RETAILERS OF INTELLECTUAL PROPERTY: THE COMPETITIVE VOICE OF CONSUMERS

Statement by John T. Mitchell[1]
on behalf of
Video Software Dealers Association[2]

Public Hearings on Competition and Intellectual Property Law and Policy in the Knowledge-Based Economy
before the
Federal Trade Commission
and the
Antitrust Division, U.S. Department of Justice

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America's home video retailers comprise the industry segment responsible for the creation of home video as we know it today. Largely unauthorized by the copyright holders, and despite vigorous opposition from them,[3] video retailers fought with each other and the studios to bring to consumers a highly competitive low cost and convenient form of family entertainment. Movies costing \$75 and shown for \$7.50 at the theater could be watched for as little as 99 cents for a one-night rental. Though the average price of a new release rental is about \$2.90, that 99 cent special of fifteen years ago is still available today for catalog titles, for which the average VHS rental (per night) is 77 cents, and the average DVD rental (per night) is \$1.29.[4] These low prices are being maintained, even though gone are the "membership fees" and cramped stores of old where little new was left on a Friday night, replaced with larger inventories and more spacious stores with "guaranteed availability" of new releases. How? Cutthroat competition among retailers who, thanks to the Copyright Act's strict limitation on the intellectual property rights of the motion picture studios, could pretty much do as they pleased with their copies, free from copyright holder control.[5]

This vigorous competition is being threatened on several fronts:

- Unilateral refusals to deal – which were almost useless in the first two decades of home video – can now be used to eliminate some competitors completely. (See Part I, at p.2.)
- Digital technology is being enlisted to extend the scope of intellectual property rights of copyright holders beyond the limits established by Congress. (See Part II, at p.9.)
- Innovation and competition in the delivery of goods and services to retailers is, for the very first time in history, being systematically eliminated in favor of ties to the services designated by copyright holders. (See Part III, at p.23.)
- Standard-setting, which had been used to ensure compatibility of formats, packaging and automation, now threatens to be employed to achieve "automated agreements in restraint of trade." (See Part IV, at p.25.)
- Pooling and cross-licensing of copyrights exponentially increases the magnitude of each of the harms identified above. (See Part V, at p.26.)

Each of these threats is addressed below.[6] In a nutshell, certain efforts are underway to privately expand the limited privileges granted to copyright holders by Congress under the Copyright Act, and to control and restrain the lawful distribution and use of copyrighted products.[7] The very digital technology used to create new forms of copies is now being used to circumvent constitutional and statutory limitations on the copyright monopoly. (For a discussion of copyright misuse, see Part VI, at p.36.) These efforts promise to undermine copyright law and the public policies it serves, suppress consumer choice and retail competition (see Part VI, at p.33), and ultimately impede the development of online entertainment to the detriment of consumers, retailers, and copyright holders.

I. The Strategic Use of Licensing: There Is Cause for Concern about Unilateral Refusals to Deal

Thanks to the first sale doctrine and Section 109(a) of the Copyright Act, the reach of copyright holder control over distribution ends when someone else owns the lawfully made copy. Indeed, the Copyright Act draws a careful line of demarcation between ownership in the copyrighted work (the intellectual property interest), and ownership of the physical medium in which the copyrighted work is fixed (the personal property interest).[8] In a standard manufacturer/distributor/retailer/consumer relationship involving prerecorded copies of copyrighted works, the manufacturer/copyright holder may choose to distribute through multiple competing companies, as illustrated in **Figure 1**.

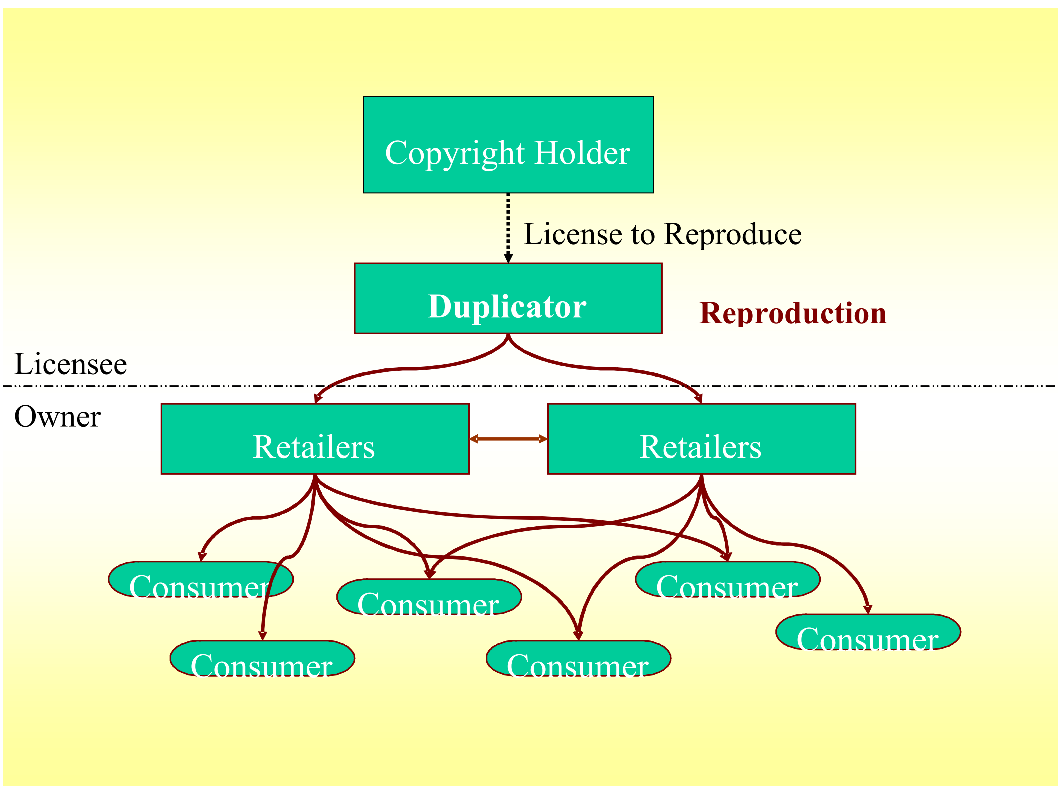

Figure 1

As illustrated in **Figure 1**, the copyright holder licenses the reproduction (dotted line) into copies, and these copies are distributed (solid line) in commerce. Once ownership over a copy passes to someone other than the copyright holder (horizontal line), the copyright holder loses all legal power under the Copyright Act to control distribution. Accordingly, if the copyright holder (assumed to also be either the duplicator or the owner of the copies made by the duplicator) chooses to sell exclusively to one retailer (either directly or through a distributor), as illustrated in **Figure 2**, competing retailers may still buy lawful copies and resell them or rent them.

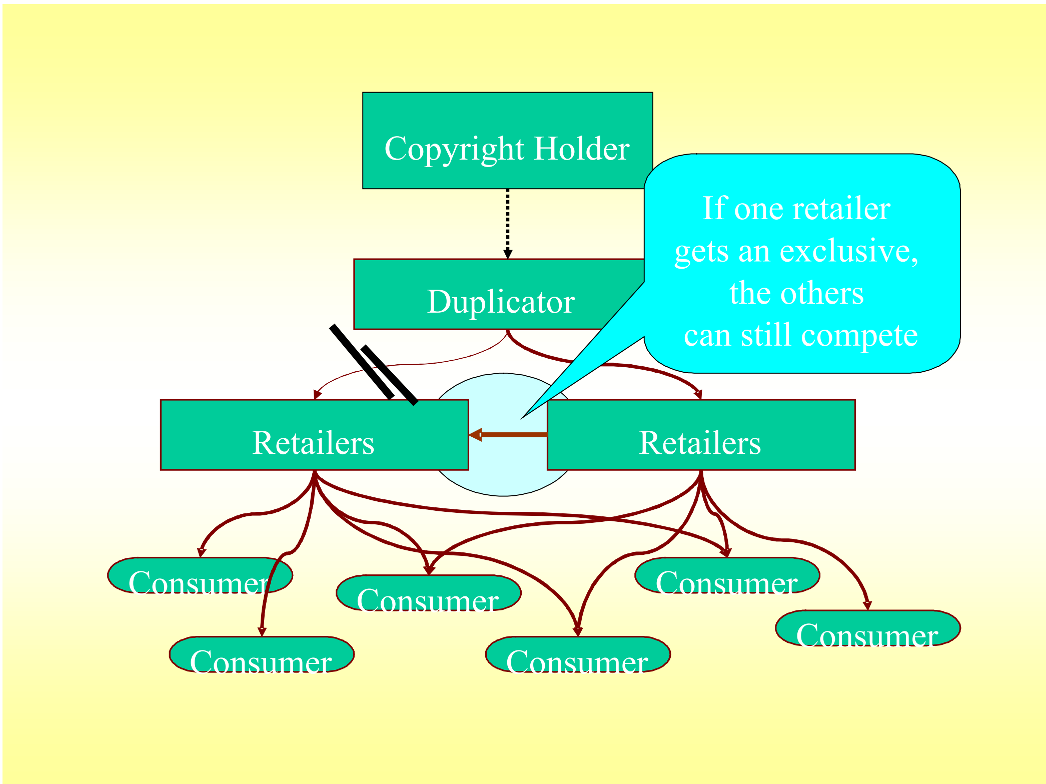

Figure 2

For example, even though McDonald's was able to get an exclusive of *Indiana Jones* copies, which it sold for $5.99 as part of a promotion,[9] video retailers were absolutely free from copyright-holder control to buy the $5.99 titles from McDonald's and place them on their shelves for resale or rental.[10] To be sure, no retailer would take too kindly to the notion of having to buy its copies from another retail competitor, but at least they would have the power to offer the copies to their customers, even if subject to a higher cost of goods.

In short, though the copyright holder has the exclusive right to license the reproduction of copies, and may license that right exclusively to one manufacturer or sell its own copies exclusively to a single entity, the copyright holder nevertheless looses all control over the copies once they enter the stream of commerce. As the House Judiciary Committee (then known as the House Committee on Patents) declared when it codified the first sale doctrine, "<u>it would be most unwise to permit the copyright proprietor to exercise any control whatever over the article</u> which is the subject of copyright after said proprietor has made the first sale."[11]

The congressional intent to prevent copyright holder control over distribution of copies owned by others can easily be thwarted in a digital copy delivery environment, however. A licensed copy reproduced onto a computer hard drive, writeable CD, writeable DVD, or flash memory, requires for its creation the consent of the copyright holder, thereby enabling the copyright holder to control what would ordinarily be a retail transaction all the way to the ultimate consumer, and beyond. This is because, rather than licensing the reproduction of a work into copies and then parting with title to the copies, the copies do not come into being until they reach the ultimate consumer. Thus, the copyright holder must license not only the reproduction to the retailer to make a server copy, but must, in addition, license the retailer to sublicense the reproduction to the consumer. Because of this additional step, licensed reproduction onto the tangible media owned by the consumer (commonly referred to as a "download" or "digital delivery" of a copy) can only occur with the copyright holder's consent.

So, while the retailer selling pre-packaged copies can do so without the authority of the copyright holder, to sell to its customers a copy that the customer makes by downloading, the customer and the retailer must have permission from the copyright holder because the transaction involves a reproduction. Accordingly, even though the resulting copies are identical in content and identical under the law, the copyright holder has the power to license the reproduction right (including rights to sublicense the right) to any retailers it chooses, and exclude from the market any it chooses. Those excluded could, under license, download copies to their company computers, but would be unable to lawfully sublicense the reproduction to their own customers without consent. **Figures 3 and 4** illustrate this:

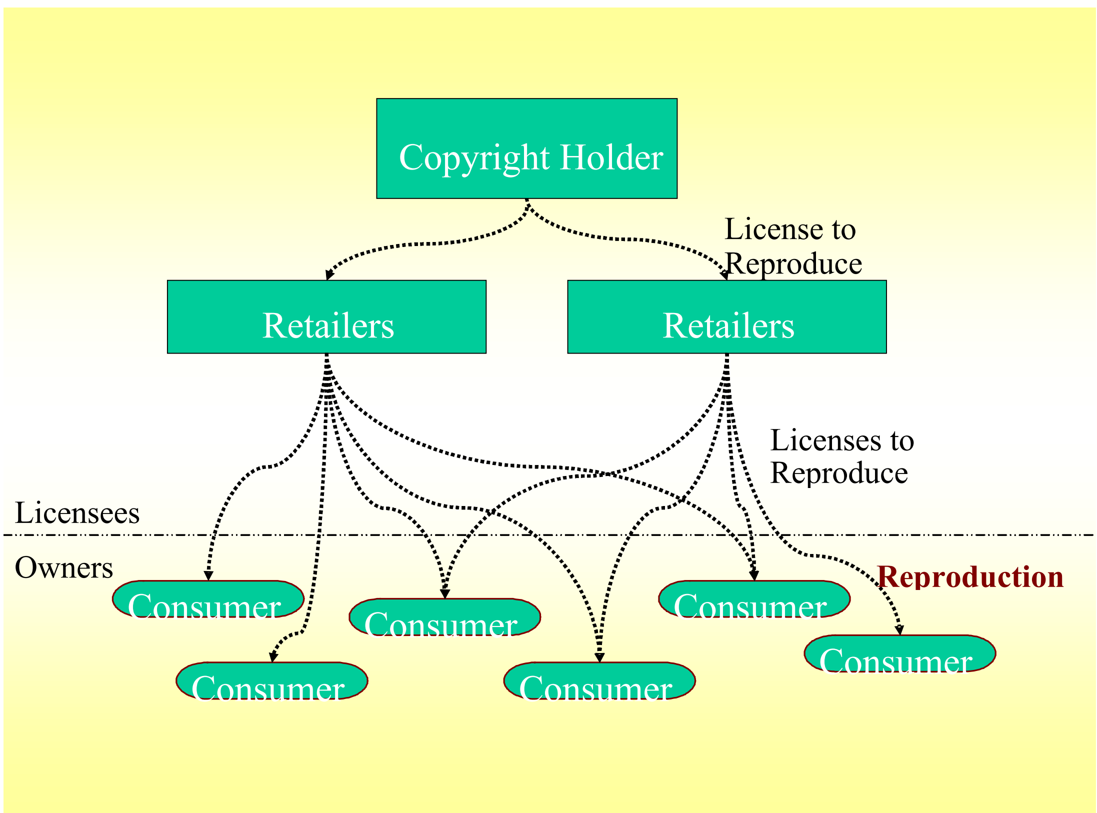

Figure 3

In this illustration, the "owners" of lawfully made copies do not come into being until the copies are made by the consumer. Thus, retailers are not the "owners of lawfully made copies," and Section 109(a) does not apply at the retail level. Instead, copyright holders get to control retail competition because each retailer must have the copyright holder's permission to let each of their individual customers download the copy. As a result, the copyright holder can shut any retailer out of the business entirely because, as illustrated in **Figure 4**, the retailer needs the copyright holder's consent to download copies from a licensed retail competitor, and also to allow its own customers, in turn, to download copies from its own site:

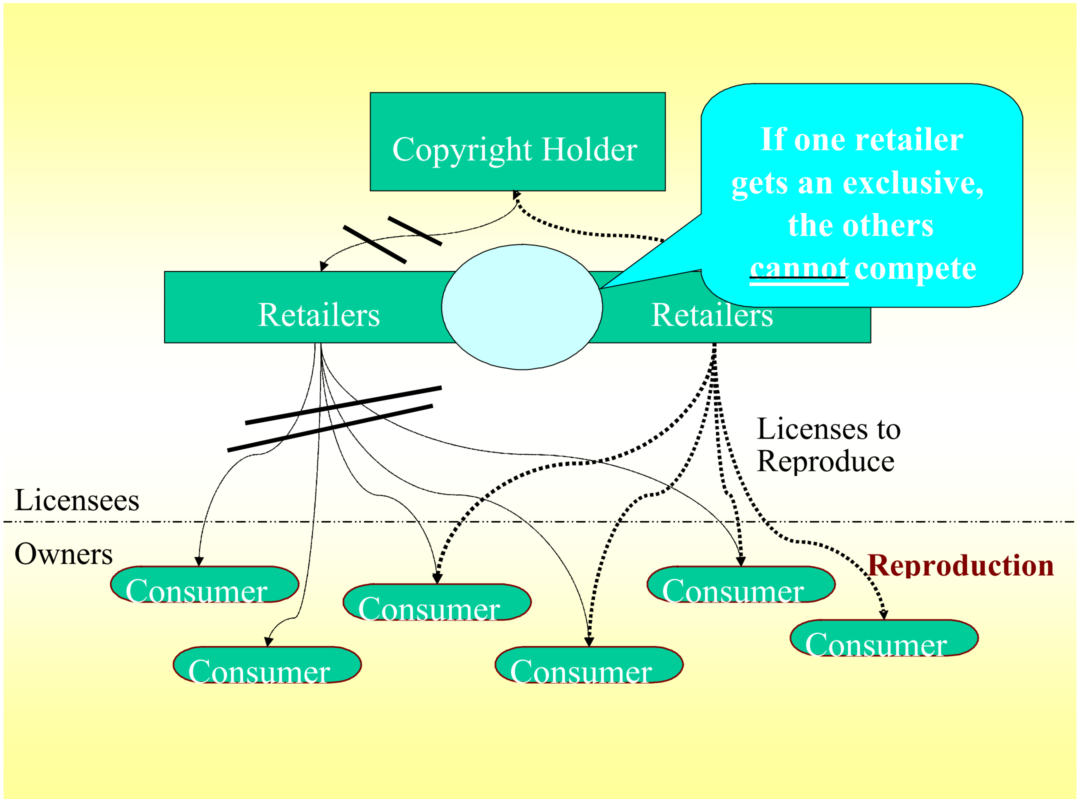

Figure 4

Legal copies may be available from the consumers (if, for example, their licensed copies were made on CDs or DVDs), and the excluded retailer is legally free to buy those lawfully made copies for resale or rental. Likewise, the excluded retailer could lawfully make its own copies on CDs or DVDs by acquiring licenses to do so from the authorized retailer. In both cases, however, the excluded retailer is prevented from competing with the favored retailer in online delivery, and can only offer the physical copies for sale or rental.[12] The excluded retailer cannot lawfully offer its customers a sublicense to reproduce copies of the same work.

Thus, we have established that regardless of the merits of exclusive dealing (or selective refusals to deal) in pre-manufactured copyrighted copies, exclusive dealing in post-manufactured copies restrains trade more completely because the excluded dealer is denied even an indirect means of obtaining the product. Indeed, any justification for surviving a rule of reason analysis in the restraint of trade in pre-manufactured copies disappears in the case of restraints of trade in consumer-manufactured copies.

As a preliminary step to our analysis, we should first dispose of the mystique often wrongly associated with "copies" under the Copyright Act. Nothing in the Copyright Act elevates the distribution of copies above the reach of antitrust laws. In fact, for the reasons explained below, restraints on the distribution of copies should be given much more scrutiny than restraints on distribution of "widgets" for antitrust purposes. But two initial observations are fundamental to this analysis. First, Section 202 of the Copyright Act makes clear that we must distinguish between the intellectual property and the physical medium in which a copyrighted work may be embodied. A CD or DVD is a piece of plastic, and Section 202 makes clear that, apart from possible import restrictions, freedom to trade in the tangible media is in no way diminished simply because the blanks have become "copies or phonorecords" by virtue of the fact that a copyrighted work has been embodied in them. Second, it is fair to say that a vast quantity of "widgets" are in fact "copies" by virtue of the fact that they are the physical media in which copyrighted works are embodied. One need look no further than to a Campbell's Soup label in a grocery store. There is no question that any such label may be copyrighted if the label is sufficiently creative to be registered in its own right. The Supreme Court itself did not even blink at the idea of treating hair care products as "copies" under the Copyright Act, not by virtue of the fact that they were hair care products, but because the product labels they bore were the physical media in which a copyrighted work was embodied.[13]

The difference between "copies" under the Copyright Act and widgets, then, is not that widgets are not also copies, because they often are, or at least their labels may be. There are only two real differences, one *de jure*, and the other *de facto*. The *de jure* difference is that one must obtain the consent of the copyright owner to make a "copy" (*i.e.*, a widget that embodies a copyrighted work), whereas one does not need any such permission to copy a widget that does not contain the intellectual property.[14] The *de facto* difference is that any number of licensees can make identical copies of virtually any copyrighted work which is in digital form, whereas the widget itself (whether a copy or not) will likely involve greater variations in quality or require more complex adherence to quality specifications.[15] These differences mean that, as it relates to digital "distribution,"[16] virtually all of the factors that can serve as pro-competitive justifications for exclusionary or discriminatory treatment in the distribution of pre-manufactured copies disappear when dealing with the licensing of consumer-manufactured copies. The "bits" are the same in either case, but in the latter, the consumer is in charge of quality control over the recording medium.

Cases abound in which a manufacturer of widgets (whether "copies" or not) chooses to deal exclusively with consumers directly, to deal exclusively through certain branded retailers, exclusively through any number of distributors that choose their own dealers or directly with some large retailers while supplying smaller ones through independent distributors, some of which may sell to smaller distributors. The justifications, however, largely relate to the manufacturer making a tactical decision concerning how to distribute its widgets most competitively with the widgets of other manufacturers. That is, it will generally not be in the widget manufacturer's interest to restrict distribution absent some pro-competitive reason, such as to simplify otherwise complex distribution logistics, to rely on dealers dedicated exclusively to promoting its brand, creating incentives for such dealers by carving out exclusive territories, or simply relying on only a few dealers in order to make the most effective use of scarce training and dealer support service capability.

These justifications begin to crumble, however, where the purpose for buying a widget is to gain access to the copyrighted work embodied in it (as opposed to gaining access to the soup or hair care product enveloped in a copyrighted label), they fall away even more where physical distribution is replaced by licensing consumer reproductions into copies, and disappear completely where the restraints are imposed by copyright holding companies which have aggregated the rights to a large number of separate copyrighted works into a single commercial enterprise.

The justifications for restraints based on inter-brand competition are unfounded when applied to digital distribution, largely because there is virtually no competition with respect to copyrighted works by "brand." That is, consumers do not go shopping for a brand of copyrighted work, but for the work itself. For example, it would be odd in the extreme for a couple on a date to say "which would you rather see tonight, a Vivendi-Universal film or an AOL/Time Warner film?" Some motion picture brands may carry a degree of association with the genre of the product, such that the "Caballero" brand may be associated with erotic movies and the "Disney" brand is associated with a family-friendly image (prompting Disney to establish the "Miramax" brand for its movies that might otherwise tarnish that image), but even if the consumer is attracted to the Disney brand, the decision on what film to watch has more to do with the strength of the particular film than the brand. When it comes to cars, computers, or vacuum cleaners, consumers may prefer one manufacturer over another, and shop for the model that best meets their budget and needs within a given brand. With copyrighted works, in contrast, the fan of Woody Alan films is not going to think more or less of a Woody Alan film just because it is associated with a different studio. One may routinely see retailers of cars, computers or vacuum cleaners carry only one or a small number of select brands, yet very rarely see any retailer deal exclusively in the works for a single copyright holder. Even in the rare instance of studio-owned retail stores like Warner Brothers and Disney, the copyright holder's purpose for the store is not to position itself as a significant competitive choice for consumers who want to rent or buy movies, but to use the stores largely as promotional vehicles to generate greater interest in their copyrighted works in general. Even on the Internet, efforts by major copyright holding companies to develop a "branded" destination site dedicated to the works in which they owned the copyrights have, to date, been commercial failures (while those independent companies that sought to compete with them by aggregating works based upon consumer demand have largely been bought out or run out of business).[17]

And, speaking of Internet or other electronic "distribution," the justifications based upon the logistics of physical distribution also fall away. Anyone familiar with setting up a business to offer downloaded copyrighted works knows that the cost of delivery may rival that of physical distribution, given the need to acquire server space and transmission band-width, to install customer service, security and accounting software, and to design and maintain the consumer interface. But these logistical factors cannot be used as a basis for finding a pro-competitive justification for exclusive dealing or other refusals to deal, or for discriminatory terms, because electronic distribution is entirely scalable. For the copyright holder receiving payment, getting a wire transfer of $100 is just as costly as getting one for $100,000. A contract that says "pay me one dollar for every reproduction of my movie you sublicense" is just as costly if the licensee sublicenses 10 downloads or 10,000. It costs the copyright holder nothing more if one million more licensed reproductions are made by its licensees. To be sure, the retailer sublicensing the reproduction to its customers will incur a significant incremental cost with each download, but even so, that cost is born entirely by the retailer. Figuratively, for the copyright holder, if a truck is required to deliver to the retailer a license to sublicense the reproduction of copies, the cost of a truckload of one copy and a truckload of one million copies is the same. The copyright holder may feel it has a greater interest in a licensee's financial ability to pay for the license if a million copies might be made, but the retailer who poses a financial risk of non-payment can certainly be asked for accelerated or even advance payments, such that the copyright holder can be guaranteed to receive a positive revenue flow even if an unworkable business model or faulty implementation bankrupts the licensee.

Thus, though risk-based adjustments may be in order, there is certainly no need for exclusion of competitors due to volume, store size (or shelf space), geographic location or distribution costs. In fact, the copyright holder need not concern itself with whether a prospective licensee's business model is sound, provided the licensee has the means to pay the license fees until it goes out of business. Lack of faith in the licensee's skill or business model is simply not a legitimate basis for exclusion.

Finally, any pro-competitive rationale falls away in the case of the major copyright holding companies that have aggregated numerous copyrighted works. A small publisher or self-published author may find that, because its access to major distribution networks is limited or it risks getting "lost in the shuffle" among major accounts, it prefers to locate or develop niche outlets to showcase its works. The author of an instructional audiovisual work, for example, may find that it can sell more copies (reproductions) by offering it through an Internet site that specializes in the area to which the instruction pertains, and may find that the only way to get the attention of that Internet site is to offer it an exclusive. The major copyright holding companies, in contrast, are tantamount to "essential facilities" for retailers. While a retailer may be able to survive without access to a given instructional video, no video retailer but a rare narrow specialist can survive without access to the works distributed through each of the seven major motion picture copyright holding companies, Warner/New Line, Universal/Dreamworks/USA, Buena Vista (Disney), Columbia TriStar (Sony), Paramount (Viacom), Fox, and MGM.[18] That is because the creative authors (writers, actors, directors) of motion pictures know that they can expect far better results having their film distributed through one of the major motion picture studios, since most of the top grossing films are, in fact, available exclusively through them.[19] Thus, while it might be feasible for a movie retailer to pass up or operate without access to isolated films, a retailer consistently denied access to the films controlled by one of the major motion picture studios (each of which controls from 4% to 20% of the supply of movies based on rental market demand[20]) would effectively be made unable to compete in a retail market in which the ability to aggregate the appropriate selection of motion pictures in highest demand is essential, since, as noted above, consumers do not shop by studio brand but by the strength of each individual copyrighted title. Unlike the small independent studio or individual author, then, the major copyright holding companies (*i.e.* the seven major motion picture studios) have no pro-competitive reason to exclude individual retail outlets, whether in physical stores or their online counterparts. Systematic exclusion is tantamount to elimination.[21]

In sum, where the studio is not involved in retail competition (and even where the studio is involved in retail competition at the physical goods level), there is no economic incentive for the studio to pick and choose among competing retail outlets to decide which should be successful. Any effort to eliminate a retail competitor in the sale of factory-made copies would run up against the excluded retailer's privilege under Section 109(a) of the Copyright Act to buy and resell or rent copies from any available source.[22] The exclusion of a retailer from participation in the delivery of downloadable copies, however, would be severely crippling, as the retailer could not compete at all in the market for consumer-made copies. If the copyright holding company chooses, then, to compete in the final retail delivery to the consumer, it has the power to suppress or eliminate any independent competitor of its choosing.

Moreover, since the aggregator function of retailers is essential, each copyright holder that chooses to compete in the retail market for downloads by excluding the most serious retail competitors will also find it essential to either cross-license to other copyright holder/retailers or joint venture with other copyright holders/retailers to realize the supply-aggregation/competitor-exclusion objective. Of course, since each copyright holder/retailer must be able to aggregate the works from other copyright holder/retailers, each will have every reason to cross-license the reproduction of their works to the other copyright holders, or to a joint venture to which they belong.

Indeed, the heads of the home video divisions of two of the largest motion picture studios acknowledged as much. As reported by a major trade publication:

> Both [Sony Pictures Digital Entertainment president Yair] Landau and [Warner Home Video president Warren] Lieberfarb said the studios' plans [for Internet-based video distribution] were for non-exclusive deals. <u>Consumers preferred to go to one place to find movies as they do in a retail environment so it didn't make sense for each studio to create its own Internet movie service.</u>
>
> "We can't wait for the movie equivalent of Napster," Landau said. <u>Studios must work together and act swiftly or "you're opening it up to someone else to aggregate the services.</u>"[23]

These studios evidently recognize the competitive advantage of aggregating films from all sources, based upon consumer demand rather than copyright ownership. Just as clearly, they fear having to compete with "someone else" who may become the aggregator of choice, and a counterpart to working together to preempt that is, most logically, to deny licenses to those who would be their competitors.[24]

At best, the excluded independent retailer could continue to trade in consumer-made (or retailer-made) copies using the licensed download services of one of its competitors, but the resulting copies would not substitute for the demand of a customer wishing to make a licensed copy by downloading. Unfortunately, as we shall see in the next section, even this limited ability to compete is also being denied, as digital technology is harnessed to eliminate sub-distribution of copies lawfully made under license by consumers or excluded retailers, and even competition in the redistribution of copies pre-manufactured in licensed factories.

II. Private Extension of the Scope of Intellectual Property Rights

As noted above, even where retailers are excluded from the market for authorizing consumers to manufacture legal copies at home (instead of purchasing those manufactured in a factory), there remains a viable market for the reselling of lawfully made copies. **Figure 5a** illustrates how, once the copies are lawfully made, Section 109(a) of the Copyright Act assures the continued private and commercial exchange of those copies without the consent of or control by the copyright holder:

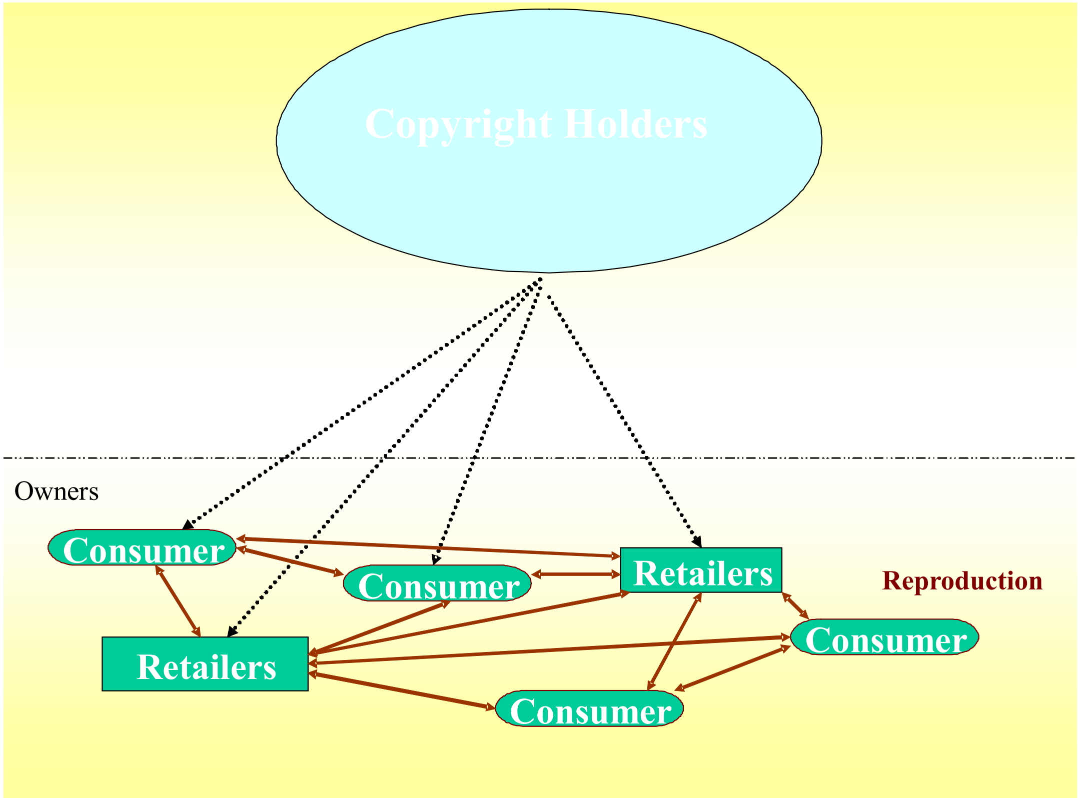

Figure 5a

Section 109(a) of the Copyright Act assures that retailers and consumers who own lawfully made copies are legally free from "any control whatever" by the copyright holder. The rationale for this provision is that the right of distribution can serve to protect the copyright owner's interest when pirated or stolen copies are distributed, but once title to a lawful copy has passed to another, "the policy favoring a copyright monopoly for authors gives way to the policy opposing restraints of trade and restraints on alienation."[25] As a result, while most consumers may acquire their merchandise from retailers or directly from the copyright holder, some consumers, as noted in **Figure 5a**, may also obtain their merchandise from each other (whether by purchasing, trading, borrowing, receiving as a gift or inheritance, or even retrieval from the garbage[26]).

Lawful copies can be mass produced at a factory or singularly by a mass of retailers or consumers at business or home computers. The owner of a lawfully made copy is the owner regardless whether the copy was purchased or, after the purchase of a blank medium, lawfully made by exercising a license to make a copy.[27] A person who lawfully makes a copy of a motion picture through a digital download at a retail location or at home is authorized, under Section 109(a), to sell it to the highest bidder, loan it, trade it or give it away, and the copyright holder is powerless under the Copyright Act to prevent it. Video retailers would also be free to rent them for profit, just as is the practice today with audiovisual works recorded on videocassettes and DVDs. But all of these lawful practices are at risk, as steps are already being taken to restrain all trade that is not expressly authorized by the copyright holding company or the joint venture with which it is aligned.

Circumventing the Owner's Entitlement to Trade

Today, technological restraints have been fashioned to give copyright holders *de facto* control over the distribution and use of copyrighted works where *de jure* control has been denied. Some in the copyright holder community seek to disable the protections that copyright law provides to legal owners of lawfully made copies of copyrighted works – and to expand the limited privileges granted to copyright holders by Congress – in order to control the lawful distribution and use of copyrighted materials into areas Congress has expressly denied to them. They seek this control in order to impose a business model under which they can charge for repeated use or multiple users of copyrighted works and, to that end, to prevent any consumer who acquires possession of a lawful copy by purchase or rental from being able to enjoy the contents of that copy without express permission from (and/or payment to) the copyright holder or its joint venture.

Though the owners of lawfully made copies have the <u>right</u> to sell them, lend them, give them and rent them, and though the copyright holders have no right to prevent such trade or commerce, the technological restraints which shall be described below have the purpose and effect of turning the lawfully made copy into a worthless piece of plastic the moment it is transferred in commerce, even by gift or inheritance. Instead of a flourishing trade and commerce as illustrated in **Figure 5a**, above, we will have the total cessation of business-to-business, business-to-consumer and consumer-to-consumer trade and commerce, as illustrated in **Figure 5b**:

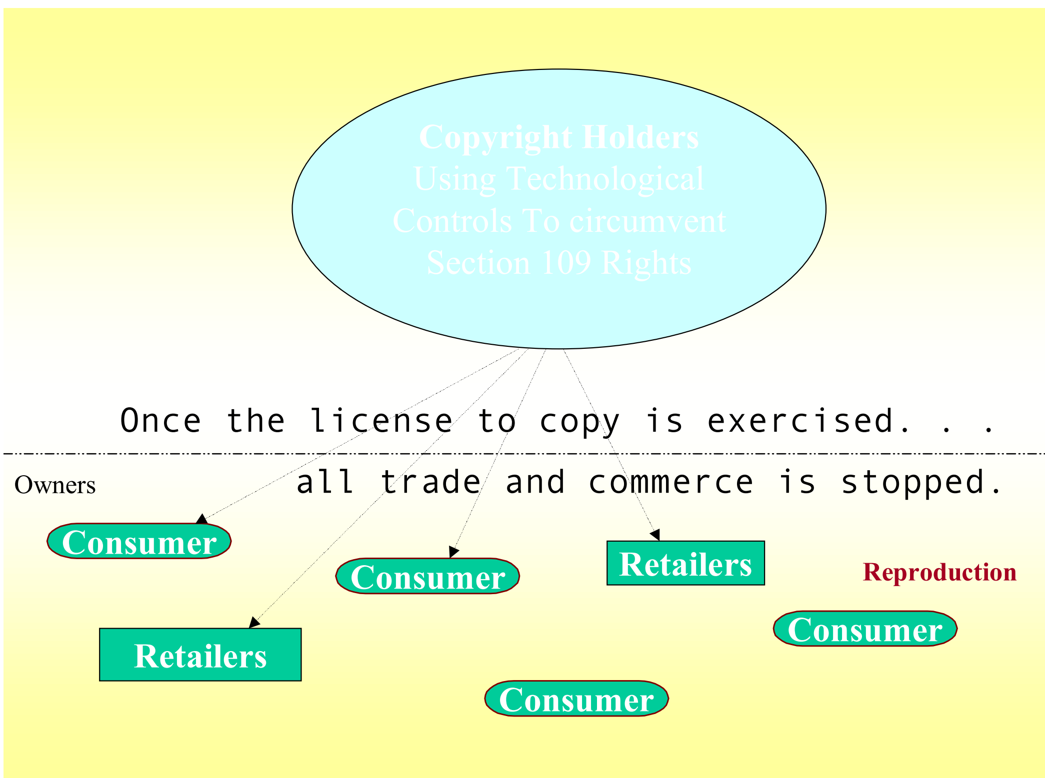

Figure 5b

Notably, some consumers who would have obtained their copies by gift, by trade, or by purchasing them though the "previously-viewed" market are cut completely off from the market, and will have no choice but to do business directly with the copyright holder at the original price. Perhaps in some industries, such restrictions would not raise concern. Certainly, if an automobile manufacturer had the power to prohibit any purchaser from selling, renting, lending or giving away its vehicles, it might theoretically increase demand for its new vehicles, but given the many alternatives, consumers would likely gravitate to other manufacturers who did not restrain their actions. Copyrighted works, in contrast, are so unique[28] that Congress saw fit to prohibit those who chose the benefits of copyright protection from placing such restraints on the alienability of copies of their works. In testimony before the Copyright Office, copyright holding companies acknowledged the fact that Section 109(a) authorizes the owners of lawfully made downloads to sell or otherwise dispose of their copies without the consent of the copyright holder,[29] but concurrently took the position that they are nevertheless free (against the wishes of Congress) to control the distribution and use of digitally delivered copyrighted works through non-negotiable contracts and access control technology.[30]

The technology exists today to enable copyright holders to prevent lawful trade in, and other lawful uses of, lawfully made copies. But because Section 109(a) of the Copyright Act furthers the important dual public policies of promoting competition and maximizing dissemination of copyrighted works, the regulatory agencies should ensure that the rights it confers are not extinguished either by non-negotiable contracts or technological controls. To conclude otherwise would make the rights granted by Congress and the first sale doctrine merely contingent on the technological prowess or goodwill of copyright holders.[31]

Indeed, the current prognosis is dire precisely because copyright holders have become more bold in seeking to employ technology where the rights of their competitors and consumers would otherwise thwart them. For example, Sony Music Entertainment has included "End User License Agreements" (commonly known as "EULAs") on some of its factory-made CDs, purporting to trump the consumers' right to dispose of their copies. An excerpt from the "readme.txt" file Sony placed on its factory-made CDs is as follows:

> SONY MUSIC ENTERTAINMENT INC. LICENSE AGREEMENT
> This legal agreement between you as end user and Sony Music Entertainment Inc. concerns this product, hereafter referred to as Software. By using and installing this disc, you agree to be bound by the terms of this agreement. If you do not agree with this licensing agreement, please return the CD in its original packaging with register receipt within 7 days from time of purchase to: Sony Music Entertainment Inc., Radio City Station, P.O. Box 844, New York, NY 10101-0844, for a full refund.
>
> 1. LICENSE; COPYRIGHT; RESTRICTIONS. You may install **and use your copy of the Software on a single computer**. You may not network the Software or otherwise use or install it on more than one computer or terminal at the same time. The Software(including any images, text, photographs, animations, video, audio, and music) is owned by Sony Music Entertainment Inc. or its suppliers and is protected by United States copyright laws and its international treaty provisions. **You may not rent, <u>distribute</u>, <u>transfer</u> or lease**

> **the Software.** `You may not reverse engineer, disassemble, decompile or translate the Software.`[32]

Thus, any owners of the CD who play it in a computer are purported to have waived all of their rights under Section 109(a) of the Copyright Act, <u>and</u> have partially waived their right of private performance, unless they return it to Sony within seven days of purchase. Having played it on one computer, they are prohibited from ever playing it on another (you may "use" it on only one computer), despite the fact that the Copyright Act confers no such right to the copyright holder to control "use" in general, nor to limit the number of computers upon which it may be played. Note also that the "Software" is defined as the "product" – the CD itself. The plain meaning of the EULA is to restrain the physical distribution or transfer of the CD – distribution which Section 109(a) absolutely authorizes the owner to do without Sony's consent. (Since this is done through a EULA, analysis of such restraint would come under Section 1 of the Sherman Act.)

Extending this concept to copies lawfully made through a digital download, the intent of Universal Music in its failed "Blue Matter" venture was to enter into EULAs in restraint of trade to an even greater extent by prohibiting even the transfer of lawfully made copies through a decedent's estate. All trade was eliminated. In fact, the plain language of Universal's EULA meant that a computer containing a collection of copies lawfully made could not be transferred under any circumstances without first destroying the legal copies.[33]

Adobe Systems has attempted to actually enforce EULAs against owners of lawfully made copies to trump the statutory right to compete in the sale of the product. In one case, it persuaded a U.S. District Court that its employment of a EULA restricting re-sales of a particular lawfully made copy to only certain buyers was enough to convert a sale into a "license" to use the copy only in accord with Adobe's restrictions on trade.[34] Fortunately, in a more recent case the owner of the lawfully made copies of Adobe's works sought a declaratory judgment challenging Adobe's right to restrain trade through use of EULAs. Adobe, as the copyright holder, purported to use a "license" over rights it did not own to prohibit a retailer from unbundling three separate works that Adobe had bundled together and wanted to keep tied at the retail level.[35] The court ruled in favor of the retailer for several reasons, and its analysis of the public interest warrants special attention here, as it addresses the public interest at the intersection of intellectual property and competition law:

> The Court finds that the provisions contained in Adobe's EULA purport to diminish the rights of customers to use the software in ways ordinarily enjoyed by customers under copyright law. Therefore, these restrictions appear to be inconsistent with the balance of rights set forth in intellectual property law. Commentators have noted that the arguments for enforcing this balance are particularly persuasive in the context of shrinkwrap licenses because the balance of rights in intellectual property law is already tilted heavily in favor of the intellectual property owner. "The only countervailing forces favoring users are those rights specifically granted to users by federal law. In this context more than any other, therefore, it is justifiable to fear that removing or

> eviscerating those user rights may bring the whole edifice crumbling down."
>
> This is an area fraught with conflicting policy considerations. Software publishers are desirous of augmenting the protections offered under copyright law. In this case, through the use of licensing, Adobe seeks a vast and seemingly unlimited power to control prices and all channels of distribution. On the other hand, in the absence of copyright law violations, the market can often best regulate prices and all subsequent transactions that occur after the first sale. Sound policy rationales support the analysis of those courts that have found shrinkwrap licenses to be unenforceable. A system of "licensing" which grants software publishers this degree of unchecked power to control the market deserves to be the object of careful scrutiny.[36]

As both a practical and legal matter, copyright holders may find it difficult to control or suppress the market for redistribution of copies of their works using "click-through" or "shrinkwarp" license agreements. We may laugh off efforts such as those of Sony and Universal, questioning whether they could ever enforce such agreements either as a practical matter or as a matter of law <u>without</u> regard to whether they violate the Sherman Act. We may chuckle at the extremes to which Adobe has gone to actually litigate its ability to restrain trade through EULAs. But the humor quickly vanishes with the realization that such efforts to extend the copyright holder's rights and restrain trade no longer require the use of agreements such as these EULAs, but may be unilaterally deployed using technological access controls. The major copyright holders have now seized upon the use of "access control technologies" that serve to either "enforce" the aforesaid terms or, as now appears to be the norm, to simply impose their will without even the semblance of agreement.[37]

The two most popular access control technologies in use today (and reportedly intended to be implemented as part of horizontal agreements to carry out joint ventures such as Movielink, as will be discussed below) automatically disable the copy after a certain amount of time or number of plays ("timing out") and/or prevent the copy from being played on any device other than the device through which it was downloaded or unlocked[38] ("tethering"). Neither of these technologies directly protects intellectual property rights of the copyright holder (such as the exclusive right of reproduction, or the exclusive right to perform a work publicly). Instead, they each directly impair rights belonging to the public – rights that Congress expressly denied the copyright holder. Each secures to the copyright holders the ability to suppress or control private performances (see below). Each also directly impairs all trade and commerce authorized in Section 109(a) unless the copyright holder authorizes it, despite the fact that Section 109(a), by its own terms, states that the owner may conduct such trade without the consent of the copyright holder.

<u>**Tethering**</u>, for example, binds the copy to either the equipment through which the copy was made or through which the copy was first accessed.[39] Any attempt to play the movie in a different machine will either result in failure or in an invitation to "purchase" another "license" (access) to play the movie. <u>**Timing out**</u> serves a similar function, in that time is allowed in which to watch the movie after the initial decryption (such as two performances, or unlimited

performances within a 24-hour period), after which the movie cannot be played without paying for an additional access period. Thus, the next person to receive the article in trade or commerce is prevented, by the copyright holder or its licensee, from privately performing the work.

There are two primary problems with this restraint on trade. The first is evident, in that, as discussed above, the Copyright Act grants owners of lawfully made copies the authority to dispose of their copies without consent of the copyright owner. Thus, these technologies serve to restrain all trade in these copies by disabling the economic or personal value the transferor and transferee would hope to derive from the transaction. Such restraint is in direct conflict with Section 109(a) of the Copyright Act and Section 2 of the Sherman Act.[40]

Second, these restraints serve to unilaterally expand the scope of the copyright beyond the limits imposed by Congress. One of those limits is the right to authorize public performances, limited by the denial of any right to control private performances. By using technological access controls to capture and control a right specifically off limits to copyright holders, copyright holders who do so are engaging in copyright misuse.[41] It is, perhaps, open to debate whether agreements entered into with the purpose and effect of restraining the public's right to perform works privately can be deemed to be a violation of Section 1 of the Sherman Act, but certainly such restraints violate the limits imposed by the Copyright Act and, because they leverage the lawful copyright monopoly into control over private performances and retail trade of articles not owned by the copyright owner, they violate Section 2 of the Sherman Act in the same manner as the "block booking" condemned by the Supreme Court.[42]

Usurpation of the Right to Perform a Work Privately

The Copyright Act gives copyright holders the exclusive right to perform a work "publicly," Section 106(4), but conveys absolutely no copyright in private performances. The freedom to perform works (including copyrighted works) privately is a right reserved to the public. Unless the public performance constitutes fair use under Section 107, the owners of lawful copies need licenses to play them in public, just like anyone else, but no one – whether the owner of the copy or not – needs anyone's permission to play them at home for private enjoyment. Just as any member of the public is free from any copyright restriction against reading a book privately or reading aloud to their child, any member of the public is free from copyright control over listening to copyrighted music or watching a copyrighted motion picture. Though it may seem strange at first blush, it is entirely consistent with the structure of the Copyright Act that it is not a copyright infringement for a thief to watch (privately perform) a stolen movie. And though a person who makes an illegal copy will have violated the right of reproduction (and would violate the right of distribution if he or she sells it), it is perfectly lawful for the pirate to watch the pirated movie. But we need not dwell on these extraordinary examples, for the concern over these restraints of trade (and concomitant enlargement of copyright power) is not with its impact on the thief or the pirate (for the law is hardly concerned with whether the pirate selling illegal copies by the thousands paused long enough to privately perform one of them). Rather, the concern is for the law-abiding individual who purchases, rents or borrows a lawfully made copy, who manufactures a lawfully made copy under a reproduction license, or who receives a lawful copy as a gift, and who is prevented from exercising the right to perform the work privately because the copyright owner has employed technological tools to take control over such right – control which Congress preferred to deny.

Just as the exclusive right to perform the work publicly belongs to the copyright owner no matter who owns the copy being performed and regardless whether the copy was lawfully made, conversely, the copyright owner has no right to control the private performances of a work, no matter who owns the copy and regardless whether it was lawfully made. In short, there is no copyright to control or in any way limit the private performance of a motion picture. For a motion picture studio to limit such performances is, from a legal perspective, the same as preventing parents from reading books to their own children. Unfortunately, by use of technological access controls, the major copyright holding companies are exercising increasing control over entirely private performances.

The individual's right to perform works privately is not dependent upon whether the private performance is made from a factory-made copy or a homemade copy (or even from memory, like singing a song in the shower). As noted above, a downloaded movie is no less a lawfully made copy than a factory made copy. Unless privileged, such as under Section 107, both require the consent of the copyright owner if they are to be lawfully made. Copies made in a factory without consent of the copyright owner, like copies downloaded without consent, may be subject to forfeiture and destruction, and the perpetrator may be subject to civil and criminal penalties. On the other hand, copies made in a factory with the consent of the copyright owner, just like copies downloaded with such consent, are "lawfully made" in that the consent to make the copy is an exercise of the copyright owner's exclusive right of reproduction. Both are licensed copies.

The techno-legal differences between downloading and streaming

Why discuss downloads – reproductions – under the heading of usurpation of the right of private performance? Because of the need to distinguish "downloading" (reproductions) from "streaming" (public performances). Both may be made over the Internet, and consequently there is often a blurring of the line between the rights a copyright holder may lawfully exercise over one and the other. So, before discussing the law of public and private performances, we should clarify the distinction between private performances of downloaded copies, on the one hand, and public performances by streaming, on the other.

The following illustration in **Figure 6** may offer a better understanding of the technical and legal distinctions between a "download" and a "stream" of a movie over the Internet:

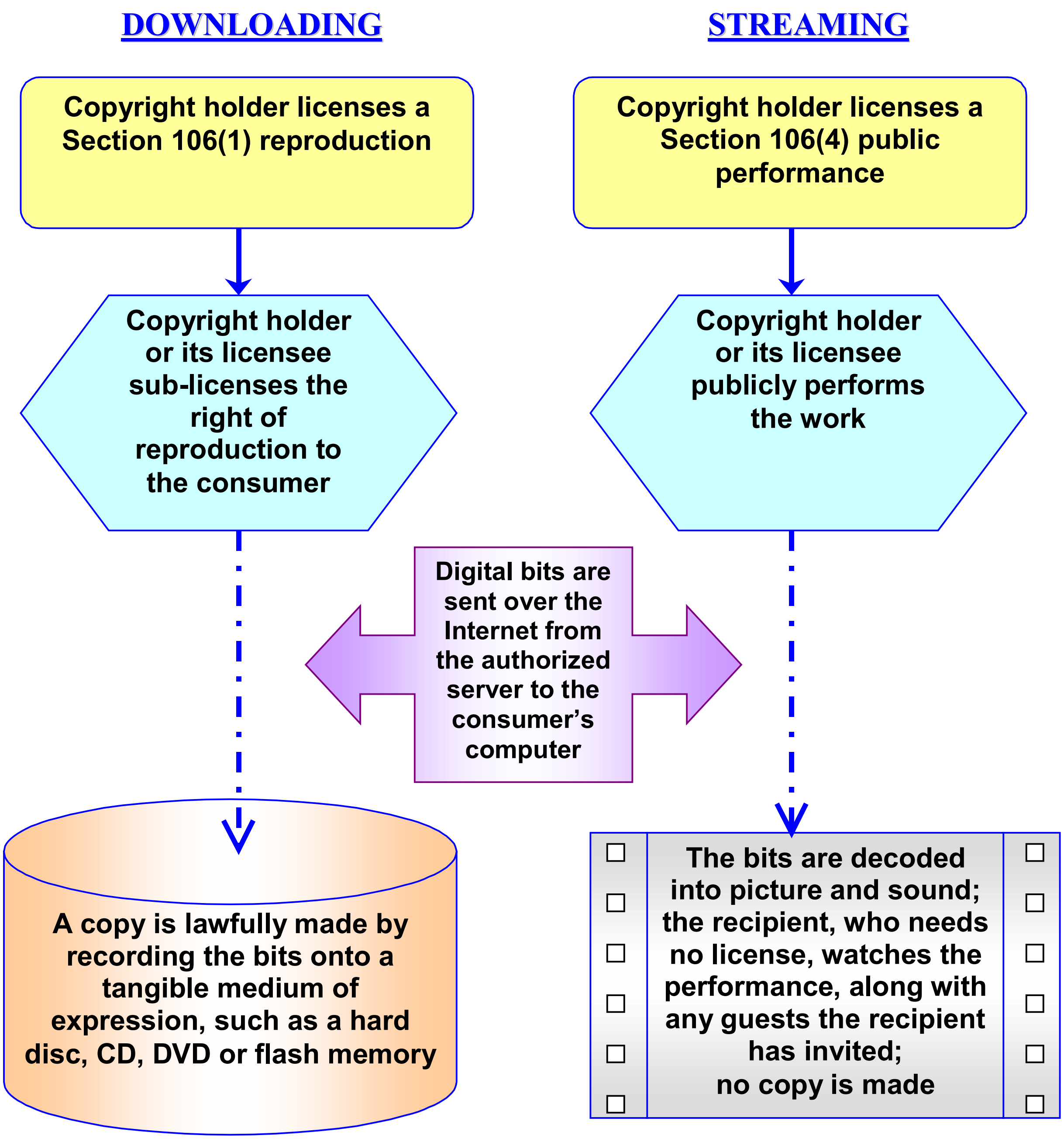

Figure 6

Thus, when a copy of a movie is downloaded, the movie may lawfully be performed privately no matter who owns the downloaded copy, and no matter in what tangible medium of expression the movie is embodied.[43] In contrast, the streaming of a copy constitutes a public performance by definition, and must ordinarily be licensed by the copyright owner. Watching a licensed public performance, however, requires no license.[44]

The statutory treatment of streaming

Section 106(4) of the Copyright Act grants the author of a work the exclusive right "to perform the copyrighted work publicly."

Section 101 states that to "perform" a work (without qualification as to public or private) "means to recite, render, play, dance, or act it, either directly or by means of any device or process or, in the case of a motion picture or other audiovisual work, to show its images in any sequence or to make the sounds accompanying it audible."

Section 101 goes on to specify that to perform a work "publicly" means one of two methods of performing it:

> (1) to perform . . . it at a place open to the public or at any place where a substantial number of persons outside of a normal circle of a family and its social acquaintances is gathered; or
>
> (2) to transmit or otherwise communicate a performance . . . of the work to a place specified by clause (1) or to the public, by means of any device or process, whether the members of the public capable of receiving the performance . . . receive it in the same place or in separate places and at the same time or at different times.

Thus, the statutory framework establishes that if you play the movie at home, whether from a VHS tape, a CD, a DVD, or a downloaded file, it is <u>not a public performance</u>. If someone else performs it by transmitting the performance over wires or over the air to your home, however, it <u>is</u> a public performance. Thus, playing a downloaded file at home is not a public performance. Streaming the performance constitutes a public performance by the transmitting entity. (Of course, enjoying a streamed program infringes no copyrights, even if the receiving person has not paid for it. Even the theft of a cable signal is not a copyright infringement.[45])

In the pre-Internet days, the Supreme Court had occasion to explain these differences as follows:

> The Copyright Act does not give the copyright holder control over all uses of his copyrighted work. Instead, §1 [now 106] of the Act enumerates several "rights" that are made "exclusive" to the holder of the copyright. If a person, without authorization from the copyright holder, puts a copyrighted work . . . to a use not enumerated in § 1, he does not infringe.[46]

Citing this passage, the Court illustrated:

> Accordingly, if an unlicensed use of a copyrighted work does not conflict with an "exclusive" right conferred by the statute, it is no infringement of the holder's rights. No license is required by the Copyright Act, for example, to sing a copyrighted lyric in the shower.[47]

No license is required to sing in the shower, nor to play a movie in the living room, because the exclusive right of private performance is excluded from the copyright grant.

The advent of the VCR brought with it entrepreneurial business models that tested the lines between public and non-public performances. In his dissent in the Betamax case, Justice Blackmun objected to the majority's exemption for private time-shifting reproductions, contrasting it with the explicit statutory exemption for private performances:

> When Congress intended special and protective treatment for private use, moreover, it said so explicitly. One such explicit statement appears in § 106 itself. The copyright owner's exclusive right to *perform* a copyrighted work, in contrast to his right to reproduce the work in copies, is limited. Section 106(4) grants a copyright owner the exclusive right to perform the work "publicly," but does not afford the owner protection with respect to private performances by others. A motion picture is "performed" whenever its images are shown or its sounds are made audible. § 101. Like "[singing] a copyrighted lyric in the shower," *Twentieth Century Music Corp*. v. *Aiken*, 422 U.S. 151, 155 (1975), watching television at home with one's family and friends is now considered a performance. 1975 Senate Report 59-60; 1976 House Report 63. Home television viewing nevertheless does not infringe any copyright – but only because § 106(4) contains the word "publicly." See generally 1975 Senate Report 60-61; 1976 House Report 63-64; Register's 1961 Report 29-30.[48]

Footnote 19 of Justice Blackmun's dissent warrants special attention:

> One purpose for the exemption for private performances was to permit the home viewing of lawfully made videotapes. The Register [of Copyrights] noted in 1961 that "[n]ew technical devices will probably make it practical in the future to reproduce televised motion pictures in the home. We do not believe the private *use* of such a reproduction can or should be precluded by copyright."[49]

Though Justice Blackmun went on to distinguish between the unlicensed performance of a home-taped movie and the unlicensed reproduction, there can be no doubt that the private performance of a lawfully reproduced copy is not an infringement of any of the exclusive rights.

Once the legality of the home video market was established, some entrepreneurs tested the boundary between public and private performances. Two leading cases discuss the elements of the statutory meaning of to "perform" a work "publicly," and address both prongs of the public performance (clause (1), involving performances to the "public," and clause (2), involving transmissions to a remote location).

The Ninth Circuit held that it was not an infringement of the right of public performance for a hotel to rent videodiscs to guests, who then performed them in the privacy of their guest rooms using hotel equipment located in the room.[50] Two years later, a hotel operator sought a declaratory judgment approving of a variation on this model, where the hotel used a bank of centrally located VCRs that each guest could operate remotely to view the movie in the privacy of the hotel room. Even though the structure was virtually the same in that they both required the playing of a lawfully owned VHS tape in a VCR, and only one guest could watch a movie at a time, the court held that such performances were not public under the first clause of the definition, but were public under the second clause because they were transmitted from a remote location.[51]

Together, these two cases offer a sound analytical framework for determining whether a given performance is public, and therefore under the exclusive control of the copyright holder, or private, and therefore beyond the reach of the copyright holder. Where digital copies are used instead of analog tapes, the outcome is the same: People who play movies in the privacy of their hotel rooms or homes are not performing the work publicly no matter whether they or the hotel own the copies. But the transmission ("streaming") of a performance of a movie to a remote location, though such location be a hotel room or a private home, constitutes a public performance under clause (2).

Of course, the person watching the public performance, whether from the bank of VCRs in the hotel or over the Internet, is not engaging in a public performance. From the consumer's perspective, the issue is much simpler: consumers can privately play what they own as often as they wish, and can leave on the radio, the television, or the Internet, tuned to their favorite broadcast or streaming station, and never fear that they will be liable for infringing the right of public performance.

In light of this line between public and private performances drawn by Congress, recognized by the courts and supported by the Register of Copyrights, there is good reason to question the legitimacy of leveraging the copyright monopoly into control over private performances by tethering, timing out, or limiting the number of plays. Charging extra for additional private performances is like charging people for the right to listen to the radio. "The exaction of such multiple tribute would go far beyond what is required for the economic protection of copyright owners, and would be wholly at odds with the balanced congressional purpose behind [Section 106(4)]."[52]

Legality of the "subscription" business model in light of the above

Given the statutory and case law background, and bearing in mind the substantive technical and legal distinctions between a download (reproduction) and a stream (public performance), it becomes clear that some of the "business models" embraced by major copyright holding companies attempt to combine elements of downloading and streaming such as to take the benefits of each while avoiding the limitations each would impose.

Often referred to as "subscription" services, these are not like any other subscriptions previously known to man. They are not at all like a magazine subscription, where the subscriber is entitled to keep and re-read (or sell as a collection on eBay) all past issues long after the subscription is cancelled. Nor are they like a cable television subscription, wherein the consumer is entitled to view all public performances by the cable operator so long as the subscription fee is paid. Rather, these online "subscriptions" are more like having membership in the Book-of-the-Month Club, with the added twist that the club members are prohibited from letting anyone read their books, and any who cancel their membership will be prevented from ever again reading any of the existing Book-of-the-Month selections in their libraries.

Though this may sound far-fetched, it is precisely what several major copyright holding companies are attempting to do individually, directly or through licensees, and jointly, through Movielink and similar joint ventures.[53] They could choose to license secure downloads, and give up all control over private performances or sales of the downloaded copies once the download is complete. They could license public performances through streaming, and give up all control over who gets to watch the public performance while knowing that the viewer will not retain a copy. Instead, they have chosen to license the downloading of lawfully made copies tied to technological restraints unrelated to copyright protection. These technological access controls allow them to meter out private performances and to nullify or impose a surcharge upon any lawful transfer of physical copies by sale, gift, rental or otherwise – transfers which Congress has stated may be made without consent of the copyright owner.[54]

Movielink, when operating under its prior name of "MovieFly," appeared to be trying to place a positive "spin" on its restraints on trade and lawful use by characterizing the transaction as a rental[55]:

Figure 12

But cloaking this wolf of a business model in the sheep's clothing of a "rental" is, at a minimum, misleading. No rental is involved, and you don't really get to watch what you want, where you want.

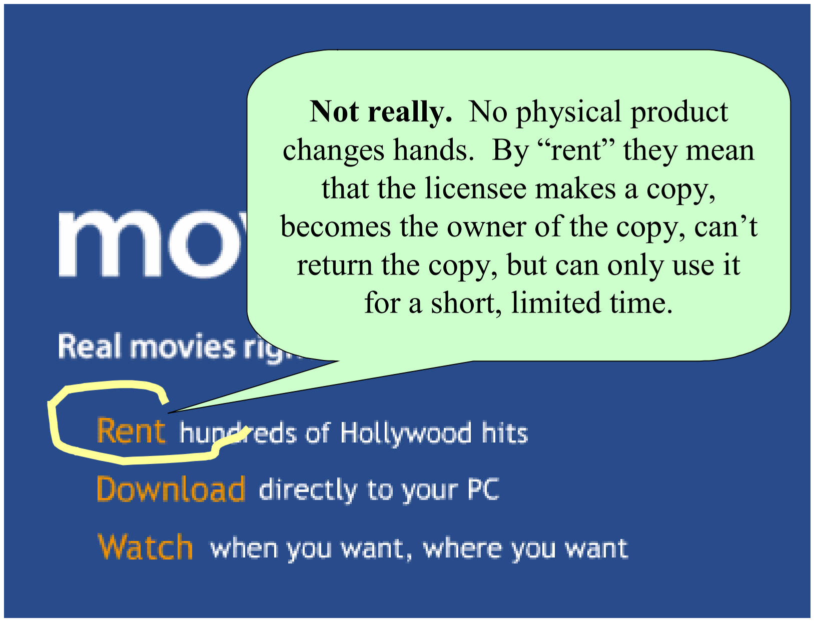

Figure 13

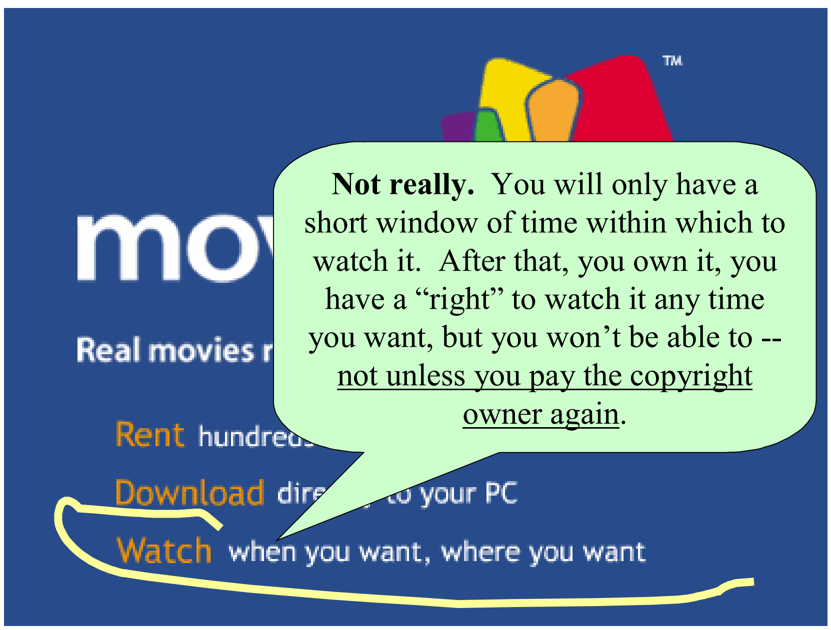

Figure 14

As noted above, Movielink, the successor to MovieFly, presents an even more sinister prospect. It intends to charge a fee for people who own their copies to play them, and is considering whether to disable or actually destroy these copies by use of technology.[56] It matters little whether the consumer solicitation is deceptive or misleading, for even an honest explanation that "we intend to charge you for the exercise of a right of private performance that already belongs to you, and to disable or destroy lawfully made copies you own," fails to cure the destruction of the Copyright Act's balance of rights or the copyright owners' theft of rights belonging to others.

To be sure, there are efficiencies to be gained. The cost of delivering the bits needed to download a copy is the same as the cost of delivering the bits needed to stream a public performance. If the cost of delivery is, for example, $1.00, a consumer who chooses to watch a $3.50 streamed movie twice would pay $7.00, but it would cost $2.00 to stream it twice, and another $1.00 for every friend who wishes to watch it. For a downloaded movie, the cost of delivery is only $1.00 no matter how many times the consumer watches it, and no matter whether the consumer transfers the lawful copy to a friend who watches it repeatedly. Thus, it makes perfect economic sense for copyright holders to try to capture the efficiencies of downloads and use technological restraints upon trade authorized by Section 109(a), plus the elimination of the right of private performance, to gain the revenue from a public performance model at the cost of a reproduction model. The problem is not the economics of the restraint, but its legality. It would certainly make economic sense for copyright holders to be able to charge more for people to read a book twice, to charge a royalty on used book sales, and even tax decedents estates if the books are passed on, but it is not lawful for them to do so. The Copyright Act reserves to the public the right to perform works privately, and entitles the owner of lawfully made copies, whether in book form or digital bits on a tangible storage medium, to sell, rent, lend or give away their lawfully made copies without the copyright owner's consent. It may be economically feasible to privately extend the scope of copyright, but it is certainly not lawful to do so.

III. Impairment of Innovation and Competition In Related Goods and Services

To better appreciate the concern here, let us begin by considering the "brick and mortar" environment of retail sales of factory-made copies. Today, retailers buy the copyrighted copies for resale or rental directly or indirectly from the copyright holder. But unless there is a separately negotiated agreement to promote or merchandise particular titles in particular ways, the copyright holder has no say in what other goods or services the retailer uses. Thus, there is unfettered competition for the retailer's business among suppliers of carpeting, security equipment, signage, advertising services, computer software for a variety of business functions (inventory management, cash registers, transaction reporting, accounting), Internet presence, merchandise displays, and so on. The copyright holder has no power to dictate which of the competing goods and services will be selected by the retailer, and the retailer can improve its competitive posture by wise and creative selection from among these competing goods and services. The copyright confers no power to determine where a retail establishment may be located, or to restrict who can purchase or rent copies from a given location.

In the online world, in contrast, copyright holders are increasingly taking it upon themselves to condition the licensing of intellectual property rights on the independent merchant also acquiring from the copyright holder or its designee the completely separate goods and services needed to carry out the online transaction. Instead of security equipment and merchandise displays, the online equivalent are such things as DRMs, codecs, and media players. (Some of these systems, in turn, may integrate or support a variety of related sub-systems.) The right to reproduce a work in copies (downloading) or the right to publicly perform a work (streaming), for example, is licensed only on condition that the licensee use a specific codec, DRM, or media player. It stands to reason, however, that if it is unlawful to grant a license to publicly perform certain television shows on condition that the licensee agree to pay cash for another television show,[57] so, too, the conditioning of access to a vast library of audiovisual works on the licensee agreeing to use a particular vendor's codec, DRM or media player would also be unlawful – particularly if there are competing technologies which can equally meet any legitimate copyright-related interests of the copyright holder. This is not like a book publisher agreeing to license on condition that a certain quality of paper and bookbinding be used. It is like a book publisher specifying the factory from which the paper must be purchased and the company that must perform the bookbinding service.[58]

The Music Industry's Comparable Track Record

Since the major motion picture studios have yet to license the right to reproduce or publicly perform their works on a sufficiently wide scale to allow serious competitive models to emerge (as they continue to invest in the development of their own joint ventures[59]), let us look at an example in the music industry.[60]

In the music industry, a number of companies compete (or competed) to provide the goods and services needed by retailers[61] to deliver top-of-the-line downloads (reproductions) and streams (public performances), and many retailers raced to be among the first and best to provide these products to consumers. In the early days, emerging codecs competed to demonstrate their technical superiority; emerging DRMs competed to demonstrate their competitive cost and ease of use; emerging media players competed to demonstrate their versatility, quality playback, compatibility, and ease of use. Some companies excelled in small pieces of the delivery puzzle, others provided integrated solutions from multiple companies, and still others attempted to provide comprehensive solutions relying more heavily upon proprietary components. Had competition continued unrestrained, there would have been a number of retailers competing with each other for customers, and each would have been selecting from among the many competing technology solutions needed to deliver the reproduction or public performance in a secure, accountable and quality fashion at the most competitive price.

Instead, retailers found it increasingly difficult to select their own delivery technologies, as copyright holders began to condition the licenses upon the use of a specific set of technologies. Copyright holders insisted that their licenses would be given only on condition that their selected shopping experience and technology would be used.[62] Thus, the power of the copyright was being used to control the market for various goods and services needed to offer digital delivery.[63]

Now that the five major sound recording copyright holding companies have established two joint ventures to capture the retail market for the reproduction and public performance of sound recordings, the result has been that each of the two joint ventures has settled on a single major competing technology provider and, since together they control over 85% of the sound recording copyrights, they have effectively shut out or severely crippled the competitive opportunities available to the competing technologies which could well be cheaper, faster, easier to use, and/or offer better sound quality and compatibility across codecs, but we will never know. MusicNet, a joint venture of RealNetworks, BMG Entertainment, EMI Music and Warner Music Group, has selected RealNetworks for its media player and related technologies, while pressplay, a joint venture of Universal Music Group and Sony Music Entertainment, has selected Microsoft's Media Player.[64] The significance of this selection was not lost on RealNetworks, when it explained the competitive risks in its Quarterly Report for the period ended March 31, 2002.[65]

In short, what could and should be a vibrant market for media players, codecs, copy management software, copyright protection software, and so on, is becoming a short race to see who gets the nod from the two joint ventures of the major copyright holding companies, after which the race, for all practical purposes, will be over, and any independent retailers lucky enough to be allowed to compete with the copyright holding companies will be forced to use the same possibly bloated and certainly less innovative technologies. The same economic package will be offered to the consumer, albeit through different (but no longer differentiated) "licensed" retailers.[66]

Studio Restraints More Onerous Than *Kodak's*

But "the granted monopoly power [in specific motion pictures] does not extend to property [such as DRMs, codecs, media players or retail outlets, nor to rights such as the consumer's right of private performance or the owner's entitlement, under Section 109(a), to dispose of a lawfully made copy without the copyright owner's consent] not covered by the patent or copyright."[67] This is because the public policy granting copyrights "excludes from it all that is not embraced" in the original copyrighted motion picture, and "equally forbids the use of the copyright to secure an exclusive right or limited monopoly" beyond the scope of the Copyright Act and which is "contrary to public policy to grant."[68]

The conduct at issue in *Kodak*[69] pales in comparison. In that case, owners of Kodak equipment who objected to being forced to use Kodak service had the option of providing their own service[70] or, despite the switching costs, selling the Kodak equipment and purchasing another brand capable of performing just as well. In this case, in contrast, there is no "self service" option for a customer who objects to having to use only the DRM, codec, player and so on, specified by Movielink (or by individual studios using similar models). To the degree that any of these effectively control access to the downloaded movie, self-service could invite criminal liability.[71] Second, the option to not sacrifice the right of private performance or the Section 109(a) right to transfer a lawfully made copy is not available. Finally, this case presents conduct more onerous than Kodak's because, instead of a patented product for which there were ample market substitutes, the Movielink restraints use copyrighted works, each of which is unique.[72] The consumer who objects to Movielink's restraints could cancel the Movielink "subscription," but would be unable to watch previously downloaded movies using other software or services, and would not be able to obtain "market substitutes" for the 66% of most in-demand movies available exclusively from the Movielink joint venture partners.

IV. "Standards" or Simply Automated Agreements in Restraint of Trade?

Standard-setting to achieve interoperability of Internet networks, codecs, and media players (both hardware and software) certainly has its place as a potentially pro-competitive activity. Traditional antitrust analysis would tend to focus on direct suppression of competition, such as whether standard-setting might tend to suppress competing standards that could, without the standard-setting, become a *de facto* and superior standard. With this opening, several motion picture studios are asking Congress for additional leverage in developing and enforcing certain standards.[73] What is passing "under the radar" is the creation of standards to enable "automated agreements in restraint of trade." Allow me to illustrate by way of example.

As we have seen, the "first sale doctrine" and Section 109(a) of the Copyright Act allow the owner of a lawfully made copy of a motion picture to sell or otherwise transfer possession of that copy, such as by rental, without the consent of the copyright owner. If a copyright holder were to agree with the manufacturers of the systems for making lawful copies and of the systems for playing them to eliminate all trade in lawful copies unless each transaction (each resale or rental) has the consent of the copyright holder, there is of course no doubt that such agreement would constitute a naked restraint of trade. If, instead, the copyright holder agreed with the manufactures of copying and playing technologies to deploy a system which simply obeys the instructions of the copyright holder (including instructions which have the purpose and effect of eliminating the resale or rental of the copy), then the agreement is certainly no better than the first. It is akin to a company saying to the prospective Sherman Act Section 1 co-conspirator: "I can't agree with you to do what you are asking because my lawyers tell me it would be illegal, so what I'll do is program my machine to do what you tell it to do, but just don't tell me." Or, to place it in the context of actual negotiations over standards such as the Motion Picture Experts Group ("MPEG"), "I can't agree to build a system for delivering and playing back your motion pictures that will prevent the owners of lawful copies from reselling them or renting them without your permission, but I will agree to build a system that will process the management, playback, and similar handling of the bits 'in compliance with rules declared by the content provider.'"[74]

There may be perfectly legitimate "rules" established by the copyright owner, but there is a vast spectrum between rules which have the purpose and effect of authorizing (or not) actions which fall within the exclusive rights of the copyright holder, as set forth in Section 106 of the Copyright Act (subject to the limitations upon those rights, set forth in Sections 107-121),[75] and rules which have the purpose and effect of restraining trade in lawfully made copies or otherwise circumventing the statutory limits placed upon the copyright.

V. Effects of Pooling and Cross-Licensing Among Major Copyright holding Companies

In the words of the Register of Copyrights:

> Copyright has sometimes been said to be a monopoly. This is true in the sense that the copyright owner is given exclusive control over the market for his work. And if his control were unlimited, it could become an undue restraint on the dissemination of the work.
>
> On the other hand, any one work will ordinarily be competing in the market with many others. And copyright, by preventing mere duplication, tends to encourage the independent creation of competitive works. The real danger of monopoly might arise when many works of the same kind are pooled and controlled together.[76]

The focus of this paper is on the restraint of trade and enlargement of copyright power involving copies lawfully made by downloading (*i.e.*, the licensing of the right to reproduce the works into copies on the licensee's media), as distinct from streaming (*i.e.*, the licensing of the right to perform a work publicly over the Internet). This is not to say that there are no concerns over conduct among the major copyright holding companies involving the pooling and joint control over streaming. (As for the licensing of public performances through a streaming joint venture, *United States v. Columbia Pictures Industries, Inc.*[77] provides an analytical framework for assessing the antitrust concerns.) Public statements concerning Movielink indicate no intention to engage in the licensing of public performances of the pooled motion pictures, however. Rather, Movielink's business model appears to be based squarely upon the licensing of reproductions by download, coupled with the suppression of all trade in the lawful copies and the unauthorized charging for private performances. Thus, concerns about Movielink's model relate to the pooling of the copyrights as well as the pooling, so to speak, of the technologically-enforced practices in furtherance of unauthorized expansion of control over each copyright being pooled.

The pooling alone of the copyrights for mutual benefit raises antitrust concerns independent of these additional restraints. Von Kalinowski observes: "Despite limited case law on the subject, it appears that it is an unlawful restraint of trade for owners of copyrighted works to pool their copyrights to secure mutual benefit to themselves."[78]

The Movielink joint venture goes far beyond mere pooling of copyrighted assets, however, as the venture involves the joint employment of the same restraints upon lawful uses – restraints which serve no purpose but to extend control over copyrighted works beyond the limits of the copyright authority.[79] In an interview with *Video Store Magazine*, Jim Ramo, the CEO of Movielink, recently explained it this way:

> "[Consumers] will simply go to a web site, search and choose titles and be given suggestions. They'll click on the movie, click 'buy' and then download it," Ramo said. "The intent is to have a per-viewing capability and a price per view."[80]

In other words, Movielink intends to charge for the right of reproduction (the download), and then usurp the right of private performance by charging the owner of the lawfully made copy on a "per viewing" basis. Indeed, the article goes on to explain that viewing these copies will be permitted during the "pay-per-view window," which is to say, consumers could get to watch their own copies only during the period in which cable systems were licensed to make public performances of the works. (The cable pay-per-view service is simply another way that <u>licensees</u> can structure payment for public performances, as an alternative to cable subscription fees or selling of advertising time during free (to the public) broadcasts.[81]) And, in case Movielink's plan to take control over private performances of lawfully made copies was not sufficiently clear, Ramo indicated a willingness to actually destroy the lawful copies belonging to others:

> "We definitely are going to have a fee-per-use basis," he said. "What will happen to the content on your hard drive, whether it self-destructs or sits there on your hard drive, will be in the software business rules."[82]

Of course, it would not really "<u>self</u>-destruct," as those "software business rules" would constitute affirmative steps by Movielink to destroy or disable the property of others.

A Note On Streaming

The reader is reminded that this paper deals with the restraint of trade in lawfully made copies, and does not address the separate question of whether it would be lawful for a joint venture between major copyright holding companies to compete in the public performance of works over the Internet ("streaming"). In the event that the joint venture's business model were to shift (or a new joint venture be formed) to compete in streaming public performances, the approach taken by the Department of Justice in obtaining a preliminary injunction against the studio joint venture the *Columbia Pictures* case would appear to be the logical analytical starting point.[83] But we need not address this here, as there is no indication that Movielink or any other studio joint venture plans to compete in streaming. Movielink plans only to download (*i.e.*, to license reproductions) coupled with restraints upon the lawful trade in the legal copies reproduced, and the imposition of unauthorized control over lawful private performances.

Size of the Copyright Pool

In the motion picture industry, a few major copyright holding companies have amassed such a large pooling of copyrights within the company as to individually trigger the "real danger of monopoly" referred to by the Register of Copyrights. As an example, **Figure 7** lays out market shares for the motion picture studios based upon rental activity for the year 2001.[84]

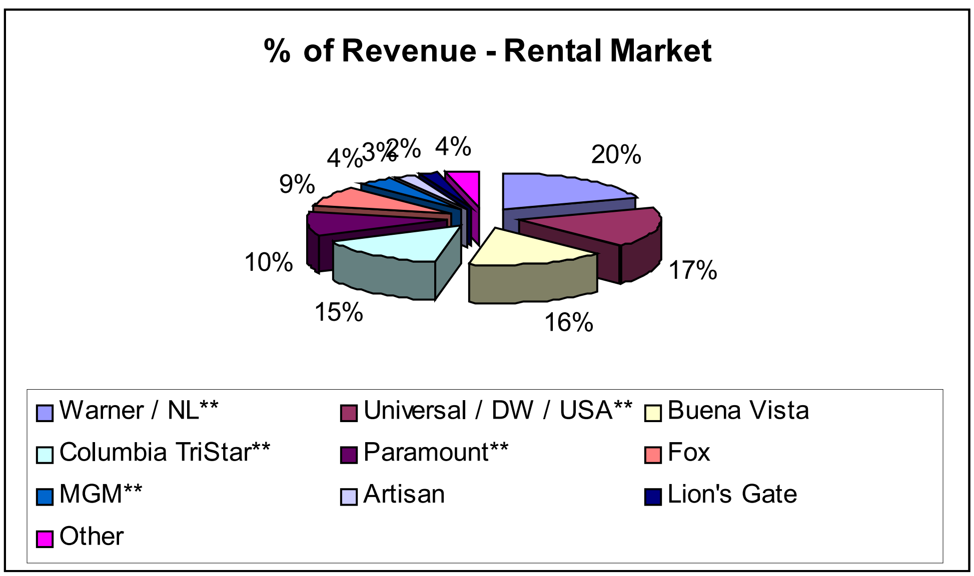

Figure 7[85]
(Studios marked with ** are in the Movielink joint venture)

In real dollars, the rental revenue from retail rental activity is attributable to the various studios' copyrighted works as follows:

2001 Unconsolidated	
Home Video Rental Market	
Studio	**Revenues**
Buena Vista	$1,350,475,699.76
Columbia TriStar*	$1,269,027,718.65
Warner*	$1,156,567,503.24
Paramount*	$845,084,873.67
Universal*	$785,402,354.73
Fox	$763,677,675.91
New Line*	$504,773,566.14
Dream Works*	$477,982,947.97
MGM*	$338,293,639.42
Artisan	$226,036,679.02
USA*	$200,768,157.29
Lion's Gate	$172,698,819.27
Other	$332,050,938.61
Total	$8,422,840,573.68

Figure 8[86]

(Studios denoted with an asterisk are part of the Movielink joint venture.)

The power of a copyright owner to use but one copyrighted work to restrain trade and unlawfully expand the reach of the lawful copyright monopoly has already been demonstrated with works as diverse as *Gone With the Wind*[87] and *Harry and the Hendersons*.[88] It is, therefore, safe to say that if only one title can be unlawfully leveraged, even a modest collection of titles can be pooled by a single copyright holding company to leverage serious restraints on trade and a more dramatic extra-judicial enlargement of the copyright. This power grows exponentially when five of the major copyright holding companies pool their own pooled copyrights into a single Internet-based delivery model. Based upon the data from **Figures 7** and **8**, above, the Movielink joint venture will achieve a pooling of copyrights accounting for approximately 66% of the consuming public's choice in home video rental for 2001 (and based on the Movielink model, no one will be able to purchase, rent or even borrow the lawful copies made by Movielink customers unless, perhaps for an additional fee, Movielink unlocks access to their copies).

Total Movielink $	**$5,577,900,761.11**
Total Movielink %	**66.22%**

Figure 9

Thus, five motion picture studios – copyright holding companies accounting for copyrights commanding 2/3 of the consumer demand for motion pictures at home video rental stores and 65 of the top 100 box office grossing films of all time[89] – have pooled their copyrighted works into a single joint venture for online delivery. This joint venture will select a single business model, will deny consumers or retailers the right to trade in what they own (if manufactured through a license from the joint venture), will choose a single set of technologies for online delivery, and so on. This 2/3 market share can be compared to **Figure 7** with the reconstituted market share portrayed in **Figure 10**:

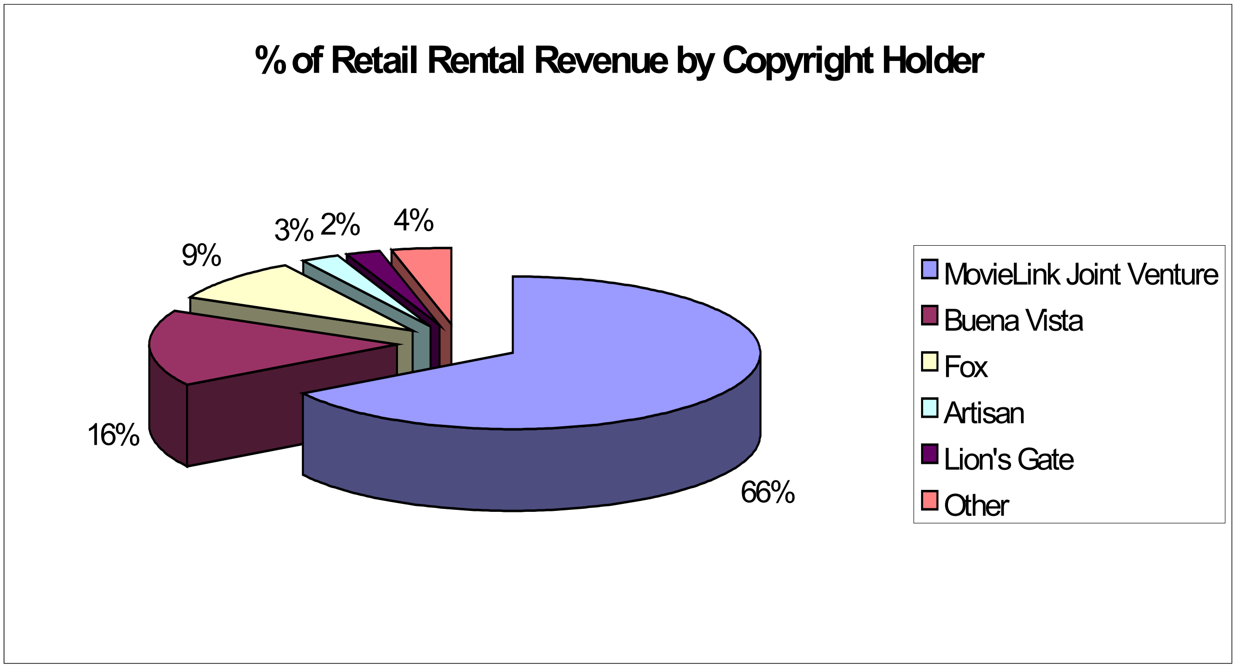

Figure 10

This mass of pooled copyright power should, without more, sound the Register of Copyrights' alarm from 1961.[90] But for good measure, let us briefly illustrate why this much control will have more devastating effects on competition and the public welfare than those which concerned the Supreme Court in the block booking cases.

Effect of Mass Pooling on Competing Independent Suppliers

The focus of this paper is on competition in the delivery, resale, rental, giving and so on of lawfully made copies. The impact of pooling on the supply of these products, too, must not be overlooked, for as the massive pooling of copyrights concentrates the supply of 66% or more of the demand-fulfillment potential, as we have seen above, competing suppliers will find that an increasing portion of prospective customers will no longer be reachable through independent retailers alone, and will find themselves forced to deal with the pooling entity. Consider, for example, **Figures 11a** and **11b**. When major motion picture studios pool their supply of 66% of the in-demand movies, we find that independent retailers are left with only one-third of the supply of available in-demand movies, unless some of the joint venture partners choose to also license the independent retailer. **Figure 11a** illustrates this:

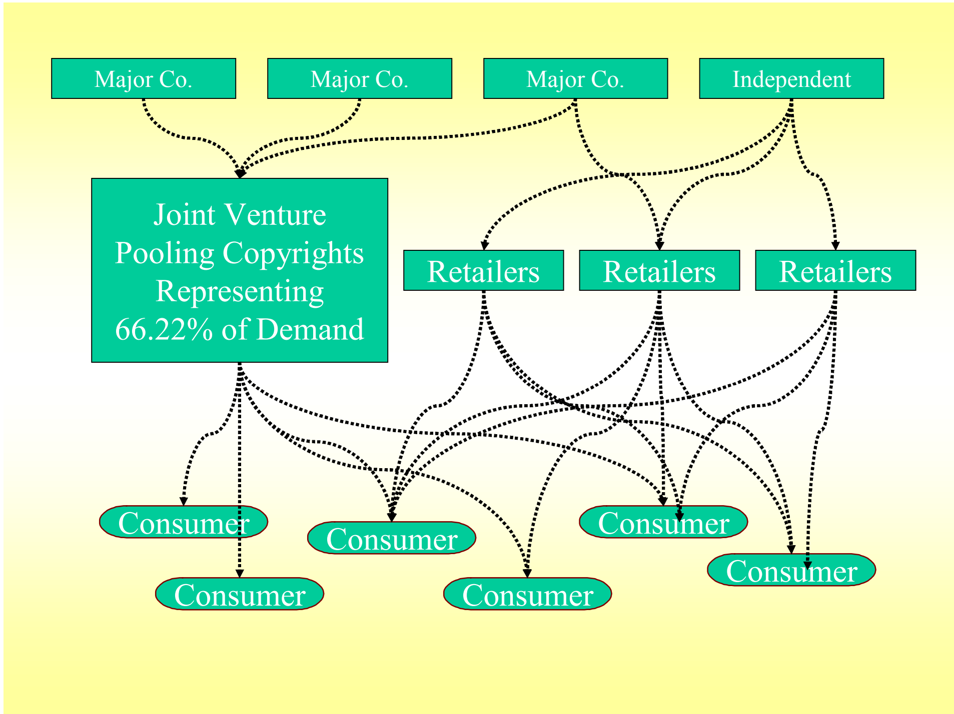

Figure 11a

The customers of the independent retailers who demand motion pictures available only through the joint venture, or through the joint venture's licensees, will be forced to also deal with the joint venture in order to obtain 100% of the movies they are seeking. Independent suppliers will, therefore, experience increasing pressure to supply the joint venture or risk losing access to those consumers (or at least that portion satisfied with a 66% offering or who are unaware of what they are missing). The net effect is that an increasing number of consumers will find between 66% and 100% of the movies they seek through the joint venture, which will serve only to increase the pressure on independent suppliers to license their products through the joint venture as well. The results are illustrated in **Figure 11b**:

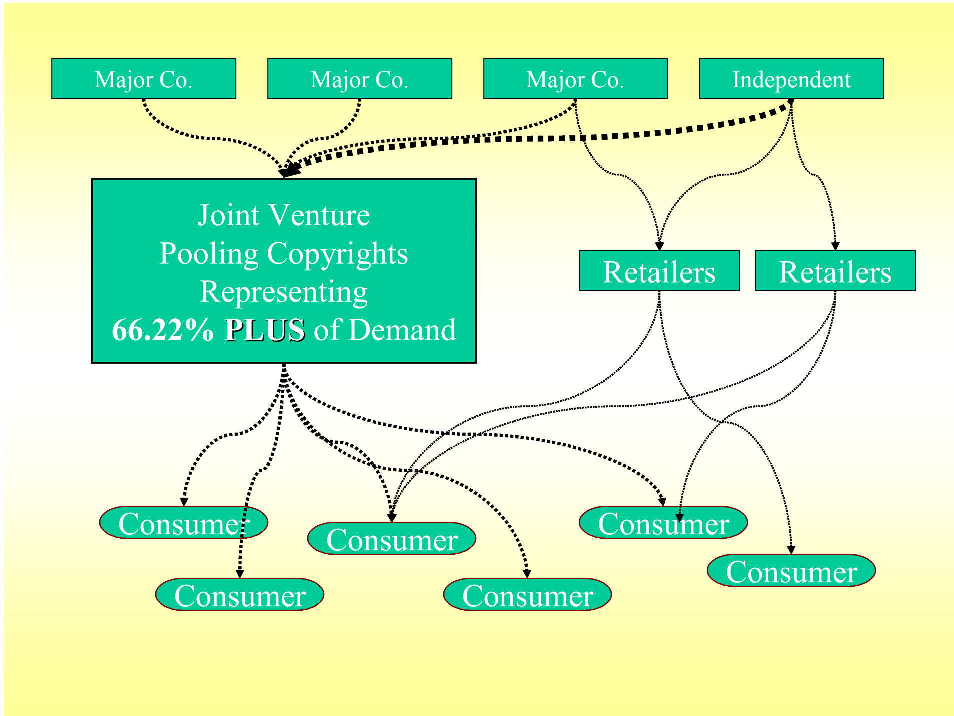

Figure 11b

The illustrated trend of concentration of supply through the joint venture will accelerate as it increasingly resembles an essential facility for the independent supplier, and the consumer loyal to the independent retailer will find that a lower price and better customer service are increasingly less able to compensate for lack of selection, thereby also leading to less competition in price and customer service.

Effect of Mass Pooling on Competing Independent Retailers

Under ordinary circumstances, each copyright holder would anxiously seek out every available competing retailer to license the right to sublicense downloads to consumers. A basic "wholesale" price per download would be offered to all takers, with possible marketing incentives added in for those retailers willing to market that company's motion pictures more heavily. Each competing retailer that is able to pay the wholesale price, provide a minimum level of security (using the approved technology of its choosing) and offer a sufficient degree of accountability for each sub-licensed download would be allowed to compete. Some would seek to be all things to all people, others would carve out niche specialties. Some would be known for the best prices, others for the best service, and still others for the best selection. Some would cross market with local pizza delivery, others would offer the lure of fan clubs and chat rooms. Some would be Internet-based only, while others might supplement the offerings of a physical store, and perhaps offer one free rental for every two downloads, or vice versa. All would have access to their choice of which movies to carry, and at what retail price. Many would fail, but the survivors would have demonstrated the superior business methods, and consumers would have obtained the most competitive prices, selection and service.

Under the joint venture approach, we can begin with the presupposition that the joint venture will be competing directly with retailers, if any, supplied by the joint venture partners.

Though the copyright holding companies may be free to offer downloads through competing retailers, they would certainly not be inclined to do so on terms competitive with the joint venture. In the first place, even if the joint venture and the competing retailer got the same "wholesale" price for the right to offer downloads, the copyright holding company would stand to earn more by adding the joint venture profits, and would have every reason to make sure the joint venture's profits are not threatened by a creative retailer with a more competitive offering. Second, the joint ventures have staked their fortunes on a business model in which consumers get to watch the movies they own for only a very limited time. It is hard to believe that the studios would permit competing retailers to offer secure downloads with no strings attached for the same price as those offered through the joint venture, with its limitations.[91] A competitive retailer would never try to make customers stop playing their own legal copies.

Thus, even if used by a single copyright holder for a single work, these "subscription" or "limited download" models would circumvent the Copyright Act's limitations upon copyright holders and rob the public of rights reserved to the commons by statute. When major copyright holding companies pool their already substantial holdings into a single business venture that makes this twisted method of delivery the only alternative for lawful downloads, Sherman Act Section 2 extensions of the copyright monopoly are carried out through use of Sherman Act Section 1 combinations to expand the individual copyright monopolies while vigorously restraining competition from the lawful trade in lawfully made copies.

VI. Comparative Observations

At the end of the day, the pure antitrust question is what actual effects the restraints upon trade discussed above have, or may be expected to have, on the market for copies of audiovisual works (and, *a fortiori*, the market for licensing the right of reproduction to make those copies in a factory, a store, or a home).

At the risk of creating a caricature, we may draw very broad lines of differentiation between a system employing the restraints discussed above and a free market in which the copyright holding companies act unilaterally and do not impose any restraints beyond those related to the protection of their true copyright interests set forth in the Copyright Act. For example:

IF: Each copyright holder sets a "wholesale" price for licensing each reproduction (download) or public performance (stream) of their works (with each title priced individually), allowing any bona fide merchant to offer downloads and streams subject only to the assurance that the licensee can (a) pay its bills, (b) add an adequate level of security from illegal copying, and (c) have auditable records to prove that it paid for each download or stream . . .

THEN: We could expect to see a variety of merchants (traditional specialists like Tower, mass merchants like Wal-Mart, online-only stores like Amazon and Netflix, new start-ups, small independents contracting with fulfillment and "back end" technology companies) compete with each other for customers; some trying to be all things to all people, others focusing on niche markets; some positioning themselves as specialists, some as low cost and no frills; some offering the copies or performances as loss leaders or bundling them in promotions; all trying to find the best codecs, players, DRMs and related technology solutions; some offering their customers "turnkey" solutions in which the retailer selects a single technology solutions package, others soliciting customers on the promise that they can find support for the customer's preferred codec or player, and still others promising to "sniff out" the customer's system and provide the best fit; all competing on price, presentation, selection, warranties, customer service, privacy policies, and anything else of value to the consumer.

IF: Copyright holders offer discriminatory licensing terms to only a select few merchants, require these merchants to use specified security technology, delivery technology and play-back technology, withhold select works for themselves to offer exclusively (or through joint ventures with "competing" copyright holders), and require that technologies be deployed to prevent consumers from privately performing or trading in these copies without additional payment to the copyright holder . . .

THEN: We could expect to see changes in consumer prices of copies and public performances reflective of the lack of lawful competition from resales, rentals, loans, gifts, and private performances. We might also expect copyright holders to forgo some initial profit from the initial reproduction by download in anticipation of the ability to extract future payments for private performances[92] and lawful transfers that are legally free from copyright holder control. We could expect independent producers to have little choice but to distribute through the studio online joint venture, and consumers who want a full array of movie selections to have to rely on the joint venture offerings because no competing retailer would be allowed to offer a full complement of aggregated product based on their own perceived consumer demand.

If half of the retailers in the free market model make the wrong decision and go out of business, that's fine, because (a) the remaining retailers will have succeeded in finding the more competitive solutions to meeting (and perhaps creating) customer demand and (b) the copyright holders will have profited from the failed businesses, as the failing ones would have been paying the wholesale price for each download or stream up until their failure.

In the market restrained by the copyright holders, in contrast, if just one joint venture makes the wrong decision, the entire industry is harmed, along with consumers, and the major copyright holders may not receive any net revenue insofar as they have gambled it on a losing business proposition.[93] Minor copyright holders who may have preferred a free market model will have been denied access to the consumer base drawn to joint ventures that controlled 66% or more of the supply of in-demand movies, unless they cooperate with them.

Regardless whether a comparison of the effects of a system with the aforesaid restraints and one without is made from the perspective of antitrust law principles or intellectual property law principles, the result in both cases will weigh heavily in favor of allowing the free market to operate within the express limitations of the Copyright Act. Both competition and copyright holders will benefit if copyright holders are prevented from using self-help technology to enlarge the scope of copyright, are prevented from licensing reproductions or public performances on discriminatory terms, and are prevented from pooling their copyright holdings with those of other major copyright holding companies into a single business and single business model.

The "Unauthorized" Home Video Market Experience

When videocassette recorders (VCRs) first emerged as a consumer electronics product in the late 1970s, few imagined how ubiquitous they would become in America's homes and how popular watching a prerecorded video of a motion picture would be. For an overwhelming majority of America's 250 million plus consumers, renting and buying prerecorded videocassettes and DVDs is an integral component of their entertainment options. More than 90% of the households in the U.S. own at least one VCR, and although the DVD is a relatively new format, it is projected that approximately 24 million U.S. households now own a DVD player. It is estimated that almost 3 billion videotapes and DVDs were rented in 2001. Approximately one-third of all video-equipped households rent a videotape or DVD weekly, while 50% rent at least once a month. More than 60% of video-equipped homes have a video library of some sort. The average videotape library contains 75 titles, while the average DVD collection contains 19 titles. Consumer spending on video rentals in 2001 was a record $8.42 billion. An additional estimated $8.5 billion was spent purchasing the most popular videotapes and DVDs in retail establishments, with DVDs representing 41% of the total dollars spent.[94]

This outcome was the direct result of the limitations the Copyright Act imposes upon copyright holders. Section 109(a) provides that, notwithstanding a copyright holder's distribution right, the owner of a particular copy or phonorecord lawfully made under U.S. copyright law "is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord." By preserving the retailers' right to sell and rent lawfully made videos and video games without restriction by the copyright holder, the first sale provision benefits society by promoting retail competition and maximizing distribution of creative works.[95]

Although the motion picture studios strenuously resisted the emergence of the VCR and the creation of the free market video rental industry, even going so far as petitioning Congress to eliminate the first sale doctrine for prerecorded videos of movies,[96] the home video industry today is an enormously profitable enterprise for the motion picture studios. Over the past several years, revenue from home video – <u>sales and rentals unauthorized by the copyright owner</u> – has accounted for <u>more than half</u> of the studios' gross domestic film revenue.

Home video has flourished precisely because copyright holders could not control the home video rental and resale market. The freedom to rent and resell videos guaranteed by law has provided consumers with access to a wide variety of affordable, quality entertainment from different sources, generated a tremendous revenue stream for the copyright holders, and created a thriving industry with a high level of competition. Of course, the retailer's freedom to compete so hard as to drive down the average per-night rental to as low as 77 cents must certainly also create pressure on other movie delivery forms to keep prices lower as well.[97]

And yes, all of this retail competition in home video is unauthorized by the copyright holders, yet fully authorized by law. Unfortunately, just as digital technology is enabling piracy by reproducing copyrighted works without the copyright holder's authorization, so, too, is digital technology enabling piracy of an entirely different sort – piracy by copyright holders intent upon diminishing the rights Congress reserved to others when it granted copyright protection.

The "limited download" (tethering, time-outs, limited plays) being implemented in concert by major motion picture studios is designed to gain the revenue stream consumers might be willing to pay for access to <u>public</u> performances of these works, while at the same time enjoying the control and efficiencies (but not the limitations) of a single digital reproduction (the download). It is intended to turn every digital player into a pay-for-play video jukebox, where the consumers own the copies, but lose their federal right to privately perform them (or transfer to others the physical medium on which they are lawfully recorded) without permission from or further compensation to the copyright holder.

Non-negotiable contracts and access control technology are being used not to prevent piracy, but to pirate away the legal rights of lawful owners to give, lend, sell, and rent the digital copies they own, and thus eliminate consumer choice and retail competition. Although technological measures may lawfully be used to prevent copyright infringement and to ensure payment for the reproduction, they should not be used to permanently control the lawful distribution and use of copies or phonorecords once the legal right to do so has been exhausted.

Such technologies are also capable of being used to obliterate the lawful secondary market for used entertainment. Consumers could then be prevented from loaning movies to a family member or friend, reselling them, donating them to charitable organizations, or even, according to some of the current business models, bequeathing them in their wills.

The Copyright Office recognized the anticompetitive potential of these technologies in its DMCA Section 104 Report to Congress. It noted that access control technologies that tether digital downloads to a single computer and non-negotiable "click-thru" contracts that attempt to override copyright law may negatively impact consumer choice and retail competition.[98] Unfortunately, the Copyright Office has failed to appreciate the full antitrust implications of such conduct.

Serious price competition in the distribution of copyrighted works is largely non-existent until the product passes to distributors and retailers. If video retailers (and their customers) cannot participate in the distribution of digitally downloaded movies, either as a lawful reseller or a rental outlet, the neighborhood video store may fade from the scene, along with the rock-bottom pricing and wide selection from among major and independent motion picture studios. They would be replaced by direct distribution by the major copyright holding companies which, by controlling the primary distribution channel, can simultaneously exclude smaller independent creators and competing retail channels. Consumer choice and competition would be further eroded.

More than 50 years ago, the Supreme Court in *United States v. Paramount Pictures*[99] struck down pooling arrangements and joint ownership agreements designed to give movie studios control over the distribution of motion pictures in theaters. It also struck down the "block booking" practices in which the motion picture studios refused to license one or more copyrighted movies unless another undesired copyrighted movie was accepted. In *United States v. Loew's, Inc.*,[100] the Supreme Court once again condemned block booking and related efforts to suppress independent distributor decisions. As discussed below, these restraints on trade should be examined not only as antitrust concerns relating to competition, but also as major public policy concerns which, if not resolved, threaten to make a mockery of the constitutional basis for Congress' authority to have enacted copyright laws in the first place.

VII. Copyright Misuse

Under the Copyright Act, the person who downloads a movie from the Movielink service owns that copy and has the right to give it away, sell it, or lend it. Are copyright holders free to nullify those rights, and if so, what is the source of their right to do so? From the discussion above, it should be clear that copyright holders have no right to prevent the owners of lawfully made copies from disposing of them by gift, sale, or even lending. In addition to the antitrust implications of such restraints on trade, such conduct constitutes copyright misuse.

Congress "has never accorded the copyright owner complete control over all possible uses of his work," but has instead limited the holder to the enumerated statutory rights in § 106.[101] The question is whether the use of that monopoly power, however limited, for the purpose of gaining control over distribution of a work after the distribution right has been terminated by law is an abuse of that copyright. The answer is straightforward: "A copyright owner may not enforce its copyright to violate the antitrust laws or indeed use it in any 'manner violative of the public policy embodied in the grant of a copyright.'"[102]

It is well established that the misuse of intellectual property rights may give rise to liability under standard antitrust analysis. But perhaps because copyright misuse so often fits within standard antitrust analysis, it is sometimes overlooked that such misuse can also give rise to liability based upon the pure enlargement of the copyright monopoly conferred in each individual copyright into control over rights that fall outside of the grant of that specific copyright. Copyright misuse case law has developed along two separate though complementary paths, as both part of and separate from standard antitrust jurisprudence. It is the latter – copyright misuse under copyright law principles – to which we now turn.

Even in the seminal "first sale doctrine" case, later codified in Section 109(a), the Supreme Court was almost prescient in anticipating the development of the copyright misuse doctrine. In *Bobbs-Merrill Co. v. Straus*[103] the Court concluded: "In our view the copyright statutes, while protecting the owner of the copyright in his right to multiply and sell his production, do not create the right to impose, by notice, such as is disclosed in this case, a limitation at which the book shall be sold at retail by future purchasers, with whom there is no privity of contract."[104] The Court added: "This conclusion renders it unnecessary to . . . examine into the validity of the publisher's agreements, alleged to be in violation of the acts to restrain combinations creating a monopoly or directly tending to the restraint of trade.[105] Thus, even in 1908 the Court was prepared to consider enlargement of the copyright under antitrust principles, but was satisfied that the Copyright Act itself provided all the limitation necessary to condemn an enlargement of the copyright by notice. How much more suspect the conduct if instead of a "notice," advanced digital technology is employed to carry out what would have been the notice's objective!

In 1917, the Supreme Court took on the issue of private enlargement of copyright, yet did so again from an intellectual property law premise. In the *Motion Picture Patents* case, it determined that the owner of an intellectual property monopoly – in that case a patented motion picture film projector – could not lawfully use a "licensing" mechanism to obligate purchasers of the machine to use it solely with motion pictures containing another patent which the company also owned.[106]

> A restriction which would give to the plaintiff such a potential power for evil over an industry which must be recognized as an important element in the amusement life of the nation, under the conclusions we have stated in this opinion, is plainly void, because wholly without the scope and purpose of our patent laws, and because, if sustained, it would be gravely injurious to that public interest, which we have seen is more a favorite of the law than is the promotion of private fortunes.[107]

Notwithstanding the fact that patent law confers both an exclusive right to "vend" and to "use," the Supreme Court concluded that the exclusive right of use could not be employed as a tool to expand the scope of the patent, and that "it is not competent for the owner of a patent, by notice attached to its machine, to, in effect, extend the scope of its patent monopoly by restricting the use of it to materials necessary in its operation, but which are no part of the patented invention, or to send its machines forth into the channels of trade of the country subject to conditions as to use . . . ."[108] In contrast to patent law, copyright law does not confer an exclusive right of "use" of the work. Thus, the Supreme Court's holding in *Motion Picture Patents* carries even greater weight in relation to use of lawfully made copies.

Even if we were to apply to these e-commerce ventures the jurisprudence of 1917, when electricity was still a novelty and digital media was not yet a pipe dream, the relevance of the Supreme Court's analysis in *Motion Picture Patents Co.* is inescapable. If it is unlawful to extend the statutory monopoly by limiting the use of a patented motion picture projector to films containing other intellectual property owned by the licensor, then it stands to reason that it is equally unlawful to condition the licensing of copyrighted works upon the relinquishment of statutory rights under Section 109(a), or to license only in conjunction with certain DRMs, codecs or digital media players – particularly if the owner of the copyrighted motion pictures also owns an interest, either through direct investment or through a joint venture, in the exploitation of the intellectual property associated with the tied technologies.

But the law did not stand still in 1917. From this premise, the law continued to develop a unique theory of misuse of intellectual property <u>independent</u> of antitrust law. In *Morton Salt*[109] the Court examined the Seventh Circuit's approval of the use of the patent monopoly in a machine for depositing salt tablets to force licensees to use only salt tablets manufactured by the patent holder. The Seventh Circuit had reasoned that, under § 3 of the Clayton Act, "it did not appear that the use of its patent substantially lessened competition or tended to create a monopoly in salt tablets."[110] The Supreme Court reversed on grounds of patent misuse, and concluded that, having done so, it was unnecessary to decide whether the Clayton Act had also been violated.[111]

> [t]he public policy which includes inventions within the granted monopoly excludes from it all that is not embraced in the invention. It equally forbids the use of the patent to secure an exclusive right or limited monopoly not granted by the Patent Office and which it is contrary to public policy to grant.[112]

Thus, the misuse claim was viewed as independent of the antitrust claim. But this line of reasoning is not limited to patent and trademark law. *Morton Salt* itself noted with approval the application of this doctrine to copyrights.[113] In *United States v. Paramount Pictures, Inc.*,[114] the Supreme Court further explained the limitations on copyright power in the context of "block booking" – "the practice of licensing, or offering for license, one feature or group of features on condition that the exhibitor will also license another feature or group of features released by the distributors during a given period."[115] The Supreme Court approved of the lower court's restriction against such practice as well as the lower court's reasoning, which was based not only on the illegality of the restraint itself, but also for reasons based squarely upon the Constitution and the Copyright Act.

> The District Court held it illegal for that [antitrust law] reason and for the reason that it "adds to the monopoly of a single copyrighted picture that of another copyrighted picture which must be taken and exhibited in order to secure the first." That enlargement of the monopoly of the copyright was condemned below in reliance on the principle which forbids the owner of a patent to condition its use on the purchase or use of patented or unpatented materials.[116]

The Supreme Court noted that, like patent law, the exclusive right granted under the Copyright Act does not include any privilege to "add to the monopoly of the copyright in violation of the principle of the patent cases involving tying clauses."[117]

Based upon these principles, the doctrine of copyright misuse has developed both as a violation of antitrust law and as an affirmative defense against copyright infringement when the copyright holder, by means of an over-reaching license or other method of control, tries "to secure an exclusive right or limited monopoly not granted by the [Copyright] Office and which it is contrary to public policy to grant."[118]

But what about an affirmative claim of copyright misuse? Though some have questioned whether a pure copyright misuse claim may be pled affirmatively,[119] the Supreme Court has shown no such reluctance. *United States v. Paramount Pictures*[120] and *United States v. Loew's, Inc.*[121] did not involve separate claims for copyright misuse. Rather, they were Sherman Act cases that could arguably serve to limit copyright misuse to just another label for a type of conduct unlawful under traditional antitrust law.[122] Nevertheless, they find "block booking" unlawful precisely because the bundled products were copyrighted. The practice "tends to equalize rather than differentiate the reward for the individual copyrights."[123] Like the bundling of copyrights with specific DRMs, codecs, media players and restrictive "rules" that rob consumers and competing retailers of their Section 109(a) and private performance rights, the Court found that each copyrighted motion picture "stands not on its own footing but in whole or in part on the appeal which another film may have,"[124] thereby unlawfully adding to the copyright monopoly power.[125]

Moreover, market power need not be demonstrated, as "either uniqueness or consumer appeal" of the product is sufficient.[126] "This is even more obviously true when the tying product is patented or copyrighted."[127] To viewers, "there is but one '*Gone With The Wind*,'"[128] and the use of it to force others to take "*Getting Gertie's Garter,*" to install and use an unwanted media player, to confer upon the copyright owner the power to meter out wholly private performances, or to relinquish a federal entitlement to sell or rent the downloaded copy, is unlawful precisely because the appeal of a copyrighted film is being used to enlarge the power and scope of the copyright in that film.

The courts continued this line of thinking, and soon the "misuse" framework's language came into wider use. In a long-running dispute initiated by CBS against ASCAP and BMI that made its way to the Supreme Court[129] and back, there was a clear recognition of an independent affirmative claim of copyright misuse during the entire history of the case. The District Court noted that the plaintiff sought "a declaration of copyright misuse under the Declaratory Judgment Act" in addition to the antitrust claims,[130] and that the fifth claim for relief was "that the activities described constitute copyright misuse."[131] Though the lower court dismissed the complaint, it did not question the validity of the legal theory as a separate affirmative claim.

The Second Circuit reversed,[132] concluding that the defendants' conduct was illegal *per se* under antitrust law <u>and that it further constituted copyright misuse</u>. After disposing of the Sherman Act § 1 claim in favor of CBS, it "dispose[d] of CBS' claim of copyright misuse in the same manner and for essentially the same reasons as the § 1 claim."[133] In its own review, the Supreme Court took the copyright misuse claim as a given: "This case involves an action under antitrust <u>and copyright laws</u>" brought by *CBS.*[134] It noted without comment or question that CBS alleged a violation of copyright laws and sought a declaration of copyright misuse.[135] In reciting the history of the case, it observed that the appellate court determined that the blanket license at issue was "price fixing illegal *per se* under the Sherman Act" and, "without more, settled the issue of liability under the Sherman Act [and] established copyright misuse."[136] The Court further noted that it was at the plaintiff's suggestion that the appellate court had "held that the challenged conduct constituted misuse of copyrights solely on the basis of its finding of unlawful price fixing,"[137] and that a question presented was the applicability of the *per se* rule and "whether this constitutes misuse of copyrights."[138] Finally, the Supreme Court reversed the judgment of *per se* liability for price fixing "and the copyright misuse judgment dependent upon it."[139]

Thus, the Supreme Court never questioned the use of the copyright misuse claim as an affirmative claim, at least in the context of a declaratory judgment action. Implicit in its observations in footnote 9 was the suggestion that, on remand, there could be liability for copyright misuse on the basis of a theory other than *per se* liability for price fixing. The appellate court appears to have agreed. On remand from the Supreme Court, the Second Circuit set forth a Scheduling Order which referred repeatedly to "misuse of copyright" as a separate ground for affirmative relief.[140]

The foundations laid by the high court should not be dismissed as "old law." In *Buffalo Broadcasting Co. v. ASCAP*,[141] the complaint alleged a Sherman Act Section 1 violation and "misuse of copyright in violation of the Copyright Act of 1976,"[142] clearly an affirmative claim, but the Court noted that the "claim of copyright misuse is tangential to the focal antitrust claim and is mentioned only briefly below."[143] The Court concluded that certain blanket licenses unreasonably restrained trade in violation of Section 1 of the Sherman Act (though this ruling was reversed), and added: "As is clear from the foregoing, the blanket licensing system . . . exists not for the convenience of local television stations but due to defendants' patent power. Accordingly, defendants' licensing practices must also be declared misuse of copyright."[144]

More recently, in *MCA Television Ltd. v. Public Interest Corp.*,[145] the Eleventh Circuit built upon the foundation of the block booking cases in a fact situation analogous to the one at issue here. Though the issue came up as an antitrust counterclaim over a contract dispute, the court's analysis was substantively one of pure copyright misuse, as it expanded the reach of *Loew's* and *Paramount* beyond mere block booking (conditioning the license to a desired work on accepting an undesired one) to cover the facts before it – conditioning the license of desired works (various television programs) on accepting another desired work (*Harry and the Hendersons*) for partial payment in cash rather than barter. Here, for example, retailers and consumers may desire all of the copyrighted films, and may also desire to use certain media players, codecs or DRMs. But they would also rather not have to "pay with first sale rights" or "pay with the right of private performance" rather than just cash.

And only last year, efforts to use an "end-user license agreement" to restrain trade by extending the copyright power through such a license were rejected in *SoftMan*.[146] Thus, the doctrine that enlargement of the copyright may be actionable independent of whether the conduct fits standard antitrust theory remains strong today. Our federal law enforcement agencies should not be reluctant to use it.

VIII. Conclusion

To use the limited monopoly power conveyed by the Copyright Act for the purpose of gaining control over distribution of a work after the distribution right has been terminated by law is a misuse of the copyright. "A copyright owner may not enforce its copyright to . . . use it in any 'manner violative of the public policy embodied in the grant of a copyright.'"[147] Because Congress saw fit to exhaust the copyright owner's right to restrict the distribution of a lawfully made copy or phonorecord once it is owned by another, any use of access control technology to circumvent the will of Congress and effectively "revive" a right that the law extinguished must be considered copyright misuse. In the same vein, if a technological control measure effectively renders a motion picture unplayable if the owner of the copy or phonorecord transfers title to another, such measure frustrates the Congressional will and technologically prohibits a transfer that the copyright owner has no lawful right to prohibit.

For the first time in history, copyright holders have the power to control mass distribution of their works (at least those in digital form) from the point of manufacture all the way to the end consumer and beyond. They are now able to distribute copies to millions of people in a matter of a few minutes, simultaneously distributing at the wholesale and the retail level. At the same time, digital technology gives copyright holders the unprecedented power to control and suppress the lawful use, resale, and rental of digitally delivered entertainment. Moreover, copyright holders can use technology to enforce absolute uniformity in the terms and conditions of sale available to all retail consumers, ignoring or supplanting efforts by retailers to offer more competitive pricing, policies and other competitive terms and conditions of sale, such as in the protection of consumer privacy and anonymity.

While it can be argued that, ultimately, business models that rely on consumer-unfriendly technology will fail, the immediate issue is whether the copyright holders will allow a competitive alternative to emerge.

Public policies for digitally delivered copyrighted works must balance (1) the rights and limitations of copyright, (2) the promotion of competition for consumer allegiance, (3) the protection of consumer rights, and (4) the stimulation of technological innovation. This statement may well be a truism. However, should the deployment of technology be found to lie outside the scope of these policies, the balance cannot be maintained. Unchecked technology puts at risk the first sale, private performance, and other rights of consumers under the Copyright Act. Copyright holders must be restrained from misusing the limited privileges granted to them by Congress under the Copyright Act to extend their copyright monopoly. Only a dynamic balance encompassing competition, consumer rights, and the rights <u>and</u> limitations of copyright will continue to stimulate artistic, business and technological innovation that benefits society, preserves competition, enhances the quality of life, and fuels economic growth.

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[1] John T. Mitchell is a partner in the DC office of Seyfarth Shaw, 815 Connecticut Ave., NW, Suite 500, Washington, DC 20006-4004, tel. 202-828-3574, jmitchell@dc.seyfarth.com.

[2] The Video Software Dealers Association (VSDA) is the international trade association representing the home video industry and video stores across the nation. Established in 1981, VSDA now represents more than 1,700 companies throughout the United States, Canada, and a dozen other countries. Membership comprises the full spectrum of video retailers, including both independents and large chains. VSDA is headquartered in Encino, California, with an Internet presence at www.vsda.org.

[3] *See generally*, James Lardner, *Fast Forward: Hollywood, the Japanese, and the Onslaught of the VCR*, Norton, New York, 1987. For commentary on more current efforts by motion picture studios to control distribution, *see* T.K. Arnold, "The Morning Buzz: Control Freakin' In Hollywood," Video Store Magazine, posted May 13, 2002, at http://www.hive4media.com/news/html/breaking_article.cfm?article_id=3108. *See also* Joan Villa, "The Return of Revenue Sharing," Video Store Magazine, posted May 10, 2002, at http://www.hive4media.com/news/html/breaking_article.cfm?article_id=3105.

[4] This data is taken from the VSDA Common Practice Survey #5 (August, 2001) of Rental Rates and Terms. Current price data is not published. At the time of this survey, the average theater ticket for a fist-run movie in the corresponding markets was $7.29, with a mode of $7.50. The survey data indicates that the home video rental price remained competitive with video rental across markets, regardless whether the theater ticket price was higher or lower than average in a given market, suggesting that a video retailer's toughest competition is another video retailer.

[5] The "first sale doctrine" created by the courts in *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339 (1908), has been codified at 17 U.S.C. § 109(a), and provides that "the owner of a particular copy or phonorecord lawfully made under this title, or any person authorized by such owner, is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord." (Unless otherwise noted, all subsequent section references are to Title 17.)

[6] Though the Notice of Public Hearings and Opportunity for Comment speaks in more general terms of "intellectual property," Chairman Muris has indicated that "The hearings will focus primarily on the implications of antitrust and patent law and policy for innovation and other aspects of consumer welfare. **Copyright and trademark issues, as they arise in particular high-tech contexts, may also be considered**." *Competition and Intellectual Property Policy: The Way Ahead*, prepared remarks of Timothy J. Muris, Chairman, Federal Trade Commission, before the American Bar Association, Antitrust Section, Fall Forum, Washington, DC, November 15, 2001 (emphasis added). As will be demonstrated, these comments deal not only with the high-tech context of digital delivery of copies of audiovisual works, but also with how "high tech" is impacting competition in the market for pre-packaged copies and ordinary retail sales and rental transactions, including the markets for used copies.

[7] Section 101 of the Copyright Act refers to "copies" and "phonorecords." The latter is the special term given to the tangible media containing sounds that do not accompany a motion picture or other audiovisual work. Tangible media embodying any other kind of copyrighted works are defined as "copies" (such as books, motion pictures, video games, and computer software), and include any tangible media, whether paper, film, magnetic tape, floppy disc, CD, DVD, flash memory or a computer hard drive. Given the disuse of the term "phonorecord,"

except where otherwise indicated this paper will use the term "copies" or "copyrighted products" to refer collectively to copies and phonorecords as defined in Section 101.

[8] "Ownership of a copyright, or of any of the exclusive rights under a copyright, is distinct from ownership of any material object in which the work is embodied. Transfer of ownership of any material object, including the copy or phonorecord in which the work is first fixed, 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." Section 202.

[9] Laurie M. Grossman, "Entertainment: for video sales it's a green Christmas," *Wall Street Journal* (December 24, 1991), p. B1.

[10] Orion Pictures, which also provided McDonald's with exclusives, reportedly "attempted to prevent McDonald's from selling tapes to retailers after reports surfaced that Trans World Music, Musicland and other retailers had purchased them at fast-food chain [sic] for resale in their stores." *Video Week* (April 5, 1993), p. 4. There is no indication that Orion's efforts met with any degree of success; nor could they, since any given McDonald's customer buying a sandwich with a premium could happen to be a video store employee doing the boss a favor. Indeed, any customer is free to resell their tapes, whether to video stores or to each other.

[11] H.R. Rep. No. 2222, 60th Cong., 2d Sess. (1909) (emphasis added). Congress first codified the first sale doctrine in the Copyright Act of 1909. At that time, the House Committee on Patents stated that this codification was intended "to recognize the distinction, long established, between the material object and the right to produce copies thereof." *Id. See* Section 27 of the Copyright Act of 1909 ("nothing in this title shall be deemed to forbid, prevent, or restrict the transfer of any copy of a copyrighted work the possession of which has been lawfully obtained").

[12] As we shall see in Part II, below, the major copyright holding companies are moving aggressively to block the lawful transfer of the physical copies as well.

[13] *Quality King Distrib., Inc. v. L'anza Research Int'l., Inc*, 523 U.S. 135 (1998).

[14] Copying of a widget that is not a "copy" under the Copyright Act may nevertheless implicate a patent or trademark right, but this analysis is limited to copyrights. One can, for example, make a hair care product or mousetrap that copies someone else's hair care product or mousetrap very closely, but without violating any intellectual property right.

[15] To take the example of a CD, the medium itself requires adherence to exacting standards of manufacturing to ensure compatibility with CD players. The copyrighted work embodied on the CD must be placed on the CD in a particular fashion in accord with those standards. But the bits of information – the series of ones and zeros making up the information, simply need to be the same as the original, and no particular "quality" will distinguish a bit copied by one licensee from the bit copied by another.

[16] "Digital distribution" is not a term under the Copyright Act, but simply describes the means of carrying out a public performance (*e.g.* "streaming") or reproduction into copies (*e.g.* "downloading") of a work. The bits that are transmitted can be to make a public performance (pursuant to the Section 106(4) right "to perform the copyrighted work publicly"), or can be transmitted for the purpose of making a copy (pursuant to the Section 106(1) right "to reproduce the copyrighted work in copies or phonorecords"). The only right of "distribution," as such, is

the right "to distribute copies or phonorecords of the copyrighted work to the public by sale or other transfer of ownership, or by rental, lease, or lending." *See* Section 106(3), which is itself "subject to" the right of the owner of a lawfully made copy to distribute it without the consent of the copyright owner (Section 109(a)). When we say, in common parlance, "e-mail me a copy," what we really mean is "use a computer program to instruct your equipment to read the bits that comprise your digital copy residing on your fixed or portable medium and transmit the bits over some wired or wireless communications network such that my equipment will receive, recognize and reproduce the bits onto a fixed or portable physical medium, thereby becoming a copy." Similarly, to "fax a copy" does not mean to physically distribute the copy pursuant to Section 106(3), but rather to have a machine convert the image into digital bits, which are transmitted and then interpreted to reproduce an image onto another physical medium, thereby becoming a second copy. Whether the bits are transmitted across the world or across a cable connecting two machines in a factory is largely irrelevant. A copyright owner could digitally transmit the bits to a manufacturing facility licensed to make thousands of copies for physical distribution, or could digitally transmit the bits to thousands of separate locations with a license to make one copy at each. The Copyright Act gives the copyright owner the exclusive right to distribute its copies (such that the factory that makes them would infringe the distribution right if it made them for the copyright holder and then sold them without permission), but if the copy is lawfully made and owned by someone else (such as the retailer or the consumer), the copyright holder cannot lawfully control their distribution.

[17] *See* Janelle Brown, "The Music Revolution Will Not Be Digitized," salon.com June 1, 2001, available at http://www.salon.com/tech/feature/2001/06/01/digital_music/. ("The recording industry's approach to the digital music business appears to have been to wallop the competition with lawsuits until they gave up -- and then pick up the bruised remains to use to their own advantage.")

[18] *See* **Figure 7** for a sample of the market shares of the major motion picture copyright holding companies.

[19] For example, 99% of the all-time top 100 grossing films at the box office were disrtributed by the seven major motion picture studios which had agreed to aggregate their films into two joint ventures (now only one 5-studio joint venture remains), and 96% of the top 100 were distributed by the six top studios. 65% were distributed through the five motion picture studios comprising the Movielink joint venture. *See* www.movies.yahoo.com/hv/boxoffice-alltime/rank.html, (box office rankings consulted as of May 15, 2002), and compare with the data in **Figures 7-10.**

[20] *See* **Figures 7-10**.

[21] That is not to say that, on occasion, a studio might not have a pro-competitive justification for yielding to the opportunity of an occasional exclusive arrangement of limited duration for a single title or discrete collection. There may be times in which the studio would seek out special ways to boost interest in a particular film, and in such cases find that it's own economic interest in an exclusive is comparable to that of the small independent studio trying to stand out. In general, however, the major studio will take the opposite route, and try to borrow from the strength of the more popular titles to drive sales of the less popular ones. Studios routinely do so through "output" deals with major buyers, in which the major buyer can obtain better per-copy terms if all titles from a given studio are taken. Where such deals are offered not as an option or

incentive, but as the only way to get the desired titles, the studio of course runs the risk of criminal and civil liability. *See, e.g., United States v. Paramount Pictures*, 334 U.S. 131 (1948); *United States v. Loew's, Inc*., 371 U.S. 38 (1962); and *MCA Television Ltd. v. Public Interest Corp.*, 171 F.3d 1265 (11th Cir. 1999). Suffice it to say that whether structured as an illegal block booking scheme or a defensible output option, the regular course of conduct of the major motion picture studios over the last several decades bears out the propensity to use the power of their aggregated copyright holdings to force retailers to carry less desirable titles, but there is no evidence that they have had any immediate economic motivation to reduce the number of retail buyers for their films.

[22] Thus, though exclusion may drive up a rival's costs, it need not necessarily eliminate the rival.

[23] Scott Hettrick, "Bishop gets MGM vid-on-demand duties: Deal mirrors studios moving to PPV delivery through Net, broadband," *Variety.com*, posted December 8, 2000 available at http://www.variety.com/index.asp?layout=print_story&articleid=VR1117790211&categoryid=18 (emphasis added).

[24] Even Blockbuster, the largest video retailer (perhaps because it was the largest), was unable to secure licenses from more than two of the major motion picture studios for its Internet-based VOD venture. *See* Paul Sweeting and Scott Hettrick, "VOD Venture Voided: Enron Pulls Out of Blockbuster Partnership," *Variety.com*, posted March 12, 2001, available at http://www.variety.com/index.asp?layout=print_story&articleid=VR1117795099&categoryid=1000.

[25] 2 M. Nimmer & D. Nimmer, NIMMER ON COPYRIGHT § 8.12[A] (2000).

[26] In *American Int'l Pictures, Inc. v. Foreman*, 576 F.2d 661, 664 (5th Cir. 1978), the court explained the first sale doctrine (even in its narrower, pre-1976 Act form) as follows (citations omitted):

> After the first sale of a copy the copyright holder has no control over the occurrence or conditions of further sales of it. Even if the copyright holder places restrictions on the purchaser in a first sale (such as specifying the permissible uses of the article), the buyer's disregard of the restrictions on resale does not make the buyer or the person who buys in the secondary market liable for infringement. The first sale thus extinguishes the copyright holder's ability to control the course of copies placed in the stream of commerce.

Of course, the reference to "first sale" based upon the prior Act gives way to the modern requirement that one need only be the owner of a lawfully made copy, without regard to whether a sale occurred. *See* 2 M. Nimmer & D. Nimmer, NIMMER ON COPYRIGHT § 8.12[B][3][c] (2002).

[27] *See United States v. Cohen*, 946 F.2d 430, 434 (6th Cir. 1991) ("This [first sale] doctrine recognizes that copyright law does not forbid an individual from renting or selling a copy of a copyrighted work which was lawfully obtained or lawfully manufactured by that individual" (emphasis added)); *United States v. Sachs*, 801 F.2d 839, 842 (6th Cir. 1986); 2 M. Nimmer and D. Nimmer, Nimmer on Copyright § 8.12[B][3][c]. The Copyright Act also makes clear that the first sale doctrine need not involve sale of the tangible medium. Rather, the pivotal question is whether the person asserting the first sale doctrine right is the "owner" of a lawfully "made"

copy or phonorecord. There is no requirement that the tangible medium of expression have been sold by the copyright holder, but only that the owner of the lawfully made copy or phonorecord be the lawful owner. The Copyright Office agrees that Section 109(a) applies to copies lawfully made in a retail store or in the home. *See* U.S. Copyright Office, "DMCA Section 104 Report," 78 (2001).

[28] *See* note 87, *infra*.

[29] *See, e.g., Joint Reply Comments of Copyright Industry Organizations Report to Congress Pursuant to Section 104 of the Digital Millennium Copyright Act*, dated September 5, 2000, submitted by the American Film Marketing Association, the Association of American Publishers, the Business Software Alliance, the Interactive Digital Software Association, the Motion Picture Association of America, the National Music Publishers' Association and the Recording Industry Association of America, p. 6; *Hearing Before the Copyright Office and the National Telecommunications and Information Administration on a Joint Study on 17 U.S.C. Section 109 and 117* (November 29, 2000) (statement of Fritz Attaway on behalf of the Motion Picture Association of America, pp. 73-74.); *Hearing Before the Copyright Office and the National Telecommunications and Information Administration on a Joint Study on 17 U.S.C. Section 109 and 117* (November 29, 2000) (statement of Cary Sherman on behalf of the Recording Industry Association of America, Inc., p. 298).

[30] *Joint Reply Comments of Copyright Industry Organizations*, *supra*., p.6 (explaining that the first sale doctrine would apply to lawfully made copies only "in the absence of licensing or technological restrictions to the contrary"). *Cf. SoftMan Prods. Co. v. Adobe Systems, Inc., 171 F. Supp. 2d* 1075, 1089 (C.D. Cal. 2001), likening that position to that of "a journalist who claimed that ownership of the copyright to an article allowed him or her to control the resale of a particular copy of a newspaper that contained that article." The *Softman* court went on to flatly reject the notion that restrictions in a "use" license could take away rights belonging to the owner. The owner of a lawful copy "is entitled to the use and enjoyment of the software, with the rights that are consistent with copyright law. The Court rejects Adobe's argument that the EULA gives to purchasers only a license to use the software." *Id.*

[31] Were federal rights voidable or avoidable by private agreement, one would expect employers to routinely require new hires to sign employment agreements waiving their rights to a minimum wage or freedom from discrimination. Where, as in the case of Section 109(a), federal rights serve an important public purpose, private agreements to avoid them are contrary to the public interest. *SoftMan Prods. Co. v. Adobe Systems, Inc.*, 171 F. Supp. 2d 1075, 1090-91 (C.D. Cal. 2001).

[32] "readme.txt" from Destiny's Child, *The Writing's On the Wall*, Columbia, 1999 (emphasis added), available also at http://www.loc.gov/copyright/reports/studies/dmca/sec-104-report-vol-3.pdf, at p. 503 (DMCA Section 104 Report, vol.3, Appendix 9, Hearing Transcript Appendix 4).

[33] The "Universal Music Group / Intertrust Technologies Corporation End User License Agreement" is no longer being offered, but its text was included in testimony before the Copyright Office and is available at http://www.loc.gov/copyright/reports/studies/dmca/sec-104-report-vol-3.pdf, at p. 491 (DMCA Section 104 Report, vol.3, Appendix 9, Hearing Transcript Appendix 3). The following are excerpts from the eight-page agreement required to download a single copyrighted work:

This license agreement ("License Agreement") is a legal agreement between you on one hand and InterTrust Technologies Corporation ("InterTrust") and Universal Music Group, Inc. ("UMG") on the other (together "Licensors"). . . . By installing, copying, or otherwise using the Software, you . . . agree to be bound by its terms and conditions. . . .

[1.] (b) . . . UMG hereby grants you a limited, nonexclusive, nontransferable, nonsublicensable right to use the UMG Software, as such software has been delivered to you, on a single computer solely as an end user or for end users. . . .

[3.] (b) . . . you will not under this License Agreement: (i) rent, lease, loan, sell, copy (except as permitted above), or distribute the Software in whole or in part; . . . .

5. Authorized Use of UMG Content. The Software may enable you to listen to, view, and/or read (as the case may be) music, images, video, text, and other material that may be obtained by you in digital form. This material, collectively "Content," may be owned by UMG or by third parties. However, in all circumstances, you understand and acknowledge that your rights with respect to Content you obtain for use in connection with the Software will be limited by copyright law and by the Business Rules with which authorized copies of the Content are electronically packaged. "Business Rules" are the rules assigned by a Content owner to its Content that limit your access to and use of Content. . . .
. . . the Content owner may grant you the right to listen to an audio track he or she owns in exchange for some payment by you or no payment by you; the Content owner may grant you the right to listen to an audio track for a specific number of playbacks or for as many playbacks as you wish; . . . In the absence of contrary Business Rules provided with a Content offer, the Business Rules listed on Schedule A (which appears below and is an integral part of this License Agreement) shall apply. . . .
. . . UMG, as a Content owner, reserves the right to use the Software at any time to enforce the Business Rules with or without notice to you. . . .

SCHEDULE A - Business Rules . . . .

3. You may not transfer your rights to use any particular copy of Content to another. For example, you may not transfer your rights to another at death, in divorce, or in bankruptcy. This is not an exclusive listing; it is only a set of examples. . . .

4. You may not transfer or copy Content (with the rights you have purchased) to another computer, even if both computers are owned by you. . . .

6. When you purchase the right to unlimited use of Content, the use rights associated with that Content terminate upon your death.

[34] *Adobe Systems, Inc. v. One Stop Micro, Inc.*, 84 F. Supp. 2d 1086 (N.D. Cal. 2000). Nimmer characterizes this result as untenable. “It manages to transform a contractual term that software purveyors unilaterally include in their contracts into a binding provision on the world – even on parties who are not in privity of contract – and one that, moreover, undoes the dictates of Congress by undermining an essential feature of the Copyright Act!” 2 M. Nimmer & D. Nimmer, NIMMER ON COPYRIGHT § 8.12[B][1][d][i] (2002) (exclamation point in original). A footnote to that passage declares that it “subverts established law” since 1908, *id.* at n. 37.37. Nimmer adds that, even if privity were to exist, “a concern would still arise ‘whether the use of state contract law to avoid the first sale doctrine was statutorily or constitutionally preempted.” Nimmer, § 8.12[B][1][d] (quoting *Central Point Software, Inc. v. Global Software Access., Inc.*, 880 F. Supp. 957, 964 n.4 (E.D.N.Y. 1995).

[35] *SoftMan Prods. Co. v. Adobe Systems, Inc.*, 171 F. Supp. 2d 1075 (C.D. Cal. 2001).

[36] *Id*. at 23-24 (footnotes omitted, quoting Mark A. Lemley, Intellectual Property and Shrinkwrap Licenses, 68 S. Cal. L. Rev. 1239, 1282 (1995)).

[37] It may be that copyright holders are preferring the use of access control technologies not only because of the effective technological enforcement, but also precisely because the use of EULAs in restraint of trade invited too much scrutiny under Section 1 of the Sherman Act. Nevertheless, the "unilateral" imposition of access control technologies without agreement from the buyer may not escape Sherman Act Section 1 scrutiny entirely, since two other agreements are needed to restrain trade. The first is the type of agreement Universal entered into with Intertrust, to employ Intertrust's digital controls to restrain trade. The more cumbersome agreements in restraint to trade, however, are those in Part IV, below, discussing the increasing efforts to convert "standard-setting" into a tool to force the technologies used by others to automatically carry out the copyright holder's instructions in restraint of trade.

[38] The right of the copyright holder to deny access to a copy until payment for the download has been secured is not disputed. It is, for example, entirely reasonable within the grant of copyright to handle delivery of the digital bits in one technological transaction, confirm that the download is complete and accurate, process the payment for the license to reproduce the copy, and finally unlock access to the lawfully made copy. Clearly, if the consumer were to fail to pay for the copy after the copy was made, it could not be characterized as a "lawfully made" copy, and access could lawfully be denied. Such denial of access serves to ensure that the copy is, in fact, lawfully made.

[39] In the latter case, encrypted copies can be made without restriction, but the process of decrypting associates the copy with the equipment's EID, or "equipment identifier," which is a 48-bit unique number used to identify a specific piece of equipment, and will not allow the copy to be played using another piece of equipment.

[40] Copyright holders often offer fear of piracy as a justification for these actions, but the fact is that tethering and time-outs are not intended to prevent unauthorized reproduction (which is a right within the copyright grant) but to prevent unauthorized private performances and transfers (both of which fall outside of the copyright grant and are rights reserved to the public). Moreover, the technology to tether or time out is distinct from the technology to prevent unauthorized reproduction. For example, a proposal made by StreamTone for EntertainmentXML before the Copy Protection Technical Working Group (CPTWG) and the Motion Picture Association of America (MPAA) gave examples of "rights" that could be governed in this new environment as "play 10, no recording." *See* http://www.cptwg.org/Assets/Presentations/StreamTone-cptwg-0402.ppt at slide 7. A restriction to 10 plays restrains conduct that is, by law, beyond the reach of the copyright monopoly right. And Macrovision, a major provider of copy protection technology used by the major motion picture studios, markets its copy protection technology apart from its DRM technology. *Cf.* www.macrovision.com/solutions/video/copyprotect with www.macrovision.com/solutions/video/drm/overview.php3.

[41] See p.36 for further discussion of copyright misuse.

[42] *See, e.g., United States v. Paramount Pictures*, 334 U.S. 131 (1948); *United States v. Loew's, Inc.*, 371 U.S. 38 (1962); and *MCA Television Ltd. v. Public Interest Corp.*, 171 F.3d 1265 (11th Cir. 1999).

[43] Because the intellectual property is separate from the copy, Section 202, the copy is not what is being performed. Rather, it is the work itself that is being performed.

[44] This is a point of confusion best cleared up by every day examples. A television station must have a license to broadcast (publicly perform) a copyrighted motion picture. The television viewer, in contrast, needs no license to watch the broadcast, whether at home, at a friend's house, or on the televisions set out as floor samples at an electronics store. *Fortnightly Corp. v. United Artists*, 392 U.S. 390, 398-99 (1968). Similarly, a theater needs a license to publicly perform a movie, but once the public performance is licensed, it does not matter how many patrons watch it. In fact, someone who sneaks into the theater to watch the movie without paying may violate local laws protecting the theater owner from theft of service or trespass, but in no way violates any copyright.

[45] 18 U.S.C. § 606, which prohibits the theft of satellite or cable signals, has nothing to do with whether the programming is copyrighted nor whether the public performance by the cable or satellite company was authorized by the copyright owner.

[46] *Fortnightly Corp. v. United Artists Television, Inc.*, 392 U.S. 390, 393-95 (1968 (citations omitted).

[47] *Twentieth Century Music Corp. v. Aiken*, 422 U.S. 151, 155 (1975) (footnotes omitted).

[48] *Sony Corp. of America v. Universal City Studios, Inc.*, 464 U.S. 417, 468-69 (1984), Blackmun, J., dissenting (footnotes omitted).

[49] *Id.* at 469, n.19, emphasis by the Court, citing the Register's 1961 Report at 30.

[50] *Columbia Pictures Indus., Inc. v. Prof. Real Estate Investors, Inc.*, 866 F.2d 278 (9th Cir. 1989).

[51] *On Command Video Corp. v. Columbia Pictures Indus.*, 777 F. Supp. 787 (N.D. Cal. 1991)

[52] *Aiken*, 422 U.S. 151, 163 (footnote omitted) (rejecting the notion that each listener needs a license for a single performance). (In a recent proceeding before the Copyright Office to establish the royalty rate for public performances through wedcasting, a major effort was underway to erode this distinction by establishing a "per listener" basis for calculating the royalty. *See* http://www.copyright.gov/carp/webcasting_rates.html for further information on this proceeding.)

[53] *See* Holly Wagner, "UPDATE: Movielink's New CEO Talks Business," *Video Store magazine*, Feburary 1, 2002, available at www.hive4media.com/news//html/industry_article.cfm?article_id=2539, and text accompanying footnotes 80 and 82.

[54] For example, pressplay boldly asserts control over private performances of lawfully made copies owned by its "subscribers," and will prevent anyone from playing their own legal copies if they refuse to continue paying a monthly fee. Under its "terms and conditions," pressplay explains this in the context of what it calls a "conditional download" at http://www.pressplay.com/terms.html:

> A "conditional download" means a Track that you may save to the hard drive of your personal computer and play back as many times as you want through the press*play* Client

for so long as your subscription is current and active. You may copy each conditional download to one additional personal computer that you own (i.e. a total of two copies) (see "Sync/Restore" below). You may not and cannot share conditional downloads with any other person or entity. press*play* will automatically renew your rights to all of your conditional downloads at the beginning of each Subscription Month (as defined below under "Charges/Billing: Agreement to Pay"), so long as your subscription remains current. This means that if you want to be able to play any conditional download at any time after the end of a Subscription Month, you must log on to the Service so that press*play* can renew your rights for those Tracks. Conditional downloads will continue to accumulate so long as you continue to be a press*play* subscriber (i.e., all Tracks that you have previously downloaded will continue to play in each new month, and you will also be able to download additional Tracks during that month equal to the amount permitted under your subscription package). However, if you do not use the maximum number of conditional downloads that your subscription package allows in any particular month, the remainder will NOT carry over to the following month (e.g. if your package includes 30 conditional downloads, but you do not download all 30 during that month, you will still be able to download only 30 the next month). The press*play* Client will count the number of times that you play a conditional download, including while you are offline, for purposes of royalty accounting to artists contributing their music to the Service.

This "royalty accounting" referenced in the last sentence is itself an aberration, as it is pursuant to an Agreement with the National Music Publishers Association to forgo the royalty due for the download (the so-called "mechanical" license) in exchange for a share of the revenue from unauthorized charges for private performances. *See* Comments of National Association of Recording Merchandisers and Video Software Dealers Association, *In the Matter of Mechanical and Digital Phonorecord Delivery Compulsory License*, Docket No. RM 2000-7B, before the United States Copyright Office, Library of Congress, February 6, 2002, available at http://www.copyright.gov/carp/dpd/dpd005.pdf.

[55] This is an image from the old www.moviefly.com site. The current site is different, and appears to be owned by Sony Pictures Digital Entertainment.

[56] Holly Wagner, "UPDATE: Movielink's New CEO Talks Business," *Video Store magazine*, Feburary 1, 2002, and text accompanying notes 80 and 82, below.

[57] *MCA Television Ltd. v. Public Interest Corp.*, 171 F.3d 1265 (11th Cir. 1999).

[58] Though beyond the scope of this paper, it is no secret that some of the major copyright holding companies are also investors in companies providing ancillary products and services they tie to their licenses to reproduce or publicly perform.

[59] The two joint ventures, which include all seven major motion picture studios, are **Movielink** (formerly MovieFly), a joint venture of AOL Time Warner, MGM Studios, Sony Pictures Entertainment, Viacom's Paramount and Vivendi Universal's Universal Studios; and **movies.com**, a joint venture of News Corp.'s Twentieth Century Fox and Walt Disney's Disney Studios. As of this writing, News Corp. had announced its withdrawal from the movies.com joint venture, while leaving open the possibility of licensing its works (presumably on the reproduction masquerading as a public performance model) to Disney's venture.

[60] After all, there is substantial overlap in ownership among major motion picture studios and major record companies, such as Sony, AOL/Time Warner, and Vivendi-Universal.

[61] I use the term "retailers" in its broadest sense to include any entity that is the ultimate link in the sales interface with the consumer of a product or service. Thus, retailers may include suppliers who make direct sales, and may include merchants who sell physical products from physical stores and those who digitally deliver products or services over the Internet.

[62] Statement of National Association of Recording Merchandisers, Hearing on "Online Entertainment and Copyright Law: Coming Soon to a Digital Device Near You," Committee on the Judiciary, United States Senate, April 3, 2001.

[63] *See* April 30, 2001 Response of Mike Farrace, Senior Vice President, Digital Business, Tower Records/Books/Video, MTS, Inc., to Written Questions Asked By Senators Hatch, Leahy and Kohl Pursuant to April 3, 2001 Hearing of the U.S. Senate Judiciary Committee on "Online Entertainment and Copyright Law: Coming Soon to a Digital Device Near You," response to question #8 from Senator Hatch, describing the types of services performed in delivery of digital downloads in comparison to pre-packaged music.

[64] *See* n.79, *infra*, for Department of Justice correspondence addressing the parallel issue of a joint venture's inclusion of non-essential patents in a patent pool.

[65] *See* Form 10-Q, Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the Quarterly Period Ended March 31, 2002, Commission File Number 0-23137, RealNetworks, Inc.

[66] *See, e.g.,* pressplay's model at http://www.pressplay.com. The five licensed "affiliates" are unable to compete on price, selection or other terms and conditions, as each will offer the same thing. Even the 14-day trial is the same, each affiliate's web page looks virtually identical, and the "terms and conditions" of each is the single pressplay terms and conditions. There is no room for serious retail competition.

[67] *Lasercomb America, Inc. v. Reynolds*, 911 F.2d 970, 976 (4th Cir. 1990) (citations omitted).

[68] *Id.* at 977 (quoting with revisions from *Morton Salt*, 314 U.S. at 492) (brackets omitted).

[69] *Eastman Kodak Co. v. Image Technical Services*, 504 U.S. 451 (1992).

[70] *Id.* at 458.

[71] *See* 17 U.S.C. §§ 1201-1205.

[72] *See, e.g.*, n.87, *infra*, and accompanying text.

[73] *See, e.g.*, the "Consumer Broadband and Digital Television Promotion Act," S. 2048, 107th Congress, 2d Session, introduced by Senator Hollings March 21, 2002, which requires that standards "shall provide for secure technical means of implementing directions of copyright owners for copyrighted works" (Section (f)), even if those instructions serve only to enlarge the copyright owner's control beyond the limits imposed by the Copyright Act, some of which limitations need only be taken "into account," Section 3(e)(1).

[74] *Intellectual Property Management and Protection in MPEG Standards*, International Organization for Standardization ISO/IEC JTC1/SC29/WG11 N3943, January 2001 - Pisa,

Section 4.2. Section 4 of the document describes the need for "two different pieces of technology: one for the identification of copyright, and one to enable its protection." There would be no antitrust concern raised by the development of standards to identify a copyrighted work and who owns the associated copyright, nor would standards to enable the protection of copyright, as such, raise a concern. The heading for Section 4.2 belies any purpose to limit the second objective to just the protection of copyright. It reads: "Protection and more" (emphasis added). And there is more. The May 21, 2002 Discussion Draft "Requirements for the Protection of Unencrypted Digital Terrestrial Broadcast Content Against Unauthorized Redistribution" published by the Broadcast Protection Discussion Group of the Copy Protection Technical Working Group requires that lawful reproductions only be technologically permitted if they are "tethered" to the "Covered Product." Tethering effectively prevents all lawful trade because the new person in possession of the lawful copy will not be able to play it. (Imagine renting a DVD that won't play because it is tethered to the first renter's player, or having a pop-up window invite you to make an additional payment to play it.) According to footnote 22 of the draft, the Motion Picture Association of America member companies oppose language that would permit the making of legal copies on removable media – media that could be sold or rented more easily than a hard drive. The net effect is that adoption and implementation of standards such as these would directly suppress completely lawful trade in legal copies (or at least place such trade under the control of copyright holders who have no right to control it under law). In apparent recognition that an agreement such as this would be unlawful, an integral part of the plan is to submit the agreement to Congress for enforcement, thereby escaping legal sanctions for what would otherwise constitute private suppression of competition and enlargement of the copyright monopoly.

[75] Section 106, which is the sole section from which copyrights are derived, begins with the words "Subject to Sections 107 through 121," which contain specific limitations such as fair use (Section 107), promotional use (Section 110(7)), and entitlements of the owners of lawfully made copies (Section 109). Thus, while some advocates for the major copyright holding companies like to characterize certain privileges specified in Sections 107-121 as merely "limitations" on the right of the copyright owner, by its own terms the grant of the copyright is subject to these limitations *ab initio*. The grant itself does not extend to, for example, control over trade in lawfully made copies owned by others.

[76] *Register's Report on the General Revision of the U.S. Copyright Law* (1961), at 5.

[77] *United States v. Columbia Pictures Indus.,* 507 F. Supp. 412 (S.D.N.Y. 1980), *aff'd* 7 Media L. Rep. 1342 (2nd Cir. 1981).

[78] Julian von Kalinowski, 4 ANTITRUST LAWS AND TRADE REGULATION, 2d. Ed., § 74.06[2] (2002) (citing *Straus & Straus v. American Publishers' Ass'n*, 231 U.S. 222 (1913) and *Alden-Rochelle, Inc. v. American Soc'y of Composers*, 80 F. Supp. 888 (S.D.N.Y. 1948)).

[79] The Department of Justice has already raised concern about the effects of pooling where the pool includes non-essential patents. "Inclusion in the pool of one of the patents, which the pool would convey along with the essential patents, could in certain cases unreasonably foreclose the competing patents from use by manufacturers; because the manufacturers would obtain a license to the one patent with the pool, they might choose not to license any of the competing patents, even if they otherwise would regard the competitive patents as superior." Letter from Joel I.

Klein to Garrard R. Beeney, Esq., December 16, 1998, at p.10. It stands to reason that this concern would be just as valid where pooled copyrighted works were made available only on condition that certain non-essential technologies or business models were employed, thereby foreclosing competition in competing and possibly superior technologies and business models.

[80] Holly Wagner, "UPDATE: Movielink's New CEO Talks Business," *Video Store Magazine*, Feburary 1, 2002, available at www.hive4media.com/news//htnl/industry_article.cfm?article_id=2539.

[81] The copyright holder has the right to authorize the public performance, but the decision whether to cover the cost of the license and earn a profit from the public performance by selling advertising on "free" television broadcasts, charge for cable subscriptions, or charge cable subscribers an additional "per-view" fee is not within the exclusive rights of the copyright holder. *See, e.g, United States v. Paramount Pictures, Inc.,* 334 U.S. 131, 142 (1948) (license to publicly perform a motion picture does not entitle the copyright owner to set minimum theater admission prices).

[82] Holly Wagner, "UPDATE: Movielink's New CEO Talks Business," *Video Store Magazine*, Feburary 1, 2002.

[83] *United States v. Columbia Pictures Indus.,* 507 F. Supp. 412 (S.D.N.Y. 1980), *aff'd* 7 Media L. Rep. 1342 (2nd Cir. 1981).

[84] Source: Video Software Dealers Association.

[85] *Id.*

[86] *Id.* This represents combined retail rental revenue from VHS and DVD formats. To be clear, this is rental revenue at retail, and does not represent either the revenue from sales of VHS tapes and DVDs to the retail stores nor does it distinguish the studio share of revenue from "revenue sharing" arrangements the studios may have entered into with some retailers. The purpose of using these numbers is to more accurately portray consumer demand in the video rental market.

[87] *Loew's*, 371 U.S. at 48, n.6. The Supreme Court's reaction to the district court's findings are instructive:

> The district judge found that each copyrighted film block booked by appellants for television use "was in itself a unique product"; that feature films "varied in theme, in artistic performance, in stars, in audience appeal, etc.," and were not fungible; and that since each defendant by reason of its copyright had a "monopolistic" position as to each tying product, "sufficient economic power" to impose an appreciable restraint on free competition in the tied product was present, as demanded by the *Northern Pacific* decision. We agree. These findings of the district judge, supported by the record, confirm the presumption of uniqueness resulting from the existence of the copyright itself.

Id. at 48 (citation to the lower court and footnote 6 omitted). Surely, the movies of today are no less unique, and no more fungible.

[88] *MCA Television Ltd. v. Public Interest Corp.*, 171 F.3d 1265 (11th Cir. 1999)

[89] *See* note 19, *supra.*

[90] *See* note 76, *supra*.

[91] The fact is, none of the joint ventures offered by the copyright holding companies in the music or movie industries remotely resemble what a serious competitive retailer would offer its consumers. MusicNet "created a service that lacked just about everything that makes online music downloads appealing." Mathews, et al., "Music Industry Finally Online," *The Wall Street Journal*, May 7, 2002, at A1. Pressplay offers subscribers the option of downloading music (*i.e.* paying for the license to reproduce the music into copies that the consumer owns), but says "You can play downloads as much as you want as long as your membership is active," which is like saying we get to take your CDs away if you stop paying us forever. *See* http://www.pressplay.com/faq.html#burns. It answers the question "If I cancel, do I get to keep my downloads?" with "If you choose to cancel your pressplay membership, you will lose the ability to play the downloads that you acquired through pressplay at the end of the period you paid through." *See* http://www.pressplay.com/faq.html#registration_06. Movielink promises a model like pressplay's in that regard. *See* Figures 12-14, and text accompanying notes 80 and 82.

[92] This is already the case in the music industry, where the Recording Industry Association of America, on behalf of its members, entered into an Agreement with the National Music Publishers Association and the Harry Fox Agency under which the music publishers would forgo the full profits from the statutory royalty due them for each downloaded music file in exchange for a share in the revenue to be generated by using technological access controls to charge consumers for private performances (every 30 days or every 12 plays) of the copies lawfully made and owned by the consumer. *See* October 5, 2001 Agreement, available at http://www.loc.gov/copyright/carp/10-5agreement.pdf, beginning at page 11.

[93] I am certainly not the first to point this out. See Timothy White, "The Music Industry's Web Of Intrigue," *Billboard* March 2, 2002, p.3. "Imagine an industry that has allocated (and mostly spent) more than $4 *billion* in funds on ventures that have thus far made back less than $1 *million* – globally. Think about it. Spending $4 billion to earn under $1 million." *Id.* (emphasis in original). "Music and media execs have told *Billboard* that they do not expect any profits in online digital music sales for at least two years." *Id.* This comfort level in passing up the immediate profits to be made from licensing to competing retailers the right to make online music sales without controlling the competition speaks volumes of the market power enjoyed by virtue of the copyright. The same scenario is unfolding in the motion picture industry, as copyright holders systematically prevent any legitimate middle ground competition to evolve between their "sole source single business model" approach and competitive piracy.

[94] Source: Video Software Dealers Association.

[95] For a fascinating examination of how the development of video rental paralleled the development of book circulating libraries, see Richard Roehl and Hal Varian, "Circulating Libraries and Video Rental Stores," *First Monday*, volume 6, number 5 (May 2001), available at http://www.firstmonday.dk/issues/issue6_5/roehl/index.html#r2. The history of the development of both models underscores the importance of maintaining free and unencumbered trade in lawfully made copies.

[96] *See* James Lardner, *Fast Forward: Hollywood, the Japanese, and the Onslaught of the VCR*, Norton, New York, 1987.

[97] *See* note 4, *supra*, and accompanying text. *See, also,* Jessica Wolf, "Is DVD Being Devalued Before Its Time?" *Video Store Magazine*, May 12-18, 2002, p.1, for observations concerning other factors, such as retail competition and sales of used DVDs, that tend to drive down the price of DVD.

[98] U.S. Copyright Office, "DMCA Section 104 Report," 75-76, 164 (2001). We do take issue, however, with the Copyright Office's conclusion that the problems raised by access control technologies and non-negotiable contracts are speculative, or premature, or beyond the scope of its report. The restrictions on retailers' rights to distribute and consumers' rights to transfer and use fully the products they lawfully purchase and download are not speculative and consideration of their impact is not premature, as evidenced by the Movielink venture. These issues also fall squarely within the Copyright Office's mandate from Congress. Yet the Copyright Office's report makes no mention of Movielink and the similar Movies.com service, despite the fact that it was public knowledge that these services were being developed. The problems created by overly restrictive access control technology and non-negotiable contracts need to be addressed now, not at some indefinite time in the future. To fail to do so leaves to the designers of access controls the allocation of rights between consumers and copyright owners, a function that should remain the exclusive responsibility of Congress.

[99] 334 U.S. 131 (1948).

[100] 371 U.S. 38 (1962).

[101] *Sony Corp. of Am. v. Universal City Studios, Inc.*, 464 U.S. 417, 432 (1989). The Department of Justice has previously taken a dim view of extensions of intellectual property rights beyond their scope or term. See Letter from Joel I. Klein to Gerrard [sic] R. Beeney, Esq., June 26, 1997, p.9 ("A licensing scheme premised on invalid or expired intellectual property rights will not withstand antitrust scrutiny").

[102] *Tricom, Inc. v. Electronic Data Systems Corp*., 902 F. Supp. 741, 745 (E.D. Mich. 1995) (quoting *Lasercomb Am., Inc. v. Reynolds*, 911 F.2d 970, 978 (4th Cir. 1990)).

[103] 210 U.S. 339 (1908).

[104] *Id.* at 350.

[105] *Id.* at 351.

[106] *Motion Picture Patents Co. v. Universal Film Mfg Co*., 243 U.S. 502.

[107] *Id*. at 519. This position was followed in *Carbice Corp. of Am. v. Am. Patents Dev. Corp*., 283 U.S. 27 (1931) (owner of a patented package that used solid carbon dioxide could not obligate licensees to use its own solid carbon dioxide). In *Carbice*, the court noted that the law had already risen to prevent the unwarranted extension of other limited monopolies, such as trademarks and trade names. *Id*. at 35 n.5 (characterizing this limitation as being "inherent" in the monopoly grant).

[108] 243 U.S. at 516. "The patent law furnishes no warrant for such a practice and the cost, inconvenience and annoyance to the public which the opposite conclusion would occasion forbid it." *Id.*

[109] *Morton Salt Co. v. G.S. Suppiger Co.*, 314 U.S. 488 (1942).

[110] *Id*. at 490.

[111] *Id*. at 494.

[112] *Id*. at 492.

[113] *Id*. at 494.

[114] 334 U.S. 131 (1948).

[115] 334 U.S. at 156.

[116] *Id*. at 157 (quoting the lower court, citations omitted).

[117] *Id*. at 158.

[118] *Lasercomb Am., Inc. v. Reynolds*, 911 F.2d 970, 976 (4th Cir. 1990), quoting from *Morton Salt*, 314 U.S. at 491. Moreover, copyright misuse is such a violation of public policy that some courts will not require that the person against whom the misuse is directed be a party to the litigation. "[T]he fact that appellants here were not parties to one of Lasercomb's standard license agreements is inapposite to their copyright misuse defense." *Lasercomb*, 911 F.2d at 979.

[119] Conversely, in *McGuire v. Regents of the University of Michigan*, No. 2:99CV1231, 2000 WL 1459435 (S.D. Ohio September 21, 2000), the court demonstrated a willingness to extend the copyright misuse doctrine to encompass an affirmative claim in the area of trademark law if the factual record to be developed would support such a theory.

[120] 334 U.S. 131, 156-159 (1948).

[121] 371 U.S. 38 (1962).

[122] *Paramount Pictures*, 334 U.S. at 159 (referencing the public policy of antitrust laws). The discussion was under the heading "Restraint of Trade," *id*. at 141. "The antitrust laws do not permit a compounding of the statutorily conferred monopoly." *Loew's*, 371 U.S. at 52.

[123] *Paramount Pictures*, 334 U.S. 158.

[124] *Id.*

[125] *Id.*

[126] *Loew's*, 371 U.S. at 45 and n.4. *See also id.*, at 48 and n.5

[127] *Id.* at 45 n.4.

[128] *Id*. at 48 n.6.

[129] *Broad. Music, Inc. v. Columbia Broad. Sys., Inc.*, 441 U.S. 1 (1979).

[130] *Columbia Broad. Sys., Inc. v. Am. Soc'y of Composers*, 400 F. Supp. 737, 741 (S.D.N.Y. 1975).

[131] *Id*. at 745.

[132] *Columbia Broad. Sys., Inc. v. Am. Soc'y of Composers*, 562 F.2d 130 (2d Cir. 1977).

[133] *Id*. at 141 n.29.

[134] 441 U.S. 1 at 4 (emphasis added).

[135] *Id.* at 6 and n.7.

[136] *Id.* at 6.

[137] *Id.*, at n.9.

[138] *Id.* at 7.

[139] *Id*. at 24 (referencing footnote 9). In 1988, Congress enacted the Patent Misuse Reform Act, which limits a finding of patent misuse in tying cases to those where the patentee has market power in the relevant market for the patented tying product. 35 U.S.C. § 217(d)(5). The fact that Congress chose not to so limit claims of copyright misuse is instructive in two ways. First, by limiting the requisite showing of market power to patent misuse, it demonstrated its intent that claims of copyright misuse not be so limited. Second, there may be more than one way to build a patented mouse trap, so proof of market power in the market for mouse traps would appear to be a reasonable prerequisite. Copyrights, in contrast, protect unique works. There may be more than one way to tell a story about characters on a plantation in the South around the time of the civil war, but there is only one *Gone With the Wind*, and the audience appeal of *Return of the Clones* is not diminished by having previously viewed myriad space-based science fiction movies or having seen every previous *Star Wars*-based movie. Given that the Patent Misuse Reform Act does not apply to copyright misuse, it stands to reason that the *per se* liability for copyright-based ties would apply, just as *per se* liability for patent tie-ins would apply prior to 1988. *See, e.g., In re Recombinant DNA Technology Patent and Contract Litigation*, 850 F. Supp. 769, 775-76 (S.D. Ind. 1994) (had it not been for the Patent Misuse Reform Act, tie-ins and tie-outs would have been adjudged patent misuse *per se*).

[140] *Columbia Broad. Sys., Inc. v. Am. Soc'y of Composers*, 607 F.2d 543, 544-45 (2d Cir. 1979).

[141] 546 F. Supp. 274, 285, n.28, and 296, n.45 (S.D.N.Y. 1982), rev'd on factual grounds, 744 F.2d 917 (2d. Cir. 1984).

[142] 546 F. Supp. at 285.

[143] *Id.* at n.28, which cross-references n.45.

[144] *Id.* at 296, n.45 (citing *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 139 (1969), and *BMI v. Moor-Law, Inc.*, 527 F. Supp. 758, 772-73 (D. Del. 1981)).

[145] 171 F.3d 1265, 1277 and n.13 (11th Cir. 1999).

[146] *SoftMan Prods. Co. v. Adobe Systems, Inc.*, 171 F. Supp. 2d 1075 (C.D. Cal. 2001). See discussion of *Softman* at notes 30 & 31, above.

[147] *Tricom, Inc. v. Electronic Data Systems Corp.*, 902 F. Supp. 741, 745 (E.D. Mich. 1995) (citations omitted).