DEPARTMENT OF COMMERCE
United States Patent and Trademark Office
National Telecommunications and Information Administration

Docket No. 130927852-3852-01

Response of the Owners Rights Initiative to the Request for Comments on Department of Commerce Green Paper, *Copyright Policy, Creativity, and Innovation in the Digital Economy*

The Owners' Rights Initiative (ORI), an organization of over 20 companies and trade associations dedicated to preserving the right to own, sell, lend, rent, and give away goods, welcomes the opportunity to comment on the Department of Commerce Green Paper on Copyright Policy, Creativity, and Innovation in the Digital Economy.[1] Below, ORI responds to question 7 concerning First Sale in the Digital Environment.

What are the benefits of the first sale doctrine? And to what extent are those benefits currently being experienced in the digital marketplace?

Justice Breyer, writing for the U.S. Supreme Court in *Kirtsaeng v. John Wiley & Sons, Inc.*, 133 S.Ct. 1351, 1363 (2013), stated that the first sale doctrine "is a common-law doctrine with an impeccable historic pedigree." He quoted a 17th century articulation of "the common law's refusal to permit restraints on the alienation of chattels," *id*., and observed that "a law that permits a copyright holder to control the resale or other disposition of a chattel once sold is similarly 'against Trade and Traffi[c], and bargaining and contracting.'" *Id*. Justice Breyer underscored "the importance of leaving buyers of goods free to compete with each other when reselling or otherwise

[1] A list of ORI members can be found at http://ownersrightsinitiative.org/about/.

disposing of these goods." *Id*. Competition, "including the freedom to resell, can work to the advantage of the consumer." *Id*.

The first sale doctrine operates at every level of our economy. It allows wholesalers to sell products covered by copyright, including products distributed in copyrighted packaging, to retailers without first securing distribution licenses from the manufacturers. The first sale doctrine likewise permits retailers to sell products to consumers without obtaining distribution licenses. Finally, the first sale doctrine permits consumers to rent or lend the products to other consumers, or to sell or give the products away when they no longer need them. The first sale doctrine reduces transaction costs and enables competition between sellers of new products as well as between new and used products. In *Kirtsaeng*, the Court recognized the importance of the first sale doctrine to libraries, used-book sellers, car dealers, technology companies, retailers, and consumers. Because the distribution right applies not only to products whose primary value is their protected expression, such as books, films, and sound recordings, but also to the protected expression in the packaging of all products, the limitation on the distribution right provided by the first sale doctrine is critical to the functioning of our economy.

The second part of question 7 asks about whether the benefits of the first sale doctrine are being experienced in the "digital marketplace." From the discussion in the request for comments, it appears that the Department is focused on the application of the first sale doctrine to digital transmissions. Given the importance of the first sale doctrine, we support the Department's examination of how the doctrine could be applied to digital goods. While we understand the need to assess carefully the nuances involving digital goods, we believe that the concept of ownership should apply in a technology neutral manner and that stakeholders ultimately should work towards a solution that enshrines the first sale principle in the context of digital goods because of consumer expectations about the goods they purchase.

At the same time, the Department should not neglect an aspect of "digital first sale" of concern to our members that affects a specific category of tangible goods: products that are distributed with pre-installed software critical to their operation. Software, of course, is a digital technology. Even though the consumers buy the physical products, ranging from high-end servers to toasters, the manufacturers often claim that they are just licensing the pre-installed software. These licenses sometimes contain a variety of restrictive terms that interfere with resale of the products, thereby harming the consumers that want to sell equipment they no longer want and the secondary market consumers that want to buy that used equipment. Often, these secondary market consumers are federal, state, and local government entities. ORI believes that manufacturers should not be permitted to use software licenses to interfere with the resale of products.

Manufacturers currently employ software licenses to place the following impediments on the alienability of physical products:

- **Prohibition on transfer.** Some license agreements provide that the software license is non-transferable. For example, the license for the software that comes installed on a NetApp product is not transferable. As a practical matter, NetApp gets paid twice for the right to use the same software: once by the original purchaser of the product, and a second time by the purchaser of the used product. Purchasers of Cisco equipment often find that it is cheaper to buy new equipment than pay the excessively high price for a license for the pre-installed software in used equipment.

- **Refusal to provide updates.** Some license agreements specify that routine updates such as bug-patches will be provided only to the original licensee. For example, Oracle refuses to supply routine updates to the purchasers of used products containing pre-installed Oracle software, unless they make an additional payment.
- **Bundling of maintenance contracts.** Some manufacturers will use control over the pre-installed software as a means of forcing purchasers of used equipment to buy additional services from them. IBM, example, will charge purchasers of used equipment a fee for software updates, but will provide the updates for free to purchasers that enter into maintenance agreements.

The legal fiction on which these restrictive practices is based is that the pre-installed software is licensed, not sold, to the purchaser of the hardware in which the software is installed. The manufacturers argue that because the purchaser is merely a licensee of the copy of the software, it does not have rights that normally accrue to the owner of a copy, such as the first sale doctrine or the right to make temporary internal copies necessary for the operation of a computer. *See* 17 U.S.C. §§ 109(a) and 117(a). The U.S. circuit courts are split on the validity of the manufacturers' argument. The Ninth Circuit has accepted this argument, *Vernor v. Autodesk*, 621 F.3d 1102 (9th Cir. 2010), while the Second Circuit has rejected it, *Krause v. Titleserv*, 402 F.3d

119 (2d Cir. 2005). Underlying this split concerning whether a person who acquires a copy of a computer program is an owner or a licensee of the copy is an even more profound split concerning preemption of contract terms inconsistent with the Copyright Act. *Compare Bowers v. Baystate Techs., Inc.*, 320 F.3d 1317 (Fed. Cir.), *cert. denied*, 539 U.S. 928 (2003)(holding that the Copyright Act does not preempt contractual terms prohibiting actions permitted under fair use), *with Vault Corp. v. Quaid Software Ltd.*, 847 F.2d 255 (5th Cir. 1988)(holding that under the Supremacy Clause of the U.S. Constitution, contract terms prohibiting copyright exceptions are unenforceable).

We recognize that the problem of restrictions placed on pre-installed software implicates complex issues of legal theory at the intersection of Constitutional preemption, the Copyright Act, and contract law. Nonetheless, this is a very concrete practical problem of manufacturers attempting to leverage the copyright in a component into perpetual control over a much larger device. At present, primarily manufacturers of computer and telecommunications equipment misuse software license agreements to interfere with resale. Yet as more products are distributed with pre-installed software, such as cars and consumer appliances, this problem will become more widespread. The solution to this problem is a simple amendment stating that the statutory rights provided under Title 17 apply to lawful possessors of software when that software is pre-installed in other products, and that these rights cannot be waived by contract. We urge the Department to support such an amendment.

Respectfully submitted,

OWNERS' RIGHTS INITIATIVE

Andrew Shore
Executive Director
Owners' Rights Initiative
Jochum Shore & Trossevin, PC
1100 H Street, NW #910
Washington, D.C. 20005