Licensing in the Contemporary Information Economy

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I. INTRODUCTION

The U.S. economy continues to experience radical changes in the source of value and in how that value is commercially distributed. One can describe these changes in various ways, but by any description, they entail a diversification of business transaction models. This diversification is occurring in what is considered appropriate subject matter for a commercial transaction and in a blurring of lines among previously distinct areas of business and law practice.[1]

Not surprisingly, changes of this scope fuel controversy and conflict. Many conflicts relate to how law should interact with the new economy. In some cases, the core of the conflict lies in a simple refusal by some to recognize that fundamental social and technological change cannot be reversed by law. In other cases, the conflicts are embedded in the fear surrounding where economic changes will lead us. Additionally, there are many issues on which

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1. *See, e.g.*, STAN DAVIS & CHRISTOPHER MEYER, BLUR: THE SPEED OF CHANGE IN THE CONNECTED ECONOMY 22 (1998).

> Clearly, it no longer makes sense to think of the world in terms of products and services Instead, we should be thinking more broadly of product-service hybrids—"offers" in blurred lexicon. Offers are "productized" services and "servicized" products. They're both fish and fowl, if you like. And more frequently, it will be hard to sell anything that doesn't represent that combination.

ROBERT REICH, THE WORK OF NATIONS (1991). Terminology and practice are both also being changed. *See* Michael L. Rustad, *Commercial Law Infrastructure For The Age Of Information*, 16 JOHN MARSHALL J. COMPUTER & INFO. L. 255 (1998); Peter Lyman, *The Article 2B Debate and the Sociology of the Information Age*, 13 BERKELEY TECH. L.J. 1063, 1087 (1998).

truly different political views exist about how a legal framework should be structured for the new economy as well as what actual interests should be protected at the expense of which others.

The rhetoric of the debate is often needlessly vitriolic, but the reality centers on a single fact: intangible assets dominate the economy and entail much different policy and transactional characteristics than transactions in the old economy. The transition is from a hard-goods economy toward an economy of information, services, and other intangibles. As a focus for transactions and legal policy, intangible subject matter invokes different policy and commercial frameworks than that applicable to goods or real estate.

This Article deals with licensing of information and, especially, licensing computer information.[2] In the past several years, the economic transition we have experienced has engendered various attacks on licensing as a practice. One surrogate focus for these attacks is the Uniform Computer Information Transactions Act (UCITA), a contract law statute modeled after the Uniform Commercial Code (U.C.C.) Article 2, but reflecting that when the subject matter of a transaction centers on rights to use information, different contractual frameworks and policy assumptions are appropriate than when a transaction deals with tangible subject matter (goods).[3] Understanding the differences is critical to understanding the new economy. UCITA follows a rich contract law tradition of tailoring contract law principles to reflect particular contractual subject matter and frameworks.[4]

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2. The term "computer information" comes from the text of the Uniform Computer Information Transactions Act (UCITA). Section 102(a)(10) defines computer information in relevant part as: "information in electronic form which is obtained from or through the use of a computer or which is in a form capable of being processed by a computer." UCITA § 102(a)(10) (2000).

3. Indeed, especially with respect to transactions involving copies of computer programs, the parallel to Article 2 is especially explicit. Of slightly more than 100 sections in UCITA, in excess of seventy percent of all those sections which deal with such transactions are directly traceable to Article 2 doctrines and often follow them verbatim. Included in these sections are all of the important rules pertaining to consumer-related transactions, such as doctrines of good faith, unconscionability, implied warranty of merchantability, and implied warranty of fitness for a particular purpose.

4. *See generally* Karl Llewellyn, *Across Sales On Horseback*, 52 HARV. L. REV. 725, 737 (1939); Raymond T. Nimmer, *Images and Contract Law–What Law Applies to Transactions in Information?*, 36 HOUS. L. REV. 1 (1999).

This Article is not a defense of licensing or of UCITA. No defense of licensing is needed realistically any more than a defense of leasing or sales should be expected. Licensing has been an important framework for dealing with information assets for generations, dating back into at least the mid-1800s in this country. UCITA simply recognizes this history and other differences between digital information transactions and other types of commercial exchanges.

Rather, this Article examines the role of licensing in our economy and discusses some misconceptions that relate, at least indirectly, to licensing as a means of distributing digital information. There are several basic points. First, discussed in Part II of this Article, is the simple fact that the modern economy, which is characterized by licensing as well as other transfers of informational assets, reflects a vibrant diversity. Demonstrably, there has not been a shrinkage or restriction of availability of information and information-based technology as some allegedly fear, but rather a vibrant expansion and diversification. In a market economy, this diversification and expansion occurs through transactional exchanges. Licensing transactions play an important positive role.

The increased economic value of information is recognized in various law developments including expanding property rights in information. But licensing and UCITA do not deal with property rights, they deal with transactions. Information-based transactions are different from the goods-based transactions of older industries. These transactional differences are recognized in UCITA. The information industries that characterize the information economy do not rely on goods, but on distribution of informational assets under conditions suited to the market. UCITA and general licensing practice recognize and build legal models on that fact.

Next, Part III examines the definition of a license and the attributes of that type of transaction in contrast to other ways of disseminating information. Licensing has an important role in the modern economy because license agreements allocate rights to use information or informational rights, and to access information resources. A license focuses directly on establishing what value is offered and what value a transferee purchases. Nonexclusive licenses are pro-distributive, they enable the information owner to give access to or rights to use informational assets to numerous persons while

retaining control of the fundamental informational asset and tailoring the rights given to a diversified marketplace.

As recognized in UCITA, understanding the contours of a license, as contrasted to other transactions, entails understanding the different legal traditions and social policies that contribute to licensing law. UCITA and modern licensing law blend traditional license law concepts (which essentially treat a license as a narrow, limited transaction) and commercial views (which view transactions as more robust giving implicit assurances to the licensee about the quality as well as the right to use the licensed technology).

Part IV turns to the legal foundations for the practice of licensing information, rather than selling copies or giving information away. The legal framework for licensing is deep and strongly embedded in our culture. It resides in the idea of a person's right to control his own property as well as the basic concept that transactional effects in modern commerce are defined by the exchange of value under which contracting parties determine the conditions on which assets will be exchanged. Licensing enables the tailoring of information transfers to fit markets in ways that cannot occur in other exchanges.

Finally, in Part V, we discuss the market effect of licensing. The impact of licensing, and of any associated property rights, cannot be assessed without accounting for the markets in which licensing functions. Examination of those market effects shows that a license allows parties to tailor rights and resulting costs in ways that less nuanced deals cannot. This allows fitting products and services to actual market demand and engaging in what one author describes as a process of "mass customization."[5] That description refers to a distribution of products to the mass market customized by contracts and technology without changes in the physical product. In allowing such practices, licensing law, as implemented in UCITA creates a structure in law that encourages information owners to distribute their products into the market, an objective which is also embedded in modern intellectual property law and that allows them to do so in an efficient manner that benefits all of us.

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5. *See* STAN DAVIS, FUTURE PERFECT (1996); DAVIS, *supra* note 1.

II. CONTEXT

The computer and digital information industries today comprise the most vibrant, competitive, and rapidly growing sector of the U.S. economy. Transactions in information account for a large portion of the gross national product; their importance continues to grow with the advent of the Internet as a focus of commercial activity.[6] Indeed, it is difficult to identify any part of our economy that does not involve information-based technology and, yet, is experiencing rapid or even consistent growth.

Industries associated with computer information led the resurgence of the U.S. economy and have a positive impact on consumers and commercial interests. Consumer choice and the richness of the marketplace for information has greatly expanded during the past several decades. There was and continues to be an explosion in the availability of information, in the options by which we obtain information, and in what types of information or functionality can be acquired. In short, this era represents broad growth and diversity with respect to information in the economy and in society as a whole. That result owes itself to the technology, to the fierce competition in the information industry, and to the diverse business, contract, and marketing models employed.

This empirical background is important in any policy discussion about licensing computer information. The factual record directly challenges the validity of a commonly-stated concern about licensing: that concern alleges that dynamic changes in marketing and distributing information entail a risk of stifling free flow of information and asserts that this risk requires mandatory rules that lock in the information economy into transactions with legally mandated accouterments of so-called first sales of copies of

6. *See* AM. ELECS. ASS'N AND NASDAQ, CYBERNATION, THE IMPORTANCE OF THE HIGH-TECHNOLOGY INDUSTRY TO THE AMERICAN ECONOMY (1998); DEP'T OF COMMERCE, U.S. INDUSTRY AND TRADE OUTLOOK 24-28 (1998). The Internet aspect involves what some describe as electronic commerce. This sector of the economy experienced rapid growth. Electronic commerce will be the single most important factor in expanding international trade in the next century. Predictions range from $144 billion to $1.5 trillion by the year 2002. *See* ORG. FOR ECON. COOPERATION AND DEV., THE ECONOMIC AND SOCIAL IMPACT OF ELECTRONIC COMMERCE: PRELIMINARY FINDINGS AND RESEARCH AGENDA 27 (1999).

information.[7] That argument is wrong in policy and in fact. The empirical reality of licensing in modern commerce is quite the contrary. Licensing contributes to efficient tailoring of an information product and its cost to meet diverse market demands. This creates far greater diversity and opportunity for access to information. As a result of the diversified approaches to marketing information, we live in a world in which availability of information, digital functionality, and innovation reaches astounding heights. At best, then, the purported concern about licensing refers to a theoretical future, rather than present reality. Courts have adequate means to respond to such threats if and when its symptoms eventually emerge.

Independent of licensing, the transition from a goods-based to an information-based economy results in changes in what modern society views as *property* or, at least, as assets appropriately subject to protection. The past two decades in this country have seen a general expansion in protected rights. These include, but are by no means limited to:

> State and federal enactment of criminal laws against unauthorized access to computer systems and disrupting the integrity of computer information, including data, within them.[8]
>
> Federal statutes expanding protection of marks and other business identifiers, such as the federal Anti-Dilution Act and the Anti-Cybersquatting Protection Act.[9]
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> Numerous statutory changes in the Copyright Act that generally expand rights and technological control of digital information products.[10]

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7. *See, e.g.*, Julie E. Cohen, *Copyright and the Jurisprudence of Self-Help*, 13 BERKELEY TECH. L.J. 1089 (1998); Mark Lemley, *Beyond Preemption: The Law and Policy of Intellectual Property Licensing*, 87 CAL. L. REV. 111 (1998); *cf.* David Friedman, *In Defense of Private Ordering: Comments on Julie Cohen's "Copyright and the Jurisprudence of Self-Help,"* 13 BERKELEY TECH. L.J. 1151 (1998).

8. *See* RAYMOND T. NIMMER, THE LAW OF COMPUTER TECHNOLOGY ¶¶ 4.04-.12 (1997).

9. *See* 15 U.S.C. § 1125 (1999) (discussing antidilution: cyber-squatting). *See generally* NIMMER, *supra* note 8.

10. *See, e.g.*, 17 U.S.C. §§ 901-914 (1994) (mask work rights); 17 U.S.C. § 104A (1994) (restored works); 17 U.S.C. § 106(6) (1994) (digital rights); 17 U.S.C. § 106A (1994) (works of

> Court decisions expanding patent law to business activities and business methods.[11]
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> Court decisions applying the tort of trespass to chattel to set non-contractual controls on unauthorized use of online systems and information.[12]
>
> Court decisions applying copyright protection to systems involving estimated or summarized data when these are not considered as "unprotected facts."[13]

As is common with all areas of property law, in many of these respects, law did not establish comprehensive protections. Critical social and legal issues remain about the ultimate scope of this expanding matrix of protection. Yet, the trend is quite clear and quite clearly oriented toward expanding rights to reflect the changing nature of economic and social value in the present economy.

Overall, this reflects a willingness by statute or by common law action to clarify rights in intangible assets. This is a direct product of social change and, in particular, of changing sources of commercial value. Digital assets and digital systems are commercially important, but rights associated with them were not explored until recently; indeed, they could not have been explored until recently.

Traditional intellectual property law regimes have a long and rich history of debate concerning the balance between proprietary rights and unprotected zones.[14] But this traditional scholarship and much of the base upon which it was founded was ripped apart and reshaped by

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visual art); 17 U.S.C. § 1101 (1994) (live performances); 17 U.S.C. 1205 § 1201 (security/ management devices).

11. *See, e.g.*, State St. Bank & Trust Co. v. Signature Fin. Group, Inc., 149 F.3d 1368 (Fed. Cir. 1998); AT&T Corp. v. Excel Communications, Inc., 172 F.3d 1352 (Fed. Cir. 1999).

12. *See, e.g.*, e-Bay, Inc. v. Bidder's Edge, Inc., 100 F. Supp.2d 1058 (N.D. Cal. 2000); Am. Online, Inc. v. Nat'l Health Care Disc., Inc., 121 F. Supp.2d 1255 (Iowa 2000) (Material issue of fact regarding responsibility for the acts of e-mailers precluded summary judgment on claim that message sender was liable for trespass to chattels; as predicted by this court, "trespass to chattels" is any unauthorized interference with or use of the personal property of another); *cf.* Ticketmaster Corp. v. Tickets.Com, Inc., 54 U.S.P.Q.2d 1344 (C.D. Cal. 2000) (no trespass claim where system was in effect open to the public without effective restrictions).

13. *See, e.g.*, CC Info. Servs., Inc. v. Maclean Hunter Market Reports, Inc., 44 F.3d 61 (2d Cir. 1994) (estimate of values of used cars).

14. *See, e.g.*, RAYMOND T. NIMMER, THE LAW OF COMPUTER TECHNOLOGY ch. 1 (1997).

computer information technologies and the opportunities as well as risks they create. Much of the historical policy base was erected when intellectual property rights were in a backwater of a goods-based or real-estate based economy. In today's economy, rights in information are very important.

Value and Commercial Exchange

To focus solely on intellectual property when discussing licensing is to miss an important point. Modern transactions in information do not always stem from intellectual property rights; often, such rights are irrelevant. As in any other commercial transaction, the central issue that determines when or whether a transaction occurs and under what terms concerns *value* in a market place. Does the transferor have sufficient valuable rights, control, money, knowledge, skill, or access to justify a transferee's willingness to promise value in return for a transfer? Alternatively, is the transferee willing to give value to the licensor sufficient to induce the transferor to transfer its value to the purchaser? These transfers are facilitated through contracts which are by definition exchanges. The values available for exchange on either side take many forms, as do the conditions under which the exchange, if any, occurs.

Value, rather than property rights, forms the basis for commercial exchange. Value comes in many different forms, of course. We could spend time trying to catalogue the sources of commercial value, but that would have little importance in this discussion. More importantly, we need to emphasize the obvious: what value is sufficient to support a contract from either side (licensor or licensee) depends on the market, not on the law regarding property rights. Property rights may sometimes be important in a market, but not always. What is critical is that there exists a sufficient basis for an exchange in light of the assets, rights, control, money, knowledge, skill, or access of both parties and in relation to the overall market.

Many who criticize licensing digital information flounder on the simple idea of a market based on value, rather than on property, and the correlative concept of a market providing guidance on how values can best be shaped and distributed. Consider, for example, the comparative market value and influence of a patent on a chemical

process and a database of unprotected public facts associated with chemical manufacturing. A prospective purchaser might value the patent at zero or a next to zero value because of competing available processes or because the patented technology entails costs that make the outcome unmarketable. On the other hand, the purchaser might place great value on the unprotected database because obtaining access to it from the particular licensor will save time, effort, and uncertainty about the reliability of the data. The property right may have far less market impact than the unprotected information.

This illustration reflects what should be the obvious: interceding between property rights in the market are a variety of market factors and individual judgments about value and about the relevance of the asset being offered. One important function of licensing in the modern economy is that it is a contractual framework that enables parties to tailor assets to the market that may exist for them. This does not mean that all licensors and licensees are invariably correct in their choice or offers, but that the net of the process enables a more diverse and richly functioning marketplace for information.

Consider the following illustration, which goes to the core of at least one aspect of the information economy:

> Illustration 1. Vendor collects data on the lifestyles of butterflies. All of the data is from public sources. Vendor places the data in an online database. It offers clients "reading access" for $100 per year under a contract that provides that the customer make no permanent copies of the data. It offers a separate agreement that charges $1,000 for access to download data on any butterfly but requires that the client not redistribute the downloaded data commercially. Client 1 agrees to the $1000 contract and downloads thirty pages of data concerning the Monarch butterfly. Client 2 declines the contract and obtains data on the Monarch butterfly from other public sources.

In this context, the Vendor used technology, effort, and contract to create two information products: (1) a product involving contractual rights to access the database created by Vendor's research, and (2) a product involving a contractual right to download certain information from that database subject to contractual limitations on use when the

data are downloaded.

Under any theory of contract law, Illustration 1 establishes a sufficient basis for a contract between Client 1 and the Vendor. Even though the butterfly data can be obtained elsewhere and even though the data are not copyrighted, obtaining access to the Vendor's database may have value to a client. The two contractual arrangements (licenses) define products with entirely different types of value. The one is a reading service, while the other (the download license) offers more permanent availability of the data for consumer use. Yet, both products come from the same digital resource and both may have value to prospective clients. Indeed, the fact that Client 1 agreed to the contract terms indicates that it believed that value was being offered. The Vendor was willing to provide value in return for a payment and a promise (no commercial redistribution). If a client's assessment of the offer's value overlaps that of the vendor, a contract may ensue if the parties each regard the exchange as beneficial to them. Contract law enforces any resulting agreement if there are sufficient indicia of assent and if the effect of the contract does not violate a fundamental public policy that overrides the policy of enforcing contracts.[15] Indeed, as we discuss later, the ability to build different products from a single digital information resources represents an important use of licensing in the information marketplace.

Why would any client contractually limit its use and agree to pay for information that could be obtained for free from other sources? The answer, of course, depends on various factors (e.g., ease of access, lack of time, reliability of the database, etc.). As the case of Client 2 in the foregoing illustration suggests, not all prospective clients will make the contract. One could ask, then, why would Client 2 refuse the contract obligation that Client 1 accepted? Again, there is no single answer. Perhaps it is nothing more than that Client 2's interest in Monarch butterflies was less than Client 1's interest. Alternatively, perhaps Client 2 meant to use the data in commercial

15. *See, e.g.*, UCITA § 105(b) (1999 Official Text). Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881 (Cal. App. 1998); *cf.* Lowry Computer Prods., Inc. v. Head, 984 F. Supp. 1111 (E.D. Mich. 1997). *See also* RESTATEMENT (SECOND) OF CONTRACTS §§ 178-99 (1979).

redistribution, while Client 1 did not and, therefore, Client 2 could not use the product that was being offered.

The foregoing represents an online version of a common circumstance in the digital information economy. The evaluation of whether or not a sufficient basis for contract exits does not depend on whether property rights exist in the subject matter. If a reasonable alternative exists that is similarly convenient and beneficial, but involves less cost (e.g., a lower price or less restrictions), the client will take that alternative transaction. If no alternative exists, the client may take the original offer if the value required matches or is more than the value that the client expects to receive as a result of the deal, or it may simply refuse to deal. Taken together, decisions of this type define the market for information or any other asset.

The variables that affect market choices are numerous and often unpredictable in the real world. To see a further illustration of this, return to Illustration 1 and assume that Vendor 1 offers the terms stated in the illustration, but Vendor 2 offers the right to download a similar butterfly database for $1,500 without restrictions on reuse of the data. Both offers may exceed what a client is willing to pay, given the availability of doing without the data or of obtaining it from free sources. Assuming that this is not true, to predict which offer a client may accept, we need to know more about the product and the context. Consider the following possibilities:

- Client does not care about making commercial distribution and, thus, receives nothing more of value from Vendor 2 than it receives from the less-expensive Vendor 1 offer.
- Vendor 2 has a reputation for more thorough collection of data than Vendor 1 and Client values thoroughness more than the price difference.
- Client has dealt with Vendor 1 before and expects to do so in the future even though, on this data, Vendor 2 has more accurate information.
- Vendor 2's data, while only needed for internal use by the Client, is obtainable in a more readily usable form than is the cheaper Vendor 1 information.

These and a myriad of other factors go to defining what value the potential client may receive from the particular transaction and how the client may decide to purchase or not contract for purchase. A similar matrix exists with respect to the value the vendor desires or can obtain from the transaction with the particular client.

Overall, of course, these interactions define elements of the market for information. Markets are based on interactive choices influenced by numerous individualized factors. It is in the context of these choices and the markets they create that contract law and property law function.

Value counts in commerce, but it also counts in law. One court, writing in 1952, commented about this analogy in the following terms:

> In a court of equity if that which complainant has acquired fairly at substantial cost may be sold fairly at substantial profit, a competitor who is misappropriating it for the purposes of disposing of it to his own profit and to the disadvantage of complainant cannot be heard to say that it is too fugitive or evanescent to be regarded as property.[16]

We could debate the question of what constitutes "property," but that debate is not relevant here. It is relevant that law and the protection or preservation of value are often intertwined. Law in this context focuses on "protected value." This result does not mean that in every case where value may exist law should provide protection for that value or a means of enhancing it. What it does mean, however, is that in any such case, protection is properly considered along with questions about the potential effects of denying protection or granting it on broader social policy issues.[17] Where value in fact

16. McCord Co. v. Plotnick, 239 P.2d 32, 34 (Cal. App. 1952) (internal quotations omitted). I am not arguing that the application of property or misappropriation concepts in this case, or for present, in any other case, represents appropriate law or law appropriate for today's economy. The point centers solely on the style of analysis.

17. *See, e.g.*, Fred Wehrenberg Circuit of Theatres, Inc. v. Moviefone, Inc., 73 F. Supp.2d 1044 (E.D. Mo. 1999) (company that used Web-posted information of another company relating to motion picture showing times did not commit misappropriation of the data where there was no proof that defendant's actions would alter the other party's incentive to post the information); Ticketmaster Corp. v. Tickets.com, Inc., 2000 U.S. Dist. LEXIS 12987 (C.D. Cal. 2000).

exists, the ordinary response in law is to recognize that some right exists to preserve that value as against at least some intrusions and, ultimately, the law recognizes the right to contract (or decline to contract) with reference to that value.

In defining rights associated with any asset, a balance must be drawn between granting rights to one party and withholding some limited rights in order to benefit the public.

One could visualize a future world in which proprietary rights expand to the point that they stifle important public access and uses, leading to adverse effects on general welfare. We are not near that point today. The idea that formulating public policy entails adjusting to a tension between proprietary and public use provides a framework for most theoretical literature on intellectual property. How law and policy will eventually draw this balance in the information age is important. But we cannot ignore the fundamental reality that balancing occurs in a market context. Thus, in gauging the effect of property rights, the influence of the market, and the relevance of values associated with other than intellectual property rights cannot be ignored.

Sources of value and wealth are shifting. The means of distributing value, and the threats to that value, are also shifting. In this context, it is difficult to conceive of an approach that establishes *a priori* restrictions on commerce and restricts markets in information, except in the very broadest terms. Stagnant markets and stagnant economies are characterized by rigidity based on prior practice. Dynamic markets are characterized by vibrant change and fluidity. The computer information economy epitomizes a dynamic market. It is important that this dynamic market not be constrained for reasons suited to an older or a stagnant economy.

Transactions in Information, Not Goods

Our focus is not property law, but rather transactions and law associated with transactions. To understand the market impact of licensing, it is important to understand the subject matter and nature of a license. On this issue, a significant disconnect exists between analyses that begin with an intellectual property framework and analyses that begin with a commercial transactions framework.

Those who come to licensing law issues from a perspective that begins with intellectual property law have no difficulty understanding that licenses concern information and informational rights. The issues from their perspective center on two questions. First, can a contractual license even exist without an underlying intellectual property right to be licensed? Second, are there situations in which freedom of contract should be closely hemmed in by public policy limitations related to information assets?[18]

A group of academic writers advocate the view that informational property rights should be narrow in order to increase the public domain of information unencumbered by property rights. For many of these academics, a corollary to this property-rights policy argues that the ability of a person to exploit information assets contractually should be similarly hemmed in to avoid circumventing the sought-after narrowed nature of the property rights.[19] Of course, the contemporary pattern in reference to informational property rights entails expansion, rather than restriction. This expansion demonstrates that many disagree with this academic narrowing theory. While the academic literature often comes from one school of thought and urges limitations, judgments grounded in real world markets often lead in a different direction which confirms and protects the rights of a property owner to control markets for its own property. Thus, for example, the Ninth Circuit decision involving the Napster system for distributing music on a peer-to-peer (private party to private party) basis can be seen simply as repudiating the idea that information distributed in the market in digital copies loses its

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18. *See, e.g.*, Jessica Litman, *The Tales that Article 2B Tells*, 13 BERKELEY TECH. L.J. 931, 941 (1998).

19. *See, e.g.*, Mark Lemley, *Beyond Preemption: The Law and Policy of Intellectual Property Licensing*, 87 CAL. L. REV. 111 (1998). When the world of policy making and commercial practice is expanded beyond that academic base, of course, this narrow view of appropriate policy is by no means the dominant contemporary philosophy. This lack of dominance is evident by the routine enforcement of contractual claims and positions in reference to intellectual property assets in which the contract terms do not correspond to the pure form of the copyright or other underlying property law statute. *See, e.g.*, ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996) (contract limits on uncopyrighted database); DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999) (licensee not the owner of a copy); MAI Syss. Corp. v. Peak Computer, Inc., 991 F.2d 511 (9th Cir. 1993) (license restriction to personal use enforced); Nat'l Car Rental Sys., Inc. v. Computer Assocs. Int'l, Inc., 991 F.2d 426 (8th Cir. 1993) (contract).

character as protected information.[20] More to the current point, the Ninth Circuit in that case flatly rejected an argument that copyright owners did not have the right to decide for themselves how their property would be used in the digital marketplace for their own works.[21]

Instead of handing this market over to others based on a claim to narrow property law rights, the court simply held that the persons who placed their copies of the music on the system for access by others and those who "accessed" the works violated the owner's copyright. The difficult issue was to what extent Napster, the system facilitator, could be held responsible for the infringements, a topic that goes beyond our present inquiry, but which was generally resolved in favor of the property owners.

In contrast to the focus from an intellectual property law perspective, those who discuss licensing from a perspective that begins with a commercial contract framework often wrestle with issues like: what is the subject matter of licenses; what contract formation rules govern; and what warranty or other characteristics should exist in a license.[22] Most commercial lawyers and academics were schooled in an environment in which commercial contracts centered on goods and real estate transactions. That background shapes their perception and frames some of their concerns about transactions in information.

One point of contention entails the mistaken belief by some, that computer information industries deal in goods. These industries do not deal in goods. Their focus is not on tangible property. They deal in information and transactions in intangibles. The software and digital information industries do not deal in goods any more than the book publishing industry sells paper. The software and digital information industries do not deal in goods any more than the music recording industry deals in plastic. The software and digital information industries do not deal in goods any more that the *motion picture* industry deals in celluloid tapes.

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20. A&M Records, Inc. v. Napster, Inc., 239 F.3d 1004 (9th Cir. 2001).

21. *Id.* at 1017 (citation omitted) (quoting A&M Records, Inc. v. Naptster, 114 F. Supp.2d 896, 915 (N.D. Cal. 2000)).

22. *See, e.g.*, RAYMOND T. NIMMER, INFORMATION LAW ¶¶ 11.09-11.25 (1996).

In each information industry, the *value* sought and obtained by the transferee lies in the intangibles and the contractual right to use them. Tangible media, like paper, plastic, celluloid, CD, may serve as a conduit, but that is all. Indeed, after loading the information into a computer, many simply discard the diskette. The tangible items do not define the product even if the transaction involves delivery of information in the form of a tangible copy.

That fact has great importance because, for information or services, the policy balance and competing commercial and social demands placed on the subject matter are entirely different for services than for goods. We traditionally treat providers of information or of services differently than sellers of goods. We do that not because of arbitrary tradition, but because what the information and services industries provide is different than goods and relates differently to how our economic and social systems function. Indeed, based in part on this difference, one frequently finds First Amendment issues raised in reference to software and other digital information systems, whereas such issues would seldom be considered in reference to the regulation of hard goods transactions.[23]

The fundamental focus of an entire economy does not often change, but when change occurs, there is a predictable reactionary response. In reference to law, that response insists that the new economy must be viewed in terms of the past and that changes should be reversed or restrained by law in order to retain the formerly comfortable patterns. That response is wrong, impractical, and ultimately, untenable.

It argues, or assumes, that nothing changed when, in fact, much changed. It asserts that law should act to preserve old economic patterns, rather than allow the economy to embrace new patterns. It asserts that law should regulate to stop change when the function of transactional law should be to promote and support a burgeoning economy that benefits all participants, including consumers. It, like those who argue for restricting the ability to license in the mass market, argues from a position of fear; even though we are in a world

23. *See, e.g.*, Universal City Studios v. Corkey, 273 F.3d 429 (2d Cir. 2001) (source code is within the First Amendment); Junger v. Daley, 209 F.3d 481 (6th Cir. 2000).

of growth and expansion where the positive benefits of change for everyone, including consumers, are evidenced daily.

Sixty years ago, Karl Lewellyn denounced lawyers, legislators, and regulators of that time who thought in terms of the prior economy, rather than focusing on the new economy and its subject matter.[24] He was describing a change in the United States from an agrarian economy to a manufactured, mass-produced goods economy. Over several decades, his arguments eventually resulted in the adoption of the current Article 2, a creature of the sales of goods economy and a law specifically tailored to deal with sales of manufactured goods. Were he alive today, Lewellyn would argue just as strongly against treating licensing of contemporary digital information under rules developed decades ago for sales of goods. In our era, those same arguments led to the promulgation of UCITA. Our economy is dominated by transactions in intangibles. It is a fundamental mistake to view word processing software as equivalent to a toaster, or a transaction to create a multi-media product as equivalent to one to manufacture refrigerators, or an online access contract as equivalent to buying a car, or to equating most other digital information contracts to purchases of manufactured hard goods. These transactions differ in many fundamental ways and call into play entirely different social values, marketplace dynamics, and opportunities for a vibrant, diversified, and responsive marketplace.

A number of early courts held that some transactions involving computer software should be handled under contract law relating to the sale of goods.[25] Most of these decisions involved cases where computer hardware or other goods predominated in the transaction. The courts used standard Article 2 analyses to hold that the entire transaction should be brought into Article 2 because goods dominated. Contrastingly, in cases dealing with software alone,

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24. *See* Karl Llewellyn, *The First Struggle to Unhorse Sales*, 52 HARV. L. REV. 873, 876 (1939).

25. *See, e.g.*, Chatlos Sys., Inc. v. Nat'l Cash Register Corp., 479 F. Supp. 738 (D. N.J. 1979), *aff'd*, 635 F.2d 1081 (3d Cir. 1980); Synergistic Tech., Inc. v. IDB Mobile Communications, Inc., 871 F. Supp. 24 (D. D.C. 1994); Neilson Bus. Equip. Ctr., Inc. v. Italo V. Monteleone, M.D., P.A., 524 A.2d 1172 (Del. 1987) (turnkey hardware and software system was contract for goods); Design Data Corp. v. Maryland Cas. Co., 503 N.W.2d 552 (Neb. 1993).

decisions split on what law governs.[26] When one reviews case law on licensing information generally, most cases hold that sale of goods law does not apply to informational assets and the vast majority never mention Article 2 at all.[27] After years of independent debate and discussion involving diverse interest groups, two different uniform state contract law projects separately concluded that software ordinarily should be treated differently than goods. U.C.C. Article 9 treats software as a general intangible.[28] UCITA develops a separate body of contract law applicable to transactions in computer information.[29]

Because of intense political lobbying in Article 2 revisions against this position, it is not clear whether any proposed revision of U.C.C. Article 2 (if one ever emerges from an eleven-year project) will maintain that position even though, for over eight years, both sponsoring groups for Article 2 expressly adopted the view that computer information was not equivalent to goods. The revisers may recede from that position under political pressure and leave the issue unanswered in the statute to satisfy those who fear reality. The choice on that issue ultimately does not matter because the reality remains that informational assets and transactions in them entail far different considerations than do transactions in ordinary goods.

The issue is hardly debatable under federal intellectual property law. There, the Copyright Act makes an explicit distinction between the tangible item and the informational rights involved, a distinction that is also adopted in UCITA.[30] Transfers of a copy do not transfer

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26. *See* Advent Sys. Ltd. v. Unisys Corp., 925 F.2d 670 (3d Cir. 1991) (goods); Architectronics, Inc. v. Control Sys., Inc., 935 F. Supp. 425 (S.D.N.Y. 1996) (not goods); DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999) (Article 2 analysis not applied; licensee not owner of a copy of a computer program).

27. *See* Raymond T. Nimmer, *Through the Looking Glass: What Courts and UCITA Say About the Scope of Contract Law in the Information Age*, 33 DUQ. L. REV. 255 (2000); *see also* William B. Tanner Co., Inc. v. WIOO, Inc., 528 F.2d 262 (3d Cir. 1975) (license for vocal and instrumental recordings to be used on the air not a "transaction in goods" within Article 2); Snyder v. ISC Alloys, Ltd., 772 F. Supp. 244 (W.D. Pa. 1991); Rosenstein v. Standard & Poor's Corp., 636 N.E.2d 665 (Ill. App. 1993) (data license not goods).

28. U.C.C. § 9-102(a)(44) (2000).

29. UCITA does not redefine goods. Instead, it takes the more direct approach of simply describing computer information and computer information transactions and making those subject matter subject to the contract law rules of UCITA. *See, e.g.*, UCITA §§ 102, 103 (2000).

30. 17 U.S.C. § 202 (1994); UCITA §§ 501, 502.

the copyright as a matter of both federal and state law. Similarly, case law on intellectual property rights issues associated with computer information treats licenses and computer information assets as different in kind from goods and sales transactions. Thus, although Article 2 states that title to goods passes on their delivery to a buyer, the Court of Appeals for the Federal Circuit held that a licensee of software does not own the copy of the software delivered to it where the license restricts use of the software in a manner inconsistent with ownership of the copy.[31] Because of that ruling, and others consistent with it, the licensee's right to use the software depends on the contract terms. That federal law principle is identical to the rule adopted in UCITA which provides that, in a license, whether the licensee obtains title to the copy used to deliver the information depends on the terms of the license.[32] Here, it is Article 2 that is mismatched to the underlying transaction and the law applicable to it since, in a sale, Article 2 mandates that title to the goods passes to the buyer no later than on delivery of the goods.[33] Of course, the fact that the Article 2 rule for sales of goods is not consistent with law applicable to licenses of information should not be surprising—a license is not a sale and the license contract focus is not on goods.

In cases where the issue centers on warranties, whether there are implied warranties associated with the transactional subject matter often depends on whether, after the fact, a court treats the transaction as involving goods, services, or information. Under current law, in most states the Article 2 warranties of merchantability and fitness for a purpose apply only to sales and leases *of goods.* They do not apply to transactions in services or in information. For example, in *Milau Associates v. North Avenue Development Corp*.,[34] the New York Court of Appeals refused to apply a U.C.C. warranty of fitness for a purpose to a contract to design and install a sprinkler system. Its rationale shows the underlying contract law that is involved here:

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31. *See* DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999).
32. UCITA § 502.
33. U.C.C. §§ 2-401; 50.
34. Milau Assocs. v. N. Ave. Dev. Corp., 368 N.E.2d 1247 (N.Y. 1977).

> [T]hose who hire experts for the predominant purpose of rendering services, relying on their special skills, cannot expect infallibility. Reasonable expectations, not perfect results in the face of any and all contingencies, will be ensured under a traditional negligence standard of conduct. In other words, unless the parties have contractually bound themselves to a higher standard of performance, reasonable care and competence owed generally by practitioners in the particular trade or profession defines the limits of an injured party's justifiable demands.[35]

Another New York court held that an online information service was analogous to a newspaper and that, unless it made an express commitment to do so, the service was not responsible for errors or misleading information that arguably caused economic loss to a subscriber.[36]

There are parallel splits in case law focused on computer programs that turn on whether the court treats the transaction as involving goods, services, or information. Faced with the intricate policy and complex history on these issues, UCITA adopts warranties that parallel those for goods in all cases where the issue deals with functional aspects of computer programs, but protects and encourages distribution of informational content (e.g., text, images) under an entire set of policy considerations and different implied terms.[37]

We live in a complex world that becomes more complex as informational assets move to the forefront as subject matter for economic exchanges. We cannot simply refuse to believe what our experience tells us. Information-based transactions deal with different sources of market value and with subject matter to which different policy perspectives traditionally apply.

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35. *Id*. at 1250.
36. *See* Daniel v. Dow Jones & Co., Inc., 520 N.Y.S.2d 334 (N.Y. Civ. Ct. 1987).
37. *See* UCITA §§ 402, 403, 404 (2000).

III. WHAT IS A LICENSE?

A license is a contract. Its subject matter is information and rights in information. The contract gives rights to a licensee to use information or resources that the licensor controls or to which it controls access. License agreements also often cover issues concerning the quality, availability, and use of the information.

If one analogizes licensing to commercial sales of goods, it might appear that warranties are the focus of license terms, since, especially in mass markets, this is a primary focus of most contracts. But licenses have far broader and very different functions than sale contracts. In many transactions, licenses entail complex agreements, while in others they merely waive the right to sue. In each case, however, the core of a license deals with contractual rights for use of, or access to, information and defines what the licensee receives.

Definition and Assumptions

UCITA defines a "license" as:

> [A] contract that authorizes access to, or use, distribution, performance, modification, or reproduction of, information or informational rights, but expressly limits the access or uses authorized or expressly grants fewer than all rights in the information, whether or not the transferee has title to a licensed copy. The term includes an access contract . . . .[38]

Under this definition, a license authorizes limited or conditional access to or use of information.[39] UCITA goes on to define default rules that flow from the creation of a computer information license. These are drawn from a blend of reported cases, modern practices, and policy judgments associated with existing commercial and

38. UCITA § 102(a)(41).

39. If one were forced to draw an analogy to the world of manufactured goods, a license resembles a lease more than a sale. The person who acquires the licensed information (or the leased car) does not own that information, but has certain rights to possess and use it. Those rights are defined by the contract. The analogy between a license and a lease breaks down, not because of the similarity of a license and a sale, but because the subject matter of a license is intangible and because a greater array of use-related provisions are common in licensing (either increasing or decreasing the licensee's permission to use the information).

intellectual property law.

Does a license give an affirmative right to use technology or information along with assurances of its quality, or does it convey less? UCITA reflects a commercial perspective on the nature of licensing and assumes that, in many cases, such contractual assurances are given. However, it recognizes that trade practice and expectations of particular contexts may alter that assumption. Indeed, in most areas of patent licensing, no implicit assurances are given that using the licensed information may not violate third-party rights. The dominant common law view treats a license as entailing few if any affirmative commitments to the licensee and as *not* entailing any assurance that the licensee can actually use the licensed subject matter without infringing another's rights. The following captures this view:

> [A] patent license . . . is in essence nothing more than a promise by the licensor not to sue the licensee . . . . Even if couched in terms of "[L]icensee is given the right to make, use, or sell X," the agreement cannot convey that absolute right because not even the patentee of X is given that right. His right is merely one to exclude others from making, using or selling X.[40]

While this quote refers to a patent license, a similar doctrinal concept applies to copyright licenses.[41]

The traditional intellectual property view treats a license as nothing more than a covenant not to sue. There are sound reasons for this. For example, the property right created under patent law is a negative right (i.e., the right to *prevent* others from doing designated acts). The patent owner might be blocked from using its own patented technology because doing so would infringe the patent rights of another party. In patent licensing, the reality of the negative right carries over to characterize what ordinarily occurs in a patent license as equally negative: e.g., no conveyance of an affirmative right to use

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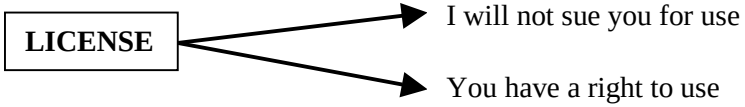
40. Spindelfabrik Suessen-Schurr Stahlecker & Gill v. Schubert & Salzer, Maschinen-Fabrik Aktiengesellschaft, 829 F.2d 1075, 1081 (Fed. Cir. 1987), *cert. denied*, 484 U.S. 1063 (1988).

41. Cohen v. Paramount Pictures Corp., 845 F.2d 851 (9th Cir. 1988).

the technology, but merely a promise not to exercise the right held by the patent owner. It is possible to expressly convey an affirmative assurance that the licensee can use the licensed technology, but under this viewpoint that assurance is not implied. This analysis was generalized to other types of licensing, including copyright licenses.

The two perspectives (commercial and intellectual property) encompass conflicting conceptions about the nature of the transaction. In the one perspective, there is no affirmative assurance to the licensee that it can use the licensed subject matter. In the other, a licensee is presumed to have a *right* to use the information unless that right or the presumption is excluded by the agreement.

Figure 1



These conflicting perspectives reflect a fundamental dissonance in what constitutes the typical or presumed nature of a license agreement. This dissonance sets a context for very different default rules governing the meaning of the agreement where the parties do not otherwise indicate their intentions. The limited transfer presumed by the intellectual property law view of a license supports few, if any, implied obligations beyond the negative promise to not sue. The commercial conception of the transaction, on the other hand, encompasses a promised right to use the licensed technology and often, various presumed other obligations.

Traditional common law approaches to license law hold that there are no assurances about the quality of the licensed subject matter. Unlike in commercial law, licensing law was, and largely remains, a field in which, in the absence of express assurances, qualitative issues about the subject matter do not exist. A doctrine of *caveat licensee* prevails. The idea that there are no implied warranties about quality reflects policies grounded in the reality that licensing practice often does not in fact assume that qualitative assurances are given and in a

policy to avoid chilling distribution of informational assets by creating transactional risks associated with the quality or accuracy of the information.[42] At most, the common law acknowledges some implied obligation in cases involving close relationships of reliance. There, the underlying assumption may be that the information provider will not act negligently. However, even that assurance seldom arises when the informational rights or content are distributed widely.[43]

This common law viewpoint conflicts with the rules regarding the sale or lease of a *good*, in either the mass market or in commercial transactions, in which the buyer receives the benefit of implied warranties about the quality of the subject matter. Of course, except in some consumer contexts, the seller or lessor can disclaim these assurances by contract; implied assurances are waivable by agreement under Article 2.

Licenses and Rights to Use

Under either view (e.g., affirmative grant or mere covenant), the main function of the license centers on permissions or agreements associated with the use of or access to informational assets, along with a licensee's promise not to exceed agreed limitations on use.[44] There are many variations on this theme. For example, while some software licenses allow unlimited types of uses, in others, the licensee agrees to use the software solely for consumer purposes. Some motion picture licenses permit public broadcast of the picture, while others permit only a non-public performance in the transferee's home. Some recording licenses allow public broadcast, while others preclude that use and allow the licensee to make and sell unlimited

42. Warranty law differentiates between the paper or plastic and the information on it. The paper or plastic may be subject to goods-based warranties, but the information is not. We do not, in this country, impose a no-fault implied warranty on information and, indeed, in most states, there is no tort liability for inaccurate information. Instead, we treat information as a creature of the First Amendment. *See, e.g.*, Winter v. G.P. Putnam's Sons, 938 F.2d 1033 (9th Cir. 1991); Cardozo v. True, 342 So.2d 1053 (Fla. Dist. Ct. App. 1977). On the applicability of the First Amendment to software, see Junger v. Daley, 209 F.3d 481 (6th Cir. 2000) (First Amendment limits permitted regulation of distribution of computer source code).

43. *See, e.g.*, Winter v. GP Putnam & Sons, 938 F.2d 1033 (9th Cir. 1991).

44. *See, e.g.*, UCITA § 701(a) (1999 Official Text).

numbers of copies of the recording.

The variety reflects the nature of the subject matter and the market. The variety is unlike transactions in goods where agreements deal with exclusive use, possession, or ownership of the tangible subject matter. Licenses, in contrast, deal with what uses are permitted. This question reflects the value that frames the transaction. Informational assets can be transferred and simultaneously retained by the transferor. In principle at least, an owner of a copyright or a patent can make an unlimited number of transfers (licenses) of that work while retaining the informational asset and otherwise exclusive rights in it. The owner of a tangible product, on the other hand, cannot both sell and retain it, nor can it lease and also retain the right to possession of it during the term of the lease. Transactions in goods are bound by the physical object, while transactions in information are bound by contractual terms associated with use of the intangible.

In a transactional context, then, the relationships consist of information passed from one party to another, mediated by an agreement which defines and apportions the transferee's right and limitations on use. The license defines the rights and, thus, defines the focus of the transaction and what value the transferee receives in a way that is simply not possible to replicate in the world of transactions in goods.

One illustration of this involves the difference between an exclusive and a non-exclusive license. The difference in these two transactions depends on the terms of the license, but they are significantly different types of value for the licensee. In law, the difference lies in whether the licensor contractually commits to not grant further licenses of the same subject matter within the same scope as that conveyed to the transferee. If the licensor promises not to do so, the license is exclusive as to its stated scope and duration. UCITA makes this traditional concept explicit.[45] In a non-exclusive license, the transaction does not give the licensee rights against anyone else, but merely a permission to use within the stated scope of the license. Reflecting this permission, general law assumes that a non-exclusive licensee lacks standing to enforce the copyright or

45. *See* UCITA § 307 (2000).

patent against third parties; that property-law right remains in the property-rights owner, the licensor or the person it represents.[46]

Sales of copies of informational assets are more like non-exclusive licenses than exclusive licenses. The buyer of a copy does not receive any commitment from the seller to not sell other copies to anyone it pleases. Sales are like licenses because, although the buyer acquires ownership of the copy, it obtains only limited rights to use the information on that copy. The copyright owner retains ownership and control of most uses of the information even with respect to the copy purchased by the buyer. The buyer of a book, for example, does not have the right to use the book to make and distribute multiple copies of the novel printed in the book. Indeed, the buyer has only the very limited right to resell its own copy, to discuss the book, rely on its context for advice, and to use the unprotected ideas in the book.

Non-exclusive licenses are inherently pro competitive and pro-distributive.[47] The contracts distribute rights in informational assets that in law could otherwise be restricted in use or access to one person, the right's owner. The license agreement makes them available in whole or in part for use by additional persons (the licensor *and* the licensee). The transaction granting another person the conditional right to use, or access, the information does not use-up the information, which also remains in the hands of the transferor. Thus, licenses increase the licensee's rights in or access to information. The extent of the increase depends on the terms of the agreement. The increase, however, leaves the licensor with the asset it held before the transaction.

Legal Foundation for Licenses

Licenses are common in the information industries. These industries use licenses for the flexibility, focus, and commercial benefits that licenses permit as compared to other transactional forms of conveying information. Since licensing is a long-standing practice,

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46. *See, e.g.*, In re Ortho Pharm. Corp., 34 U.S.P.Q. 2d 1444 (Fed. Cir. 1995).

47. *See* U.S. Dept. of Justice and Fed. Trade Comm'n, *Antitrust Guidelines for the Licensing of Intellectual Property, available at* http:/www.usdoj.gov:80/atr/public/guidelines/ipguide.wp5 (Apr. 6, 1995) [hereinafter *Antitrust Guidelines*].

it is not surprising that a firm legal foundation exists for it—actually, there are many overlapping bases.

The core legal foundation is grounded in the role of contracts in a free-market economy. The formula is simple. One party owns, controls, or knows something of value. Another party desires to acquire access to or use of it. The terms of the transaction, if any, are shaped by the market and the choices of the parties. They are implemented by a contract. The general rationale for enforcing the contract rests in sustaining a market economy and in the basic theme of U.S. law that agreements between and among parties should be enforced in the absence of abuse.

Assuming that two parties make an agreement reflecting an exchange of value, is further legal justification required to enforce the contract? Ordinarily, the answer should be "no." While there may be some cases in which public policy precludes certain contracts or contract terms, the core of mutual promises provides sufficient basis for enforcement. Some argue that further justification should be required. But that argument is not accepted in modern cases.[48] In fact, quite the opposite. Many modern cases enforce licenses, even if the underlying subject matter is information involving no intellectual property rights at all.[49] The few modern cases that decline enforcement typically do so because, in a particular case, contractual assent was not obtained or statute of frauds rules were not met, rather than because of any broad conceptual bar on licensing in any marketplace.[50]

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48. Especially from 1950 until the early 1980s, some courts and federal agencies acted with distrust and hostility to the use of intangible property rights to leverage commercial results outside their scope. *See* ROGER B. ANDEWELT, TECHNOLOGY LICENSING AND THE ANTITRUST LAWS-THE VIEW FROM THE DEPARTMENT OF JUSTICE & TECHNOLOGY LICENSING 401 (1982). However, no court during that period doubted that intangible property rights support licensing. *Cf. Antitrust Guidelines*, *supra* note 47.

49. *See, e.g.*, ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996); Rosenstein v. Standard & Poor's Corp., 636 N.E.2d 665 (Ill. App. 1993). This pattern is especially clear in reference to online licensing of access to information or other services. *See, e.g.*, Caspi v. Microsoft Network, L.L.C., 732 A.2d 528 (N.J. Super. Ct. App. Div. 1999) (holding that choice of exclusive forum enforceable in online contract); Hotmail Corp. v. Van$ Money Pie, Inc., 47 U.S.P.Q.2d 1020 (N.D. Cal. 1998) (finding online terms of service enforceable).

50. *See, e.g.*, Step-Saver Data Sys., Inc. v. Wyse Tech., 939 F.2d 91 (3d Cir. 1991) (holding that a shrink-wrap warranty disclaimer is not enforceable in a battle of forms); Klocek v. Gateway, Inc., 104 F. Supp.2d 1332 (D. Kan. 2000) (finding that silent retention of the

As the Seventh Circuit Court of Appeals commented when presented with the question of whether a license could be enforced for information that was neither patented nor copyrightable, "a contract is a contract, our system of law assumes that contracts should be enforced in the absence of fraud, duress, criminality, unconscionability or similar problems."[51] Licenses of information serve important functions in the economy. There is no basis to preclude them where relevant contractual assent was obtained, and there are not clearly overriding public policies against a particular contractual term.

Of course, many licenses involve information covered by intellectual property rights or held in a location controlled by the licensor. In such cases, additional factors provide a way of understanding the foundations for licensing. These relate to the licensor's right in law to control access to or use of the relevant asset. Licensing in such contexts rests in part on the licensor's right to apportion the extent to which it releases to another or reserves to itself control over or access to its informational assets.

Information, Copies, and Retained Rights

Copyright, patent, trademark and trade secret law, conceive of intellectual property rights in terms of preconditions which, if met with respect to particular subject matter, yield defined rights with respect to that subject matter. In copyright and patent law, these rights are described in statutes.

- Copyright: Property rights attach to works of authorship without any governmental approval or registration. Such rights give an owner the exclusive right to make copies of the work, distribute copies, make derivative works from it, publicly perform the work, publicly display the work, and

computer was not express assent to terms that sought to modify contract already formed between the parties where party did not have notice that contract terms would be presented).

51. ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996).

publicly perform the work by means of a digital audio transmission.[52]

- Patent: Property rights attach to specific claims that pass standards of inventiveness and utility resulting in the issuance of a patent by federal authorities. Property rights include the right to prevent anyone else from making, using, selling, or offering to sell the patented invention.[53]

One can license any of the listed rights, while retaining control of the others. One can license or transfer such rights on an exclusive or a non-exclusive basis. Similarly, one can subdivide any of the rights through limitations in a license. One might condition any of the licensed rights on the performance of stated activities. These contractual choices comprise enforceable contractual distributions of the rights, unless they offend competition law or other fundamental limiting policies.

We discuss later the market benefits that flow from the flexibility created by license agreements. For now, the important point is that a contract that grants one right (or a part of it) does not imply that any other right is granted under the license. Indeed, in the absence of other indicia of a broader agreement, a license conveys only what was expressly granted or what can reasonably be inferred from that express grant.[54] There is no assumption that a transferor (rights owner) grants all rights except those it expressly withholds. In effect, information transactions are presumed to be limited conveyances, rather than comprehensive transfers and this is true whether the transaction entails a license or a sale of a copy.

This corresponds to a policy of preserving and protecting the rights-owner's control of its property in order to enhance incentives encouraging the creation of the informational asset. Both patent and copyright law are grounded in a policy to enhance this incentive.

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52. 17 U.S.C. §§ 102, 106 (1994). The last three of the listed rights are limited to particular types of works, but that limitation has no relevance to this discussion. *Id*. *See generally* RAYMOND T. NIMMER, INFORMATION LAW ¶1.05 (West Group, 1996).

53. 35 U.S.C. §§ 101-04. *See generally* DONALD S. CHISUM, CHISUM ON PATENTS: A TREATISE ON THE LAW OF PATENTABILITY, VALIDITY AND INFRINGEMENT (1999).

54. *See, e.g.*, S.O.S., Inc. v. Payday, Inc., 886 F.2d 1081 (9th Cir. 1989); *see also* A&M Records, Inc. v. Napster, Inc., 239 F.3d 1004 (9th Cir. 2001).

Licenses that optimize a person's value from the rights are fully consistent with this underlying property law policy.

As a matter of fact, most transactions do not convey away all rights in information. Indeed, except when there is an express assignment of all rights, virtually all transactions in information are partial transfers at most. Ordinarily, the transferee is subject to substantial rights retained by the transferor. This fact is true in both the upstream market where information assets are created, modified, and developed, and in downstream mass markets. The idea of a limited rights conveyance under a license, in the context of this ordinarily conditional transactional framework, is thus neither surprising nor unusual. Indeed, the buyer of a book would be shocked to learn that it thereby purchased the copyright to the novel; the author and publishing house would be even more surprised by that result.

This last point has significance for computer information licensing. Unlike a sale of goods, a sale of a copy of a copyrighted work or patented article leaves the buyer subject to restrictions in its use even with respect to the copy it acquired. Sale of a patented article exhausts only some patent rights with respect to that particular item.[55] The buyer, for example, cannot examine the patented item it bought and use that information to make additional identical items. There are also patent law restrictions on the extent to which the copy owner can reconstruct and repair the machine without permission of the property rights owner. Similarly, an authorized sale of a copy of a copyrighted work leaves substantially all of the copyright owner's rights intact and held by the copyright owner, giving the copy buyer only limited flexibility in that copy—chiefly to transfer it (except by rental for a computer program) and, with respect to computer programs, to make a back up and a copy or adaptation essential to the owner's use. All other copyright rights remain in the copyright owner.[56] The Copyright Act makes this explicit:

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55. *See* Mallinckrodt, Inc. v. Medipart, Inc., 976 F.2d 700 (Fed. Cir. 1992).

56. *See, e.g., A&M Records, Inc.*, 239 F.3d at 1004; Red Baron-Franklin Park, Inc. v. Taito Corp., 883 F.2d 275, 280 (4th Cir. 1989) (first sale does not give the buyer the right to make public performances; that right remains in the copyright owner).

> Ownership of a copyright . . . is distinct from ownership of any material object in which the work is embodied. Transfer of ownership of any material object . . . does not of itself convey any rights in the copyrighted work embodied in the object; nor, in the absence of an agreement, does transfer of ownership of a copyright or of any exclusive rights under a copyright convey property rights in any material object.[57]

This rule is repeated in UCITA as a matter of state contract law. UCITA states that:

> If an agreement provides for conveyance of ownership of informational rights in a computer program, ownership passes at the time and place specified by the agreement but does not pass until the program is in existence and identified to the contract . . . . Transfer of a copy does not transfer ownership of informational rights.[58]

In effect, an authorized sale of a copy is best viewed as a form of license. In that license, the parties rely on first-sale or exhaustion doctrine to supply default terms about what the transferee receives as against the dominant intellectual property rights of the rights owner. If the transaction does not involve a sale, however, the uses granted and withheld are not affected by these default rules and, even when a copy is sold, it remains possible to alter them by contract. Under federal law, whether the person acquiring a copy becomes the owner of the copy depends on the terms of the contract and whether the contract places limitations on the person's use of the information that are materially inconsistent with the rights given under a first authorized sale.[59] The UCITA rule for licenses follows that federal law approach.

In practice, some licenses increase, while other licenses decrease the use privileges that go to the transferee if the comparison is to a

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57. 17 U.S.C. § 202 (1996).

58. UCITA § 501 (2000).

59. *See supra* text accompanying note 58. *See generally* DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999); MAI Sys. Corp. v. Peak Computer, Inc., 991 F.2d 511 (9th Cir. 1993); Adobe Syss. Inc. v. One Stop Micro, Inc., 84 F. Supp.2d 1086 (N.D. Cal. 2000).

first sale.[60] Illustrations of each effect are common even in the mass market. In general, however, the uses enabled by a first sale are not the appropriate comparative measure for determining whether licensing expands or contracts a licensee's rights. Rather, a license is simply one means by which the parties might agree to distribute and receive information or technology and rights to use it. Under copyright law, for example, if a copyright owner chooses to sell copies of its work without further conditions, the buyer at an authorized sale owns the copy and obtains the privileges defined by first-sale doctrine. But nothing in the law requires that the rights owner sell copies of its information, any more than the law requires the owner of a car to sell it. The copyright owner can offer its work in whatever framework it chooses. The success or failure of any offer depends on the market and the willingness of others to accept the proffered conditions.

The proper measure of the effect of a license on the licensee or the licensor begins with the premise that the rights owner controls the property rights defined by statute. The license, if any occurs, reflects the parties' bargain about the scope of the rights conveyed, the conditions on which they are given, and of course the price. Illustration 2 indicates a common context in which a license gives rights greater than a first sale in one respect, but less than a first sale in another respect.

Illustration 2. Distribution License

> ABC licenses Digital to distribute up to 100,000 copies of the copyrighted software so long as the distribution meets stated conditions, including that any end-user must agree to a license with the ABC (publisher) to use it and that the license restrict the purchaser to consumer use of the program in the computer sold by Digital. The Digital license requires ABC to deliver

60. *See* Green Book Int'l Corp. v. Inunity Corp., 2 F. Supp.2d 112 (D. Mass. 1998) (shrink-wrap increases rights); Frontline Test Equip., Inc. v. Greenleaf Software, Inc., 10 F. Supp.2d 583 (W.D. Va. 1998) (mass market license allowed unlimited copying, but prohibited commercial distribution).

one copy of the software and to license Digital to make and distribute 100,000 copies from that master copy.

Illustration 2 depicts a transaction that is common in software and other digital information industries.[61] In it, the copyright owner elects not to make, sell, or deliver copies for resale by the buyer, but to allow a distributor to make and distribute copies pursuant to a license. The publisher's property rights include the exclusive right to *make* and to *distribute* copies. Thus, the distribution license gives conditional (often non-exclusive) permission to the distributor to make and distribute copies despite the overriding property right it holds. Making or distributing copies outside the agreed contractual scope breaches the contract and infringes the copyright.[62]

The agreed terms in the license in Illustration 2 exceed any right to make copies that might arise from the "first sale" of a copy. Thus, the license goes beyond first-sale rights. On the other hand, the licensee's right to distribute copies is controlled by agreed conditions focused on the purposes of the distribution, the requirement that the transferee agree to further terms, the location in which the end user can use the program, and the purposes of such use. These limitations as to a particular copy arguably comprise lesser rights given to the transferee than the right of a first-sale buyer to distribute its copy as it chooses. Neither difference, however, is particularly germane to examining the market effect of licenses of this type.

The more relevant analysis centers on the fact that licensing enables tailored transactions and more efficient distribution. In this setting, the analysis centers on the options available to the parties. One way to understand the options would be to ask what would be the effect of a rule that precludes licensing and requires software to be distributed solely through a first sale of copies. The most obvious effect would be that a transaction involving delivery of one copy and a license to make additional copies would be foreclosed. Presumably, however, since the parties in the hypothetical (and in the real world)

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61. *See, e.g.*, *In re* DAK Indus., Inc., 66 F.3d 1091, 1094-97 (9th Cir. 1995) (discussing and applying the Microsoft master copy distribution license in a bankruptcy proceeding).

62. *See, e.g.*, Sun Microsystems, Inc. v. Microsoft Corp., 188 F.3d 1115 (9th Cir. 1999) (distinguishing between a covenant breach and a breach of scope provisions); Graham v. James, 144 F.3d 229 (2d Cir. 1998); *MAI Syss. Corp.*, 991 F.2d at 511.

opt for the single copy/license framework, their judgment was that this framework yields a net benefit to the transaction. The possible reasons why this might be so are apparent. The master-copy license eliminates costs associated with delivering and handling 100,000 copies, including the risk that some copies may be lost or damaged. It places the cost of copying on the licensee, but in many instances that will be a relatively minor increment (e.g., where the copies are simply installed in the licensee's hardware). Overall, there may be a net reduction in transaction-related costs with an overall benefit that is reflected in the agreed price. Whether that benefit exists in fact and produces an agreement to this form of distribution depends on many things, including from the licensee's perspective, whether this publisher's software is more desirable and offered on beneficial terms as compared to that of other licensors.

Modern cases routinely enforce a copyright owner's decision to license computer information, rather than merely sell copies, even when the information is delivered on a tangible medium.[63]

Under the license described above, a distributor that makes or distributes copies in a manner outside the terms of the license breaches the contract and infringes the copyright.[64] A distribution outside the conditions of the license is unauthorized. A transferee at an unauthorized sale or other transfer is not a buyer at a first sale, but rather possesses an infringing copy.[65] As a result, in this framework, the end user's right to make a copy of the software in its computer and otherwise to use the software depends on it being taken through an authorized distribution chain and, given the conditions imposed, on its having a valid license or other authorization from the copyright owner—the publisher.[66] The unauthorized transfer gives no rights against the copyright (or patent) owner.[67]

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63. *See, e.g.*, DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999); *MAI Sys. Corp. v. Peak Computer, Inc*., 991 F.2d at 511; Adobe Syss. Inc. v. One Stop Micro, Inc., 84 F. Supp.2d 1086 (N.D. Cal. 2000).

64. *See Adobe Syss.*, 84 F. Supp.2d at 1086.

65. *See* Microsoft Corp. v. Harmony Computers & Elecs., Inc., 846 F. Supp. 208 (E.D.N.Y. 1994); Microsoft Corp. v. Grey Computer, 910 F. Supp. 1077 (D. Md. 1995).

66. *Id.*

67. *See* Accusoft Corp. v. Mattel, Inc., 117 F. Supp.2d 99 (D. Mass. 2000) (holding no rights obtained by merged entity).

Ultimately, such cases reflect a principle mentioned earlier: a property right in informational assets gives the property owner, like any other property owner, a right to control the manner and form in which its property enters commercial markets. The copyright owner can allow transfers of its property in a "stand-alone" market or preclude that use or, much more likely, choose one means of distribution for uses in networked computers and a different means of distribution for stand-alone copies. One can trace the right to make market choices to the basic idea of property itself, which consists in part of the right to transfer or not transfer the property as one chooses. Indeed, in one recent case dealing with a different, but relevant issue, the court held that a company that made copyrighted recordings available to its subscribers engaged in indirect copyright infringement and not protected fair use.[68] In effect, according to the court, the defendant was usurping a market that copyright law reserved for the copyright owner.[69]

Embedded in this is a fundamental concept about the role of property rights in markets. The argument that the property owner should not complain because another party acts without permission strikes a hollow note in reference to most types of property law. A similar argument with reference to informational property should strike a similarly hollow chord. The existence of a property right implies the owner's right to choose whether to distribute it, and under what terms distribution is offered. The market determines whether the offered terms are viable and influences or ultimately controls the

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68. UMG Recordings, Inc. v. MP3.com, Inc., 92 F. Supp.2d 349 (S.D.N.Y. 2000).

69. Defendant argued that plaintiffs had not shown that such licensing was "traditional, reasonable, or likely to be developed." Moreover, defendant argued,

> its activities could only enhance plaintiffs' sales, since subscribers could not gain access to particular recordings made available by MP3.com unless they had already purchased . . . or agreed to purchase, their own CD copies of those recordings. Such arguments . . . are unpersuasive. Any allegedly positive impact of defendant's activities on plaintiffs' prior market in no way frees defendant to usurp a further market that directly derives from reproduction of the plaintiffs' copyrighted works. A copyright holder's "exclusive" rights, derived from the Constitution and the Copyright Act, include the right, within broad limits, to curb the development of such a derivative market by refusing to license a copyrighted work or by doing so only on terms the copyright owner finds acceptable.

Id. at 352.

owner's choice. The initial choice, for better or worse, resides in the property owner. Nothing indicates that courts are better able to make and administer such marketplace determinations.

In the Napster illustration mentioned earlier, if property rights owners determine, either because of market demand or because of desired financial gain, to support the peer-to-peer file-exchange system, they will implement that decision through licensing, rather than merely selling copies. One approach would be to license a service to operate such a system (indeed, one publisher made that agreement with Napster). Another would be to license directly (online one presumes) individuals to participate in peer-to-peer exchanges. The other alternative would be to offer to mass market purchasers of copies a license to distribute copies on a peer-to-peer system.

The court in *Napster* held that each individual copy owner that made its copy available on the system and each individual person that downloaded a copy infringed the copyright.[70] A license could authorize such use. A copyright owner will presumably make such licenses available if it believes that the net benefit to it of offering the licensed copies at a price the market will bear exceeds the net loss it suffers from authorizing the making of additional copies of its property, or if it believes that offering such licenses will reduce a net loss that would otherwise occur. Numerous empirical and judgment factors go into resolving that question, including a judgment about whether the market will pay the price demanded for a license to do something that cannot be done by the owner of a copy. The *Napster* case, however, stands for the proposition that, as a matter of law, the decision to offer that choice rests entirely in the copyright owner.

In a format in which the mass market marketing choice is a license the license will often involve either a so-called shrink-wrap contract, or a click-screen agreement under which the terms of the license and the request for assent to it are presented on the computer screen when the prospective licensee first uses the work. Both types

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70. *Id.* at 353. In the actual case, there were a limited number of publishers/performers that authorized this type of distribution or, at least, were not objecting to it. But that does not change the illustration which presumes an absence of such acquiescence.

of license are generally enforced under ordinary contract law.[71] Under UCITA, they are enforceable *only* if the licensee had reason to know that they would be presented and the licensee affirmatively assents to the license.[72]

Putting contract formation questions aside, what is at stake here? The end user does not ordinarily deal directly with the publisher. The publisher, however, controls the copyright. The function of the *publisher's* license is to establish the direct license between the publisher and the end user. An enforceable license validates the distribution and establishes the end user's rights to copy and otherwise act with respect to the digital information as allowed in the license. An unenforceable license leaves the end user in possession of an unauthorized distribution and no right to use the software.

The functions of an end user license then are different from that of a manufacturer's warranty in sales of goods. In the distribution of goods, the sale to the distributor and the subsequent resale give the eventual buyer all rights to use the particular goods; indeed, the buyer obtains complete ownership. In contrast, the end user license represents the only authorization by the property rights holder that allows the end user's intended use of the digital information. It is a direct, necessary contractual relationship, rather than a mere warranty commitment or disclaimer.

A license implements property rights permissions to end users (or other persons contractually acquiring a license) in return for a price that is either paid directly to the publisher or indirectly to an

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71. *See, e.g.*, ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996) (contract enforceable; limits use of database to consumer purposes only); Hill v. Gateway 2000, Inc., 105 F.3d 1147 (7th Cir. 1997) (holding contract requiring arbitration enforceable based on use of computer without objecting to contract terms); M.A. Mortenson Co., Inc. v. Timberline Software Corp., 970 P.2d 803, 808 (Wash. 2000) (holding license to be enforce when it followed purchase order: "Reasonable minds could not differ concerning a corporation's understanding that use of software is governed by licenses containing multiple terms"); Mgmt. Computer Controls, Inc. v. Charles Perry Const., Inc., 743 So.2d 627 (Fla. Dist. Ct. App. 1999) (holding that forum selection clause in shrink-wrap license enforced); Rinaldi v. Iomega Corp., 1999 WL 1442014 (Del. Super. Ct. 1999) (holding conspicuousness of disclaimer not affected by fact it was delivered in shrink-wrap format); Lieschke v. Realnetworks, Inc., 2000 WL 198424 (N.D. Ill. 2000) (The court did not dwell on enforceability, but assumed it. The license was displayed as a precondition to installing the software by the user who downloaded the software.).

72. UCITA § 208 (2000).

intermediary, such as the retail store at which a copy is acquired. The justification for licenses in the mass market or, indeed, elsewhere using such distribution chains, lies, in part, in the fact that they enable an efficient means of offering differentiated products to the mass market. The efficiencies lie, in part, in avoiding the need to individually negotiate each license with the potentially millions of individual licensee-purchasers who desire to acquire the licensed rights. Instead, the options can be presented at an appropriate price and participants in the market can choose to accept the terms or not. Both sides benefit by reduced acquisition or transfer costs and by the fact that parties can choose the product they desire based on price and usefulness to them.

For example, a publisher might offer two products distinguished by the terms of the license. Product 1 may be the latest musical recording hit contained on a digital copy sold without any license for $20.00. Product 2 may be the same record licensed with the right to engage in peer-to-peer exchange for $35.00. Which product succeeds in the market depends on whether (or how many) licensee-purchasers are willing to pay $15.00 for the additional right to engage in peer-to-peer exchanges. That decision might be affected by the scope of the additional rights offered. Regardless of the market result, however, both sides benefit from standardization of contract terms since, unless the publisher is expected to simply give up its property right, the alternative would involve negotiation costs that would be distributed in the form of additional prices. It might, for example, cost a company $5.00 to ascertain and acknowledge the consumer's choice by telephone or e-mail and this knowledge would elevate the costs of the two products to $25.00 and $40.00 respectively.[73]

This is an illustration of mass customization that defines one of the opportunities involved in modern computer-information markets and in which it can be said truly that the license defines the product in ways not present in other types of products. That a licensor might misjudge the market or that some people simply ignore the law and

73. It should be obvious that, while the numbers might change, this negotiation cost would continue to be present even if the publisher only required those who desire the additional rights to call (or mail) and request to pay for them or, in the alternative, only those who do not desire the rights to call (or mail) to request that they be deleted in return for a refund.

the contract cannot be said to detract from the positive effect that the transactional framework has in actual markets. Thus, in the example, a purchaser that does not desire the rights is not required to pay to subsidize others to acquire rights to participate in *Napster*-like distributions. The purchaser not wanting distribution rights can acquire the lesser-cost product.

Similarly, the purchaser-licensee is not required to subsidize the cost generated by those who desire to negotiate the license (sale or broader authorization); those costs are avoided by a low-cost, highly efficient means of offering the alternatives without person-to-person negotiation. A rule that requires that these costs be incurred raises the price of the product and, in some cases, will force prospective purchasers into a position of being unable to pay or simply unwilling to make the purchase. That result adversely affects any social interest in enhancing and encouraging the actual distribution of informational assets because it takes some people out of the purchaser market.

In this distribution method, some risk might exist that a purchaser-licensee inadvertently acquires the wrong package of rights, or might be tricked into doing so. Cases involving misled purchaser-licensees are readily solved under ordinary misrepresentation law and deceptive trade practices laws. In fact, there are no reported case law instances of such cases in software distribution.

The risk of mistake deals with the information available about the transaction. A prospective purchaser-licensee will make rational choices if it knows its options. Some purchaser-licensees may not be aware of their options or may inadvertently choose the wrong one. How often this mistake will occur has never been shown, nor has any showing been made about the costs that result. On the other hand, it is clear that this risk exists in all markets; there is an established body of law to deal with it. Thus, if a consumer acquires a toaster believing it to be a five slice machine, but in fact it is only four slices, the resolution of the problem depends on a variety of factors, including why the consumer had a mistaken belief and, in fact, whether the consumer had that belief.

One could argue that the risk of mistake means that license practice should be banned in order to avoid the costs of mistakes. To sustain that argument, however, the advocate should be required to show that the costs to the few who make mistakes are not offset by

the potentially large economic and personal choice benefits to the many who make unmistaken choices. One should also have to show that the loss to the federal property-rights owner (e.g., effectively telling it that the property right has been usurped) do not exceed the benefit of preventing mistakes by mandating that products cannot be differentiated based on how they might be used. Ultimately, the burden would be to show that on net, the social benefits of the practice do not exceed the social costs of mistake. That argument has never been made or effectively supported. Perhaps understanding this, courts consistently enforce such contracts.

UCITA addresses the information and mistake issue in several ways in the mass market. [74] In UCITA, the purchaser-licensee is guaranteed advance notice (reason to know) and the ability to rely on the express agreement (if any), an opportunity to actually review the terms before assenting, and a right to a refund of any payment made if the terms do not conform. In that regime, most if not all cases of actual mistake are readily resolved without disrupting what is a socially beneficial practice.

Online Access Contracts

With the advent of the Internet, massive amounts of information are provided through online access systems, many of which use a framework under which contractual permission, described as an "access contract," is required to enter and use the information resources.[75]

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74. UCITA §§ 112, 208, 209 (2000). It provides for rules including the following:

> The license terms cannot contradict the express agreement of the parties (e.g., they cannot take away what was actually promised).
>
> The license terms are not enforceable unless the licensee has reason to know that they would be presented (e.g., the licensee must be engaged in a transaction where it has reason to know that terms will control its use).
>
> The license terms are not enforceable unless the licensee has an opportunity to review them before assenting and, if it declines, a right to a refund of any amounts paid for the information.
>
> The license terms must be presented no later than the first use of the computer information.

Id.

75. The term, "access contract," comes from UCITA and is defined in the following

An access contract is a license that grants the licensee a right to access a computer or similar information-containing system. In an access license, the value offered does not depend on whether the information is protected by copyright or patent law. The value arises from a license: the access provider controls a system and its content and agrees to permit another person to use that system under stated conditions. The right to control unauthorized access to a computer is grounded in several areas of law and in simple technological or physical control; it does not depend on intellectual property.

Reported cases enforce online licenses when assent is properly obtained.[76] The case-law approach is consistent with standards set out in UCITA (e.g., there must be a clear manifestation of assent to the terms with reason to know assent is being inferred and occurring after having had an opportunity to review them).[77] If an opportunity to review the contract or if a manifestation of assent to it did not occur, the contract may be unenforceable.[78] If the contract is unenforceable, however, that leaves open whether the user's access to and use of the information was authorized or whether it constitutes trespass, infringement, or even a criminal act.[79]

Access licenses deal with numerous issues. Among the most important are those concerning when and under what conditions access is allowed and defining the permitted use of information obtained from the site. In effect, these contract terms define what product the system provider offers (e.g., "access for consumer use") and what value the licensee obtains. The information in the system

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manner: "'Access contract' means a contract to obtain by electronic means access to, or information from, an information processing system of another person, or the equivalent of such access." UCITA § 102(a)(1) (2000).

76. *See, e.g.*, Caspi v. Microsoft Network, L.L.C., 732 A.2d 528 (N.J. Super. Ct. App. Div. 1999); Hotmail Corp. v. Van$ Money Pie, Inc., 47 U.S.P.Q.2d 1020 (N.D. Cal. 1998) (enforceable); Rudder v. Microsoft Corp., 1999 Carswell Ont. 3195 (enforced); Jessup-Morgan v. Am. Online, Inc., 20 F. Supp.2d 1105 (E.D. Mich. 1998) (enforced); Groff v. Am. Online, Inc., 1998 WL 307001 (R.I. Super. 1998); DiLorenzo v. AOL, 2 ILR (Pike &Fisher) 596 (N.Y. S. Ct. 1999); CompuServe, Inc. v. Patterson, 89 F.3d 1257 (6th Cir. 1996); *In re* RealNetworks, Inc. Privacy Litig., No. 00 C 1366, 5 ILR (Pike & Fisher) 3049 (N.D. Ill. 2000).

77. *See* UCITA §§ 208, 112 (2000).

78. Ticketmaster Corp. v. Tickets.Com, Inc., 54 U.S.P.Q.2d 1344 (C.D. Cal. 2000).

79. Micro Star v. FormGen, Inc., 154 F.3d 1107 (9th Cir. 1998) (lower court enforced online license; appellate court held that either the license barred the conduct or there was no license to prevent claim of infringement).

may be copyrighted, but the primary value that frames the contract lies in the access provided on a conditional basis.

From their earliest emergence, access contracts were recognized as a new way of distributing information which presents market and other issues unique to their own circumstance. Thus, in 1996, the U.S. Office of Technology Assessment commented:

> [E]lectronic dissemination—unlike printing—does not involve the publication of copies. As a consequence, copyright ownership is transformed from the right to reproduce a copyrighted work in copies for sale to the right to control access to the copyrighted work for any reason. [When] copyright is applied to works that are electronically disseminated, the balance between the rights held by the proprietor and those retained by the public is changed.[80]

In these contracts, access, instead of or in addition to intellectual property rights, forms the value-base for making the contract (that is, what the licensor offers and what the licensee decides to acquire). Analogies to print publications and sales of printed copies provide little insight for this market context or for what, if any, legal restraints might be placed on providers of information in this format. This is a new method of distribution with its own market characteristics.

Consider the following illustrations:

Illustration 3. NYT Online

> NYT website offers articles and other information about current events at cost to the user. It requires a party entering the site to agree to terms before accessing the site by a click on an on-screen button. The user has access to the terms before agreeing. The agreement allows use only for non-commercial purposes, allows reading but not copying or distributing, and disclaims warranties of accuracy.

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80. OFFICE OF TECH. ASSESSMENT, INTELLECTUAL PROPERTY RIGHTS IN AN AGE OF ELECTRONICS AND INFORMATION 204-05 (1986).

Illustration 4. Consumers' Union Online

> Consumers' Union Web site allows open access to a *public* part of the site, but requires agreement to terms and conditions of use for a person to access the *reports* portion. Agreement is indicated by a click on-screen. One contract term precludes the user from using the reports for commercial advertising.

In both illustrations, the terms and conditions are licenses. The licenses enable creation of a diversified system that makes a strong positive contribution to the modern economy. By contractually regulating use, copying, and quality commitments, these contracts allow the providers to make available a new resource in the mass market. The consumer benefits are enormous. Contracting for access is a form of commerce that could not exist in paper-based media.

Online licensing or distribution systems often do not involve static databases and the industry involves many different formats.[81] Methods of delivery are constantly changing. The line between services and information products is no longer clear; it is blurring.[82] In the modern context, the decision to provide software or other computer information by online access, by delivery of tangible copies, or by a right to access remote functionality is a marketing decision driven by market factors. Systems that do not deliver tangible copies are increasingly used.

What are the contractual attributes of an access license? Express contract terms control. In the absence of express terms, there is little case law on what are the implied obligations of the parties. UCITA provides some guidance. Under UCITA, the vendors must provide access with a reliability consistent with similar contracts in the online

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81. In many cases, publishers of other computer information make information and functionality available online pursuant to licenses. Even more significant, one of the directions in which many believe that the software industry will move in the near future consists of making the functionality of software available primarily by remote access to online systems which can be accessed by low cost systems on the customer's end. Under this approach, the end user licensee will not receive a copy of the program, but a contract right of access to, and use of, the software. The software remains on a remote computer. Again, at least in part, the legal basis for such contracts rests in the provider's right to control access to its own information and systems and in the force and effect of contracts made in an open economy.

82. DAVIS & MEYER, *supra* note 1.

industry.[83] The obligation necessarily varies depending on the context: time sensitive, real-time data systems have higher obligations of accessibility and reliability than historical databases with no immediacy considerations involved.

UCITA also deals with what default rule applies for permitted uses of information obtained from the access. Section 611(3) states:[84] "Unless it is subject to a contractual use term, information obtained by the licensee is free of any use restriction other than a restriction resulting from the informational rights of another person or other law."[85] This premise uses intellectual property rights as the baseline in the absence of express contract terms. Thus, if the information is not copyrighted or otherwise subject to intellectual property rights, it may be freely used unless the agreed license places express contractual restrictions on use. If express contract terms are established, they govern unless they violate a fundamental public policy of the state.[86]

Some may see the issue as whether, in the absence of intellectual property rights in the accessed information, any contractual restriction should be permitted on use of the information once it is accessed. However, where adequate value sustains the creation of a contract, the obligations and limits undertaken by contract should be enforced unless public policy reasons exist to vitiate the premise that agreements are and should be enforceable. UCITA, for example, provides that a court may invalidate a contract term if that term conflicts with fundamental public policy that, in the context, outweighs the fundamental policy of enforcing contracts.[87] As this indicates, there may be a need to balance interests. Most often, however, contract limits on use serve important commercial interests and do not impinge on any conflicting fundamental public policies. These terms should be enforceable.

Should a consumer testing agency be allowed contractually to prevent its subscribers from using test results to comment publicly on

83. UCITA § 611 (2000).
84. UCITA § 611(a)(3).
85. *Id*.
86. UCITA § 105(b).
87. UCITA 105(b).

the evaluation of their own products or those of competitors? If the answer were grounded solely in copyright law, the governing rule might be that copyright law does not give exclusive rights in facts and, thus, does not support the restriction, but that it does not preclude such a restriction under other law or under contract.

One could argue that copyright law reflects an affirmative public policy that factual information (e.g., the results) cannot be protected from use and disclosure:[88] the negative rule under copyright law ("facts cannot be copyrighted") could be viewed as an affirmative public policy that use of facts cannot be restricted in any manner. This view has no case law support in reference to contractual relationships.[89]

The contrary theory is that the customer agreed to the contract as part of the value given to the licensor (or the restriction required by the licensor) to obtain the value of access to the information. This generally establishes an enforceable contract. The relevant issue is whether contract law enforces the particular term. Under UCITA, that question would be addressed in terms of whether a court should bar enforcement of the term because the term conflicts with fundamental public policy outweighing the fundamental public policy of enforcing valid contracts.

The proper answer, ultimately, is that a contract term does not ordinarily conflict with and is not overridden by any policy in copyright (property) law about property rights in published facts.[90] Copyright law establishes property rights enforceable against any and all other persons with respect to the subject matter. Even if copyright law embraces an affirmative policy that no property rights can exist in published facts, it preempts only state laws that provide property

88. It is doubtful that this bare statement would be made since it has long been recognized that a proper claim of trade secrecy can be established with respect to information, including information that would not be protected under copyright law (e.g., facts). In the online case, however, we are involved in a situation where the information is made available to members of the public who subscribe to the service. This situation might challenge the ability to make any assertion of the type of confidential relationship ordinarily required to create a valid trade secret claim.

89. *See, e.g.*, ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996) (no preemption of contract claim); Register v. Verio, Inc., 126 F. Supp.2d 238 (S.D. N.Y. 2000).

90. *See* ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996).

rights equivalent to copyright.[91]

But contracts are agreements and are not equivalent to property rights; they are enforceable only as between the contracting entities. Indeed, copyright law and all other forms of property presume that contracts will be made and enforced with respect to their subject matter and that these contracts will add to or subtract from property rights as between the parties to the agreement.

IV. MARKET EFFECTS AND CHOICE

The impact of licensing and of any associated property rights cannot be assessed without accounting for the market in which licensing and information rights function. In the marketplace, practices that offer significant efficiencies or other benefits should not be restricted without strong cause to do so. Licensing readily fits into that category of efficient transactional forms.[92]

One fact emerges when one examines contemporary distribution of information: the information economy entails a vibrant diversity which creates a richness in what and how information, technology, and services can be obtained by consumers and businesses. Licensing contracts contribute to diversity in a way that could not be accomplished without this transactional format. The context in which this occurs is complex. We can begin to understand aspects of it, however, through Figure 2, which reduces the complex context to a limited framework consisting of three tiers or levels of decision regarding whether to distribute the information, how to do so, and what transactional format to use.

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91. 17 U.S.C. § 301 (1994).

92. On the other hand, it must be made very clear that it is not true that a practice (or a property right) should be permitted in law only if it is proven to have positive impact in the market. Any such standard concedes too much to theory and regulation, without allowing the dynamics of the actual market to flourish. In effect, such a rule would place too much weight on our limited understanding of how markets and law interact. In a market economy, the fundamental means for distributing value lie in the actual market comprised of actual transactions and other interactions in which different approaches are tested and accepted or rejected by the market. Indeed, some of our most accepted methods of doing business while supported by law, cannot be shown clearly to have positive economic impact in theory. *See, e.g.*, Robert E. Scott, *The Truth About Secured Financing*, 82 CORNELL L. REV. 1437 (1997) (economic benefit not proven); Steven L. Schwartz, *The Easy Case for the Priority of Secured Claims in Bankruptcy*, 47 DUKE L.J. 425 (1997).

Figure 2

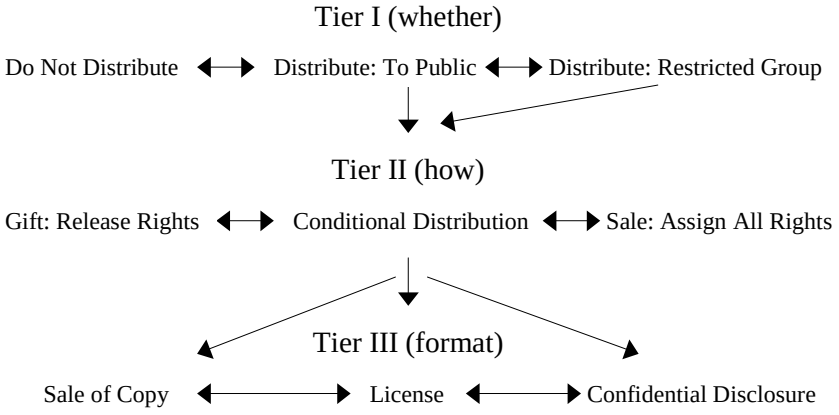

Figure 2 depicts choices from the perspective of the licensor (transferor). It is thus incomplete. It may imply that the licensor's unilateral choices control, but that is not the case. In many of the options in Figure 2, effectuating the licensor's choice in distributing the information requires a contractual interaction with other persons (transferees) in a given marketplace. If potential transferees do not value or desire the distribution method and cost chosen by the transferor, no transactions occur unless the transferor alters its choices. Markets are not one-way streets, but are defined by exchanges.

Decision Whether to Distribute

A person who controls information may elect not to distribute the information, but to hold the information entirely to itself (Tier 1 in Figure 2). Unless mandatory disclosure laws govern, the law protects that decision. Indeed, tort and criminal laws protect the information owner against unauthorized intrusions inconsistent with its decision about whether to distribute and how to distribute its informational asset. The right to refuse to distribute (license or sell) is recognized

even as a defense to various forms of antitrust liability.[93] It is a byproduct of the property right itself.

A decision not to distribute information places the person outside the market and tends to exclude the information from that marketplace and from the public. This choice is the option against which other market choices, including licensing, must be compared. One policy of copyright and patent law is to encourage creation and dissemination of information. In Figure 2, achieving that objective can be seen as a matter of how law affects when a person will choose to distribute, rather than to hold the information itself.[94]

An individual or company will distribute its information if, accounting for costs, the person believes distributing the information will yield greater value than not distributing it. Value and costs need not refer to monetary gain or loss. Many writers freely distribute on the Internet because they obtain personal value and satisfaction from peer reactions without receiving any monetary compensation. Just as often, people write secret diaries and artists conceal their art for fear of public rejection and to preserve their own satisfaction with it.

Law plays a role, but that role is limited because of the many personal and contextual variables involved. For example, law cannot control some issues such as whether anyone desires to hear about or to purchase the information the owner desires to distribute. That being said, law might contribute to encouraging or discouraging a decision to distribute the information as compared to holding it secret

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93. *See, e.g.*, *In re* Indep. Serv. Orgs. Antitrust Litig., 203 F.3d 1322 (Fed. Cir. 2000); Image Technical Servs., Inc. v. Eastman Kodak Co., 125 F.3d 1195 (9th Cir. 1997).

94. It should be obvious that the structure discussed here also pertains to decisions about "creating" information assets at the outset. Thus, arguably, a person will be less likely to undertake the task of writing a book if at the end of the day there will be no ability to control distribution of the work or to obtain financial benefits from the distribution. Similarly, expensive motion picture projects will be less likely to occur if the developer of the work knows that the completed motion picture can be freely appropriated by anyone who chooses to do so. On the other hand, of course, the book or movie, once created, may serve as a basis for work by subsequent persons, thus establishing the peculiar circle that arises in reference to all forms of property law: creating protected rights benefits the current rights owner, but creating too strong of rights may impinge on the creation of subsequent value by other parties. *See* Wendy Gordon, *On Owning Information: Intellectual Property and the Restitutionary Impulse*, 78 VA. L. REV. 149 (1992); Edmund Kitch, *The Law and Economics of Rights in Valuable Information*, 13 J. LEG. STUD. 683 (1980). In this Article, we have dealt with transactions, rather than property law, and I will leave that issue for another time.

and close to the licensor's vest.

In general, law encourages distribution if it reduces costs to the information holder and increases the owner's perceived likelihood of return value if it elects to distribute. In both respects, of course, as a matter of policy, one must draw various balances in allocating risk, reward, and opportunity for future use. There is a core philosophical question here: should choice be dictated by statute or regulation, or should law enable the market to define this balance, subject only to exclusions against grossly abusive practices. Ordinarily, in a transactional (market) environment, statutes, regulation, and judicial enforcement of limitations are less effective than market choices. The ultimate decisions are best left for the marketplace. This is especially true in a situation where information about products (information products or products of other types) is rapidly and broadly available, as is true in the Internet era.

Liability risk

Law encourages an information-holder's decision to distribute information by reducing liability risk for the information provider or, by allowing the information provider by agreement to control or exclude the liability risk. In contrast, to the extent that law creates a liability risk not controllable by agreement, it creates incentives not to distribute the information. Obviously, in some cases, the policy balance may accept such disincentives as a price to be paid for achieving other social goals, but that should be true only if the goals and the likelihood of their achievement is are clear and outweigh the goal of encouraging distribution.

In sales of goods law, numerous cases and statutes examine the balance between manufacturers, distributors, and customers on issues of liability. The net result is that one group of rules exists for liability for mass market goods, and a different risk allocation framework is permitted for goods distributed other than in the mass market. The liability rules arise under contract and tort law, including products liability law. They generally require the mass market distributor of consumer goods to assume risk of causing personal injuries by a defect in its product when it places goods into the stream of commerce, but do not require that the manufacturer assume the

unavoidable cost of compensating a transferee for economic losses resulting from defects in such goods.[95] Allocation of risk for economic losses can be governed by contract terms.

For information, different rules are appropriate and followed in case law. In general, the policy rationale for placing liability on an information provider is less than that for a manufacturer of goods. On the other hand, in public distributions of information policy limiting liability that would otherwise discourage distribution of information is supported by more substantial public policies associated with encouraging free speech.[96] This balance differs from that in reference to mass market goods and shapes current law. For example, the Restatement (Third) of Products Liability holds that information is not a *product* under product liability law and, thus, not subject to the nondisclaimable, strict liability rules of that area of tort law even for cases where defective information causes personal injury.[97]

Dealing with contract law UCITA sets three different implied warranty obligations in reference to digital information transactions. In each case, UCITA permits an agreed disclaimer or limitation of the implied obligation. The three obligations are: (1) a rule of no implied warranty liability for informational content distributed to the general public; (2) an implied obligation of reasonable care for accuracy of informational content distributed to a client in a special relationship of reliance; and (3) an implied warranty of merchantability for computer programs.[98]

UCITA enacts the idea that the implied quality commitment for the functional aspects of computer programs should be measured under standards ordinarily associated with transactions in goods. Precedent links the character of the software provider's implied obligations to a court's determination of whether the contract is predominantly for goods, services, or information. UCITA holds that functional products are subject to an obligation of merchantability which, as is the case under U.C.C. Article 2, can be modified by the

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95. *See, e.g.*, E. River S.S. Corp. v. Transamerica Delavel, Inc., 476 U.S. 858 (1986); Moorman Mfg. Co. v. Nat'l Tank Co., 435 N.E.2d 443 (Ill. 1982).

96. *See, e.g.*, Winter v. G.P. Putnam's Sons, 938 F.2d 1033 (9th Cir. 1991).

97. RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 19 (1998).

98. *See id.*; UCITA §§ 403, 404 (2000).

parties' agreement.

The other aspects of the UCITA implied warranty structure are important. They distinguish between published informational content and informational content provided in a special relationship of reliance. As indicated in Figure 2, a decision to distribute information is not an all-or-nothing event. The information holder can distribute information broadly (publish it) or narrowly (limited groups). Liability for generally published content is narrow or non-existent unless expressly undertaken by the agreement of the parties. The rationale for this stems from First Amendment concerns and the goal of encouraging broader, rather than narrow distribution.

Beyond implied warranty (or default) rules, cost allocation involves the ability of the parties to control cost (liability risk) by their agreement. Laws that support an agreement on risk allocation encourage distribution. For sales of consumer goods, modern law holds that placing dangerously defective goods into commerce exposes the manufacturer to liability for any personal injury regardless of contract terms; in contrast, law generally does not create an unavoidable exposure for economic loss.[99] The focus on personal injury and the creation of liability without a right to control the risk by contract represent a tailored response to public policies associated with distribution of mass-produced consumer goods.

Flexibility

Law should encourage decisions to distribute information. This occurs to the extent that it supports choices and flexibility in how an information owner can distribute information. Law discourages decisions to distribute information to the extent that it confines or narrows the choices available.

Transactional flexibility gives the information owner a greater ability to tailor its distribution to fit its goals and its own assessment of how to obtain optimal value. Of course, such individual decisions may not create for the actor the results it desires. To limit choice because a person may make a mistake makes little sense practically,

99. *See, e.g.*, All-Tech Telecom, Inc. v. Amway Corp., 174 F.3d 862 (7th Cir. 1999); Fireman's Fund Ins. Co. v. SEC Donahue, Inc., 679 N.E.2d 1197 (1997).

conceptually, or philosophically. It suggests paternalism and control not acceptable in an open society.

A decision to distribute information requires a prediction about future events. The decision will not always be correct. We talk here about personal choices, not abstract, perfect decisions. An individual or company making choices on how to distribute information may make an incorrect choice, misjudging the market, the personal or the legal and practical effect of its choice. Yet, the possibility of error is not relevant. Errors do not detract from the general premise: supporting the ability to make choices based on the owner's knowledge and discretion enhances the likelihood it will choose to distribute. Personal choices by market participants are more likely to positively influence behavior than are *a priori* judgments of regulators with no direct market involvement or after the fact judgments of courts.

Simply put, legal support for personal choices about how to distribute information will encourage the distribution of information. On the other hand, it could be argued that giving information holders the right to choose allows them to arbitrarily impose conditions inconsistent with intellectual property law. That argument incorporates a fallacy about both property and contract law. The fallacy assumes that the information holder's choice is unfettered unless constrained in law. The reality is different. Choices are cabined in by the market and the responses that potential transferees make. The reality is easy to portray if an author or publisher "chooses" to sell copies of a digital book, only if the buyer pays $10,000 per copy and agrees to not re-transfer the copy, no mass market will exist for that product if the ordinary market for digital books involves a much better alternative, i.e., purchases for $11.00 with a right to re-distribute the copy. Decisions or choices in a market are never unilateral if the party making the choice desires to contractually benefit from its decision.

Contract terms can be imposed unilaterally only if the terms are acceptable to a sufficient number of purchasers. Terms must be considered in light of the value they expect or if no reasonable alternatives exist for a necessary product, including the alternative of foregoing it. A rational information holder faced with market rejection of its offer to distribute its work will either withdraw the

work or alter the terms for distribution.

Licenses enable an array of opportunities to tailor distribution in a manner that, when tested in the market, gives a flexibility beneficial to both the transferor and the market of transferees. There are contract terms or practices that should not be permitted in a market context. These, however, are largely defined in antitrust law.

Method of Distribution

If a person decides to distribute her information assets, she may license it, sell (assign) all her rights for a price or may give the information away.[100] The availability of licensing does not mandate either choice. The choices are governed by personal values, costs, and judgments about contextual opportunities. For example, an academic that conducts research on a topic may personally decide that publishing the results in an academic journal is the most personally valuable use for it. Alternatively, an academic may decide to sell the data to a third party. The person who desires the personal benefits of free public dissemination is not likely to feel influenced by the fact that, were it to so choose, it could license its results for a fee.

Between the extremes of giving away or selling the information, there are various options that release some rights. These options rely on contract terms to define what is given and what is withheld or what use limitations are imposed. A decision to make a conditional distribution can be implemented under various transaction frameworks–e.g., sale of a copy, license, confidential disclosure to a few people.[101] Of these alternatives, the benefit of licensing is best seen in the fact that it allows a distributor to tailor the distribution according to the market. For example, licensing permits a price that is supported by the market according to the person's perceptions.

One illustration of the interaction between contract terms and market choices involves the "free-software" or "open-source" movement. Here, the premise of this near-religious movement is that software made freely (1) available without use restrictions, (2) with

100. *See supra* Figure 2, Tier II.
101. *See supra* Figure 2, Tier III.

access to the source information, and (3) allowing modification of the software contributes to the social good in a way that software distributed with proprietary use restrictions cannot. Yet, in the most common form of this type of distribution, the distribution method entails the assertion of strong copyrights and a licensing system. As the preamble to one prominent "free-software" licenses states:

> To protect your rights, we need to make restrictions that forbid anyone to deny you these rights or to ask you to surrender the rights. These restrictions translate to certain responsibilities for you if you distribute copies of the software, or if you modify it . . . . We protect your rights with two steps: (1) copyright the software, and (2) offer you this license which gives you legal permission to copy, distribute and/or modify the software. Also, for each author's protection and ours, we want to make certain that everyone understands that there is no warranty for this free software. If the software is modified by someone else and passed on, we want its recipients to know that what they have is not the original, so that any problems introduced by others will not reflect on the original authors' reputations.[102]

The license to which this quote refers limits copying and distribution of the software in a way that implements free software concepts. The user can use the software but cannot require payment for further licenses of the product or claim proprietary restrictions on the transferee other than the open-source terms. It cannot however, distribute the software or derivatives of it other than under a license that gives the licensee a right to modify, use, and distribute the software without use restrictions other than those placed on the first licensee.

As this use of licensing indicates, the transactional option of a conditional transfer of rights to use information permits a wide variety of transactional frameworks suited to different transactional objectives. As a practical matter, however, an information owner offers information as a product defined by a license, but the license success is based on the response of the market. Sustainable

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102. GNU *General Public License*, ¶ 1 (2001), *at* http://gnu.org/copyleft/gpl.html#SEC2.

distinctions in products depend on whether they attract positive market response. A producer may desire to distribute its information under a license requiring a fee for each use of the product, but that desire goes for naught if the market rejects it. In essence, the producer might offer value of a particular type for a given price, but if the market regards the cost or terms as excessive or less desirable than alternative products, the product fails.

Information assets placed into a market are subject to market restraints just like any other asset. While a copyrighted or patented work might be unique unto itself, in the market it competes with potential substitute information products.[103] It is true, of course, that a work governed by a copyright or a technology covered by a patent cannot be duplicated without permission of its owner, but that falls far short of proving that licensing and other distributive choices are not affected by the market. For example, the impact of a copyright owner's choice to sell copies of a history book about Abe Lincoln for $100 per copy is affected by the existence of another book on Abe Lincoln offered for $10. All other things being equal (e.g., author reputation, quality of writing and research, availability of copies), the market should favor the $10 book. The fact that the $100 book is copyrighted does not matter. Other things being equal, a database of animal images priced at $1 per access will succeed if competing against a similar database priced at $100 per access. Whether market success is affected by the fact that one license allows only non-commercial use, while the other allows multiple copies also depends on the market demand. Similarly, a patent on a specific technology does not prevent, but may in fact induce, development of technology that works around or circumvents the patented technology. The likelihood that this result will occur hinges in part on how or whether the patent owner makes its technology available by license.

There is more here in reference to computer information assets than other assets. In computer information transactions, the capability to tailor products by contract or technology to fit given markets is amplified because the tailoring does not require physical modification of the asset. An automobile, once built, can be significantly modified

103. *See* ANDEWELT, *supra note* 48. *See generally* NIMMER, *supra* note 8, at ¶ 7.05.

only with skilled effort and physical changes in the asset. A digital database, on the other hand, carries within it the capability to alter its utility to react to a different market demand. While some distinctions lie in the information itself (e.g., a horror movie as compared to a love story), even for identical information, differentiation occurs through license terms,[104] technology controls,[105] and the ability to deliver similar information in different ways. These distinctions, when made, are market-based choices. Some succeed, while some fail, but the process of differentiation is what is important.

Myth of First Sale, Reality of License

Licensing yields a richly textured environment in which market options abound. The diversity is created in part by contractual terms that differentiate among transactions in the same or similar information.

One trap embraced by those who resist the idea of licensing is that they adversely contrast this diverse environment against a fantasy world in which information and technology is distributed solely by selling copies or machines with resulting statutory or common law first-sale rights going to the buyer. There are two myths at work here. First, the one myth is that sales are the mandatory method by which most information is transferred. Second, the other myth is that a sale leaves information unencumbered while licenses inherently limit rights.

Market Choice and First Sale

As to the first myth, few authors, motion picture producers, libraries, or software developers should believe it. Many mass market publishers today *sell* copies not because the law mandates they do so,

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104. *See, e.g.*, DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999); ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996); Frontline Test Equip. Inc. v. Greenleaf Software, Inc., 10 F. Supp.2d 583 (W.D. Va. 1998).

105. Technological controls shape the scope and nature of uses of, or access to, copyrighted and other types of information products. This control was recognized in the Digital Millenium Copyright Act with the exception of some uses that qualify as fair use under applicable copyright law. *See* 17 U.S.C. § 1201 (1998).

but because the world of print and analog information believes that this way is the optimal way to distribute in the mass market.

As indicated in Figure 2, the fact that some owners distribute by selling copies is due to market choices, not legal mandate. No laws bar Blockbuster Video or the local library from renting copies of works as long as rental does not violate the property owner's copyright.

The myth that the sole way in which information was made available in the 1960s and 1970s was through so-called "first sales" of copies in the mass market is wrong. Even before the digital information revolution and the advent of the Internet, various distribution systems existed. In addition to much information made available for free (e.g., given away), these included:

- Television and radio broadcasts done under license from the rights owner;
- Cable television subscription contracts that allow selective access to shows;
- Motion picture theater performances based on licenses and ticket purchases;
- Library procedures allowing check-out and loan of a copy;
- Video store rentals of motion picture cassettes and other works;
- Background music provided in public locations under license

Information distribution in this country has always been diverse. With the advent of digital systems and the Internet, that diversity mushroomed.

First Sale: A Sterile Transaction

The second myth is that a sale of a copy gives less encumbered rights than a license. In fact, the first-sale doctrine is a legislative statement of limited privileges that a buyer receives *if* the rights owner authorizes sales of copies of its work and does not seek other

agreed contractual conditions for the transfer. It is effectively a license (a conditional grant of limited rights) created by statute and characterized by default terms. These default terms can be altered by the parties to the transaction by using a different type of transaction. The doctrine does not apply where the rights owner restricts the terms of a transfer of a copy or a patented machine, and this restriction can occur in a manner inconsistent with the idea that it authorized a simple sale.[106] But more importantly, a sale of a copy is a sterile, limited transaction which cannot accommodate the numerous ways in which productive markets beneficial to consumers and businesses might be established.

Some academic literature creates an aura around a first sale. They imply that the first-sale doctrine is associated with the First Amendment while licensing circumvents the First Amendment. Even those who articulate this argument must understand the fallacy of their position. First Amendment concepts affect both sales and licenses because First Amendment concepts create background law for the information economy. To the extent that it applies, the First Amendment prevents any improper use of governmental controls to restrict or regulate speech. In cases of abuse, First Amendment concepts directly restrict some contract terms or, at least, indirectly define policy restrictions on contracts.[107] These are not first-sale issues and they are not cut-off by licenses. The First Amendment is fundamental U.S. law, not an encapsulation of first-sale concepts. The first-sale concept only provides that a buyer can distribute a copy (or do other designated acts) without infringing the copyright. Whether a contractual term in a particular contract is invalid under

106. *See*, *e.g.*, DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999); Mallinckrodt, Inc. v. Medipart, Inc., 976 F.2d 700 (Fed. Cir. 1992). The latter case dealt with application in patent law of a doctrine similar to the first-sale doctrine in copyright law. In patent law, the concept refers to "exhaustion" of the patent rights by an authorized first sale. But the conceptual premise and the court's approach in each case is consistent. By authorizing only a restricted or limited transfer of rights, the copyright or patent owner and the transferee are not governed by first-sale concepts as a matter of property rights law.

107. For a discussion of this, see UCITA § 105(b) official cmt. UCITA is the first uniform law that expressly recognizes the right of a court to invalidate a contract term if the court finds that the terms offends fundamental public policy and that this policy clearly outweighs the policy of enforcing contracts.

the First Amendment or related public policy has nothing to do with first-sale.

First-sale doctrine and its parallel in patent law (patent exhaustion law) are sterile concepts in that they engage only a narrow, defined set of privileges for the buyer. They involve *conditional* transactions, but without the potential for rich diversity that licenses offer. They do *not* give the transferee–buyer full rights in the information as compared to a license. Indeed a first-sale is, in itself, a form of license under which the transferee-buyer receives limited privileges in the copy while the copyright or patent owner retains most rights. This statutory distribution of privileges occurs if the rights owner elects to sell a copy and not to seek agreed restrictions on use of the information contained in that copy or to offer agreed expansions of the rights that come from a sale. First-sale is in fact a narrow and limited doctrine.

To understand this, consider what an authorized first sale does not give to the buyer. First, an authorized first sale does not transfer the copyright or patent. The copyright or patent owner retains most of the rights in its information. Second, an authorized first-sale does not give the buyer the right to modify or make multiple copies of the work. Third, an authorized first sale does not give the buyer the right to publicly perform the work.

The sale of a copy of a book merely gives the buyer of a book the ability to transfer *that book* to another person. A similar doctrine gives the *owner* of a copy of a computer program the privilege to make a copy or an adaptation essential to its own use, to make an archival copy and to transfer its copies to another person, as long as it does not also retain a copy, without being charged with infringement.[108]

While there are more public policy issues here, they have little to do with the first-sale doctrine. Instead, they deal with the social policies surrounding for transfers of information in the mass market.

In the print and analog recording industries, the sale of a copy to a mass market buyer carried with it no further contractual terms regarding use of the information. That sterile transfer was never

108. 17 U.S.C. § 117 (1994).

mandated by statute. It arose simply because of ordinary business decisions. In effect, in transactions where parties do not make other agreements about use, first-sale doctrine provides a statutory, standard-form license. Because its terms are narrow, however, both transferees and transferors (licensees and licensors) often modify the terms of distribution.

A transaction that merely sells a copy of information leaves the buyer with limited rights. The buyer does not have the right to make or distribute copies, publicly perform the work or, in the case of computer programs, to rent the work. In many cases, however, transferees prefer different rights, either greater or lesser, for commensurate payment. That is true in commercial markets and mass market transactions. The function of a license in either context is to establish that different allocation of rights and privileges to suit the market. There are many reasons for a consumer to seek *different rights* than those under a first-sale if those *different* rights are offered under a license.

A sale of a copy is one way to distribute digital information. However, an unrestricted sale stands in stark contrast to the various contractual arrangements which might benefit both publishers and end users. In commercial markets, differentiation by contract has long been recognized as an appropriate procedure. In the debates over UCITA some large companies sought to preclude that option and require a transaction that in all cases presumptively exceeds the rights given by a first sale by allowing an unlimited number of simultaneous users of a copy. That argument, even if not preempted by federal law, would require property rights owners to increase the cost of ordinary licenses.

For example, assume that the price at which software is offered by its publisher is gauged by +100 based on a reasonable assessment of the market and cost for each use term indicated below. Also assume that a consumer values the software based on the value to it of rights important to it and that the prices of the publisher correspond to the consumer's valuation. The various rights or limitations that might be given in a transaction include:

1. Use only for consumer purposes;
2. Use only for business purposes;

3. Make up to five copies for simultaneous use;
4. Make more than five copies for simultaneous use;
5. Transfer the original copy without retaining a copy of it;
6. Distribute copies made from the original;
7. Publicly display or perform the work.
8. Right to make a back-up copy.

In this context, an unrestricted sale of a copy requires a +400 price (use for consumer purposes, use for business purposes, right to transfer the copyright to a back-up). Other combinations that might be achieved by a license yield different prices. The price of obtaining the software with all of the above-indicated rights is +800.

Consumers are *harmed* by a rule that requires sales of copies. For a consumer, the ability to use the software for business purposes has no value so paying for that right is paying for a useless right. But under a first sale, such payment is required if we presume that there are no restrictions on the use of the work. In most cases, a buyer does not obtain value from a right to transfer its copy of digital information if he cannot also retain a copy. A rule that requires copies to be sold without restriction pursuant to a first sale forces the consumer to pay for +400. A license giving the buyer the right to use a work for consumer purposes would only cost +100. If a buyer does not desire the business use or transfer right, he must pay an additional +200 for rights he does not desire.

Would requiring a sale of a copy benefit a business transferee? In most cases, the business purchaser is also disadvantaged. The business purchaser must pay for consumer uses (which he does not desire). Also, since a sale does not give him a right to make multiple copies, the business user must make numerous additional purchases to obtain sufficient copies to allow multiple simultaneous users. In contrast, a license for multiple users based on a delivery of a single copy eliminates the costs involved in multiple purchases.

Licenses provide a transactional framework that can be tailored to suit the individual needs of the parties and allow for pricing that reflects those needs. Thus, for example, in the foregoing illustration, the cost of a right to make a consumer use is not likely to be the same

as the appropriate market price for a license to make a business use or to make and allow use of multiple copies. Indeed, this fact makes the benefit of licenses even more pronounced for consumers. A software publisher that seeks a consumer market might reasonably price licenses to fit that market (e.g., to permit consumer use only). This market would give consumers access to the information at a cost far lower than if the publisher would be required to average out prices for consumer and business uses in each transaction that it conducts.

There are a much larger number of possibilities, but the point remains the same. Licensing gives computer information markets the opportunity to arrive at suitable prices and terms that may optimize distribution to all participants and value to the publisher.

In large part, the debate over licensing in the mass market centers on two complaints. First, licenses (as compared to sterile sales) will be used to stifle rights to comment about, examine, and exercise free speech rights with respect to information distributed in the mass market. Second, licensing, rather than selling, has no economic justification, but represents an attempt by publishers to control and exact financial gains from their market.

Both views are demonstrably wrong. License agreements are the manner in which a different permitted range of uses can be efficiently established. We have already discussed an illustration of this situation. There are many other illustrations.

Illustration 4. Consumer Product

> Publisher creates a digital work that appeals to consumers and to commercial entities. Rather than distributing the work online via an access license, publisher distributes it in copies in a retail market. The work contained in each copy is identical. Some copies however, are subject to a license that restricts use to "consumer purposes," while others are subject to a license that permits commercial use. The consumer licenses are made available for $10 each, while the commercial licenses cost $10,000.[109]

109. One might express concern about consumer fraud (paying $10,000 for a work that is

As the Seventh Circuit Court of Appeals emphasized in *Pro-CD, Inc. v. Zeidenberg*,[110] being able to make such price and product differentiations creates benefits for consumers. A consumer can obtain an attractive information product for a fraction of the cost he would otherwise be required to pay. A first sale would not permit contractual differentiation based on use. Only a single price could be charged because all products would have the same use conditions. As a result, consumers would pay a substantially higher price. The license here efficiently establishes a basis to differentiate prices based on type of intended use.

Of course, the publisher could offer a different product. It could strip out the "commercial" features of the product and offer to consumers at a low price a minimal version with functions limited to those perceived as useful to consumers, i.e., limited functions that justify the low price. That would create a market differentiated by the actual functionality of the software, bringing into play all of the inefficiencies associated with similar differentiation in sales of goods. It would also yield fewer software features for consumers, a result that most consumers do not want.[111] The license differentiation allows publishers to offer feature-rich products to consumers, discerning between customers and basing prices on contractual use restrictions.

Consider Another Illustration

Illustration 5. Database Software

Publisher develops database processing software. It distributes the software (1) by allowing it to be accessed and downloaded

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subject to a consumer-use-only license). That risk is like any risk of fraud in the modern marketplace and is met by various statutes, regulations, and common law rules giving remedies for fraud. Also, when UCITA is adopted nationally, it will provide a direct response to this problem. Under UCITA § 209, the terms of a mass market license cannot alter the terms expressly agreed to between the parties. An agreement to provide a commercial use license is not overridden by a consumer use license. *See* UCITA § 209 (2000).

110. 86 F.3d 1447 (7th Cir. 1996).

111. Ben Z. Gottersman, *Software*, PC MAG., July 2000, at 201. ("PC Magazine readers don't like watered-down software. In our survey, respondents tend to prefer more advanced tools to simpler and less feature-rich alternatives.").

> from Publisher's Web site, or (2) through distributors who distribute the software in copies. In both contexts, some distributions are licensed for "educational uses only," while others permit "commercial or any other use." The license fee for educational use is $1,000, while the general (commercial) use license fee is $75,000. The software is identical.

Again, differentiation based on the terms of the license enables a price and product differentiation that permits the publisher to respond separately to two active markets and therefore allows end users to acquire software capability tailored to their needs. In fact, major online databases have made this distinction for years, with huge savings to educational users. On the other hand, a simple first sale would alter both the marketplace and the price of the software.

The ability to enforce the use restriction comes from both contract law and intellectual property law. As the court in *Adobe Systems, Inc. v. One Stop Micro, Inc.*,[112] observed, if a person acquires software under an education use restriction but violates that restriction in making or distributing copies of the software, copyright infringement occurs.

The foregoing illustration involves licenses that restrict the end user's rights in a manner that prevents uses that would be permitted in an unconditional first sale. One cannot reasonably argue that these restrictions harm the market for computer information products. They contribute to establishing a vibrant and diverse market in information. They take an otherwise sterile environment and provide a diversity of value and functionality tailored to particular consumer or business markets.

Yet, many mass market licenses give greater rights than would pass to the buyer at a first sale. Licenses define the product. Depending on the market being targeted by the publisher, those product definitions may and often do exceed the authority given to a buyer at a first sale. To review this side of licensing, consider the following:

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112. 84 F. Supp.2d 1086 (N.D. Cal. 2000) (distribution agreement was a license rather than a sale conveying ownership).

Illustration 7. Clip-art Software

> Publisher distributes a "clip art" product for use in connection with various popular programs that enable users to make and display slide presentations for use in speeches. Copies of the clip art are made available through mass-market outlets, online, or at retail stores. The clip art license provides that the end-user may 1) make copies of the art in slide presentations, 2) publicly display copies of the art in connection with speeches and other presentations, and 3) make and distribute paper copies of slides containing the clip art so long as those copies are not sold for a fee separate from any speaking or similar fee the user receives.

In this scenario, the license contractually removes limitations that copyright law would otherwise place on a person who buys a copy of the clip art. *The licensee receives greater rights than a buyer*. The buyer at a first sale does not have the right to make and distribute copies. Had a buyer done such things and litigation ensued, they might have been treated as fair uses that did not infringe the copyright anyway, but the license makes clear the enhanced rights of the licensee. In this case, unless the licensed rights could be granted, the product would have no value. In effect, the license creates a new product and, in practice, created a new field of commerce.

Illustration 8. Document preparation software

> Publisher develops software that allows users to create and send electronic documents. The documents are created using the "Create" program provided with the software. To be viewed by the recipient, the recipient must have access to a "Viewer" program, a copy of which is included in the product. The publisher distributes the software in copies in the mass-market. The license gives the end-user the right to make and distribute an unlimited number of copies of the Viewer program to be distributed to any person he chooses.

Once again, the license authorizes making and distributing copies (of the Viewer program) in a manner that would not be permitted under a simple first sale. *The licensee receives greater rights than a*

buyer. The court in *Green Book Int'l Corp. v. InUnity Corp.*[113] said, that without the shrink-wrap license and the distributed Viewer programs, the product would be worthless.[114] Yet, a first sale gives the buyer neither the right to make, nor the right to distribute, unlimited numbers of copies of the work. That right arose solely through the contract.

Illustration 9. Free Shareware

> Publisher develops a program (a type of software sometimes described as shareware) which it makes available free of charge to the mass market. It distributes the software by online access to the program at Publisher's Web site. There is a license which disclaims warranties but also provides: "Copy this game! . . . Remember—copies must be unaltered and complete . . . Don't charge for copies or try to make a profit from TaskMaker or its distribution . . . Commercial distribution prohibited, as is distribution in exchange for compensation or any other consideration."

Without a license, a person who downloads a copy of the game would not have a right to make additional copies and distribute them. It would be possible, perhaps, for a court to find an implied license, but some courts would not do so and the license here makes clear both the breadth and the limitations of the right to make copies. Under such circumstances, the court in *Storm Impact, Inc. v. Software of the Month Club*[115] held that it was not a fair use to make copies and distribute them for a fee, but it would have been an authorized (licensed) use for that same person to make and distribute copies for free if the license created an effective contract.

The information market entails a mass customization that exists in no other context. Mass customization occurs because a digital information provider can create and publish (either online or in copies) a single work, but customize it in ways that fit narrow or individual markets or market niches *without changing the work itself*.

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113. 2 F. Supp.2d 112 (D. Mass. 1998).
114. *Id.* at 116.
115. 13 F. Supp.2d 782 (N.D. Ill. 1998).

That capacity flows from the license. For example, the difference between a single-user word processing program and a 100 person product rests in the terms of use in the license. The program itself is identical; what changes is the scope of use authorized under the license. Similarly, the distinction between a consumer use and a commercial use license may entail multiple dollar values, but rests only in what uses the license authorizes.

Mass Market Licenses

Some argue, that licensing in the mass market produces a great disadvantage for the consumer and other mass market transferee. This disadvantage clearly does not exist. In fact, we have already discussed a number of cases in which it is clear that a mass market license provides palpable *benefits* to consumers as well as to publishers.

Licensing facilitates a unique combination of mass distribution and availability along with tailored use terms and opportunities—consumers benefit. A tailoring effect is efficiently achieved here that cannot be replicated under other formats. There is also a benefit in the preservation of property rights which, presumably, have in themselves a net gain in promoting innovation and distribution of innovative or creative products.

The functions of a license in the mass market are different from that of a manufacturer's warranty in sales of goods. A license implements property rights permissions to end users (or other persons contractually acquiring a license) in return for a price that is either paid directly to the publisher or indirectly through the purchase from an intermediary, such as the retail store at which a copy is acquired. The core justification for standard-form licenses lies partly in the fact that they enable an efficient means of offering differentiated products to the mass market. The fact is that the efficiencies of mass market licensing practices benefit both the producer and the purchaser-licensee in terms of lower acquisition or transfer costs and by the fact that parties can choose the product they desire to provide or to acquire based on price and usefulness to them.

VII. SUMMARY

Licensing computer information is not a mere re-characterization of commercial practice with respect to sales of goods. Licensing is the transactional structure that supports the unique and diverse range of computer information products and establishes a functional and efficient distribution channel allowing wide distribution of computer information to consumers and others. It is a method of doing business used throughout a multi-billion dollar industry that leads the modern economy. Numerous illustrations show this practice as a practical matter and also document that the effect of licensing in consumer and other markets is diverse, productive, and efficient.

In the consumer market and elsewhere, the license is the product because the license defines what uses the licensee may make of the licensed information. Mass market licensing allows publishers to facilitate and establish a vibrant market for digital information that benefits consumers both as consumers and as members of an economy and that provides a means for mass availability of customized information and services.

The legal justification is clear. The vast majority of all courts that have addressed the question hold that licenses of digital information under standard form contracts are enforceable, whether the contracts are made online, in direct contact between the publisher and the end user, or through so-called shrink-wrap licenses where the end user and publisher do not directly deal with each other.[116]

This is an important area in commerce. It is vital that fears of the future and images of the past do not lead us to act in a way that wrongly encumbers and constrains one of the true sources of innovation and economic growth that has been fueling the modern economy and generating formerly undreamed of benefits.

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116. *See, e.g.*, ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996); Register.com, Inc. v. Verio, 126 F. Supp.2d 238 (S.D.N.Y. 2000).