

Exhaustion of copyrights on the Internet?

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1. Introduction

1.1 Notion of the principle of exhaustion.

The concept of copyright law was traditionally intended to protect authors in their original and creative, literary and artistic works. As a consequence States granted authors exclusive rights to ensure that they will continue to create and that they will receive an appropriate remuneration for use of their works.

In general, authors are granted the exclusive rights to make reproductions, decide how and when a work should be made available to the public and to sell or in any other way distribute, perform or display a work to members of the public. The authors may also transfer some or all of their exclusive rights to a third party by contractual agreement or by less formal consent that authorizes some kind of exploitation of works.

However, intellectual property rights may be deemed as a monopoly, it is worth keeping in mind that States had granted exclusive rights to authors in return for their works are being made available to members of the public.

Thus, the copyright protection is also justified by the public interest. The States impose certain limitations thereto. Copyright protection is always of limited duration. After a certain period of time, works fall into the public domain and may be used freely by all. Some limited uses of works are also unconditional. The copyrighted work may be subject to statutory licensing with a view to preventing the copyright owner from restraining the use of it. It follows from the foregoing that States try to strike the balance between the contrary interest of authors and members of the public.

State attempts to keep a balance between authors and public interests are well exemplified by the principle of exhaustion of copyrights¹. The theory of exhaustion affects the exclusive right of distribution of copies in a tangible form. The theory is based on the principle that after the first sale the right holder is unable to invoke his/her intellectual property rights and particularly the right to distribution. Once a work has been distributed by right owner or with his/her consent, the distribution right in that particular copy is

¹ J.A.L. Sterling, World Copyright Law, Sweet & Maxwell London 2001, p.621.

exhausted. As a result the copyright holder can no longer prevent sale or other distribution of that copy.

In other words the buyer of a book may do with it what he or she pleases. One can read it or not, can sell it to his/her friends or even throw it away. The copyright law explicitly gives him/her the right to do this, once the tangible copy of a work has been sold by or with the consent of copyright owner.

The doctrine of exhaustion gives expression to the limitations imposed on the exercise of the exclusive right of distribution. It is important to keep in mind that literary and artistic works, by or with the consent of copyright holder, may be subject to commercial exploitation by means other than the first sale.

This applies for example to the rental of video-cassettes, which reach a different public from the market for their sale or gifts. The exhaustion does not take place for copies made available to the public with the consent of a copyright holder, but not subject to the sale.

It should also be noted that problems arise concerning the meaning of consent. It can be found on the basis that the time for copyright protection had run out, that the copyright holder had enjoyed his/her legitimate protection, and therefore the goods can move freely. It can alternatively be decided that the sale of a work, in such a situation, was not with the consent of the copyright holder, but only because the copyright had run out and therefore there is no consensual exhaustion of rights. The European Court of Justice adopted the latter course².

It is also contented that the limit of the principle of exhaustion is territorial; the exhaustion is restricted to the European Union. Within the EEA the principle of Community exhaustion also applies; once the copy of a work is put on the market anywhere within EEA by or with the consent of copyright owner the copy can circulate freely within EEA and the right owner can not prevent its further sale or distribution.

² Case 341/87, EMI Electrola GmbH v. Patricia Im und Export (1989) ECR 79.

1.2 The legal context of the principle of exhaustion.

It is apparent from the scope of the principle of exhaustion that it provides means to reconcile the free movement of goods with the territorial character of intellectual rights. After the first marketing the right holder is unable to invoke his intellectual property rights, and particularly the right to distribution in another Member State, in order to prevent the sale of work via parallel imports³. The EU Market is treated as a domestic market. The exhaustion rule will, however, not apply if the work is placed on the market by a third party without the right holder consent.

The principle of exhaustion therefore is an integral part of the law laid down in Article 30 to 36 of the EC Treaty, which deal with the free movement of goods. Article 30 provides that Articles 28 and 29 will not preclude prohibitions on imports or exports, which are justified, inter alia, on grounds of the protection of industrial or commercial property.

At the international level the question of the exhaustion of the rights is not covered in the Berne and Rome Conventions.

On the other hand, the express references to the principle of exhaustion can be found in the TRIPs Agreement⁴. Following the TRIPs Agreement, Article 6 “For the purpose of dispute settlement under this Agreement, subject to the provision of Articles 3 and 4 nothing in this Agreement shall be used to address issues of the exhaustion of intellectual property rights”⁵.

According to wording of TRIPs Agreement, States remain free to regulate the question of exhaustion, provided they treat non-nationals in the same way as nationals. In addition, for future treaties, Conventions create obligations concerning the principle of exhaustion, the most favorable treatment, that such agreement may provide would have to be extended to nationals of all countries that are part of the TRIPs Agreement.

³ See Para 1.

⁴ The TRIPs Agreement: Agreement on Trade- Related Aspects of Intellectual Property Rights, WTO and WIPO(http://www.wto.org/english/tratop_e/trips_e/7t_aglm_e.htm).

⁵ The TRIPs Agreement, Article 3 is concerned national treatment and Article 4 with most-favored national treatment.

The principle of exhaustion has also been tackled in secondary legislation. The Directive on legal protection of computer programs⁶ provides in Article 4 (c) " ... The first sale in the Community of a copy of a program by the right holder or with his consent shall exhaust the distribution right within the Community of that copy, with the exception of the right to control further rental of the program or a copy thereof."

Another example is the Rental Right Directive⁷. Article 1(4) states that the right to authorize or prohibit the rental and lending of originals and copies of copyrighted works and other protected matters " shall not be exhausted by any sale or other act of distribution of originals and copies of copyright works and other subject matter". Article 3 specifies that this Directive is without prejudice to the provision on the rental of computer programs in the Computer Program Directive. Moreover the Rental Right Directive, Article 9 (2) states that "The distribution right shall not be exhausted within the Community in respect of object... except where the first sale in the Community of that object is made by right holder or with his consent."

Following the Report on implementation of the Software Directive⁸, the Commission has explicitly stated that the exhaustion "only applies to the sales of copies i.e. goods, whereas supply through on-line service does not entail exhaustion."

The first observation, which arises, is that the European principle of exhaustion applies only to physical not digital copies of copyrighted works.

1.3. Technological impact on copyright law.

The Internet has become the instrument by which people throughout the world exchange and share ideas, information and gradually, goods and services.

The recent growth of Internet Computer Services has created the entirely new environment for exploitation and access to works protected by copyright law.

⁶ The Directive 91/250/EEC of 14 May 1991 on the legal protection of computer programs JOB L 122 17.05.1991.

⁷ The Directive 92/100/EEC of 19 November 1992 on rental right and lending right and on certain rights related to copyright in the field of intellectual property JOB L 346 27.11.1992 p.61.

⁸ The Report on the implementation of Software Directive of April 10, 2000. COM (2000) 199, s. VII. 1 p.17 Fn.17 refers to an answer of Commissioner Monty to an oral question in the Parliamentary Debates of July 11, 1995.

Text, music and images are reduced to digital data and can be transmitted in digital form at high speed. Everybody with connection to the Internet can obtain perfect copies of digital originals throughout the world, partially without any costs.

The enactment of the WIPO Internet Treaties in 1996 confirmed that the copyright law is prevailing in the digital environment. A number of exclusive rights have been formally introduced. Among these are the right of distribution, the rental right and the right to communicate the work to the public. At the close of the Diplomatic Conference on the WCT, the delegation adopted the following Agreed Statement; “ The reproduction right, as set in Article 9 of the Berne Convention, and the exceptions permitted there under, fully apply in the digital environment, in particular to the use of works in digital form. It is understood that the storage of a protected work in digital form in an electronic medium constitutes a reproduction within the meaning of Article 9 of the Berne Convention”⁹.

This migration of intellectual property onto the Internet can be seen with respect to each species of rights. Unfortunately very much connected to the nature and existence of the Internet is a problem of unauthorized distribution and reproduction of copyright protected materials. Best known for illegal practice is the Napster Service, which was shut down following litigation in the USA¹⁰.

In the field of copyright, vast numbers of works; literature, film and art, and notably computer programs, have already been transferred to the digital environment. For instance, one commercial operation, Ebrary, offers consumer paid access to more than 10,000 recently published titles, as well as maintaining a database of digital books for libraries¹¹.

According to Forrester Research¹², “... while only 3 % of all current online (business to consumer) sales consist of digitally- downloaded products, this level could reach 22 % of all online sales by 2004. The most dramatic growth in direct, digital download sales will probably be in the music sector, (while the sales could rise from 0,1 % of online sales in 1999 to 25 % in 2004) followed by software (rising from 7 % of online service to 40 % in 2004) and books (from 1 % of books sales online in 1999 to 13 % in 2004).

⁹ The Agreed Statements to the WIPO Copyright Treaty. WIPO Documents CRNR/DC/96 December 23, 1996 (1).

¹⁰ A and M Records v Napster Inc., 239 F 3d 1004 (9th Cir. 2001).

¹¹ www.ebrary.com .

¹² The U.S. Department of Commerce, Economics and Statistics Administration, Digital Economy 2000 p. 21, referencing Forrester Research, Spectacular Growth of Digital Delivery February 7, 2000 reported by Nua Internet Surveys. (<http://www.nua.ie>).

It follows from the foregoing that, the Internet provides a new mechanism for delivery of goods and services permitting the immediate downloading of works. Although online sale and delivery of copies of digital products such as software, books, and music-files is modeled on offline transactions the lack of consistence between offline and online purchase and delivery of these products can be observed. In particular the application of the theory of exhaustion to the digital copies of work is controversial and raises many legal problems.

|1.4. Purpose of the discussion.

The aim of this paper is to investigate factual and legal contents of application of theory of exhaustion of copyrights on the Internet. In particular I will endeavor to answer the question of to what extent, if any is the principle of exhaustion of copyrights related to or premised on Internet environment or methods of distribution?

2. Purchasing books online. Classification of transaction.

2.1 Application of the principle of exhaustion on-line. The European Union approach.

There is no doubt that the Internet facilitates creations, access, distribution, use and similar activities. This is strengthened by the fact that works circulate in non-material form in an electronic environment.

It should however also be noted that products and services available on the information superhighway are not always subject to the same rules as in the analogue world. The principle of exhaustion can exemplify this issue very well.

According to the wording of the Copyrights Green Paper¹³ “... as regards exceptions a large consensus exists that no exhaustion of right occurs with respect to works exploited on-line, as this qualifies as services”¹⁴.

The Copyright Directive¹⁵ takes the step further in restrain of an application of the principle of exhaustion on the Internet. Article 4 (2) states that:” The distribution right shall not be exhausted within Community in the respect of the original or copies of the work, except where the first sale or other transfer of ownership in the Community of that object is made by right holder or with his consent.

When this Article is read in the light of recital 28 of that Directive¹⁶, it becomes obvious that the exhaustion is restricted to the distribution of the work incorporated in tangible carriers. Moreover the Directive recital 29 states that: “... the question of exhaustion does not arise of services and online services in particular. This also applies with regard to a material copy of a work or other subject matter made by a user of such a

¹³The Follow up to the Green Paper on Copyright and related Rights in the information Society of November 20, 1996 Com (96) 568 final CH.2, Para 4.

¹⁴ See Para. 10.

¹⁵ The Directive 2001/29/EC of European Parliament and of the council of 22 May 2001 on the harmonization of certain aspects of copyright and related rights in information society OJ L 167 22.06.2001. p.10.

¹⁶ The Copyright Directive, Recital 28 “ Copyright protection under this Directive includes the exclusive right to control distribution of the work incorporated in a tangible article. The first sale in the Community of the original of a work or copies thereof by the right holder or within his consent exhausts the right to control resale of that object in Community. This right should not be exhausted in respect of the original or of copies thereof sold by right holder or with his consent outside the Community. Rental and lending rights for authors have been established in Directive 92/100/EEC. The distribution right provided for in this Directive is without prejudice to this provisions relating to the rental and lending rights contained in chapter 1 of that Directive”.

service with the consent of the right holder.... Unlike CD-ROM or CD-I, where the intellectual property is incorporated in a material medium, namely an item of goods, every online service is in fact an act which should be subject to authorization where the copyright or related right so provides.”

It can be supposed that on-line sale and delivery of products were considered to be a kind of on-line service (Recital 19), which can be equivalent to online exploitation, for example broadcasts. Furthermore as an act that must be authorized separately every time without prejudice to the future form of exploitation¹⁷.

To some extent this analogy could be found relevant. The act of broadcasting a film on television or performing a film in the cinema does not exhaust the right of copyright holder to authorize or prohibit further broadcasting or projection. Similarly, an act of uploading a work, to a website does not automatically imply the right to copy the work on the user’s computer for future reference.

Although there are a few things are common for providing an online delivery and broadcasting service the following contrast may be mentioned.

First of all, it is the broadcaster who determines the time of transmission whereas an on-line delivery is provided at a time individually chosen by the user. Unlike a broadcasting service, on-line delivery requires an active and specific request by the user. While a broadcasting service is point to multipoint communication, the online transmission is point-to-point communication¹⁸.

Another situation that should to be taken into consideration, is the case where the copyright holder expressly sells a digital product and transmits it to the buyer for downloading onto his computer. In this example, the user, due to the sales transaction is entitled to make a permanent copy of the work. It is questionable whether in this situation online delivery should be treated as broadcasting; especially since transmission is only directed to the particular user.

It follows from the foregoing that the European Commission has expressly excluded digital copies from the scope of the principle of exhaustion. This policy can nonetheless be problematic.

¹⁷ The Database Directive in recital 33 and 44 follows the structure of the Copyright Directive. Directive 96/9/EC of the European Parliament and the Council of 11 March 1996 on legal protection of databases OJ L 077 27.03.1996 p.20.

¹⁸ Kounoupias Nick; Hill Keith, on-line Distribution: Mechanical Right, Performing Right or both, Computer Law and Security Report 1996, p.226-232.

2.2 Application of the doctrine of first sale online, the American approach.

The balancing of incentives to create and provide public access to ideas and content is fundamental to U.S. copyright policy.

Pursuant to that public purpose, the Copyright Acts grants to authors the exclusive right to distribute copies of their works, 17 U.S. Code § 106 (3) but limits that right by extinguishing the copyright holders distribution right upon the first sale of each copy 17 U.S Code § 109. Section 109(a) of Copyright Act provides that "... the owner of particular copy or phonorecord lawfully made under this title... is entitled, without the authority of the copyright owner to sell or otherwise dispose of the possession of that copy or phonorecord". The provisions of that section relate clearly to material copies. As a part of an effort "to move national laws to the digital era" the Congress enacted the Digital Millennium Copyright Act¹⁹. Section 104 of the Digital Millennium Copyright Act directed the Register of Copyrights and Assistant Secretary for Communication and Information of Commerce to submit a report to the Congress evaluating the effects of the amendments made by title 1 of the DMC -A²⁰ and development of electronic commerce and associated technology on section 109 (doctrine of first sale) of title 17, United States Code and the relationship between existing and emerging technology²¹.

According to the reports there is little consensus with respect to the application of first doctrine on the Internet²². Both the proponents and the copyright community seem to agree that if the files are downloaded with the consent of the copyright owner, a "lawfully made copy or phonorecord" will have been created on the PC hard drive or tangible portable medium. Thus the doctrine of first sale (Section 109 of 17 U.S Code) would apply to the owner of that new digital copy or phonorecord²³.

Consequently in the United States digital works sold and delivered online can be subject to the principle of exhaustion while in the European Union they are not.

¹⁹ H.R. report No. 105- 551 pt2, at 21(1998), www.ntia.doc.gov .

²⁰ Title I creates two new copyrights prohibitions; one prohibits circumvention of technological measures used by copyright owner to protect their works and the other tampering with copyright management information. Technological measures are divided into two categories; measures that prevent access to a copyright works and measures that prevent unauthorized copying of work.

²¹ The Executive Summary, Digital Millennium Copyright Act, section 104 report p.1.

²² The National Telecommunication and Information Administration Report of March 2001, Part IV Conclusion p.12 www.ntia.doc.gov/ntiahome/occ/dmca2001/104gdmca.htm .

²³ See Para 19.

2.3 Classification of transactions.

There are few ways to sell printed books. The most traditional one is to distribute a book through bookshops. The copy of a book is usually sold with the consent of the copyright holder given to the publisher on the basis of a publishing contract.

A protected literary work is usually recorded on a physical carrier such as paper or bound into book and what is actually sold is a copy of this bound into a physical carrier, not the work.

In general, someone who wants to buy a book has to go to a bookshop then has to choose the book he/she likes and in form of a single transaction (a seller gives a book to the client in return for received payment) buys it. The principle of exhaustion does apply to such transaction.

Modern technology has however created a number of new ways to sell books, moreover it has created the environment for exploitation of book in new format such as electronic books.

Nowadays, it is no longer necessary to go to a bookshop in order to buy a book, unless one wishes to. Desirable books can for example be purchased by press of a button.

The web shopping sites consist of databases with associated programs stored on web server. These databases include information about products or services for sale. Web databases are also used to complete shopping transactions with users²⁴. When a user decides to buy a book online, he or she must fill out a form and send in his credit card information. That information is sent to a web database. The database, in turn, checks the validity of the credit card. If it is valid, the database sends confirmation to a user and then sends off an order to a warehouse or other distribution method that ships the product to a buyer.

In light of the European legislation one would say that the principle of exhaustion does not apply to the foregoing scenario.

However for the purpose of the discussion of the application of the principle of exhaustion principle on the Internet, the analysis of three transactions is required;

- transaction involving “ distribution service” where a book is selected, purchased online but delivered by conventional means,

- transaction involving telecommunication transport function,
- transaction, which is completed entirely online from selection to delivery.

Although these transactions are to some point alike, the key difference between them resides in distribution methods and the formats of purchased books.

2.3.1 Transaction involving “distribution service” in which a book is selected and purchased online but delivered by conventional means.

The Internet enables books to be selected and purchased online but delivered by conventional means to the mailbox of the buyer. There are numerous .com companies that rely on business models that trade in physical objects of intellectual property.

One of the most popular services for buying books online is the Amazon.com portal. In order to place the order the user of Amazon.com website has to browse or search for the items he/she would like to order. The next step is to click the title or the name of an item in order to see its product information page. All items purchased by the user will be placed in his/her Shopping Cart. Then the user has to enter his/her e-mail address and click the “Sign in” button, and enter a Shipping Address. After obtaining from the user the place of shipment, the Amazon store will estimate shipment costs and delivery dates on the order form, and in the e-mail confirming the order which the user will receive after placing his/her order. As the last step the user has to click the Place Your Order button to submit the order²⁵.

Like in the sale transaction carried out in a bookshop, online transaction results in the end in the distribution of a physical copy of a book. Repeating a standard formula of the principle of exhaustion, that the distribution right will be exhausted after the first sale by the copyright owner or with his consent the tangible copy of the work, it should be concluded that the application of the principle of exhaustion to this example is justified.

²⁵ www.amazon.com .

2.3.2 Transaction involving telecommunication transport function.

It is a fact that modern technology has enabled the sale of books in an electronic format. Nowadays electronic books are available for sale on different websites. It is also a fact that the electronic book can be fully sent to a buyer in a digital environment. It can be argued that the following scenario exposing a transaction involving telecommunication transport function is possible.

The user visited that websites, tempted by the special price, selected and purchased the book. One of the website's shipping terms and returns policies states that he/she can choose one of these shipping preferences:

1. Group my items into as few shipments as possible
2. I want my items faster. Deliver them as quickly as possible

One decided to choose the second option. As a result, the book in digital form was made available for downloading from a website onto his/her computer. In order to be able to enjoy the book, he/she had to print it. When he had printed it out the file stopped working.

In the scenario described some elements of transaction must be underpinned.

First of all, the copy printed by the user was authorized by the copyright holder. Secondly, the transmitted content was meant to be copied and permanently stored by printing it. That is why the printed copy of the book that firstly was downloaded onto the user's computer in digital format is conceptually not different from a copy sold to a buyer in a bookshop. In both cases the copy was lawfully made with the consent of the copyright holder. The difference resides only in the fact that in the event of electronic delivery it is the user who makes a copy. The technical conditions of transmission are distinguished. In both situations, at the end there is the original in the hands of copyright holder and a copy in the hands of the buyer/user.

It can be concluded that as a result of the online transaction the user is in possession of the tangible copy of the work and the copy has been distributed in the sense of the copyright law.

One might argue that distribution right is an exclusive right to control the dissemination of copies of a work. Particularly, that distribution means the transfer of a tangible product from one person to another and does not apply to the scenario described. As support for this opinion one could also argue that first of all the content from the website is transferred from the server to the user's RAM. The user, though, did not receive a tangible product but only electronic signals. Secondly, the RAM storage has only ephemeral

character. While in the case of distribution the work or copy of it remains permanently with the buyer.

On the contrary, it should be observed that in the environment of digital networks work is seldom distributed without a prior reproduction of copyrighted material and it is a copy and not the original that is distributed²⁶. In the scenario presented not only the exclusive right of making works available to the public but also the distribution right is exercised. As a consequence of the transaction described the user is in possession of a tangible copy of a book and that is why the principle of exhaustion should apply.

2.3.3 Transaction, which is completed entirely online from selection to delivery.

In this example the book was reduced to digital data with the consent of or by the copyright holder and then offered for sale on one of the shopping websites. As opposed to the previous scenario, this time the user received a book in an electronic format.

An electronic book is intended to be read on the computer screen or portable digital reading device. A reader is software that must be installed on the computer or device onto which the user downloads his/her e-book in order to read it. As a consequence of security features incorporated into software e-books readers can not manipulate, print or copy the document. One can “turn” the pages or insert a bookmark.

In this scenario, the user does not purchase a copy of the book in the sense of tangible good. It can be contended that the principle of exhaustion does not apply to the sale of e-books.

Detailed discussion on the legal aspect of digital books will be presented in the next chapter of this paper.

²⁶ Comments of the Copyright Industry Organizations (CIO Comments) August 4, 2000.

2.4 Communication on-line as an alternative to distribution right.

There is general agreement that the storage of protected works in a digital medium amounts to a reproduction within the meaning of Article 9 of the Berne Convention²⁷. The words “in any manner or form” in this provision are clearly meant to cover all methods of reproduction. There is a reproduction whenever protected works are stored in digital form or uploaded or downloaded to or from a host computer to the server. Any further duplication of the digitally stored work will be considered as a subsequent to the act of reproduction.

But since the uploaded copy is accessible for users of the network, according to the Copyright Directive²⁸ Article 3(1), the economic right such as a communication to the public is at stake rather than the right of distribution. This means that a copyright owner makes works available online not by the act of distribution but by the act of communication.

The application of the right of communication to the public instead of the right of distribution on the Internet has a significant meaning. The right should be understood in a broad sense covering all communication to the public not present at the place where communication originates. This right should cover any such transmission of a work to the public by wire or wireless means, including broadcasting²⁹.

The Internet infrastructure enables users to actively communicate with information providers. Works are made available in such a way that members of the public may access them from a place and at a time individually chosen by them (interactive on-demand transmission). But this does not mean that transmission involves distribution of copies of the transmitted works. Distribution, unlike communication, traditionally means a transfer of a tangible product from one person to another. The user, in most of cases, does not receive tangible products but only electronic signals transferred from the server to his/her computer random access memory.

On the Internet the copyright law provisions have intended to provide authors with a wide exclusive economic right. The right of communication to the public applied to an

²⁷ The Agreed Statements to the WIPO Copyright Treaty, which have been adopted by the majority of the participants of the WIPO Conference. Agreed Statement to Article 1 Para. 4 of the WIPO Copyright Treaty. WIPO Document CRNR/DC/96 December 23, 1996 (1).

²⁸ See Para 12.

²⁹ The Copyright Directive, recital 23.

online environment places the copyright owners, in position to control the use of their works with a view to getting appropriate remuneration for use and preventing unauthorized exploitation of their works.

According the Copyright Directive Article 3 the right of communication to the public consist of two elements; making a work available to the public and granting access to such works³⁰. On the Internet, making works available is a distinct act from granting actual access to them.

The exclusive right to control access may take different forms, additionally authorization given for the one type of use does not mean that other use is authorized too. Encryption methods and other techniques coupled with anti- circumvention legislation and contractual practice will allow copyright owner to block access to their works altogether or monitor the actual use that a user make of copyrighted works.

In other words a user, who wants to download the digital copy of work, prior to this, must obtain authorization by means of the consent from the copyright holder or has to lean on a statutory provision. One may easy observe that in general no explicit consent is given, as the website does not usually specify under which conditions a user may access or use the presented material.

³⁰ The Copyright Directive, Article 3 follows the structure of Article 8 of WIPO Copyright Treaty; “Without prejudice to the provision of Articles 11(1)(ii), 11bis(1)(I) and (ii), 11ter(1)(ii), 14bis(1) of the Berne Convention, authors of literary and artistic works shall enjoy exclusive right of authorizing any communication to the public of their works, by wire or wireless means, including the making available to the public of their works in such a way that members of the public may access these works from place and at a time individually chosen by them”.

3. Books as digital products.

3.1 The problem of digital products classification.

Goods and services are not difficult to distinguish in analogue world. Goods are usually characterized as tangible and movable personal property other than money (things that have value).

Service, are for instance in legal theory described as the formal delivery of writ, summons or other legal process³¹. The service has a physical presence, usually is of certain period of time and involves a purpose of acquisition of product. The service will typically be characterized as a process or an activity, goods by contrast are considered as stable and individually storable products.

It is also not difficult to differentiate when the same services and goods are placed online. However status of products, which were treated as goods in analogue world, and then reduced to digital data, appears to be very problematic.

Works in digital form loose tangibility. The user receives only electronic bits on his/her computer's random access memory. If one takes under the consideration the transmission process of these products, picture of the nature of digital becomes even more deceptive.

When a user orders online digital product; the user's software makes a copy of the order in the memory, splits into packets and sends those packets via the Internet. Different host computers copied and transmitted those packets along their journey. Finally the software of recipient of order receives the message as a file. The original packets never arrive. Each computer that handles packets does so by making and passing on copies and discarding the packets it received³². The result of all these activities is that digital product exists in multiple locations, but for all practical purpose it is the same digital product. It has the identical information content as the original one.

The question that arises in this perspective is whether the digitized products can be classified as services or goods or whether other kind of classification is required.

Following the statement of ECJ in the case of *Faaborg-Gelting Linen A/S v. Finansmant Flensburg*; "... in order to determine whether transactions constitute supplies of goods or

³¹ The Blacks Law Dictionary, seventh edition, B.A.Garner, West Group, 1999.

³² Preston Gralla, *How the Internet Works*, sixth edition, September 2001.

services, regard must be had to all circumstances in which the transaction in question takes place in order to identify its characteristic features”³³.

So in order to differentiate between digital service and good online one has to examine separately the purpose, function and character of each digital product.

3.2 Is a digital product a service or a kind of good?

The Sixth Directive on VAT³⁴ embodies different rules to determinate where taxation takes place. These rules hinge on the type of supply; whether it is supply of goods or services. The Directive on VAT defines in Article 9 (e) that “ intangible service” as transfer and assignment of copyrights, advertising services, data processing, the supply of information and several personal services.

For the taxation purpose by electronically supplied service is meant service that;

- in the first instance is delivered over the Internet or an electronic network and then
- the nature of the service in the question is heavily dependent on information technology for its supply (i.e., the service is essentially automated, involving minimal human intervention and in the absence of information technology does not have viability.)³⁵

Therefore on the basis of this two step test, an electronically supplied service includes digitized products generally. It is worth to emphasize that under this category also falls the digitized content of books and other electronic publication³⁶.

The similar approach can be found in the conclusion reached by the OECD Committee on Fiscal Affairs stating that; “the transfer of digitized products should not be treated as the supply of goods”³⁷.

It should be observed that the nature of tax law requires strict rules on taxation in order to ensure predictability and certainty to the parties and that the approach in this field of law is not necessary relevant to the copyrighted works. Moreover goods do not become service simply because they are being delivered in different way.

³³The European Court of Justice case C-231/94, ECR 1996 I-2395.

³⁴The Directive on harmonization of the law of the Member States relating to the turnover taxes, the Council Directive 77/388/EEC, O.J.L 145 13/06/1977, p. 1-40.

³⁵The European Commission, Tax Policy, VAT and other turnover taxes, Guidelines 67 Meeting 8 January, 2003, TAXUD/2303/03 Rev 2 final- EN, Brussels, 15 January 2003.

³⁶See Para 33.

³⁷A discussion Paper on Taxation Issues, September 17, 1998, p.20, www.oecd.org/daf/fa/e-com .

The first observation, which arises, is that all digital products have similar functions as tangible products. One of main reasons for buying books is to have a pleasure of reading them. When a user downloads an electronic book from the Internet onto his computer, the reason remains the same. The only difference is that the book is made available to him in electronic format. Secondly the copy, which the user receives, can be unique due to technical solutions. If the copy downloaded on the user's computer interacts with Digital Rights Management an identification of the product will be included. Additionally, one more feature of tangible products such as stability can be found in digital products. Electronic books are stored on the harddisk of the computer or portable-reading devices in consistence with this one can assume that they are stable and easy to identify.

This is no doubt that classification of digital products as goods is not the perfect one and is easy to be questioned. In my opinion, it is much more proper to classify digital products as goods rather than service. However, one may argue that digital products are not tangible by nature and on this basis they can not be treated as goods. The contra argument can be presented that the lack of a physical carrier in the light of the foregoing discussion is not sufficient to declassify digital products as goods.

3.3 Is a digital product neither services nor goods?

The Internet enables literally works to be supplied free of carrier and without need for an extensive distribution chain.

Inasmuch as the carrier medium is no longer an integral part of product the information is most important part of the transmission process. The Internet makes able "pure" information to be supplied and property rights lie in the transferred information. The pure information can exist at different places at the same time. Many persons can avail of themselves it, at the same time without having to contest for their share³⁸. The quality of such products is not diminished by the use. It follows from the foregoing characteristic that digital products could be classified as something else then services or goods. The support for this assumption can be found in the nature of the Internet infrastructure.

³⁸ A. Wiebe, Perspective of European Intellectual Property Law, International Journal of Law and Information technology Vol 8 Nr 2, 2000.

The user receives an information product in electronic format, which in principle permits multiple copying with no derogation of quality, and also permits the product to be made easily available to the other Internet users. The creator of an information product therefore requires the right to prevent such activities which otherwise would quickly destroy the market for the product in the first place. In other words the act of downloading must be authorized separately every time and without prejudice to the future forms of exploitation.

Books in an electronic format can be very good example of information products.

3.4 E-book as an example of information products

Electronic books are revolutionizing the way authors or publisher makes works available to the readers. An e-book can be given for free for a while and charged later if a buyer wants to keep it. The buyer can be charged based on usage (pay per read page).

When the author creates an original work he/she usually submits it to an e-book publisher. The publisher converts the work to an e-book format, and then employs DRM encryption to “lock” the file and generate a unique encryption “key”. E-books, unlike digital word-processing documents that can be edited and changed, retain the publishers’ design. The e-books readers can not manipulate, print or copy the content.

The e-book distributor (shopping website) manages the encryption key and locked file, ensuring that unauthorized users can not view the protected works. E-books as information products include not only content but also metadata³⁹. The Digital Right Management system interacting with e-books ensures that the following elements are associated with system; (1) identifiers, i.e., numbers or codes permitting the unique identification of the piece of content, (2) metadata, i.e., information about the piece of content which may include, for example, the identity of the right holder, the price for using the work, and any other terms of use and (3) technological protection measures, i.e., systems designed to ensure that certain usage are complied with, in particular those concerning access and copy control⁴⁰.

³⁹ It is part of product, which describes the content, but it is not computer program. Information of information product.

⁴⁰ Severine Dusollier , Copyright And Access to Information in digital Environment, Study prepared for the Third UNESCO Congress on Ethical , Legal and Societal Challenges of Cyberspace Infoethics 2000, Paris, 17 July 2000.

Once an e-book is properly formatted it can be distributed without conventional distribution chain and printing costs.

Moreover, an e-book enables a vast amount of new and successful business possibilities. For example, Stephen King published his new book “Riding the Bullet” exclusive on the Internet at price USD 2.50 per copy. It was possible because the price did not include printing, shipping, storage, distribution or other traditional publisher costs. After being on sale for just 48 hours, author sold 500,000 downloaded copies worldwide⁴¹.

Although, E-books are intended to be read on computer screens, portable digital reading devices like Rocket e-book⁴² or Personal Digital Assistants such as the Palm, ordering and obtaining the key to decrypt it is very easy.

For example an Amazon.com buyer/user can purchase an e-book by adding it to his/her Shopping Cart and proceeding through Amazon.com orders form. Soon after he/she placed his/her e-book order, an e-mail containing a link to a website, where e-books will be posted and available for downloading on his computer, will be sent to the e-mail address associated with his Amazon.com account. The access to website will be secured by password. It is worth to mention that user from European Union can not purchase e-book from American Amazon.com website. The can do this on Amazon.co.uk and Amazon.de sites⁴³.

⁴¹ www.ebook.org, newsletters.

⁴² Gemstar e-book devices are available in two different forms GEB 1150 and the GEB 2150. Each device can carry thousands of pages of books, periodicals. They are about the size of paperback book. www.gemstar-ebook.com/ebcontent/devices.

⁴³ In the similar way e-books were offered by Gemstar e-book retailer. Before buying and reading Rocket Edition (specially prepared electronic reading materials from on-line bookstore powells.com) buyer had to register his Rocket e-book. According to the announcement on 18 June 2003 of Gemstar E-book Group Limited, they will be no longer selling e-book devices, but the service will continue to be available for at least the next free years.

4. Access control.

The theory of exhaustion is based on principle that once the copy of a work has been sold by or with the consent of the copyright holder the distribution right in that particular copy is exhausted. If a copyright owner could forbid the resale of his/her work, which had been first sold by or with his/her consent, he/she would be able to maintain restriction on the free trade. Moreover the property right in work would be unduly impaired if distribution rights were remain intact after the goods are put on the market by or with the consent of copyright holder. Inasmuch as the copyright owner has been adequately compensated for the initial act of putting the work on the market, he/she does not “deserves” additional compensation for any subsequent act of distribution. If the exhaustion could affect the existing distribution right, the copyright owner would no longer need to be fully compensated for the first sale, he/she might, then, decide to amortize his/her investment over a string of primary and subsequent acts of distributions⁴⁴, which would be in contravention of legitimate interest of buyers.

As it follows from the foregoing the principle of exhaustion gives expression to the limitation imposed on the exercise of exclusive rights, with view to keeping a proper balance between interest of copyright owners and members of the public.

The principle of exhaustion, in the light of the provisions of the Copyright Directive, does not apply to the services and online services in particular. This also applies with regard to material copy of a work made by the user of such service with the consent of the right holder.

Every online service, where the copyright or related rights so provides is an act, which should be subject to authorization⁴⁵. Since the right of communication replaced the right of distribution, on the Internet, copyright holders has had an exclusive right to make a works available to the users and as distinct act form making works available grant actual access to them⁴⁶.

The use of digital technology is modifying the creation, distribution and consumption patterns of copyright works. Right owners are in better position, then in the analogue world to decide the terms of use of their works. Encryptions methods and other techniques

⁴⁴ B. Hugenholtz, *Adapting Copyright To The Information Superhighway*, University of Amsterdam, www.ivir.nl.

⁴⁵ The Copyright Directive, Recital 29.

allow copyright holders to block access (does not matter if it is legal or illegal) or monitor actual use that a user makes of one. It makes also copyright holders capable of collecting royalties for every authorized act. Contracts, in addition to the technology can be seen as another way of determining the conditions of use of the works.

The emergence of modern technology, indeed, has changed the idea behind the principle of exhaustion and it can not be supposed that it has happen without consequences for users/consumers rights.

The analysis of the scope of access granted to users by means of license agreements and interacting technology will enable to decide whenever the lack of the application of the principle of exhaustion was a right choice with a view of protecting copyright holders in their creative works on the Internet.

4.1 Emergence of license agreements.

The copyright holders have traditionally chosen to commercialize their works by means of a sale transaction. Works has been offered for sale in return for payment, as a reward for their creativity and investments.

In legal theory sale consist of four elements; parties competent to contract, mutual assent, thing capable of being transferred and prize in money paid or promise. Upon the compilation of a sale transaction, possession and title to thing pass to a buyer. The buyer due to the sale transaction is in legal position of former owner.

The Internet infrastructure enables copyright holders to transact directly with information users. However the conclusion of the contract seldom occurs on-line.

On the Internet, it has become common practice that digital products are being downloaded by the user onto his/her computer under the terms of licenses agreements rather than sale transactions. On-line, the license is presented to the user as a standard form without possibility to modify.

The license agreement, unlike the sale transaction, does not constitute the transfer of ownership. Licensing means that in return for payment the user will acquire the right to use the work. The user's rights to use the work however are limited by terms and conditions of the license.

⁴⁶ The Copyright Directive, Article 3.

In the case of e-book a user does not actually buy the e-book, he/she in return for payment enters into legal relation with the copyright owner, on basis which the user can enjoy the work in certain well-defined circumstances.

Under the license agreement the user has usually a right to make a single copy onto his/her computer, while the original copy remains in the hand of the copyright holder. When the license does not have exclusive character, the same right can be licensed to more than one user and more the one can obtain the copy of digital product.

It is fact that, digitalization has not only brought new ways of disseminating works, but it is also due to its nature has jeopardized exclusive rights of copyright holders. In this light application of copyright provisions to protect literally works might seem to be inefficient or ineffective. The copyright owner must be protected against unauthorized acts of exploitation of works. That is why, in the case of disclosure of works copyright holders have started to rely on licensing contracts rather the sale transactions. This can not however lead to the situation there the user is forced on the basis of unilateral contractual clauses to waive the rights granted to him/her under the copyright law. The question of an enforceability of such license agreement will be addressed as follows.

4.1.1 Licensing.

There are two ways to authorize access to protected works by means of licensing agreements. The authorization can be given by implicit or explicit license.

There are still groups of copyright holders, who do not mind dissemination of their works unconditionally and free of charge. On the contrary they are delighted if somebody at all shows an interest in their works. Moreover they are eager to upload subject matter on the Internet, in order to make it known to the public, so users can access and use matter.

In this scenario the placement of works on a website can be considered as authorization to use them by means of implicit license.

As with all implicit licenses, the scope of such license is unclear. Wagle and Ødegaard express the general notion of implicit license as follows;” ... when the author chooses to publish his work on the Internet, it is assumed that he also authorizes a normal use of the work, considering the medium. Users, will by that, be granted extended rights to utilize works that are lawfully published on the Internet. By the extended right to utilize the

work, we understand that users will have a wider right of disposal than granted under copyright law. The actual extent of this disposal right will depend on the way material is published⁴⁷.

The licenses implied by placing works in a formatted form for the purpose of use in a digital environment probably authorize all users of subject matter. It is less clear if such a license gives the user right to print or further distribute protected works.

Since it is less unclear what kind of rights are given to the user under the implicit license copyright holders can offer their works under the terms and conditions of the explicit license.

In the case of an explicit license, when user orders and downloads digital products directly onto his computer, the terms and conditions of use appear on the screen. In order to use a work he/she must show his/her consent to the terms and conditions by clicking the cursor on an icon I Agree.

Online explicit licenses are preferable because the copyright holder retains an element of control over the work. In the case of enforcing his/her exclusive rights against an infringement the copyright holder has concurrent rights of action with the user.

4.1.2 Collective licensing.

The Internet infrastructure enables rights owners to control themselves directly the use of works. They can also submit the management of rights to collection societies.

Representation and practice of collective bodies vary from country to country. The principal functions of collective management can be characterized as follows;

- to enable rights owners to enforce and administrate their copyrights effectively and cheaply,
- to negotiate licensing terms with groups of users,
- to provide service to users by facilitating access to copyright works and making it possible for users to comply with their obligation under the law to obtain licenses for the use of copyright works⁴⁸.

⁴⁷ Wagle, Anders M. og Ødegaard Magnus 1997, *Opphavsrett i en digital Verden*. Oslo, (translated by) Gier Kielland *The Doctrine of implicit licenses in the intellectual property law – and its relevance to electronic agents*.

The representatives of collective societies negotiate on behalf of copyright holders with users or groups of users and authorize their use of works against payment and on certain conditions. The collective management organizations distribute payments to its members according to established rules.

Management of collecting societies plays a particularly important role in music industry, where it would be difficult for copyright holders control and manage rights in recorded works on an individual basis. This is well illustrated by considering the situation of discos, radio stations, which typically wish to broadcast wide selection of worldwide music. In the absent of collecting societies, radio station would be forced to identify and negotiate with the right holder of each song.

It is difficult for collecting societies to adjust and to play the same role on the Internet. The difficulties result from the fact that collective management is organized on the basis of territoriality and they are entitled to grant license for that particular territory.

An online environment enables copyright holders to control access to their works and to obtain payment in more direct way without intermediaries. Whereas in the present world of physical copies royalties are calculated on a per-copy basis, on the Internet users can be charged per actual use.

4.3. Enforcement of online license.

An online license sets conditions for use of products protected under copyright law to be made available to users on the Internet. Generally, when a user buys an electronic book on the Internet his/her rights to use a work are limited due to license provisions that copyright holder sets to the exploitation of his work.

From on-line agreements one should also distinguish browse- wrap agreements. An example of browse-wrap agreement is the standard terms of use typically found on most of websites. Browser agreements do not require the user to indicate their assent to the terms, or even view the term's online agreement before allowing users to access materials. This way of presenting terms of use is similar to shrink-wrap agreement.

The precursor to the online license is a shrink-wrap license.

⁴⁸ Gillian Davies, Copyright and the public interest, Second Edition, London Sweet &Maxwell 2002.

Although the shrink-wrap licenses are typical used for purchase of software products their validity and legal problems they cause will be discussed in more detail. Since online licenses are more or less derived from the shrink-wrap license, the discussion on a later one applies also to the same extent to on-line licenses.

The name shrink-wrap was derived from the clear plastic wrap that manufactures used to seal the box containing software programs. The shrink-wrap license, itself is an unsigned, self-executing agreement and packed with the software box.

It can take many forms. For example, the envelope licenses where the license is printed on the exterior of a sealed envelope. The box top licenses, which can be read before opening of the box. Finally the referral license where it is a sticker indicating that the CD-ROM should not be opened prior to reading the license⁴⁹.

The common feature for all of these forms of shrink-wrap license is that they can not normally be read prior to purchase.

The use of shrink-wrap licenses in transactions raises important issues of contract law. The enforceability of such agreements concerns two fundamental features of contract law-formation and assent. The formation of contract between buyer and seller typically occurs before buyer takes possession of goods. They negotiate the terms of sale often recording it in written documents. A contract is traditionally in force at the moment the parties sign an agreement.

When the buyer purchases software the terms of use are usually displayed at the time of installation. The buyer is asked to consent to terms of license after he has taken possession of the goods.

In USA, for years courts held that shrink-wrap license were not valid.

In *Vault v. Quaid*⁵⁰ the court held that shrink-wrap license were unconscionable for the user, and therefore unenforceable. In both *Step- Saver v. Wyspe*⁵¹ and *Arizona Retail System v. Software Link*⁵² the court decided the shrink-wrap license were unenforceable because the sales contract between the producer and the user had already been concluded before the user learned about the license terms. According to the courts the shrink-wrap terms could not change the terms of the already existing sale of goods contract⁵³.

⁴⁹ A. Flint, "Shrink Wrap, Click Wrap, Power-on Wrap What Next?", *Business Law Review* 37, 1999.

⁵⁰ *Vault v. Quaid* 847 F.2d 255, 270 (5th Cir. 1988).

⁵¹ *Step- Saver v. Wyspe* 939 F.2d91 (3rd Cir.1991).

⁵² *Arizona Retail System v. Software Link* 831 F.Supp 759 (D.Ariz 1993).

⁵³ Dr Bernardin Trompenaars, Dr. P Bernt Hugenholtz, *Formation and validity of on-line contracts*, Institute for Information Law, Amsterdam June 1998.

However the current position of validity of shrink-wrap agreement has been changed. The majority of courts in the USA hold that these agreements are enforceable against consumers.

The central case in which the validity of a shrink-wrap license was affirmed is ProCD v. Zeidenberg⁵⁴. Zeidenberg bought a package of SelectPhone, a CD-ROM database produced by ProCD. The CD-ROM was delivered to him in package. The text to the package referred to the license terms in the use guide inside it. The license stated thereby using the discs, the user would agree to be bound by the terms of the license; if the user could not agree to these terms, he should promptly return the disk and user's guide to where he had obtained it. Once the CD-ROM was activated, the PC screen showed again a text referring to the terms of license. The defendant placed the contents of disk on the Internet in spite of prohibition in terms of license to commercialize the data. Zeidenberg held that the shrink-wrap license was unenforceable, since he did not know its content at the time of sale. The court admitted Zeidenberg had not been able to know the contents of license at the moment he bought the CD-ROM. But at the moment he concluded the contract, he had been aware that the license terms could be part of the contract. He had not rejected the goods after inspecting the package, learning of the license and trying out the software. By this conduct he had accepted the terms. Applying general contracting principle contained in the Uniform Commercial Code the court cited Article 2-204, which states that, a “ contract for the sale of goods may be made in any manner sufficient to show agreement, including conduct, by both parties which recognizes the existence of such contract”.

In M.A.Mortenson Co. v. Timberline Software Corp., a Washington state court followed the reasoning of ProCD and enforced the terms of license agreement in which the licensor disclaimed liability for incidental and consequential damages⁵⁵. The terms of license were printed on the outside of sealed envelope in which the diskettes containing the software were delivered and on the inside cover of the user manual⁵⁶. Moreover, each time the program was opened, the introductory screen contained a reference to the license⁵⁷. Although the plaintiff asserted that he never saw any license or disclaimers, the court rested in decision upon the “ commercial realities of software sale”, and observe that “

⁵⁴ ProCD v. Zeidenberg (No. 96-1139, US Court of Appeals for the 7th Circuit), 86 F. 3rd 1447.

⁵⁵ M.A.Mortenson Co. V. Timberline Software Corp 970 P.2d 803 (Wash.App.1999).

⁵⁶ See Para 69.

⁵⁷ See Para 69.

reasonable minds could not differ concerning a corporation`s understanding that use of software is governed by licenses containing multiple terms”.

The Mortenson court determined that, under UCC§2-2007, the terms of license become part of the contract that the license documented in the purchase order that contained no reference to the licenses terms. The court reasoned that, even if the license provision could be viewed as a request for additional terms, the plaintiff`s conduct in installing and using the software constituted assent to the additional terms⁵⁸.

One court decision dealing with the enforceability of shrink-wrap license has been reported in Netherlands the case of Cross Holland B.V v. TM Data Nederland B.V.⁵⁹. Distributor TM Data supplied software, produced by Raima, to user Cross. According to the TM Data the text of Raima`s shrink-wrap license terms were enclosed in the package of the software. Cross denied the terms were presented in the packing. When the computer program turned out not to function properly and attempts to repair it failed, Cross claimed damages from TM Data. TM Data refused to pay damages contending that the TM Data was not part to the shrink-wrap license, the license being concluded between Cross and Raima. The court rejected this defense. It held simply opening the packing of software could not form a license agreement. A license agreement can only be concluded validly if a user is aware that by opening the packing he becomes a part to license agreement. Moreover the contents of license terms will have to be clear to users beforehand. From that judgment one can conclude that under the Dutch law the shrink-wrap license may be enforceable provided that users are aware of such license and know the contents of license terms before agreement is formed.

Thus it appears that courts seem to recognize shrink-wrap licenses as the standard within the software industry and for this reason are willing to give legal affect to the terms embodied in the licenses. However the courts giving legal effect take under consideration the fact that users are aware and familiar with the terms of license.

⁵⁸ See Para 69.

⁵⁹ Cross Holland B.V v. TM Data Nederland B.V. , the Amsterdam court of first instance of May 24, 1995, see para 68.

4.3.1 Recognition of online license in the European Union law.

There are different ways of displaying the terms of license to the users and not all of them have the same legal affect. Due to the time and place of presentation to the user some of them can be considered invalid.

An online license can be displayed to the user at the time of concluding the contract⁶⁰ on a mandatory page of contracting process before downloading purchased products.

The license can be intrinsic part of downloaded product. It will be displayed on the users computer screen once he has downloaded the product but before he will install it.

The provisions of license also can be disclosed to a user by a hyperlink which directs to terms and conditions placed on a separate screen. The user has to click and open page self in order to read the terms of a license.

Validity of contact between copyright holder and user is based on an assumption that the license provisions will bind the user from the moment he has clicked the bottom “I Agree”, “I Accept”. That way a user should only download the product if he agrees to the terms of license.

In online transaction between a distributor and a user it is technically possible to ensure that; the user knows that the transaction is a subject to a license, the license terms are read before the licensed product is ordered and that licensee takes affirmative steps to signify agreement. Additionally it is recommended that license should be disclosed and made clearly visible to the user prior to the first use of the licensed, purchased materials and should give clear notice that transaction is subject to such license.

In the European Union online licenses (the click-wrap licenses) are governed by e-commerce laws as well as consumer⁶¹ protection laws.

As a general principle in the Europe, contracts are valid independetly of how they are formalized. Law sometimes imposes legal requirements such as the contracts being made in writing⁶².

⁶⁰ One has to keep in mind that in the case of on-line license they are presented to the user as a standard form without possibilities to modify. This means that a contract with user can contain license but a license need not to be created by a contract.

⁶¹ According to the European Directives, consumer is understood as any natural person who is citing for purpose, which is outside his trade, business or profession.

⁶² Formalities as the need for a written documents are useful to reduce potential disputes regarding terms and conditions of transactions, they express contractual process becoming evidence of competition of transactions.

The European Commission seeks to harmonize the national requirements regarding online contracts. The Directive on electronic commerce⁶³ in Article 9 provides that; “Member States shall ensure that their legal system allows contract to be concluded by electronic means. Member States shall in particular ensure that the legal requirements applicable to the contractual process neither create obstacle for the use of electronic contract nor results in such contracts being deprived of legal effectiveness and validity on account of their having been made by electronic means”.

In other words this article includes the formal requirements of copyright licensing. Moreover national law of Member States will have to be adopted in order to allow on-line licensing after the Directive has come into effect 17 January 2002.

Additionally the Directive on electronic commerce imposed in Article 10 obligations on Member States to ensure that certain information clearly, comprehensibly and unambiguously and prior to the order will be provided to the recipient of the service;

- the different technical step to follow to conclude the contract
- whether or not the concluded contract will be filed by the service provider and whether it will be accessible
- the technical means of identifying and correcting input errors prior to the placing of the order
- the language offered for the conclusion of the contract
- the contract terms and general conditions provided to the recipient must be made available in a way that allows him to store and reproduce them⁶⁴.

The complexity of the technological tools used to conclude contracts and the non-negligible possibility of the inadvertent clicking do diminish the “expressiveness” of the purchaser’s actions on the e-commerce platform⁶⁵.

That is why the objective of this Article, it is to draw the attention of contracting parties especially the attention of recipient of the services to the contractual process and the notion of given consent by on clicking order or on acceptance button.

As an additional protection the Directive on the protection of consumer in respect of distance contracts⁶⁶ in Article 7 provides the consumers with the right to withdrawal.

⁶³ The Directive on certain legal aspects of information society service, in particular electronic commerce in the Internal Market, The Directive 2000/31/EC of the European Parliament and of the Council.

⁶⁴ The Directive on electronic commerce Article 10 (1,3).

⁶⁵ Santiago Cavanillas , An Introduction to Web Contracts, Electronic Commerce Legal Issues Platform, ESPRIT Project 27028 www.eclip.org .

⁶⁶ The Directive on protection of consumers in respect of distance contracts, Directive 97/7/EC of the European Parliament and of the Council of 20 May 1997. The Directive concerning the protection of consumers in

According to this Article the service provider should offer to the user right to revoke the contract within at least seven working days, free of charge and without giving any reason. The only charge that may be made to the consumer is the direct costs of returning goods.

However one has to keep in mind the right of withdrawal is excluded from some products of contracts⁶⁷ and more important is that this right granted to the consumers protects them against their reckless decisions and not to the credits or payments conditions. Its intent is to allow the consumer to detect that he made a bad choice in buying product, but not to discover that credits charges are more burdensome than he had thought⁶⁸.

The Directive on unfair terms⁶⁹, in Article 6 states that unfair terms used in a contract concluded with a consumer by a seller or a supplier shall not be binding on the consumer and that contract shall continue to bind the parties upon those terms if it is capable of continuing in existence without the unfair terms. By the unfair terms is meant a contractual term which has not been individually negotiated, if contrary to the requirements of good faith, it causes a significant imbalance in the parties rights and obligations arising under the contract. Moreover a term is not individually negotiated where it has been drafted in advance and the consumer has therefore not been able to influence the substance of the term, particularly in the context of a pre-formulated standard contract⁷⁰.

Unfortunately case law on the enforceability of on-line license in European Union to my knowledge has not yet been reported. Inasmuch as of the technical advantages of on-line licenses commentators are positive about their enforcement⁷¹, in spite of the fact that in many cases users are being required through use of on-line licenses to waive rights granted under copyright law.

respect of distance contracts, defines the distance contract as “ any contract concerning good or service concluded between supplier and the consumer under the organized distance sale or service provisions scheme run by the supplier, who, for the purpose of the contract. Makes exclusive use of one or more means of distance communication up to and including the moment at which the contract is concluded”.

⁶⁷ The Directive on protection of consumer in respect of distance contract, Article 6 (3).

⁶⁸ See par 80.

⁶⁹ The Directive on unfair terms in consumer contracts, Council Directive 93/13/EEC of 5 April 1993.

⁷⁰ The Directive on unfair terms, Article 3.

⁷¹ See par 68.

4.3.2. Case law concerning online contracts in the United States.

In the United States the validity of on-line contracts and licensing agreement have generally developed from the case law. It appears that courts will hold online licensing agreements to be valid and legally enforceable as provided the terms and conditions contained in the agreement are clearly presented and the user is required to show his/her assent to the agreement in some manner.

In the case *Register.com. v. Verio*⁷² court held terms of Use agreement (browser-wrap agreement) valid and enforceable even though the user did not see the terms until after a query had been submitted and was not asked or required to click a button indicating assent to the terms. Register.com, an authorized ICANN domain registrar, was required to impose on the public with access to the Whois database certain restriction regulating the use of data. Verio, Inc., a provider of web hosting, high speed Internet access, and e-commerce products, used software robots to collect information from Register.com`s. The Whois database in order to send telemarketing and e-mail solicitations to the registrants. The court found that Register.com terms of use created a binding contract between Verio and Register.com. Verio argued that it had not assented to Register.com terms of use. Register.com terms of use are clearly posted on its website. The conclusion of the terms paragraph states ` by submitting this query, you are agreeing to abide by these terms`. Verio did not argue that it was unaware of these terms. Only that it was not asked to click on an icon indicating that it accepted the terms. However in the light of this sentence at the end of Register.com terms of use, Vero showed its assent to be bound by it and contract was formed and subsequently breached”⁷³.

In *i.LAN Systems v. Netscout Service Level Corp.*⁷⁴, i.LAN entered into a Value Added Reseller (VAR) agreement with Netscout Service Level Corp.. Whereby it agreed to resell Netscout software to consumers. i.LAN claimed that according to the purchase order associated with the VAR agreement, it purchased the unlimited right to use Netscout software, including perpetual upgrades and support, and could rent rather than sell the software to consumers. Netscout believed that it was not obliged to provide the perpetual upgrades and support as per a click-wrap license that i.LAN subsequently agreed to when

⁷² *Register.com. v. Ver Inc.*, 126 F. Sup. 2d 239 (S.D.N.Y. 2000), Case Summaries, Internet Law & Business, April 2003.

⁷³ See Para 67

⁷⁴ *i.LAN Systems v. Netscout Service Level Corp.* 183 F. Supp. 338 (D.Mass 2002), Case summaries, Internet Law & Business, April 2003.

it used the software. The court held that click-wrap license agreement was enforceable because when i.LAN clicked on the “I agree” box during the installation of software it explicitly manifested assent to the terms. The software agreement was held to be enforceable either under BCC 2-204 as the acceptance of offer, or under BCC 2-207 as the acceptance of additional, non material terms because the original Value Added Reseller agreement incorporated the click-wrap license agreement by reference and specifically stated that Netscout liability to end users of the software would be limited by the click-wrap license agreement.

One case that may be distinguished from the cases discussed above is the case of *SoftMan Products Co. v. Adobe Systems, Inc.*⁷⁵. The district court in this case concluded that Adobe sold rather than licensed, its software to authorized distributors, ignored industry standards and created precedent. Adobe System Inc. is a software development and publishing company that produces, among other things, Adobe Collections consisting of individual Adobe products bundled together as collective Adobe “Retail Boxes”. SoftMan Products is a distributor of software products. The company main distribution channel is its website, www.buycheapsoftware.com. Adobe alleged that since November 1997, SoftMan began distributing Adobe products without authorization, which consisted of software components separated from unbundled Adobe Collections. Adobe contended that by distributing the individual software components from unbundled Adobe Collections, SoftMan infringed upon Adobe’s exclusive right of distribution of products. More specifically Adobe argued that SoftMan unbundling of Adobe Collections and distribution of individual components “exceeded the scope“ of end user license agreement, which stated that the end user could transfer all his rights to the use of that software to another person, provided that he also transfer the end user license agreement and all other software or hardware bundled with particular Adobe product. SoftMan argued that its resale of Adobe Collections software was allowable under the first sale doctrine. Adobe contended that throughout the stream of commercial transactions involving Adobe software, the software is always licensed. The court concluded that the transfer of Adobe software to the end user is a sale not a license moreover that Adobe sells its software to distributors. Second the court held that SoftMan did not assent to the end user license agreement terms and therefore was not bounded by it. The court reasoned that because the end user is asked to agree to the electronically recorded license terms only when he attempts to install the

⁷⁵ *SoftMan Products Co. v. Adobe Systems, Inc.* 171 F. Supp. 2d 1075, 1080 (C.D. Cal. 2001)

software and SoftMan never loaded the software that SoftMan never agreed to be bound by the end user license agreement. Additionally, the court explicitly noted that it would not determine the general validity of click-wrap license⁷⁶.

⁷⁶ See Para 69

5. Technological protection against unauthorized access and use of copyrighted works on the Internet.

One of fundamental problems as regards copyright matter on the Internet is how to protect from unauthorized use copyrighted materials online.

The technology used by copyright holders to protect their works is extremely varied; some have been specifically designed to answer the digital threat to copyrights and to protect any kind of digital content.

From a legal point of view the copyright protection requires that; (1) the creator of a protected material is authenticated, (2) the integrity of the material is guaranteed, (3) the unauthorized copying, transmission or further communication to the public is prevented if the creator so wishes, (4) an access can be limited to certain authorized persons, (5) the terms and conditions of a contract such as a license can be recorded, (6) the material can be securely transmitted, (7) the reception of the material can be adequately proved, (8) the creator can ensure appropriate payment⁷⁷.

It may be distinguished between technological measures that protect an act falling under the copyright holder's exclusive right, a system of conditional access, tools for marking and identification and an electronic management system⁷⁸.

Under the first category fall anti-copy devices, which prohibit performance of any act of use (i.e., printing, digital copying, modifying) or use that it is an exclusive right of copyright holders. Systems of conditional access are based on such technological solutions as cryptography, passwords, set-top boxes, and digital signatures. However they control only initial access to the protected information. Deactivating the access control devices is done either by payment or by other terms of permission agreed with copyright holders.

Many technologies can be used to identify and mark works. These technologies serve as visible or invisible means of inserting information about the work, whether it is the title of work, the identity of copyright holder or the conditions of use. Due to these techniques, each separate copy of the work distributed to a user in a digital environment may have incorporated a digital serial number.

⁷⁷ Jan Kaestner Law and technology convergence: copyright, Institute fur Information's-, Telecommunications-, und Medienrecht (ITM) University of Munster.

⁷⁸ See Para 47.

This technological measure can be well illustrated by Digital Object Identifier, an initiative set up by the Association of American Publisher⁷⁹. It identifies the content of copyrighted materials, which can be predefined by copyright holders. The Digital Object Identifier is a large system of “handles” developed by Corporation for National Research Initiatives. The “handle resolver” is a browser plug in software, which redirects their handles to URL’s or other pieces of data, or content. Without resolver, typing in the handle simply directs the user to few proxy servers, which understand the handles protocols. The interesting feature of the system is its ability to resolve to multiple locations⁸⁰.

This means that; if the content and related resources reside in secondary information multiple resolutions enable content owners to identify their intellectual property with bound collections of related resources at a hyperlink’s point of departure. A content owner is able to control and manage all the related resources⁸¹.

The Digital Object Identifier can be a very practical tool in the case of an electronic book. It can be assigned to every e-book or to every part (chapter, section, or paragraph) of it. Such technology makes each e-book a unique one. This enables also pay per view or print on demand models.

Another protection measure that should be mentioned is the Digital Rights Management system, although one must be aware and not to think of it as a specific kind of technology. The DRM system consists rather of combination of many tools and technologies designed to play several roles⁸².

A DRM system consists of two modules; content and a license module. The content module contains; digitized media, such as text or audio files, which have been securely packaged using encryption, and is available for distribution through the DRM system. Before the content is encrypted it is embedded with metadata such as copyright holder name, title format. The licensing module generates digital licenses, which automatically grant the end-users access to content⁸³.

⁷⁹ An International Digital Object Identifier foundation was set up and invited all publishers American and Non-American alike to apply unique DOI prefix www.doi.org.

⁸⁰ www.doi.org.

⁸¹ www.ebookweb/stories/storyReaderS228.

⁸² S.Gouthornet, ” On-line service and data protection and the protection of privacy”, A study for the European Commission DL.XV, p.31, www.eu.int/gerinfo/info.

⁸³ P.Ganley, Access to Individual: Digital Rights Management system and the intersection of informational and decisional privacy interests, Informational Journal of Law and Information Technology, Vol.10 No.3.

It is difficult to draw up a specific list of technological devices either in current use or being developed, just as it is impossible to predict the future of these technologies in the area of protecting works under copyright law⁸⁴.

5.1 The legal context of technological measures

The recognition of the emerging role of technological protection measures and online management can be found first of all in the WIPO Copyright Treaty⁸⁵, Article 11 and the WIPO Performance and Phonograms Treaty⁸⁶, Article 18. The enacted legislation requires Member States to provide two types of technological adjuncts to the scope of protection of copyright and related rights.

The first technological adjunct is generally referred to as an “anti-circumvention” provision. The WIPO Copyright Treaty in Article 11 states;”... contracting parties shall provide adequate legal protection and effective legal remedies against the circumvention of the effective technological measures that are used by authors in connection with the exercise of their rights under this Treaty or the Berne Convention and that restrict acts, in respect of their works, which are not authorized by the authors concerned or permitted by law.”.

As a second technological adjunct, the Treaties protect “rights management information”, establishing a legal support for rights management system in the WIPO Copyright Treaty, Article 12 of. The Article obliges the contracting States to provide for adequate and effective legal remedies against any person knowingly, removing or altering any electronic rights management (ERM) information without authority or distributing works where ERM information has been removed or altered if this will induce, enable, facilitate or conceal an infringement of any right covered by the WTC or the Berne Convention. Additionally Article 12 defines “rights management information” as information, which identifies the work, the author of the work, the owner of any right in the work, or information about the terms and conditions of use of the work.

⁸⁴ D.Geruais, electronic rights Management and Digital Identities System, WIPO Advisory Committee and Management of Copyrights and Related Rights in Global Information Network, Geneva 14-15 December, 1998, www.wipo.org.

⁸⁵ WIPO Copyright Treaty and Agreed statements concerning the WIPO Copyright Treaty, www.wipo.int/clea/docs/en/wo.

⁸⁶ The WIPO Performance and Phonograms Treaty, www.wipo.int/clea/docs/en/wo.

In the light of Treaties remains E.U. Copyright Directive⁸⁷. The E.U. Copyright Directive in Article 6(1) requires Member States to provide legal protection against "... manufacture, import, distribution, sale. Rental, advertisement for sale for rental, or possession for commercial purposes of devices, products or components of the provision of service" for the purpose of circumventing technological measures, including encryption, scrambling or other copy control mechanisms.

The Directive in Article 6(3) defines technological measures as;" ... any technology, device or component that, in the normal course of its operation, is designed to prevent or restrict acts, in respect of works or other subject-matter, which are not authorized by the right holders of any copyright or any related to copyright as provided by law or the sui generis right provided for in the Database Directive". The subparagraph to Article 6(3) provides that technological measures shall be deemed "effective" where the use of a protected work or other subject-matter is controlled by the right holders through application of an access control or protection process, such as encryption, scrambling or other transformation of the work or other subject-matter or a copy control mechanism, which achieves the protection objective⁸⁸.

One may observe that the Copyright Directive, in contrast to the WIPO Treaties defines the criterion for efficiency needed for the protection, although the language is rather vague. However the Directive does not explicitly distinguish between access control devices and copy control devices.

The provisions in Article 6 including definition of effective technological measures embodied in Article 6(3) are mandatory, but the exact form of domestic legislation giving effect to it is left to the discretion of each Member State.

⁸⁷ See Para 13.

⁸⁸ The Copyright Directive, Recital 14.

5.2. Exceptions and limitations as delimitating factors.

Ideally the rules on copyright should guarantee sufficient protection for creators to maintain their level of investment in the production of new works distributed on-line, while maintaining the public's right to consume those works, including the possibility to make in certain well- defined circumstances, limited use of those works without the right holder's consent⁸⁹. It has always been recognized that in certain cases limitations or exceptions, should be placed on the exercise of granted rights.

However in order to place certain limitations or exceptions on copyright holder's exclusive rights, the first disclosure of the work to the public has to be made with the consent of copyright holders⁹⁰. Otherwise exceptions do not apply.

In most of Member States there are limitations concerning copying for private use, for scientific and educational purposes and for library and archival purposes.

The restrictions may appear in the form of compulsory or statutory license or permitted uses, which are not subject to a formal procedures or payment⁹¹.

It is formally accepted that the members of the public can access protected literary works for private use. The private use doctrine provides for the use of copyright material in particular circumstances without first obtaining permission from copyrights holder. In particular the doctrine supports individuals making a limited number of copies of protected works for their personal use, exceptions for uses of works for education or research. It is a common consensus that such use does not seriously affect the interests of the copyright holders.

Moreover the restrictions take into account not only exceptions to rights but also, within the area of copyright, freedoms and major societal interests⁹². Thus, for example, exceptions concerning private use are designed to protect individual privacy, while an exemption for teaching and research purposes to guarantee the right of people to knowledge and education.

⁸⁹ L. Guibault, "The nature and scope of limitations and exceptions to the copyright and neighbouring rights with regard to general interest mission for the transmission of knowledge: prospects for their adaptation to the digital environment". Institute for Information Law, University of Amsterdam, June 2003.

⁹⁰ Jon Bing, Intellectual property exclusive access rights and some policy implications, Norwegian Research Center for Computers and Law, Faculty of Law, University of Oslo.

⁹¹ See Para 1 p. 345.

⁹² Striking a Proper Balance, IFLA/IMPRIMATUR Conference, Amsterdam, 30-31 October 1997, www.ivir.nl.

By the virtue of the Berne Convention, a provision of Article 9 (2), taken in conjunction with the TRIPs Agreement⁹³ Article 13 of, there is a three step test which regulates the way in which limitations and exceptions are to apply. Under this test the exceptions are permitted in “certain special cases” that “do not conflict with normal exploitation of the work“ and “do not unreasonably prejudice the owner’s legitimate interest”. But what does constitute a normal exploitation of a work on the Internet?

Online, each access to protected materials involves an act of copying. The act of displaying the content of a website requires the computer to make temporary copies of data in the user’s computer random access memory. Moreover in most cases works are not subject to a sale transaction but to a license agreement. Such a practice, with view to protecting works on the Internet, has an impact on the application of exceptions and limitations or the principle of exhaustion.

The Copyright Directive includes a detailed and exhaustive list of exceptions to the reproduction right and the right of communication to the public. Within the scope set forth in the Copyright Directive Article 5 (2), (3) and (4) the Member States may provide not only exceptions to copyright protection but for statutory licensing as well. It is not allowed to create exceptions or limitations other than those included in the list. Although the list is exhaustive, all the exceptions are optional. The Member States can chose and implement only those exceptions they need or find expedient. Such a freedom of implementation of the Directive can hinder a harmonization effect of one.

The Copyright Directive requires Member States to provide copyright holders with fair remuneration to compensate them adequately for the use made of their protected works in certain cases of limitation or exceptions. In certain situation where prejudice to the right holder would be minimal no obligation for payment may arise⁹⁴. It is worth to mention that such exceptions or limitations should not inhibit the use of technological measures or their enforcement against circumvention.

On the Internet technological measures allow copyright holders to monitor who is looking at a work and exactly what the users are doing with it or block a lawful licensee’s access to digital content by activating a control and device embedded in code.

⁹³ The TRIPs Agreement, Article 13 states;” Members States shall confine limitations or exceptions to exclusive right to certain special cases which do not conflict with a normal exploitation of the work and do not unreasonably prejudice the legitimate interests of right holder”.

⁹⁴ The Copyright Directive, Recital 34.

The tendency in reducing the scope of exceptions in digital age is not only typical for the European Union law. American case law is also limiting fair use in the light of the possibilities now open to copyright holders.

In the case *American Geophysical Affair v. Princeton University Press*⁹⁵, the judge ruled that the electronically granted permission to make photocopies of articles taken from books or newspapers, constituted a market for photocopies of scientific articles, so that photocopies made by a company for its research department could no longer be consider as falling within the area of fair use⁹⁶.

The fair use argument was rejected because application of this exception violated the normal exploitation of the work insofar as it was possible to negotiate the authorization by contractual and technological means⁹⁷.

One of the terms of the three-step test, the absence of conflict with the normal exploitation of the work, could well support such a ruling.

⁹⁵ *American Geophysical v. Princeton University Press*, 60 F. 3d.913 (2d. Cir 1994), 116 S. Ct.592 (1995).

⁹⁶ The United States copyright Act, 17 U.S.C. §107 determines if a use falls within the fair use doctrine by engaging in a four balancing test. The four step test examines: 1) the purpose and the nature of the use including whether such use is of a commercial purpose or is for nonprofit educational purposes; 2) the nature of copyrighted work; 3) the amount and substantiality of the portion used in relation to the copyrighted work as a whole; and 4) the effect of the use upon the potential market or value of copyrighted work.

6. Conclusion

In the European copyright law, the principle of exhaustion is restricted to the distribution of works incorporated in tangible carriers, and *inter alia* does not apply to the Internet. The principle of exhaustion does not apply to the material copy made by the user of online service with the consent of the copyright holder either.

It must be underpinned that the copy obtained by the user in latter example is conceptually not different from a copy sold to a buyer in a bookshop. The copyright owner is adequately remunerated in both situations. The difference resides only in fact that that in the event of electronic delivery it is a user who makes a copy.

Lack of the compliance between legal rules on the purchase of a copy of the same book online and offline can lead to unequal legal situation of buyers/users. Digital products are usually offered online under the terms of license agreements rather than sale transactions.

Consequently, an online delivery of books or software does not give the user/consumers same rights as an offline delivery of hard copies. It is going to serve disadvantage, at least from user/consumer point of view.

The discussion presented in this paper shows that it is not so easy to draw clear line and state that exhaustion principle should only apply to the sale of works in the analogue world.

To some extent the application of the principle of exhaustion should also be justified online. In the most of cases it should hinge on terms and conditions of delivery or purchase agreement. If the copyright holder does not make explicit what the purpose of transaction is, the court will probably have to decide whether copyright holder exclusive rights were infringed.

The copyright owner must be protected against unauthorized acts of exploitation of their works especially on the Internet, but also limited use of those works in well- defined circumstances (for example statutory licenses) without the consent of a right holder should be allowed.

The technology and license agreements enables copyright holders to determine the conditions of every single act of use of their works but this does not that they should be allowed to do this. The restrictive licensing practice and use of technological protection measures may risk stifling creation and impinging on freedoms of users.

It should not be imagined, however, that contractual obligation can be repudiated by the user/consumer merely because he/she was in weaker bargaining position. Further the law will

not permit a person of full age and understanding who failed to read the license agreement or to appreciate full important and effect to escape from it.

It appears that courts seem to recognize license agreements as the standard form to exercise the exclusive rights of copyrights holders on the Internet and for this reason are willing to give legal affect to them. However the courts giving legal effect take into consideration the fact that users are aware and familiar with terms of license.

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