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"The Shrinkwrap License Wins Its Day in Court and Plays a New Symphony:" "Wrap-CD Anew,"

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by David M. Mirchin

The proliferation of photocopying machines in the 1960's and 1970's made it easy for libraries and their patrons to copy articles from the library's collections. After this practice had become widespread, Congress recognized this standard practice by creating a "library exemption" in the 1976 Copyright Act. This is just one example of law playing catch-up with changes in business. And now comes another: the first United States court case to proclaim that shrinkwrap licenses are enforceable.

Software producers have for years been using "shrinkwrap" licenses. (In common parlance, any software license agreement that does not require a signature is often referred to as a shrink-wrap license. The term "shrink-wrap" comes from the transparent plastic in which mass-market, physically delivered, software is often encased.) But the court cases dealing with these software licenses have either cast doubt on their enforceability or sidestepped the issue--until now. In a ruling that is stunning for its boldness and awareness of commercial realities, the 7th Circuit Court of Appeals held, in ProCD, Inc. v. Zeidenberg (decided June 20, 1996), that shrinkwrap licenses are as enforceable as any other contract.

In addition to confirming the widespread existing business practice of using shrink-wrap licenses, this ruling explicitly supported the new business practice of using "click-wrap" licenses. These are electronic licenses which set forth the terms governing the use of software and information products. Unlike a shrinkwrap, a "click-wrap" is not delivered on paper, but is presented to the purchaser or user on their computer screen before they access information or install or download the software from the internet. The purchaser or user accepts by clicking the "Enter" key or taking another affirmative act to indicate acceptance. The ProCD case could give a high-publicity boost to electronic licensing, which in turn could make it easier and less expensive to distribute software and information products.

THE DISTRICT COURT RAPS SHRINKWRAPS

ProCD, Inc. is a company based in Danvers that produces and markets a database on CD-ROM under the name SelectPhone™. The database contains 95 million residential and business listings from 3,000 publicly available telephone books. ProCD sells SelectPhone in boxes that state in small print that its use is covered by a license. The license agreement is found inside the box. Once the product is installed on the user's computer, a screen reminds you that use of SelectPhone is subject to the license. Along comes Matt Zeidenberg, a Ph.D. student in computer science. He purchased SelectPhone at a store in Madison, Wisconsin, downloaded the telephone listings onto his hard drive, and then posted this information on the Internet for free. ProCD sued Zeidenberg, and in a January 1996 opinion, the Wisconsin District Court upheld Zeidenberg's position on all counts. The District Court held that the license was not enforceable because it was inside the box rather than on the outside, thus depriving the purchaser of the opportunity to review all of its terms prior to purchase.

The District Court went on to say that, even if the shrink-wrap licenses were contracts, they were unenforceable because they were preempted by federal copyright law.

THE CIRCUIT COURT HAS SHOPPED IN EGGHEAD

The 7th Circuit categorically reversed the District Court. The Circuit Court said that buyers of software must obey the licenses. It does not matter that the terms are inside the box. The court recognized that software licenses are (alas for us lawyers!) not the most important thing for software purchasers, saying: "Vendors can put the entire terms of a contract on the outside of a box only by using microscopic type, removing other information that buyers might find more useful (such as what the software does, and on which computers it works, or both.)" The court recognized that "notice [of the license terms] on the outside, terms on the inside, and a right to return the software for a refund if the terms are unacceptable...may be a means of doing business valuable to buyers and sellers alike."

The Court then gave some common examples of transactions in which the exchange of money precedes the communication of detailed terms. When a traveler books a plane reservation, he or she pays and then receives a ticket, which contains elaborate terms, such as the limitations of liability imposed by the Warsaw Convention. If you use the ticket, you accept the terms. In the logic of the District Court, the terms on the ticket would be irrelevant because the traveler paid before receiving them. Consumer goods work the same way, the Circuit Court said. You buy a television set, and a warranty limitation is included inside the box. You buy medicine, and it contains an elaborate package insert.

In summary, the Circuit Court held that ProCD had proposed license terms which the buyer would accept by using the software, after having an opportunity to read the license. Zeidenberg did use the software, and the Circuit Court held that he is bound by the license.

The Circuit Court then turned to the copyright preemption issue that had been raised by the District Court. (The 1976 Copyright Act preempts states from creating rights that are "equivalent to any of the exclusive rights within the general scope of copyright.") The Circuit Court in ProCD held that the license agreement is not preempted by federal copyright law. In a well-reasoned insight, it said that "a copyright is a right against the world." Copyright law applies to everyone. It gives rights to the author to restrict the options of people who are strangers to the author. Copyright law, for example, forbids duplication or public performance, unless the person wishing to copy or perform gets permission. Contracts, by contrast, generally apply only to the contracting parties. Strangers may do as they please. To illustrate, a person who found a copy of SelectPhone on the ground would not be bound by the contractual terms.

The Circuit Court went on to give examples of contracts which dealt with non-copyrighted intellectual property, such as public domain information. Contracts between two parties about this non-copyrighted subject matter would still be enforceable. Similarly, the court concluded, the ProCD license was enforceable.

IMPLICATIONS FOR BUSINESS

The Circuit Court's decision could have a broad impact on how software publishers and content providers disseminate and protect their products.

- This is the first court case to unambiguously validate shrink-wrap licenses. Accordingly, companies now have the first solid support that courts will enforce a shrink-wrap license, eliminating the need to undertake the expense and effort of obtaining a signed license agreement.

- The court stated that "shrinkwrap licenses are enforceable unless their terms are objectionable on grounds applicable to contracts in general (for example, if they...are unconscionable)." This is an easy test to meet. Publishers can take great comfort that only extremely overreaching provisions in their licenses will be held unenforceable.
- The court approved "click-wrap" electronic licensing. It commented favorably that ProCD "splashed" the license on the screen and would not let the buyer proceed without indicating acceptance. If software producers have not already done so, now is the time to consider the appropriateness and resultant cost savings of replacing paper licenses with an electronic license.
- This case permits a less expensive, less cumbersome telephone ordering procedure for software. Some earlier cases held that when customers order over the telephone, they would be bound by the license only if they could review the license before placing the order. This left the software company with a lesser-of-two-evils choice: sending the customer the license prior to accepting the order (which would make the terms enforceable but was expensive and delayed the customer's receipt of the information), or sending the license with the product, and risking that the license would be unenforceable. The Circuit Court's ProCD decision permits the publisher to implement the simpler process of sending the license with the product, with a greater degree of assurance that the license is enforceable.
- This ruling explicitly permits publishers to protect uncopyrightable information by contract. The court assumed that the ProCD information would be uncopyrightable after Feist. (In 1991, the U.S. Supreme Court held in Feist Publications, Inc. v. Rural Telephone Service Co. that telephone directories which are merely alphabetical compilations are not copyrightable since they are not arranged in an original manner and lack even a minimal degree of creativity.)

LINGERING QUESTIONS

This decision could have a dramatic impact on the use of shrinkwrap licenses, click-wrap licenses, and "web-wrap" licenses--licenses for products delivered over the Internet. This much seems clear.

What is less clear is whether the parties can agree, by contract, to override specific copyright provisions. Copyright law can be seen as a framework to protect and encourage original works, and also a framework to enhance free speech and the free flow of ideas by providing that original works eventually end up in the public domain or are never eligible for copyright protection. For example, facts are not eligible for copyright protection. By contract, however, ProCD protected a compilation of facts. The Circuit Court opinion has tipped the balance very much in favor of contract and held that the parties can provide for any provisions in a contract, unless they are unconscionable. Does that mean, for example, that a publisher can provide by contract that its copyright extends not just for the author's life plus 50 years, as set forth in the Copyright Act, but for 100 years after the author's death? This seems unlikely.

Or could the "first sale doctrine" (which provides that a purchaser of a copy of a copyrighted work can choose to deal with it as he chooses) be overcome by a publisher's contract which deprives the purchaser of that right? At what point does a contract become, in the words of the ProCD Court, "unconscionable"? Would it be unconscionable for Cracker Jacks to replace the prize in its box with a license agreement, which states that you can't share them with a friend?

Finally, an open question is whether companies may use this decision to do a contractual end run around the Feist decision (which provided no copyright protection for telephone listings). The ProCD ruling indirectly resurrects the "sweat-of-the-brow" line of cases. These held that publishers can protect information which is not copyrightable, but which they put together with a significant

investment of time, effort and money. This would be a dramatic coup for publishers, but one that runs squarely into Feist. Accordingly, publishers should find more reliable protection for their uncopyrightable databases by supporting the Database Investment and Intellectual Property Antipiracy Act introduced by Rep. Carlos Moorhead in May, 1996. This bill would protect producers of databases who invest a substantial amount of human or financial resources in developing their products against commercially harmful extraction or re-use of data from their products.

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*This is the draft as submitted to the Boston Business Journal. The BBJ ran a condensed version in their September 6-12, 1996 issue.