

In order to determine the circumstances under which a person becomes an owner or a licensee of a copy of copyrighted computer software, the Ninth Circuit re-evaluated precedent within the Circuit.⁷⁶ The court observed that *Wise* did not stand for the proposition that selling software restricted by a license agreement without requiring the return of the software allows the owner to have full ownership rights over the copy.⁷⁷ Instead, the Ninth Circuit concluded that the court in *Wise* considered “all of the provisions of the agreement to determine whether the transferee became an owner of the copy or received a license” to use the copy.⁷⁸ Similarly, the *Vernor* court observed that the “MAI trio” of cases also evaluated all of the provisions of the agreements in order to determine ownership versus licensee status.⁷⁹ The *Vernor* court concluded that three factors should be considered to determine whether a software user is an owner or a licensee of the copy of the computer program.⁸⁰ Under this three-factor test, a court first considers “whether the copyright owner specifies that a user is granted a license.”⁸¹ Second, the court evaluates “whether the copyright owner significantly restricts the user’s ability to transfer the software.”⁸² Lastly, the court determines “whether the copyright owner imposes notable use restrictions.”⁸³ In applying the first factor, the court found that the license specifically stated

⁷⁵*Vernor*, 2010 U.S. App. LEXIS 18957, at *24.

⁷⁶*See id.* at *14.

⁷⁷*See id.* at *14–16, *29–30.

⁷⁸*Id.* at *17–18.

⁷⁹*Id.* at *18–19.

⁸⁰*Id.* at *23.

⁸¹*Id.*

⁸²*Id.*

⁸³*Id.*

that “Autodesk retained title to the software. . . .”⁸⁴ Applying the second factor, the court found that Autodesk imposed significant transfer restrictions including the inability to transfer the software out of the Western Hemisphere.⁸⁵ Applying the third factor, the court concluded that the license also imposed significant use restrictions including a prohibition against modifying, translating, or reverse-engineering the software.⁸⁶ Therefore, the court concluded that CTA was a licensee and not the owner of the copy of software.⁸⁷ Consequently, the first sale doctrine did not apply, and Vernor had no right to resell the software.⁸⁸

At the end of the opinion, the court also addressed a possible circuit split with the Second Circuit’s decision in *Krause v. Titleserv, Inc.*⁸⁹ The Second Circuit, in the absence of a licensing agreement, inquired into whether the defendant “exercises sufficient incidents of ownership over a copy of a program to be sensibly considered the owner of the copy.”⁹⁰ Applying this test to the facts of the case, the *Krause* court noted that the following indicia made the defendants the owner of the copy of the program: (1) the consideration paid by Titleserv to develop the programs, (2) the consideration was for the benefit of Krause only, (3) the software was customized to serve Titleserv’s operations, (4) the copies were stored on a server owned by Titleserv, (5) Krause never reserved the right to repossess the copies used by Titleserv, and (6) Krause agreed that Titleserv had the right to continue to possess and use the programs forever.⁹¹ After weighing the factors, the Second Circuit concluded that Titleserv owned the copies of the computer program simply because all of the factors favored of Titleserv.⁹² The Ninth Circuit distinguished *Krause* on the grounds that the parties in *Krause* “did not have a written license

⁸⁴ *Id.* at *25

⁸⁵ *Id.* at *26

⁸⁶ *Id.* at *25–26.

⁸⁷ *Id.* at *25.

⁸⁸ *Id.*

⁸⁹ *Id.* at *32; *Krause v. Titleserv, Inc.*, 402 F.3d 119 (2d Cir. 2004).

⁹⁰ *Id.* at 124.

⁹¹ *Id.*

⁹² *Id.* at 124–125.

agreement, the defendant-employer had paid the plaintiff-employee significant consideration to develop the programs for its sole benefit, and the plaintiff had agreed to allow the defendant to use the programs forever.”⁹³ Therefore, the Second Circuit had no choice but to evaluate the indicia of ownership to determine that Titleserv was the owner of the copies of the software.⁹⁴

IV. “ENFORCEMENT OF LICENSE RESTRICTIONS” AS A NEW FACTOR

Applying the *Vernor* test to the new Apple iPhone4 SLA illustrates the ease with which a company may license a copy of software to a user instead of providing full title in the copy.

A. Applying the Vernor Test to the Apple iPhone4 SLA

Under the *Vernor* test, the first factor to consider is whether the copyright owner specifies that the user is granted a license and not ownership.⁹⁵ The Apple SLA states that “the software . . . that came with your iPhone . . . whether in read only memory, on any other media or in any other form are *licensed, not sold, to you by Apple Inc.* for use only under the terms of this License.”⁹⁶ Thus, under *Vernor*, this factor leans heavily in declaring that the possessor of the program copy is merely a licensee. The second factor is whether the copyright owner significantly restricts the user’s ability to transfer the software.⁹⁷ Section III of the Apple SLA states that the user “may not rent, lease, lend, sell, redistribute, or sublicense the iPhone software.”⁹⁸ Apple does, however, allow the user to make a one-time permanent transfer to another user provided that:

⁹³ *Vernor*, 2010 U.S.App. LEXIS 18957, at *32–33.

⁹⁴ *Id.* at *32.

⁹⁵ See *supra* Part III.B.

⁹⁶ APPLE, INC., IPHONE SOFTWARE LICENSE AGREEMENT: SINGLE USE LICENSE (Update Rev. 2010) (emphasis added), available at <http://images.apple.com/legal/sla/docs/iphone4.pdf>.

⁹⁷ See *supra* Part III.B.

⁹⁸ APPLE, INC., *supra* note 96, at 1.

(a) the transfer must include [the] iPhone and all of the iPhone Software, including all its component parts, original media, printed materials and this License; (b) [the user does] not retain any copies of the iPhone Software, full or partial, including copies stored on a computer or other storage device; and (c) the party receiving the iPhone Software reads and agrees to accept the terms and conditions of this License.⁹⁹

Although the language of the agreement gives the impression that an iPhone user's ability to transfer the software is restricted, it could be argued that it is not a significant restriction since the user has the option to transfer to a new user under the conditions described above. This factor would fall in favor of declaring the iPhone4 user an owner of the iPhone software loaded onto her phone simply because the restriction is not absolute. The final factor is whether the copyright owner imposes notable use restrictions.¹⁰⁰ The Apple SLA states that: (1) the iPhone software cannot exist on more than one Apple-branded iPhone at a time; (2) the user may not distribute or make the iPhone software available over a network; and (3) the user may not decompile, reverse engineer or disassemble the iPhone software.¹⁰¹ This seems to be a sufficient restriction on use to lean in favor of declaring the user is a licensee and not an owner of the copy of the iPhone software. Considering all the factors, it appears that the software loaded onto the iPhone4 is licensed to the user instead of owned by the user. If the Copyright Office had the *Vernor* test during its hearing on whether to allow this new use of software, it might have concluded that the iPhone4 users are licensees and, therefore, have no power to modify the software loaded onto their phones.

B. *A Proposal to Consider a New Factor in the Vernor Test*

As illustrated above in Part IV.A, it would not be difficult for any copyright owner to pass the *Vernor* test by drafting a contract that purports to give the user only a license to use the copy of software.¹⁰² Given the ease with which these types of agreements can be created and implemented, there should be another factor to

⁹⁹ *Id.*

¹⁰⁰ *Id.*

¹⁰¹ *Id.*

¹⁰² See *supra* Part IV.A.

consider when determining whether a user is a licensee or owner of a copyright. Specifically, the courts should consider evaluating the measures taken by copyright owners to monitor and prevent violations of their agreements.

The court in *Vernor* noted that Autodesk takes significant measures to enforce license agreements. They assign serial numbers to each copy of AutoCAD and track registered licensees.¹⁰³ Using the serial numbers, Autodesk assigns activation codes to customers allowing them to use the software.¹⁰⁴ Autodesk only issues the codes once they confirm “that the serial number is authentic, that the copy is not registered to a different customer, and that the product has not been upgraded.”¹⁰⁵ Autodesk’s enforcement seems to be a fairly effective way to monitor the distributed licenses and shows the court that the software owner is sincere about restricting the use of its software and retaining ownership.

One reason courts should inquire into the methods copyright owners use to protect their software is to prevent copyright owners from relying purely on licensing agreements to enforce rights. In theory, a contract is negotiated between two or more parties with equal bargaining power.¹⁰⁶ In some instances, especially with standard-form contracts between a commercial entity and a user,

¹⁰³ *Vernor*, 2010 U.S.App. LEXIS 18957, at *5; Other software developers use similar methods to protect their software. For example, Microsoft requires users to input an activation code before their software can be used. Once the activation code is entered, Microsoft then verifies that the code is not in use on more than the limited number of computers that is indicated in the software end user license agreement. *Activation and Registration of a Microsoft Product* MICROSOFT (Oct. 19, 2010), <http://support.microsoft.com/kb/326851>. Adobe offers the user a 30-day grace period during which a user can use the software without activating. Once the 30-day period is up, you are no longer able to use the software until you activate. Adobe does allow a user to transfer the software to another computer or user by transferring the activation code. *Product Activation Center*, ADOBE (2010), <http://www.adobe.com/ap/products/activation/version1/>.

¹⁰⁴ *Id.*

¹⁰⁵ *Id.*

¹⁰⁶ See Daniel D. Barnhizer, *Bargaining Power In The Shadow of the Law: Commentary To Professors Wright and Engen, Professor Birke, and Josh Bowers*, 91 MARQ. L. REV. 123, 123 (2008).

the terms are prepared by one party and the other party has the option to take-it-or-leave-it with no room to negotiate.¹⁰⁷ These are normally called contracts of adhesion.¹⁰⁸ Most SLAs are contracts of adhesion or “shrink-wrap” agreements, simply because the consumer has no option to negotiate the terms of the contract.¹⁰⁹ They are forced to accept the contract as-is or leave the product.¹¹⁰ Normally, a party would have the option to go to another software vendor in order to obtain a better bargaining position but nearly all software vendors provide similar types of contracts with their products.¹¹¹ This leaves the customer at a severe disadvantage and forces the customer to agree to terms that may not favor him. Given the leverage that copyright holders have in these contracts, courts should consider inquiring into how strongly software copyright owners enforce their license agreements as a way to counterbalance this leverage.

Currently, many software developers have the ability to integrate enforcement measures into their software. One of the primary methods that copyright holders of software utilize to inhibit unauthorized use of their technology is through the use of digital rights management (“DRM”).¹¹² DRM is a general term that covers the variety of methods used to limit sharing of digital

¹⁰⁷ The law has recognized there is often no true equality of bargaining power in such contracts and has accommodated that reality in construing them. *Standard Oil Co. of Cal. v. Perkins*, 347 F.2d 379, 383 n.5 (9th Cir. 1965).

¹⁰⁸ “Adhesion contract” is a shorthand descriptive of standard form printed contracts prepared by one party and submitted to the other on a “take-it-or-leave-it” basis. *Id.*

¹⁰⁹ See Batya Goodman, *Honey, I Shrink-Wrapped the Consumer: The Shrink-Wrap Agreement as an Adhesion Contract*, 21 CARDOZO L. REV. 319 (1999).

¹¹⁰ *Id.* at 321.

¹¹¹ See Pratik A. Shah, *The Uniform Computer Information Transactions Act*, 15 BERKELEY TECH. L.J. 85, 93 (2000) (“[G]iven the bargaining power of most licensors over licensees in the mass-market shrinkwrap context, where adhesion contracts are the norm, this apparent efficiency could come at the licensee's expense.”).

¹¹² See Patrick Murck, *Waste Content: Rebalancing Copyright Law to Enable Markets of Abundance*, 16 ALB. L.J. SCI. & TECH. 383, 407 (2006).

copyrighted material.¹¹³ Though DRM has many flaws¹¹⁴ and, in some cases, can be easily circumvented, the copyright holder can show courts that by using DRM it is attempting to enforce the licensing agreement in ways other than simply relying on the agreement to deter wrongdoers. Apple may currently have only a few methods to track the users of its devices but Apple has given every indication that it has the ability to implement new features in the future to detect violators of their SLAs.¹¹⁵ Under the new factor proposed, these forthcoming features should give Apple a stronger argument that it really intends to only give their customers a license to use the iPhone software.

Another reason courts should inquire into how a company plans to enforce its agreements is the fact that many common household items today come with software. For example, microwaves,¹¹⁶ TVs, remote controls, and cars all have computer programs that assist their operation. It would not be difficult for the manufacturers of these items to include standard-form contracts which give the purchaser a license to use the computer programs loaded onto the devices instead of full ownership of the copies of the programs on their devices. Without full ownership of the program copies loaded into these devices and assuming manufacturers include contracts with severe restrictions on transfers, users will be unable to resell the devices under the first sale doctrine.¹¹⁷ If the designers of these devices can show that

¹¹³ See *id.*; see also *Digital Rights Management*, WIKIPEDIA (Sept. 20, 2010, 4:00 PM), http://en.wikipedia.org/wiki/Digital_rights_management.

¹¹⁴ See generally Jeremy Kirk, *Researcher: DRM Has Deep Flaws*, PCWORLD (Mar. 27, 2006, 4:00 PM), http://www.pcworld.com/article/125227/researcher_drm_has_deep_flaws.html (discussing the flaws surrounding digital rights management implementations).

¹¹⁵ See generally Nick Spence, *Apple Patent Could End iPhone Jailbreaking*, PCWORLD (Aug. 23, 2010, 10:19 AM), http://www.pcworld.com/article/203884/apple_patent_could_end_iphone_jailbreaking.html (discussing Apple's new patent to prevent jailbreaking of phones).

¹¹⁶ Curt Franklin & Dave Coustan, *How Operating Systems Work*, HOWSTUFFWORKS.COM (Aug. 14, 2000), <http://computer.howstuffworks.com/operating-system.htm> (discussing computer programs in microwaves).

¹¹⁷ See *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339, 350–51 (1908); see also 17 U.S.C. § 109 (2006).

they have the ability to enforce their agreements, then they should rightly prevent their customers from selling those devices to another party. If they are unable to enforce their agreements using DRM or any other means, then the users of these devices should own the software and be able to resell the devices to another consumer.

V. THE PRACTICAL EFFECTS OF THE *VERNOR* TEST ON FUTURE COMPUTER PROGRAMS AND SOFTWARE DISTRIBUTION

The ruling in *Vernor* has split the software user community into two camps. There are those who feel that the ruling by the Ninth Circuit is the death knell of ownership of software and all other property.¹¹⁸ Opponents of the *Vernor* decision argue that now, by simply adding the correct language into any shrink-wrap licensing agreement, software developers can keep ownership of the copies of their software and prevent users from selling the software to other parties.¹¹⁹ On the other side are those that feel that the Ninth Circuit's ruling correctly aligns with new trends of software ownership.¹²⁰ Next, this Recent Development will discuss how the *Vernor* test may impact current software but its use and effect may be significantly reduced in a cloud computing world.

A. *Vernor and Software I Can Use and Touch*

An initial evaluation of how the *Vernor* ruling would apply to future users of software products offers a very bleak picture. As shown above in the iPhone4 SLA, it is not difficult to create a contract that purports to give the user a license only.¹²¹ As a result of *Vernor*, software developers might very well include these

¹¹⁸ See Corynne McSherry, *You Bought It, But You Don't Own It*, EFF.ORG (July 15, 2008), <http://www.eff.org/deeplinks/2008/07/you-bought-it-you-dont-own-it>.

¹¹⁹ *Id.*; see also *supra* Part IV (applying the *Vernor* test to the iPhone4 SLA).

¹²⁰ See Larry Downes, *The End of Software Ownership—And Why to Smile*, CNET NEWS (Sept. 20, 2010, 4:00 AM), http://news.cnet.com/8301-1001_3-20016864-92.html.

¹²¹ See *supra* Part IV.

“magic words” in their licensing agreements to prevent re-sale of their software.¹²²

Companies wish to prevent resale of their software for multiple reasons. The primary reason is that companies do not receive compensation when works are re-sold to other consumers.¹²³ Unlike other tangible used items, such as a worn table or an old TV, the quality of software does not degrade over time. Consumers who buy used electronic software from a consumer are buying the exact same software that the creator has created with no quality degradation in most cases.¹²⁴ On the other hand, customers unable to afford the latest version of software can purchase an older version for much cheaper.

Although the advantages and disadvantages of re-sale are obvious and pertinent to many consumers and companies, the *Vernor* ruling will destroy the market for used software, such as old video games and previous versions of software, since consumers can no longer rely on the first sale doctrine to protect their software transactions.¹²⁵ Under the first sale doctrine, owners of a physical copy of a work may legally resell that same copy without obtaining permission from the copyright owner and without paying any additional royalties to the copyright holder.¹²⁶ Since the decision in *Vernor* allows owners to draft licenses that only give consumers a license to use the copy instead of full ownership, consumers will no longer have the ability to legally resell software either individually or through retailers such as Gamestop and eBay.¹²⁷

B. *The Cloud*

¹²² McSherry, *supra* note 118.

¹²³ See generally Nate Anderson, “Can I Resell My MP3s?”: *The Post Sale Life of Digital Goods*, ARS TECHNICA (Dec. 17, 2008, 11:05 PM), <http://arstechnica.com/tech-policy/news/2008/12/post-sale-life.ars>.

¹²⁴ *Id.*

¹²⁵ See Part IV.

¹²⁶ See *Vernor v. Autodesk, Inc.*, No. 09-35969, 2010 U.S. App. LEXIS 18957, at *11 (9th Cir. Sept. 10, 2010); see generally 17 U.S.C. § 109 (2006).

¹²⁷ See *supra* notes 2–3.

Though the picture looks bleak for current software, the effects of the *Vernor* decision on the first sale doctrine will be mitigated as software transitions to cloud computing. There are many forms and definitions of cloud computing but the form that is particularly relevant to this discussion is the concept of Software-as-a-Service (“SaaS”). In SaaS, commercially available software is available for use by customers using the Internet but the software is physically stored on the company’s servers.¹²⁸ The company then provides the user the ability to use the software through a website or other interface located on a PC, cellular phone, or other device.¹²⁹ The user would never own or possess the program on his home computer but would instead would have the ability to use the program on-demand.¹³⁰

Some observers feel that this is the future of software distribution.¹³¹ Taking video games as an example, a shift has occurred in the distribution of video games from selling physical copies of the games to the concept of cloud computing video games. In 2009, OnLive introduced a new type of game system and a unique way to distribute the games using SaaS concepts.¹³² The idea is that OnLive would be the primary possessor of copies of the games developed by third parties and OnLive allows the user to play games on their servers using a small device and an Internet connection.¹³³ There is no physical distribution of video games and theoretically no way for users to access the games on

¹²⁸ See Definition of SaaS, PCMAG.COM, <http://www.pcmag.com/encyclopedia/> (enter SaaS into the “Search Encyclopedia” box).

¹²⁹ See *id.*

¹³⁰ *Id.*; see generally David Morgenstern, *Cloud Computing: Apple vs. Microsoft*, ZDNET (Jan. 6, 2009), <http://www.zdnet.com/blog/apple/cloud-computing-apple-vs-microsoft/2730>.

¹³¹ See Downes, *supra* note 120; see generally Evan Brown, *Vernor v. Autodesk: Does It Matter in an Age of Cloud Computing?*, INTERNET CASES: A BLOG ABOUT LAW AND TECHNOLOGY (Sept. 10, 2010), <http://blog.internetcases.com/2010/09/10/vernor-v-autodesk-does-it-matter-in-an-age-of-cloud-computing/>.

¹³² Daniel Terdiman, *OnLive could threaten Xbox, PS3, and Wii*, CNET NEWS (Mar. 23, 2009), <http://news.cnet.com/onlive-could-threaten-xbox-ps3-and-wii/>.

¹³³ *Id.*

the company servers.¹³⁴ The user would simply be buying the privilege to use the game, and a license agreement would govern how the user may use the game.¹³⁵ Currently this idea is limited by the bandwidth limitations imposed by a user's Internet Service Provider ("ISP"), but as the caps on Internet use increase, the idea will become more feasible.¹³⁶ SaaS is already being used in similar ways by companies such as Google, Microsoft and Netflix.¹³⁷

C. *Vernor and the Cloud*

As stated earlier, the ruling in *Vernor* will be mitigated once software distribution is replaced by cloud computing and one aspect of the ruling in *Vernor* aligns well with this new form of software distribution. In the future, a majority of software will not be owned by the user of the software or even possessed by the user. The user will simply access the copyrighted software stored on the copyright owner's systems using a browser or other program.¹³⁸ The copyright owner would not have to deliver full-blown applications but only the ability to access its software through the Internet.¹³⁹ Since the user will no longer "own" a physical or electronic copy of the software, neither the *Vernor* test nor the *Krause* test will be applicable in these situations. Software license agreements should morph into software use agreements that govern the conditions under which the user can access the software on the cloud. Therefore, similar to the focus of the *Vernor* test, an evaluation of the license agreement would be the ideal way to consistently determine a user's rights in all types of agreements

¹³⁴ *Id.*

¹³⁵ *Id.*

¹³⁶ *Id.*

¹³⁷ Netflix is a company that streams videos. The company keeps the videos on their servers and allows users to view the videos through the Internet. <http://www.netflix.com>; Microsoft has created a new version of Microsoft Office to compete with Google Apps. Jaime Anderson, *Microsoft Bets on Cloud Computing with Office 365*, THE MONEY TIMES (Oct. 20, 2010), <http://www.themoneytimes.com/featured/20101020/microsoft-bets-cloud-computing-office-365-id-10132410.html>.

¹³⁸ See *supra* Part IV.B.

¹³⁹ *Id.*

covering software distributed physically, electronically, or on the cloud.

VI. CONCLUSION

The Register of Copyrights' inability to determine whether an iPhone owner is the owner or a licensee of the copy of the iPhone software seems to have been resolved by the Ninth Circuit's decision in *Vernor*. The Ninth Circuit's three-part inquiry evaluated only whether the license agreement grants a license or ownership of the software copy, whether there are significant transfer restrictions, and whether there are significant use restrictions. Applying this test to the recently released iPhone4 software license agreement shows the ease with which a copyright owner may grant a user a license only. Even though the iPhone4 user is given a license to use the iPhone software using the *Vernor* test, the courts should consider using an additional factor to help determine ownership status. Courts should consider inquiring into the methods that the copyright owner used to enforce their agreements and licenses. One reason behind this requirement is the fact that commercial licensing agreements already significantly favor commercial entities. Also, the emergence of computer programs in products other than computers could lead us down a slippery slope where any product that contains or uses a computer program can be licensed and taken out of the first sale doctrine. Though the *Vernor* test will have immediate short-term effects on licensing agreements and the first sale doctrine, those effects should be mitigated in the long-run with the spread of cloud computing and other new forms of software distribution that enable software developers to keep possession of the software. In the future, people will no longer own physical copies of many types of software but will have the ability to use the software governed by a software use agreement.

