120. THE SHRINK-WRAP LICENSE: Old Problems In A New Wrapper

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. . .(must it be our ideal to have everything wrapped in cellophane)?

Ludwig Wittgenstein:

Remarks On the Foundations Of Mathematics, Rev. Ed., III, 81

I. *INTRODUCTION*

The "shrink-wrap" license is an intriguing development in the rapidly changing field of computer law. The use of these licenses in connection with the distribution of software has been hailed by some as a fresh solution to the problem of piratical copying of computer programs. In fact, the shrink-wrap license is simply a new version of an old approach to problems that have plagued the business world for many years.

The shrink-wrap license typically is a contract of adhesion printed in reasonably legible type on the outer wrapper of a package for a computer program that is stored on magnetic media, usually floppy disks. The license (and the package itself) however, are covered by a transparent "shrink-wrap" which allows the potential purchaser to see and read the terms of the license before purchase, or at least before removal of the outer transparent wrapping. The license states that opening the shrink-wrap will be deemed an acceptance of the terms of the license. In some cases, the purchaser may be able to remove one layer of wrapping in order to peruse the terms of the license, and is then given the opportunity to return an inner-wrapped package for a full refund if the terms of the license are not acceptable. The obligations imposed by the license typically include: no copying (or one copy only for back-up purposes), use of the program only on one device, nontransferability, and no right to disassemble or decompile the program. Disclaimers of warranties are often added.

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Two states, Louisiana and Illinois, have passed statutes which purport to legitimize and allow enforcement of the terms of shrink-wrap licenses.[1] Bills are pending at the date of writing of this article in California, Arizona, and Hawaii. The specific terms of the statutes differ, but the general thrust is as described above.

This article will examine the validity of the statutes that purport to make shrink-wrap licenses enforceable. Part II will examine the legitimacy of shrink-wrap licenses in the context of the law of equitable servitudes as it has developed in connection with chattels. Part III will consider shrink-wrap licenses within copyright law, focusing in particular on potential pre-emption of state shrink-wrap statutes, in whole or in part, by federal copyright law.[2]

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[1] The Louisiana statute is already being tested in court. The case, Vault Corp. v. Quaid Software, Ltd., CA85-2283 (E.D.La. 1985), was filed in the Federal District Court for the Eastern District of Louisiana in May 1985. A preliminary decision dismissing the suit for lack of personal jurisdiction was reversed by the Fifth Circuit. The case addresses some of the fundamental issues involved in the enforcement of shrink-wrap license legislation. The plaintiff, Vault Corporation, makes a copy protection system for software known as "Prolok." Quaid Software, Ltd., the defendant, a company in Toronto, Canada, publishes a program which defeats the copy protection systems used in several different kinds of popular software available to consumers. The lawsuit alleges that Quaid decompiled the "Prolok" program in order to produce a program called "CopyWrite," which is advertised to defeat "Prolok." A trial was held on plaintiff's motion for a preliminary injunction in April, 1986; on February 11, 1987, the District Court denied the motion on the ground that the Louisiana statute was preempted by federal copyright law.

[2] This article will not attempt to explore the impact of trade secret law on shrink-wrap licenses, a subject which has already been examined in other articles. *See, e.g.*, Rice, *Trade Secret Clauses in Shrink-Wrap Licenses*, 2 COMP. L. 17 (1985). Also, the article will not attempt to deal extensively with the impact of the Uniform Commercial Code.

Section 2-204 of the Uniform Commercial Code will undoubtedly be appealed to as support for the validity of shrink-wrap licenses, whether under state statutes specifically providing for their validity, or under general principles of commercial law. Section 2-204 provides:

> (1) A contract for sale of goods may be made in any manner sufficient to show agreement, including conduct by both parties which recognizes the existence of such a contract. (2) An agreement sufficient to constitute a contract for sale may be found even though the moment of its making is undetermined. (3) Even though one or more terms are left open a contract for sale does not fail for indefiniteness if the parties have intended to make a contract and there is a reasonably certain basis for giving an appropriate remedy.

By its terms, section 2-204 supports the validity of shrink-wrap licenses. But the issue becomes less clear when the cases on contracts of adhesion are examined. The UCC requires that there be "conduct by both parties

II. *EQUITABLE SERVITUDES*

Almost sixty years ago, Zechariah Chafee, Jr., wrote the last word on equitable servitudes on chattels.[3] Chafee's article dealt exhaustively with the efforts of the "commercial classes" to establish a marketing system in which the manufacturer could reach down to the ultimate consumer and control the use of goods, even though legal title had passed through several intervening hands. Chafee wrote that "[j]ust as sellers of land [desire] to limit its use by remote owners, sellers of chattels and other kinds of personal property [wish] to impose restrictions on these while in the hands of subsequent purchasers."[4] Chafee analogized to the "triumphant development"[5] of the law of unfair competition, which, in the Twenties, was "still rapidly developing through injunctions with almost no help from damage suits."[6] Chafee pointed out that "equity has responded admirably to the wishes of participants in modern business transactions, although at times imposing limitations on relief because of considerations which were not recognized by the desires of the commercial classes."[7]

Chafee found the analogy with unfair competition useful, and pointed out that the marketer intends that its advertising and promotional efforts will establish a direct relationship between the manufacturer and consumer, notwithstanding the intervening transfers of legal title to wholesalers, distributors, dealers and retailers. From our vantage point in the second half of the 1980's, we note how times have changed, as we read of Chafee's sympathy for the manufacturer, who, but for the law of unfair competition

> "finds himself helpless to stop vague but fatal and rapidly spreading rumors that some packages of his dentifrice have failed to prevent pyorrhea; or that a smoker has actually coughed after lighting one of his cigarettes; or that his automobile is so unsuccessful, that he is glad to have occasional dealers sell his new model at a twenty percent discount in order to get rid of his stock."[8]

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which recognizes the existence" of the contract. The line of authority in the adhesion cases protects the person whose conduct may be ambiguous when a contract is thrust upon him on a take-it-or-leave-it basis, as are shrink-wrap licenses.

[3] Chafee, *Equitable Servitudes on Chattels*, 41 HARV. L. REV. 945 (1928).
[4] *Id.* at 946.
[5] *Id.*
[6] *Id.* at 945.
[7] *Id.*
[8] *Id.* at 946–47.

Chafee went on to analyze attempts to extend the powers of equity in the field of servitudes on chattels. He mentioned restrictions on resale prices, territorial restrictions, restrictions on the form in which an article may be resold, restrictions on the use of the chattel itself, and tying restrictions. He discussed methods of binding sub-purchasers, such as by subcontracts, by notice or by equitable servitude, and he also reviewed extensively the judicial attitude toward these efforts. Chafee's review of the cases pointed out that the courts have not dealt analytically with the fundamental question whether the equitable theory of a covenant running with the land can be extended to an equitable servitude on chattels. Chafee concluded that "[a]t the close of my inquiry it must be admitted that I am much less convinced of the desirability of equitable servitudes on chattels than when I began"[9] But he went on to say that "[s]ervitudes on chattels still seem possible and reasonable, although my long investigation has not disclosed a single square decision establishing such a conception in a court of last resort."[10] On a note that will appeal to the more technically inclined computer programmer, Chafee concludes:

> I must end by echoing the frankness of the mathematician who, knowing that there is no upper limit for prime factors, was nevertheless obliged to conclude his search for new examples with the statement: "This result represents the sixth attempt and failure to discover a larger prime than 2^{127}-1 found by Lucas in 1877."[11]

The passage of 57 years has not dimmed the desires of today's commercial classes to achieve a similar goal in the marketing of software for computers; the so-called "shrink-wrap" license is the equitable servitude of the computer age.

If the problem of equitable servitudes was a complex one in 1928, it is no more simple in 1987. Shrink-wrap licenses (sometimes called box top, or tear-open licenses) are now widely in use as an attempt to prevent the two greatest evils perceived by developers of computer software -- unauthorized copying and reverse-engineering accomplished by disassembly or decompilation of the object code that can be read from the magnetic media. Copy protection schemes engineered into the programs have their following, but many of these are technically unsound

[9] *Id.* at 1013.
[10] *Id.*
[11] *Id.* (citation omitted).

for various reasons. Copy protection, for example, may prevent the consumer from making a perfectly legitimate backup copy to protect the consumer's investment, or may make a floppy disk unsuitable for use with the user's hard disk drive in the computer.

The shrink-wrap license typically is a forthright effort to use the power of the law to reach down to the ultimate program consumer and impose upon him or her a list of contractual obligations. The question whether the law of equitable servitudes will support this effort is complex. There has not been much case law or commentary on equitable servitudes since 1928, when Chafee wrote his article.

One type of equitable servitude, price maintenance schemes, has not fared well in the courts. Beginning with the Supreme Court's decision in *Straus v. Victor Talking Machine Co.*,[12] and continuing with two more recent cases involving Clairol products, *Clairol, Inc. v. Cosmetics Plus*[13] and *Clairol, Inc. v. Cody's Cosmetics, Inc.*,[14] manufacturers' attempts to sell the same product through retail and professional channels and enforce different price levels have been unsuccessful. In the *Clairol* cases, the courts allowed jobbers to break up packages marked "For Professional Use Only" and sell them at retail. In two other state court cases, *Fleischer v. W.P.I.X., Inc.*,[15] and *Nadell & Co. v. Grasso*,[16] equitable servitudes were upheld where the purchasers of chattels were third parties who had notice of contractual obligations between the sellers and prior owners of the chattels. In the federal courts, cases invoking the doctrine of equitable servitudes have upheld the binding effect of contractual obligations on third party purchasers of chattels with notice.[17] In another case, *Independent News Co. v. Williams*,[18] a legend on comic books, restricting sales for reading purposes to authorized dealers, was not effective to prevent a waste paper dealer from reselling the comic books for reading purposes.

Two cases involving the sale of phonograph records labelled "Not Licensed For Radio Broadcast" came to directly contradictory results in the late 1930's. The two cases, *Waring v. WDAS Broadcasting*

[12] 243 U.S. 488 (1917).
[13] 130 N.J. Super. 81, 325 A.2d 505, 184 U.S.P.Q. 234 (1974).
[14] 353 Mass. 385, 231 N.E.2d 912 (Mass. Supr. Jud. Ct. 1967).
[15] 30 Misc. 2d 17, 213 N.Y.S. 2d 632 (Supr. 1961).
[16] 175 Cal. App. 2d 420, 346 P.2d 505 (1959).
[17] *See* American Bell Inc. v. Federation of Tel. Workers of Pa., 736 F.2d 879 (3d Cir. 1984); Kenyon v. Automatic Instrument Co., 160 F.2d 878 (6th Cir. 1947); In re Waterson, Berline & Snyder Co., 48 F.2d 704 (2d Cir. 1931).
[18] 293 F.2d 510 (3d Cir. 1961).

Station, Inc.,[19] and *RCA Manufacturing Co. v. Whiteman*,[20] are discussed extensively below from the perspective of copyright law. They may also be analyzed, however, from the standpoint of equitable servitudes. The *Waring* case upheld the validity of the restriction and barred a radio station from broadcasting the music on the phonograph record without the consent of the orchestra leader. The *RCA* case came to a diametrically opposite conclusion and is good law today. Broadcast stations do not operate under any equitable servitudes with respect to recorded music.

Analysis of the equitable servitude cases cited above shows that manufacturers have had success only in the cases where purchasers of chattels had prior notice of pre-existing contractual obligations affecting the chattels. In the cases involving price maintenance or "legends" or both, with the single exception of *Waring*, the equitable servitude has not been upheld. The conclusion is inescapable that the law of equitable servitudes does not provide strong support for the enforceability of shrink-wrap licenses. We turn now to the question of the effect of federal copyright law.

III. COPYRIGHT

Computer programs today are generally protected by copyright. There may be some remaining areas of uncertainty, but the principle is now clearly established that protection under the Copyright Act of 1976[21] is available for computer programs, and there is no question that literal copying of a program by an unauthorized copier constitutes infringement.

One might well question why shrink-wrap licensing is necessary if federal copyright protection is clearly available.

Copyright protection is limited. For example, current law may not protect a copyright owner from the expert engineer who legally purchases a copy of a program and decompiles, disassembles, or otherwise reverse-engineers the program to see how it works.[22] The knowledge gained by such an effort can then be used in some cases to create a

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[19] 327 Pa. 433, 194 A. 631 (1937). *Cf.* Waring v. Dunlea, 26 F. Supp. 338 (D.N.C. 1939).

[20] 114 F.2d 86 (2d Cir.), *cert. denied*, 311 U.S. 712 (1940).

[21] 17 U.S.C. §§101–810 (1978) (hereinafter cited as 1976 Act).

[22] This may be because it is impossible, from a practical standpoint, to detect such activities performed in private; or it may be that some court will hold someday that such activities are not within the scope of "copying" that is prohibited by the 1976 Act; or, if they are within the scope of the copyright owner's rights, it is a fair use.

program which may appear to be totally different from the original, but which makes use of underlying concepts or techniques which were not apparent before the reverse-engineering. Whether the new program created in this manner infringes the original, and what the tests are for determining such infringement, is the subject of current litigation and extensive discussion.[23]

Shrink-wrap licensing is an attempt to give the owner of the copyright in the program additional protection that is either not available under copyright law as it is presently interpreted or that might not be available at all under any scheme of copyright within the constraints of the U.S. Constitution. The conclusion of Part III of this article is that the attempt is doomed to failure, because the shrink-wrap licenses, and the shrink-wrap statutes that purport to legitimize the licenses, are nothing more than attempts to take copyright beyond its constitutionally permissible bounds.

The Copyright Act of 1976 recognizes that there are rights akin but not equivalent to copyright that are not protected by the Act and may be protected by state law. Section 301 of the 1976 Act provides that the Act exclusively governs "all legal or equitable rights that are equivalent to any of the exclusive rights within the general scope of copyright. . ." provided that the works to be protected are "fixed in a tangible medium of expression" and "come within the subject matter of copyright. . . ."[24] The section then notes that nothing in the 1976 Act "annuls or limits any rights or remedies under common law or [state statutory law] with respect to [material outside] the subject matter of copyright [or] rights that are not equivalent to [copyright] rights."[25]

The *Vault Corporation v. Quaid Software* case[26] provides an example of an attempt to use a shrink-wrap license statute to reach an activity that may not prohibited by federal copyright law. Plaintiff in that case has asserted that defendant would not have been able to learn the secret of its protection system without violating the terms of the Louisiana statute which prohibits the disassembly of plaintiff's software by an owner of a copy of that software.[27]

[23] *Cf.* Q-Co. Industries, Inc. v. Hoffman, 625 F. Supp. 608 (S.D.N.Y. 1985) with E.F. Johnson Co. v. Uniden Corp. of America, 623 F. Supp. 1485 (D. Minn. 1985) and Whelan Associates v. Jaslow Dental Laboratory, 797 F.2d 1222 (3d Cir. 1986).

[24] 17 U.S.C. §301(a).

[25] 17 U.S.C. §301(b).

[26] *See* note 1, *supra*.

[27] Since this article does not focus on trade secret law (*see* note 2, *supra*), it will not pursue the interesting inquiry whether shrink-wrap licensing protects

Shrink-wrap statutes, such as the one passed recently in Illinois,[28] allow the licensor of software to retain ownership of each "copy of computer software"[29] acquired by a consumer-user. If title has been retained, then the licensor may also enforce provisions prohibiting the modification or adaptation of the copy of the software, including without limitation prohibitions on translation, decompiling, disassembling, or creating derivative works based on the software.[30] The licensor may also prohibit further transfer, assignment, rental, or sale of that copy or any other copies made.[31] The licensor may prohibit use of the copy on more than one computer at the same time or use by more than one individual user at the same time.[32] The rights of a licensor are limited, however; section 7 of the Illinois Statute provides that nothing in the statute

> "shall be construed to affect or alter any existing individual or business rights granted by the copyright laws of the United States, as now or hereafter amended, that such individual or business would have were such individual or business a purchaser of a copy of the computer software that is the subject of the license agreement."[33]

Conflicts between the Illinois Statute and federal copyright law are immediately apparent. While the Illinois Statute purports to enable a prohibition on the making of copies, section 117 of the 1976 Act provides that the "*owner* of a copy of a computer program" may make another copy or adaptation of the program, provided that the new copy

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a "trade secret," as the "Prolok" software was alleged to be. This inquiry would lead to a review of the impact of Section 301 of the 1976 Act on state trade secret law.

[28] For convenience, this article will focus on one state's statute, the Illinois shrink-wrap statute (hereinafter cited as Illinois Statute). The complete text of the statute is set forth in the Appendix.

[29] Ill Rev. Stat. ch. 29, §3.

[30] Ill Rev. Stat. ch. 29, §4(3).

[31] Ill Rev. Stat. ch. 29, §4(4).

[32] Ill Rev. Stat. ch. 29, §4(5).

[33] Ill. Rev. Stat. ch. 29, §7. The Illinois legislature appears to have been concerned that some provisions of the Illinois Statute might be pre-empted by the 1976 Act, but the author of section 7 of the Illinois Statute has said, "My intention was to gut the bill" and "I don't think we have a law at this point. It's so internally contradictory I don't think it's worth the paper it's written on." 2 Computer People Monthly 1 (May 1968) (quoting State Rep. Ellis Levin).

or adaptation is an essential step in utilization of the program, or the new copy or adaptation is for archival purposes.[34] Since section 7 of the Illinois Statute gives a person acquiring a copy of software the rights of a "purchaser of a copy" under federal law, its effect is to incorporate by reference rights under federal law that would otherwise be denied by the Illinois Statute.

Other interesting issues are raised by the Illinois Statute's prohibition on the rental of any copy and the prohibition on reverse-engineering. There is a considerable amount of law in the copyright field on the attempted prohibition of copyright-related activities that are not clearly prohibited by copyright law. Some of this law is not, on its face, analogous to the legal issues presented here, but a careful analysis will show that the analogies bear significantly on the issues at stake here and must be considered. As a result of such consideration, the conclusion of this article is that the shrink-wrap laws cannot be validly enforced.

The Illinois legislature has attempted to define as a license a transaction that would otherwise be viewed as a sale, as the word "sale" is normally used in American law. (In Illinois, it is worth noting that a person acquiring a copy of software in the usual kind of retail transaction does not pay the tax that applies to sales, but also does not pay the tax that applies to leases.) The Illinois legislature could also have attempted to treat this kind of transaction as one subject to a contract of adhesion, so that the person acquiring a copy of software is bound by the terms of the "license" (*supra*, note 2). The difficulty that the legislature has got itself into is that at least some of the rights affected are rights equivalent to the "exclusive rights within the general scope of copyright", and the result is that section 301 of the 1976 Act must be allowed its preemptive force. In addition, the legislature has become inextricably tangled in the constitutional limits on the federal scheme of copyright. No matter what the legislature may say it is doing, it is in fact interfering with both statutory and constitutional limits on its powers with respect to that form of "Writing" known as software.

From the standpoint of copyright law analysis, the prohibitions of the Illinois Statute can be divided into two areas -- first, the sections that are clearly preempted by the 1976 Act and, second, the prohibitions that attempt to govern the grey area of activities not preempted on their face by federal copyright law, which are perhaps subject to the control of state law. These are analyzed below.

[34] 17 U.S.C. §117 (Supp. 1986) (emphasis added).

A. *Preemption by the 1976 Act*

First, to the extent that the prohibition against copying in section 4(2) of the Illinois Statute tracks the provisions of the 1976 Act which give copyright owners the exclusive right to "reproduce the copyrighted work in copies,"[35] the shrink-wrap law is clearly preempted by the effect of section 301 of the 1976 Act. Since the author's right is effectively protected, however, the question is probably moot. Section 117 of the 1976 Act, which gives the "owner" of a copy of a software program the right to make an additional archival copy, must also be considered. Section 7 of the Illinois Statute, which gives the Illinois user the rights of a "purchaser of a copy" under federal law, seems to allow section 117 its preemptive effect, and, again, this question appears mooted. Second, the prohibition against "adaptation" in section 4(3) is contradicted by section 117 of the 1976 Act, which also permits the making of an adaptation, but once more, section 7 of the Illinois Statute saves the day by giving the Illinois user the rights extended by federal law to the "purchaser of a copy." Third, the prohibition against creation of derivative works in section 4(3) also seems to track the prohibition in section 106(2) of the 1976 Act against the preparation of derivative works based upon the copyrighted work. It is difficult to see how a successful argument could be made that the Illinois Statute is not preempted by federal law with these three prohibitions.

The fourth issue, the prohibition against modification of a copy of computer software in section 4(3), raises more difficult questions. If the owner of a copy of software wishes to modify a copyrighted program for the owner's own private purposes, there is no readily apparent provision of federal copyright law which prohibits such an activity, and indeed section 117 of the 1976 Act permits the making of an adaptation, which may be the same thing.[36] There is nothing in copyright law to prevent the owner of a single copy of a book, for example, from physically rearranging its pages if it suits the reader's convenience, nor is there anything to prevent the owner of a copy of copyrighted sheet music from making personal modifications either by marking the copy or in the course of private performances.[37] The question then arises whether

35 17 U.S.C. §106(1).

36 Of course, if a user were to modify a program and distribute or sell copies of the resulting new program, the exclusive rights protected by the 1976 Act would clearly be violated and the Illinois Statute would equally clearly be preempted by Section 301 of the 1976 Act.

37 *But see* WGN v. United Video. 693 F.2d 622 (7th Cir. 1982). In that case, the 1976 Act was construed to prohibit modification of a television signal by a satellite carrier which otherwise had the legal right to transmit the signal to its customers.

Illinois law can prohibit modification of software in light of the preemption language in section 301 of the 1976 Act. To the extent that any modifications are made by private users for private purposes, this prohibition will probably never be the subject of litigation. Illinois law attempts to reach this activity by labelling the sale of the copy of software a "license" and then authorizing restrictive terms by the licensor. As stated earlier, it is the conclusion of this article that such attempt fails.

An interesting case can be conceived, however. Suppose a user finds a bug or develops an improvement in a program subject to the Illinois statutes and publishes information about the modification or improvement. If the information suggests that program users go into the machine language of the program to make the modification, there could be an interesting question of the applicability of section 4(3) of the Illinois Statute, because the suggestion would involve a breach of a license term purportedly authorized by the Statute.

Finally, the prohibition against multiple uses in section 4(5), such as the use of shrink-wrap license protected software in more than one computer, or by more than one user, also raises an intriguing issue of preemption. Whether use of a single software program in a network of interconnected computers constitutes an infringement of the copyright protected right to "copy" is an issue of current concern. If a company operates its computers in a network consisting of a mainframe and "dumb terminals," may it buy one copy of a database or spreadsheet program and make the program available to all terminals? Does the result change if the user of the program has a network of personal computers interconnected and exchanging data between them although the program itself is resident only on one personal computer? If, of course, the 1976 Act applies to prohibit such copying, then again the Illinois Statute is preempted. At this time, it appears to be another fertile source of litigation.

B. *Extension of a Licensor's Rights beyond Copyright - The Constitutional Issues Raised by State Legislation Inhibiting the Dissemination of Ideas*

1. The Prohibitions against Reverse-Engineering and Transfer of Copies

Although preemption raises serious questions, the Illinois Statute would not have been passed if the legislature merely intended to offer parallel protection under state law of monopoly rights already protected by federal law. The Illinois Statute purports to extend the monopoly powers of distributors of software by granting rights that are not embodied in the federal copyright scheme. These areas of extension include the prohibition against reverse-engineering in section 4(3) and the prohibition against transfer of a copy of a software program in section 4(4).[38]

In one sense, the prohibition against reverse engineering is a trade secret issue; it is an attempt to preserve the secret or confidential status of information embodied in the magnetically coded signals or magnetic media, which cannot readily be translated into information directly perceivable by human beings. The trade secret aspects of this question will not be pursued here.[39] From a copyright standpoint, however, the prohibition against reverse-engineering is an attempt to limit the dissemination of ideas, and as argued more fully below, therefore runs afoul of traditional limitations built into the federal constitutional and statutory copyright scheme.

The prohibition against transfer of a copy of a software program is also an attempt to extend the software distributors' monopoly position beyond the protection afforded by the copyright laws and suffers from the same infirmities as the prohibition against reverse engineering. Sections 109 and 202 of the 1976 Act articulate the traditional distinction between ownership of copyright and ownership of the material object embodying a copyrighted work and give the owner of the material object certain rights under copyright law. Specifically, section 109(b) of the 1976 Act provides that the "owner of a particular copy lawfully made" is entitled to sell or otherwise dispose of the possession of that copy. Section 109(c) states that these privileges do not extend to any person who has acquired "possession of the copy" "by rental, lease, loan or otherwise without acquiring ownership of it." The Illinois Statute obviously is drafted so as to attempt to slip under the quoted language of section 109(c); it provides in section 4(1) that ownership of "title" in the material object may be retained by the licensor. But what about section 7? It gives the Illinois "licensee" the rights that a "purchaser of a copy" would have under federal law. State Representative Levin, its author, was probably right when he stated, "My intention was to gut the bill."[40] It appears that, notwithstanding section 4(4), a person acquiring a copy of software in Illinois, subject to a license authorized by the Illinois Statute, may still sell or dispose of possession of the copy.

[38] If section 7 were not part of the Illinois Statute, several other provisions would also represent extensions of the monopoly power of the software distributor.

[39] *See* Rice, *supra* note 2 at 20, concluding that similar provisions in the Louisiana shrink-wrap license law are invalid. His conclusions apply with equal force to the Illinois Statute.

[40] *See* note 23, *supra*.

2. The Copyright Background -- The Question of Publication

The attempts to prohibit reverse-engineering and the transfer of a material object embodying intellectual property (the disk containing a program) run into further problems with respect to federal law. There is an interesting analogy under federal copyright law with regard to the treatment of certain expressions of ideas that have been widely distributed. The touchstone of copyright treatment of the mass distribution of a work has been the question whether such distribution constitutes "general publication" so as to place the work in the public domain. The heart of the issue is that of access to ideas. The copyright cases dealing with this subject are relevant to the legitimacy of the state shrink-wrap statutes because such statutes attempt to restrain access. The sensitivity of courts to this issue in the publication cases provides the best support for the argument that statutes like the Illinois statute go too far in restricting access. The cases cited below show that there comes a point where some forms of mass distribution deprive the copyright owner of the power to control some (but perhaps not all) aspects of the use of the copyrighted work.

In *King v. Mister Maestro, Inc.*,[41] the publication issue was raised by the famous 1963 "I Have a Dream" speech of the Rev. Martin Luther King, Jr. The speech was delivered to an audience estimated at over two hundred thousand persons and was also disseminated by radio and television broadcasts, theatrical newsreel coverage, and extensive newspaper coverage. Notwithstanding this dissemination, the court held that there was no "general publication," and King was able to enjoin the sale of phonograph records of the speech as a copyright infringement.

On the other hand, consider the performers' or record manufacturers' contribution to recorded versions of music that are sold to the public in copies. (It is irrelevant that the music may or may not itself be the subject of copyright.) The same question of "general publication" is involved, and a short digression into the history of this aspect of copyright law may be useful.

Under the provisions of the Copyright Act of 1909,[42] phonograph records (as opposed to the music contained on the records) were not protected by federal law against copying, until February 15, 1972. This was the effective date of Public Law 92-140[43], which added section 1(f) to the 1909 Act. Prior to that date, numerous atempts were made under state law to prohibit such copying; these attempts were finally successful when the United States Supreme Court upheld the constitutionality of

[41] 224 F. Supp. 101, 106 (S.D.N.Y. 1963).
[42] 17 U.S.C. §§1-65 (hereinafter referred to as 1909 Act).
[43] 85 Stat. 391 (1971).

the California anti-piracy statute in *Goldstein v. California*.[44] Although the case was decided two years after the passage of the federal anti-piracy provision in section 1(f), the decision is still important because it allows state law to protect phonograph records produced prior to February 15, 1972 against piratical copying.

Under the 1976 Act, the copying of phonograph records is prohibited in §106(4). The 1976 Act (as amended in 1984) also provides special treatment for phonograph records, or "phonorecords," as they are referred to in section 101. Owners of phonorecords may not "for purposes of direct or indirect commercial advantage" dispose of a phonorecord by rental, lease or lendng.[45] This is an example of an area where Congress could constitutionally extend the protection of copyright law so as to prohibit previously lawful conduct, and did so.

The prohibition on lending provides an interest parallel to the prohibition in the Illinois statute against the transfer of a software program. Congress has allowed the owners of a material object embodying a copyrighted work, other than a phonorecord, to transfer that material object; thus, it has established a special category of treatment for the owners of phonorecords. Obviously, Congress could amend the 1976 Act so as to prohibit the transfer of copies of software programs. It would preempt the Illinois Act by doing so. Since Congress has not taken any such action, the Illinois Statute, prohibiting the transfer of a copy of software, falls in a limbo area similar to that of state statutes concerning sound recordings under the old copyright law before 1972.

Without further analysis, *Goldstein* could be cited to support the proposition that the Illinois statute is valid until specifically preempted. Some older law on the question of "general publication" and its application to phonograph records indicates that the courts might not stretch the reasoning of *Goldstein* to that extent.

In *Ferris v. Frohman*,[46] the Supreme Court held that public performance of a play, which had neither been printed nor distributed in written form, did not dedicate the play to the public domain. It remained "unpublished." In the broadcast field, this rule was extended in *Uproar v. NBC*,[47] to cover original material broadcast by radio. Since 1936, it has been generally assumed that broadcasting does not constitute such publication as to divest common law copyright. Likewise, public exhibition of a motion picture film for profit, leased for that purpose by the

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44 412 U.S. 546 (1973).
45 17 U.S.C. §109(b).
46 223 U.S. 424 (1912).
47 8 F. Supp. 358 (D. Mass. 1934), *modified*, 81 F.2d 373 (1st Cir. 1935), *cert. denied*, 298 U.S. 670 (1936).

copyright proprietor, generally does not dedicate.[48]

There is also a division of authority on the question whether sale of phonograph records dedicates the music contained thereon. Judge Igoe of the Northern District of Illinois once overruled a motion for new trial on a copyright infringement case by saying that plaintiff dedicated his composition by permitting the sale of records. Plaintiff had previously lost on the grounds that he was not the original composer of the music in question.[49] Whether Judge Igoe's statement is a holding or not is unclear. The matter is further confused by the fact that he cited *RCA Mfg. Co. v. Whiteman,*[50] a case which probably has been overruled with respect to its holding on the New York law concerning dedication. In the latter case, it was held that a record manufacturer and a performer on a phonograph record could not restrain a radio station from broadcasting the recorded music even though the record bore a restrictive legend, "Not Licensed for Radio Broadcast." In the opinion, Judge Learned Hand stated that any rights possessed by the manufacturer and performer were divested when the first record was sold. This was a diversity case, but Judge Hand never mentioned New York law. As noted above it is in direct conflict with a case decided by the Pennsylvania Supreme Court, *Waring v. W.D.A.S. Broadcasting Station, Inc.*[51]

A subsequent case in the New York state courts, *Metropolitan Opera Ass'n., Inc. v. Wagner-Nichols Recorder Corp.,*[52] practically ignored the fact that the Metropolitan Opera was authorizing the sale of recorded versions of its operas, while holding that the sale of records made from Met radio broadcasts, without authorization, was an infringement of the Met's property rights in its radio broadcasts. The court held that the radio broadcasts did not dedicate.

When this same issue returned to the Second Circuit, in *Capitol Records, Inc. v. Mercury Records Corp.,*[53] the majority held that *New York* law now required, in a diversity case, the holding that the sale of records does not dedicate the performance thereon. Judge Hand

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[48] DeMille Co. v. Casey, 121 Misc. 78, 201 N.Y.S. 20 (Sup. Ct. 1923). However, Blanc v. Lantz, 83 U.S.P.Q. 137 (Cal. Super. Ct. 1949) holds that distribution (by lease) of cartoon films dedicated plaintiff's original "Woody Woodpecker" laugh.

[49] Shapiro, Bernstein & Co., Inc. v. Miracle Record Co., Inc., 91 F. Supp. 473 (N.D. Ill. 1950).

[50] 114 F.2d 86 (2d Cir. 1940). *See also* notes 19–20, *supra* and accompanying test, discussing equitable servitudes.

[51] 327 Pa. 433, 194 A. 631 (1937). *See also* notes 19–20, *supra,* and accompanying text.

[52] 199 Misc. 786, 101 N.Y.S. 2d 483 (1950).

[53] 221 F.2d 657 (2d Cir. 1955).

dissented. In a previous case, he had pointed out that the *Metropolitan* decision is not one in which the New York courts take any position on the question whether sale of *phonograph records* dedicates, but rather is a holding that radio broadcasts do not dedicate.[54] Judge Hand went on to state that all questions of what constitutes publication of material which is constitutionally capable of federal copyright must, under the federal Constitution, be decided by federal law.[55]

RCA Mfg. Co. v. Whiteman is still considered good law in the broadcast industry for the proposition that a restrictive legend on a phonograph record is inoperative to prevent subsequent broadcast of the music on the record. This is true despite *Waring*'s decision to the contrary. *Waring* has no practical effect today, even in Pennsylvania, so far as radio and television stations are concerned.

At this juncture, the state of the law regarding general publication does not provide much guidance on the question whether the Illinois Statute's attempt to keep title in the owner-developer of a software program will be successful to allow the owner-developer to acquire rights not extended by the federal copyright law. Judge Hand's dissent in *Capitol Records*, asserting the preemptive effect of federal copyright law even where the statute itself is silent, however, anticipated the next significant treatment by the courts of the question of publication and pre-emption.

3. The Constitutional Limits Applied

In *Sears, Roebuck & Co. v. Stiffel Co.*,[56] and *Compco Corp. v. Day-Brite Lighting, Inc.*,[57] the United States Supreme Court held that the state courts could not, under "unfair competition" principles, prohibit copying of the design of functional objects, where the objects were incapable of meeting the standards of design patent law or other federal statutory protection.[58] The Court concluded that the state statute involved was preempted by the federal exercise of power under Article I, Section 8 of the U.S. Constitution and the implementing federal patent and copyright statutes.

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[54] G. Ricordi & Co. v. Haendler, 194 F.2d 914 (2d Cir. 1952).

[55] Although Judge Hand made it clear that he considered the sale of phonograph records to dedicate the recorded material, as a matter of federal law, he did not state a position on whether a broadcast dedicates the material.

[56] 376 U.S. 225 (1964).

[57] 376 U.S. 234 (1964).

[58] The objects in question probably could not have been protected by copyright.

The *Sears* and *Compco* decisions would appear to vindicate Judge Hand and provide strong support for the argument that a state law like the Illinois Statute cannot pass constitutional muster because the monopoly power of the licensor (the power to prohibit the transfer of a copy of a copyrighted software program) could be established by federal law, but is not. That argument, however, would now come up against the decision in *Goldstein v. California*, in which the California statute prohibiting piractical copying of phonograph records was upheld. In *Goldstein*, the Supreme Court held that California could prohibit the duplication of phonograph records containing material then unprotected by federal copyright, namely, the performers' performances and the manufacturer's contribution to the production of the records. The Court held that federal copyright law had *not* preempted the field at the time in issue.

Distinguishing *Sears* and *Compco* from *Goldstein* is difficult, if not impossible. The Supreme Court discussion is not of much help. It contains a long discussion of the distinction between types of materials protected and standards for protectability, but this appears to be a distinction without much difference.[59] The *Goldstein* decision, however, has two premises -- a major premise that the validity of a state monopoly-subsidy system is to be "measured by each system's own lights in terms of the balance it strikes between private incentive and public access,"[60] in other words, an empirical test.[61] The minor premise of *Goldstein* purports to apply the empirical test. In each case, the courts must balance the monopoly rights that protect authors on the one hand with public access to ideas on the other. Another way to put it is that the legislature and courts must determine how best to advance competition in a presumed "market-place" of ideas. The *Goldstein* decision says that the federal courts should defer to state legislative action in this area and suggests that there must be some exploration of the extent of the monopoly in terms of time and area. In the *Goldstein* decision, the fact that the state-created monopoly was perpetual, and the fact that it was limited to the state of California, were both discussed.[62] The questions of

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[59] The best discussion of the decision is Goldstein, *'Inconsistent Premises' and the 'Acceptable Middle Ground:' A Comment on Goldstein v. California*, 24 BULL. COPR. SOC'Y 25 (1973). (The author of the article is not related to the party in the case.)

[60] *Id.* at 36.

[61] It should be noted that one of the *Goldstein* dissenters said that *Sears* and *Compco* created a *per se* test and that there should be no empirical question involved.

[62] Under the tests suggested by the *Goldstein* decision, the perpetual duration of the protection afforded by the statutes to shrink-wrap licensors is not

access to ideas and the limitations on access imposed by state shrink-wrap statutes are of much greater concern. In *Goldstein*, the Court concluded, "[n]o restraint has been placed on the use of an idea or concept; rather, petitioners and other individuals remain free to record the same composition in precisely the same manner and with the same personnel as appeared on the original recording."[63] The shrink-wrap statutes extend the monopoly power of software distributors by prohibiting reverse-engineering and the transfer of copies of software, activities which would be legitimate under the federal copyright scheme.[64] These inhibitions on the dissemination of ideas are the most significant weakness of the statute under the *Goldstein* decision and the constitutional principles embodied in *Goldstein.*

IV. CONCLUSION

Whether viewed from the standpoint of equitable servitudes or copyright, the Illinois legislature's attempt to legitimize the shrink-wrap license appears doomed to failure. There is little or no support for the Illinois Statute in the law of equitable servitudes as it has developed since Professor Chafee's article in June 1928. And, with or without the ambiguous help of section 7 of the Statute, the Statute does not meet the most significant of the tests articulated by the *Goldstein* decision, the test of public access to ideas.

There is much debate about the kind of legal protection that should be afforded to the developers of software, and there is no question that technological developments may require creative legislative enactments to keep pace with new structures of ideas, expressions, and copying. The conclusion of this analysis of Illinois' attempt to extend protection afforded to software developers is that the attempt has failed; the subject matter of the Illinois Statute is an area best left to Congress, within the Constitutional framework of the patent and copyright statutes.

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necessarily fatal; there is still an open question as to the territorial impact of the state statutes. The latter question may be decided by Vault Corp. v. Quaid Software, Ltd. *See* note 1, *supra.*

[63] 412 U.S. at 571 (1973).

[64] At the time this article was written, legislation has been introduced in Congress, the Software Rental Act of 1986, HR 4949, which would prohibit the rental of computer software without the permission of the publisher, paralleling the prohibitions in the 1976 Act prohibiting the unauthorized rental of phonorecords.

APPENDIX

Section 1. Title. This Act shall be known and may be cited as the Software License Enforcement Act.

Section 2. Definitions. For purposes of this Act the following terms shall have the meanings set forth below, unless the context clearly requires otherwise.

"Computer software" means a set of statements or instructions to be used directly or indirectly in a computer in order to bring about a certain result in any form in which such statements or instructions may be embodied, transmitted or fixed, by any method now known or hereafter developed, regardless of whether such statements or instructions are capable of being perceived by or communicated to humans, and includes associated documentation and materials, if any.

"License agreement" means a written document on which the word "license", either alone or in combination with other words, appears conspicuously at or near the top so as to be readily noticeable to a person viewing the document.

"Reverse engineering, decompiling or disassembling" means a process by which computer software is converted from one form to another form which is more readily understandable by human beings, including without limitation decoding or decrypting computer software which has been encoded or encrypted in any manner.

Section 3. Requirements for enforceability. A person who acquires a copy of computer software will be conclusively deemed to have accepted and agreed to those provisions of the license agreement accompanying the copy which are described in Section 4 below, if:

(1) A written legend or notice is affixed to or packaged with the copy of computer software and states clearly that use of the copy of computer software will constitute acceptance of the terms of the accompanying license agreement, or that the opening of a sealed package, envelope or container in which the copy of computer software is contained will constitute acceptance of the terms of the accompanying license agreement; and

(2) The legend or notice is affixed to or packaged with the copy of computer software in such a manner that the legend or notice is clearly and conspicuously visible so as to be readily noticeable to a person viewing the copy of software and related packaging; and

(3) The legend or notice is prominently displayed in all capital letters and in language which is readily understandable; and

(4) The legend or notice states clearly that a person who receives the copy of computer software and does not accept and agree to the terms of the accompanying license agreement may, within a reasonable time,

return the unused, unopened copy of computer software to the party from whom it was acquired, or to some other identified party, for a full refund of any money paid for the copy; and

(5) The terms of the accompanying license agreement must be clearly and conspicuously stated in the license agreement in language which is readily understandable, and the license agreement must be attached to or packaged with the computer software or copy thereof in such a manner that the terms are readily noticeable before the act which is deemed to constitute acceptance occurs; and

(6) The person acquiring the copy of computer software takes such action as is stated in the legend or notice to constitute acceptance of and agreement to the terms of the accompanying license agreement; and

(7) No agreement relating to the use, return, resale, copying, decompiling, disassembly or other right related to the computer software has been entered into between the person acquiring the computer software and the person holding title thereto; and

(8) The computer software has not been developed according to the acquirer's specifications or otherwise custom-made either by an outside vendor or an internal department of the acquirer.

Section 4. Terms deemed accepted. The following provisions will be deemed to have been accepted under Section 3 above if the provisions are included in a license agreement which conforms to the provisions of Section 3:

(1) Provisions for the retention of title to the copy of computer software by a person other than the person acquiring the software.

(2) If title to the copy of computer software has been retained, provisions for the prohibition of any copying of the copy of computer software for any purpose, limitations on the purposes for which copies of the computer software can be made, or limitations on the number of copies of the computer software which can be made.

(3) If title to the copy of computer software has been retained, provisions for the prohibition or limitation of rights to modify or adapt the copy of the computer software in any way, including without limitation prohibitions on translating, decompiling, disassembling, or creating derivative works based on the computer software.

(4) If title to the copy of computer software has been retained, provisions for prohibitions on further transfer, assignment, rental, sale or other disposition of that copy or any other copies made from that copy of the computer software.

(5) If title to the copy of computer software has been retained, provisions for prohibition on the use of the copy of computer software on more than one computer at the same time or use of the copy of computer software by more than one individual user at the same time.

(6) Provisions for the automatic termination without notice of the license agreement if one of the foregoing provisions of the license agreement is breached.

(7) Provisions for award of reasonable attorneys' fees and court costs to the prevailing party in any action or proceeding brought in connection with an alleged breach of one of the foregoing provisions of the license agreement.

Section 5. Enforceability. The provisions of this Act will not limit in any manner the effectiveness or enforceability of any of the other provisions of a license agreement accompanying computer software under other provisions of the laws of this State, whether statutory or common law. The provisions of this Act and the enforceability of a license agreement will not be nullified, curtailed or limited by the manner in which the ownership rights are held in the medium on which the computer software is embedded.

Section 6. Nothing in this Act shall be construed to alter any rulings of the Illinois Department of Revenue on the taxable status of computer software under the "Use Tax Act", approved July 14, 1955, as amended, the "Service Use Tax Act", approved July 10, 1961, as amended, the "Service Occupation Tax Act", approved July 10, 1961, as amended, or the "Retailers' Occupation Tax Act", approved June 28, 1933, as amended, or any of their related Acts.

Section 7. Nothing in this Act shall be construed to affect or alter any existing individual or business rights granted by the copyright laws of the United States, as now or hereafter amended, that such individual or business would have were such individual or business a purchaser of a copy of the computer software that is the subject of the license agreement.

Section 8. Nothing in this Act shall be construed to alter or amend any provision of the Consumer Fraud and Deceptive Business Practices Act.

Section 9. This shall take effect July 1, 1986.