KAREN BELT

SHRINK-WRAP LICENCES, MASS MARKET SOFTWARE AND DE FACTO INTELLECTUAL PROPERTY

LLB(HONS) RESEARCH PAPER

INTELLECTUAL PROPERTY (LAWS 535)

LAW FACULTY

VICTORIA UNIVERSITY OF WELLINGTON

1998

CONTENTS

ABSTRACT

Traditionally, information products have been commercially exploited by selling copies of the information, with the creator relying on intellectual property rights to protect his or her investment in the work. However, software, an intangible information product, has typically been licensed. Mass market software is sold with a standard licence known as a shrink-wrap licence.

This paper looks at the interaction of copyright law, mass market software and shrink-wrap licences. It suggests that shrink-wrap licences are beneficial as they allow software producers to practice price discrimination by restricting the uses that may be made of the software. However, as non-negotiated contracts between parties of unequal bargaining power, they may also allow software producers to expand their rights in the software over and above the rights granted by intellectual property law.

The terms of shrink-wrap licences are typically only available to the purchaser after the software is purchased and so the validity of such licences is in doubt under black letter contract law. After a discussion of the relevant case law and legislation, the paper concludes that New Zealand should validate shrink-wrap licences by statute. It discusses how to prevent software producers from using valid shrink-wrap licences to create de facto intellectual property rights for which there is no commercial justification.

Word Length

The text of this paper (excluding abstract, contents page, footnotes and bibliography) comprises approximately 14482 words.

I INTRODUCTION

Historically, intellectual property has been commercially exploited by selling copies of the intellectual property embodied in a tangible object. Hence, it was possible to treat contacts for these products in much the same way as contracts for other tangible goods. Where information was subject to intellectual property laws, the tangible copy of the information was sold subject only to intellectual property restrictions. Where it was not subject to intellectual property law, information was either protected by means such as trade secrecy and confidentiality or was free to be taken by all.

With the computer revolution of the second half of the 20th century, a commercially important industry has developed based on intangible electronic information. The fluid nature of this information has made it vulnerable to free riders. Consequently, producers have attempted to protect their investment through contractual means. The result has been the licensing of rights to use information, rather than the sale of a copy of the information.

However, the combination of intangible information products, new methods of contract and intellectual property law has lead to concerns that producers may be able to "privatise" a greater amount of information than was possible when information products took a tangible form. This concern is principally related to the ability of producers of mass market software to present one-sided contracts to users in the form of "shrink-wrap" licences. Formerly, there was considerable doubt as to the enforceability of such licences. However, recent legislative proposals and case law indicate that attitudes to enforceability may be becoming more liberal.

The purpose of this paper is to look at the interaction of copyright law, mass market software and contract as it impacts on public access to information. Chapter II discusses the development of intangible intellectual property products. Chapter III examines mass market software and shrink-wrap licences. Chapters IV and V discuss overseas case law and legislation on shrink-wrap licences. Chapter VI considers aspects of the draft Article 2B of the United States Uniform Commercial Code, which would validate shrink-wrap licensing as part of a separate contractual regime for transactions in intangible information. Chapter VII considers how a New Zealand court is likely to treat a shrink-wrap licence transaction. Finally, in chapter VIII, I consider what would be the optimal response for New Zealand, as a small, net importer of intellectual property, to the issue of shrink-wrap licensing.

II FROM TANGIBLE TO INTANGIBLE INTELLECTUAL PROPERTY

A Historical Review

When the technology for producing literary works consisted of pen and parchment, there was no need for a law of copyright. The time and labour required to produce a copy precluded wholesale copying, either by the author or others. Copying of literary works was encouraged. With the advent of the printing press, the commercial exploitation of literary works became possible. Printing technology created an opportunity for the author to create and sell multiple copies of his or her work. However, it also enabled others to free ride by exploiting the work for commercial purposes without recompense to the author. The law responded, after a few hundred years, with the development of an intellectual property right.[1] Copyright enabled the author to capture the benefits of the commercial exploitation of his or her literary work, but allowed for public access to the information created. Further, the property right was of limited duration and the protected material eventually ended up in the public domain.

[1] Statute of Anne 1709 (GB), 8 Anne, c 19.

With the advent of digital technology,[2] the possibilities for the commercial exploitation of information have expanded again. A huge industry based on digital information has developed. The basic information product of the digital economy is software. Software is comprised of a computer program or programs. After some years of doubt, computer programs have come to be universally recognised as literary works and thus protected by copyright.[3]

Software differs from tangible copyright products in several respects. The most important difference is the ease with which software may be copied. While tangible copyright products, such as books, are also vulnerable to copying, software is especially vulnerable. Copying a book requires some expenditure of time and money. However, copying software is instantaneous and practically free.

This was problematic for the development of a mass market for software products. A free and competitive market system requires excludability and rivalry.[4] These factors were initially missing from the software market because of the ease with which software could be copied.

Excludibilty refers to the ability of sellers to exclude users unless they pay.[5] Physical goods are naturally excludable as the producer owns them and will not hand them over without compensation. Tangible information products are also excludable. Excludabilty is artificially created by state guaranteed intellectual property rights. It is also naturally present, to a certain extent, because of the investment required to produce additional copies. However, when software was first developed, it was not clear that it was protected by the laws of intellectual

[2] "Digital technology" refers to the technological ability to reduce information to binary digits. For example, books, paintings, music, films, databases and documents may all be recorded digitally. These binary digits form a code comprehensible only to a computer.

[3] World Intellectual Property Organisation Copyright Treaty 1996, art 4 [WIPO Copyright Treaty 1996].

[4] J Bradford De Long and A Michael Froomkin "The Next Economy?" 2 at <http://www.law.miami.edu/^froomkin/articles/newecon.htm> (last modified 6 April 1997) ["The Next Economy"].

[5] "The Next Economy" above n 4, 2.

property. Being cheaply and easily copied, it was difficult for the software owner to exclude others from using it.

Rivalry means that two consumers are not able to use a product as cheaply as one.[6] Rivalry exists naturally in tangible goods, including tangible intellectual property, because of the investment required to produce extra copies. Software, however, is not rival because cost free copying means that no extra resources are required to allow additional users to consume the product.

1 The move to licensing software

Software required a considerable investment to produce, but lack of excludability and rivalry meant it was difficult for the producer to recoup this investment from the market. Producers attempted to solve this problem by re-creating excludability and rivalry through contractual means. This was achieved by licensing the purchaser to use the software rather than selling him or her a copy.

(a) provides excludabilty

If the producer sold a copy of the software, the purchaser was able to freely copy, unhindered by intellectual property law or a need for physical resources. However, licensing enabled the producers to claim that their programs were trade secrets and therefore protected by trade secrecy law.[7] In a licensing transaction, the producer could assert a proprietary right in the software and bind the licensee to confidentiality. Even when the software was sold to the general public, the intangible nature of the software meant that no-one could perceive the information merely by looking at the physical medium of the disk. As only the licensees were privy to the information, the producer could maintain

[6] "The Next Economy" above n 4, 2.

[7] Mark A Lemley "Intellectual Property and Shrink-Wrap Licenses" (1995) 68 S Cal L Rev 1239, 1243; Page M Kaufman "The Enforceability of State "Shrink-Wrap" License Statutes in Light of *Vault Corp. v Quaid Software Ltd*" (1988) 74 Cornell L Rev 222, 233.

that the software remained confidential. This solved the problem of excludabilty.

(b) provides rivalry

Licensing also allowed the producer to grant the user only a limited right to use the information. This was particularly important in the USA, where the "first sale doctrine" grants a purchaser certain rights which may not be contractually limited by the seller.[8] Licensing enabled the producer to control the user's rights to use the information so that the use reflected the price paid. Common restrictions to ensure a fair return in respect of use were limits on copying, restricting the licensee from allowing others to use the information, restrictions on the number of concurrent users, and bans on assignment. This solved the problem of rivalry, as producers were able to create a contractual bar to more than one user benefiting from the software without paying for the privilege.

(c) limits liability

Producers also used the licence to limit their liability to users. The degree to which producers may limit liability by contract often turns on whether a transaction is subject to statutes regulating the sale of goods. A contract for the sale of goods is typically subject to certain implied warrantees.[9] These can usually be contracted out of.[10] However, in consumer transactions this ability is often limited.[11] The use of licensing and the intangible nature of software raised the issue of whether such transactions were sales of goods.

---

[8] The first sale doctrine has been codified in the Copyright Act 1976, 17 USC s 109 (1998). The New Zealand Copyright Act 1994 also has a version of the first sales doctrine. Section 16(1)(b) makes issuing a work to the public an exclusive right of the copyright owner. However, under s 9 this right is limited to putting into circulation copies not previously put into circulation. Acts of subsequent distribution or sale of those copies (with the exception of the rental of computer programs) are excluded.

[9] The Sale of Goods Act 1908, s 16.

[10] The Sale of Goods Act 1908, s 56.

[11] The Sale of Goods Act 1908, s 56A; Consumer Guarantees Act 1993.

B The Extension of Private Rights in Information?

Intellectual property rights in computer programs are now universally recognised and are embodied in the latest World Intellectual Property Organisation (WIPO) Copyright Treaty.[12] Thus, the need to re-create excludability by contractual means no longer exists. However, licensing remains vital to the development of the software industry because of the need to create rivalry. Licensing also remains useful as a means of limiting the software producer's liability to the end user. Nevertheless, a number of commentators are concerned that licensing software gives producers an opportunity to expand their private rights in information at the expense of public access.[13] This is due to the different impact of copyright on tangible and intangible information products.

Copyright does not protect information or ideas, only the manner in which they are expressed.[14] The information or ideas in a book can be accessed by reading, which is not a copyright restricted act. The restrictions that are imposed by copyright (principally copying and issuing copies to the public) are themselves limited.[15] Copyright does not prevent fair uses, such as copying for private study.[16] Nor does it limit the distribution of the book after the first sale.[17] It is not practical for the information producer to try and limit such uses by contract. Even if the purchaser were, for example, bound by contract not to make fair use of a book, third parties, who could read the book without copyright

---

[12] WIPO Copyright Treaty 1996 above n 3, art 4. New Zealand has not yet signed the Treaty but the Minister of Commerce has stated an intention to do so. (Information supplied by the Ministry of Commerce, 23 September 1998).

[13] See, for example, Pamela Samuelson "Legally Speaking: Does Information Really Want to be Licensed?", unedited copy, scheduled to be published in September 1998 issue of *Communications of the ACM* <http://sims.berkeley.edu/^pam/papers/acm_2B.html> (last accessed 30 June 1998); Mark A Lemley "Intellectual Property and Shrink-Wrap Licenses" (1995) 68 S Cal L Rev 1239.

[14] The "sweat of the brow" cases, such as *Waterlow Directories v Reed Information Services Ltd* [1992] FRS 409, do protect information to a certain extent. However, broadly speaking, the statement is correct.

[15] Section 16 of the Copyright Act 1994 lists the acts restricted to the copyright owner. Part III of the Act deals with acts permitted in relation to copyright works.

[16] Copyright Act 1994, s 43.

[17] Copyright Act 1994, s 9.

infringement, would not be bound. Contract cannot bind these third parties so the producer is reliant on state enforced property rights.

Software is also protected by the law of copyright.[18] However, the crucial difference between software and a tangible copyright product such as a book is that software does not bear its information on its face. Intangible information cannot be comprehended by humans unless it is transformed into tangible form. This applies to both the copyrighted object code[19] that makes the computer "perform" and to the (possibly copyrighted) information that is displayed on the screen. For either to be "read" by a human, the copyrighted object code must be copied by a computer.[20]

This will generally be a copyright restricted act. Making a permanent copy of a program on the hard disk of computer is generally accepted as a copyright restricted act by jurisdictions that protect computer programs as literary works. Transfer of the program to the random access memory (RAM) for ephemeral display is accepted as a copyright restricted act in England,[21] and by a line of controversial cases in the USA.[22] Whether ephemeral display should be a copyright restricted act was a topic of fierce debate at the negotiations on the WIPO Copyright Treaty 1996.[23] The situation is unclear in New Zealand. Section 2 of the Copyright Act 1994 defines "copying" as reproducing or recording the work in any material form, including, in relation to a literary work, storing the work in any medium by any means. The term "material form" may or may not include transient copying. However, even if such copying is not forbidden by the law of copyright, the licensor can bind the

---

[18] The Copyright Act 1994, s 2, states that "literary work" includes a computer program. Some computer programs have also been granted patent protection overseas but this is rare.

[19] Object code consists of a series of 1s and 0s that are read by the computer in executing the program.

[20] There are certain limited exceptions to this. It is possible to reverse engineer object code.

[21] Copyright, Designs and Patents Act 1988 (UK), s 17(6).

[22] *Triad Systems v Southeastern Express Co* (1995) 64 F 3d 1330 (9th Cir); *MAI Sys Corp v Peak Computer Inc* (1993) 991 F 2d 511 (9th Cir); *Advanced Computer Systems v MAI Systems Corp* 845 (1994) F Supp 356 (ED Va).

[23] The final Treaty did not refer to the subject.

original licensee through contract so that it may not provide such access to third parties.

Thus, in order to legally access the information in the software, it is necessary to become a licensee. A licensee may be bound with all sorts of restrictions that are not imposed by copyright law. As licensees are invariably restricted from allowing others to use the software, it becomes impossible for anyone not bound by the licence restrictions to access the information. This provides software producers with an opportunity to use contract as a means of creating new de facto intellectual property rights.

The producers' position has been further strengthened by the development of technical means to enforce contractual limits. For example, programs may be designed to limit the number of concurrent users of software to the number specified in the licence. Or a program may be protected from copying. These technical devices have become increasingly important as software producers have gained legal protection against attempts to disable such devices.[24]

III MASS MARKET SOFTWARE AND SHRINK-WRAP LICENCES

Software may be broadly divided into two types, customised and mass market.[25] Customised software is created to the customer's requirements, there is a direct relationship between the parties and the terms of the contract are negotiated between them. In contrast, mass market software is standardised and mass produced. It is offered to the public via a standard form, non-negotiated contract. There is usually a chain of supply between the producer and user. The software is ordinarily delivered via the sale of a disk or CD-ROM.

[24] The New Zealand Copyright Act 1994, s 226, makes illegal the provision of devices intended to circumvent copy-protection of electronic copyright works. The WIPO Copyright Treaty 1996, art 11, obliges signatories to provide adequate legal protection against the circumvention of technological measures used to protect copyright works.

Mass market software typically contains what is known as a shrink-wrap licence. This is a licence packaged with the disk containing the software.[26] The terms of the licence may or may not be visible without opening the package. A notice on the packaging alerts the purchaser to the presence of the licence and states that the purchaser agrees to the licence by opening the shrink-wrap packaging.

The on-line version of such licences are called click-wrap licences. On accessing the software, the purchaser proceeds through a series of screens that alert him or her to the existence of the terms and offer an opportunity to read them. The user cannot proceed without clicking on a button to indicate consent to the terms.

A Shrink-Wrap Licences May Expand Property Rights in Information

The danger of software producers using a combination of licensing and technology to expand their de facto rights in information at the expense of publicly available information is particularly associated with mass produced software and standard form licences. Contracts for customised software involve bargaining between the parties. The software producer will not necessarily be in a more powerful position than the purchaser. Consequently, if the licensee knows what his or her rights are under intellectual property law, the producer of customised software will not necessarily be able to acquire stronger rights in the information. Further, customised software is not generally publicly available. Thus, any extension of the software producer's rights in the information would only be at the expense of the licensee, not the public.

[25] This is, of course, a simplification of the situation. Non-customised software packages may be heavily customised for a particular client. The line may perhaps be drawn by considering how much customisation was required and whether there was a negotiated contract.

[26] It may also be printed on the outside of boxes containing computer software, included somewhere in the box or shrink-wrapped with the owner's manual accompanying the software.

In contrast, mass market software is sold with a non-negotiated licence that is written by the software producer. The licensor is invariably in a more powerful position than the licensee. This makes the licensing of mass market software a much more potent tool for extending software producers' property rights in information. These licences typically limit many uses that would not be proscribed by copyright law. While some of these restrictions may be necessary to create rivalry, this is not always the case. For example, there may be restrictions on reverse engineering, bans on adverse comment on the software, and restrictions on use to particular items of hardware or a particular site, even if the extent of actual use does not change. Competition between producers does not appear to effectively limit this. Thus, despite the apparent public availability of these information products, the producer has effectively limited the public's ability to make use of them in ways not proscribed by intellectual property law.

B Are Shrink-Wrap Licences Enforceable?

The use of restrictive licence terms in mass market software licences is only problematic if the licences are enforceable. Despite being used world wide, the enforceability of shrink-wrap licences has often been doubted by academic commentators.[27] Under black letter contract law, the terms of a contract must be known before the contract is concluded.[28] Many shrink-wrap licences are not capable of being read until after the money and software have changed hands. Consequently, the terms come too late to be part of the contract. Another problem is privity of contract. Most retail software is sold through a distributor. Therefore, it is hard to fit the software producer into the contract as a party who can enforce the licence terms. Nevertheless, recent cases have found shrink-

[27] "Are Shrink-wrap Licences Legally Effective?" (1997) 10 Australian Intellectual Property Law Bulletin 91; David Bainbridge *Software Copyright Law* (2 ed, Butterworths, London, 1994) 180.

[28] John F Burrows, Jeremy Finn and Stephen Todd *Law of Contract in New Zealand* (Butterworths, Wellington, 1997) 189-191.

wrap licences to be enforceable.[29] There have also been moves to validate shrink-wrap licences by statute.[30]

C Is Mass Produced Software "Goods"?

It is unclear whether transactions in mass market software are sales of goods or something else. This issue is important because the categorisation will determine what body of law will apply to the transaction. If shrink-wrap licences are enforceable, categorisation of the transactions as sales of goods will provide consumer protections that software producers may not contract out of. If shrink-wrap licences are not enforceable, the categorisation will determine which set of contractual default rules will apply to the transaction.

This is particularly important with regard to warrantees. For example, the provision of software (particularly without a physical medium) could be categorised as purely a licence to use the intellectual property. An implied warrantee with regard to a pure licence would probably be limited to a warrantee that the producer owns the intellectual property and will not sue for use. On the other hand, such a transaction could also be categorised as the sale of a good (particularly if the software was supplied on a physical medium). Such a transaction would be subject to an implied warrantee of merchantability and fitness for its purpose.[31]

---

[29] *Pro-CD v Zeidenburg* (1996) 86 F 3d 1447 (7th Cir); *Beta Computers (Europe) Ltd v Adobe Systems (Europe) Ltd* [1996] 5 FSR 367 (Scottish Court of Session, Outer House).

[30] Louisiana Software License Enforcement Act, LA REV STAT ANN §§ 51:1961-1966 (West 1987 & Supp. 1995) [Louisiana Software License Enforcement Act]; Illinois Software Enforcement Act, ILL REV STAT Ch 29 para 801-808 (1986) (repealed) [Illinois Software Enforcement Act (repealed)].

[31] Sale of Goods Act 1908, s16.

IV THE CASE LAW ON SHRINK-WRAP LICENCES

A Canada

In *North American Systemshops Ltd v King*,[32] a computer program was distributed inside a shrink-wrapped booklet. A copyright symbol and a licence agreement were placed on the inside cover of the booklet. They were not visible to the purchaser at the time of purchase. Judge Veit held that copyrighted computer programs may be sold subject to restrictive conditions.[33] However, in an over-the-counter sale, where no explicit restrictions are brought to the notice of the purchaser, there is an implied granting of permission to the purchaser to do whatever the purchaser wished with the program.[34]

The Judge's reasoning was based on a number of patent cases in which patent holders had tried to restrict the use of patented products after sale.[35] These cases showed that patented articles were different from normal goods in that restrictions may be imposed on the use of these goods when they were sold. Those restrictions ran with the goods. The Judge found that copyright goods belong to a similar category.

However, as with patented goods, a sale of copyright goods without explicit restrictions on use vested full rights to use the goods. This was especially so in the case of over-the-counter sale of computer software because it cannot be used without being copied at least once into the computer's memory. As the plaintiff did not bring home to the defendant that there were any restrictions on use at the time of purchase, and as no implied restrictions were necessary to the sale, the defendant was impliedly granted the right to do whatever he wished with the program.

[32] *North American Systemshops Ltd v King* 68 Alta LR (2d) 145 (QB).

[33] *North American Systemshops Ltd v King* above n 32, 154.

[34] *North American Systemshops Ltd v King* above n 32, 155.

[35] *Betts v Willmott* (1891) LR 6 Ch 239 (CA); *Incandescent Gas Light Co v Cantelo* (1895) 12 RPC 262 (QBD); *Liverpool City Council v Irwin* [1977] AC 239 (HL); *Nat Phonograph Co of Australia ltd v Menck* [1911] AC 336 (PC).

1 *Critique*

This case recognised a right for software producers to limit the use of their software as long as the restriction is brought to the attention of the purchaser at the time of sale. However, the right was based on an analogy with patented goods, rather than the recognition of a need for software owners to recreate rivalry in order to efficiently market their products. The right of patentees to restrict the use of patented products is based on the statutory monopoly granted the patentee to use or vend the patented item. However, because the enforcement of these rights would prevent the purchaser of a patented product from using it, the law assumes that a sale without explicit restrictions grants all rights to use the article.

Copyright, in contrast, only grants the author the right to control certain uses of the intellectual property.[36] All other uses are available to the purchaser of a copyrighted product. The Judge did not discuss these differences between copyright and patent products. The breach of licence in question, copying the program onto several computer hard disks, was a copyright infringement. Thus, the Judge may have merely meant that the copyright owner may, by explicit notice, restrict copyright uses only. This certainly seems the only acceptable extension of the patent analogy to copyright works.

Allowing the software producer to contractually restrict copyright uses only would not appear to allow the creation of de facto property rights in information. Nevertheless, it does potentially grant the producer power to control all uses, as the computer program must be copied to be used. Thus, non-copyright restrictions may be linked to copyright restrictions in a single take it or leave it contract. The Judge noted that a purchaser could not use the software without copying it but did not discuss the implications of this.

[36] Copyright Act 1994, s 16, is a New Zealand example of this.

The Judge noted that the manner of selling the software, with no warning of the licence inside the booklet, was no longer current. He did not comment on whether a visible shrink-wrap licence or visible notice of a licence would be enforceable. This has led commentators to state that it is unclear whether shrink-wrap licences are enforceable in Canada.[37]

B Singapore

In *Aztech Systems Pte Ltd v Creative Technology Ltd*,[38] the High Court of Singapore dealt in passing with a shrink-wrap licence. The case concerned sound cards produced by the defendant that were sold to the public together with a package of ancillary software. The plaintiffs purchased a copy of the sound cards and software. They then developed sound cards designed to be compatible with the defendant's sound cards. In doing so, they studied the defendant's sound card while running the software. This necessarily involved reproducing the program in the memory of a PC. The defendant alleged that this infringed its copyright in the computer program.

The Judge found that the use was fair dealing for the purposes of private study. However, the software apparently contained a shrink-wrap licence in the manual restricting such use. The Judge discussed the issue in terms of whether a copyright owner, having sold a copyright product, has any right to restrict the use of the product by the purchaser. Like Judge Viet, he drew an analogy with the sale of patented articles and concluded that a sale without restrictions granted the purchaser all rights to use the product.

At no time up to the point of the purchase was the defendant's attention drawn to any limitations as to the use of the software. The limitations in the manual would only have come to its attention after the purchase. Thus, the purchaser of

[37] Sunny Handa "Reverse Engineering Computer Programs Under Canadian Copyright Law (1995) 40 McGill Law Journal 621, footnote 87.

[38] *Aztech Systems Pte Ltd v Creative Technology Ltd* [1996] FSR 54 (HC).

the software was entitled to exercise the rights of ownership. These include using it, running it on as many PCs and as often as he pleases, studying it and experimenting with it, regardless of the fact that using it in this fashion involved making a copy of the software on the PC's memory. However, he cannot make and distribute copies of the software as that is not using it.

The High Court's decision was reversed in the Court of Appeal.[39] The Court of Appeal pointed out that, because of the patent owners rights to control the use and re-sale of the patented article, it was necessary to imply a term that the patent owner had consented to use or re-sale in order to give business efficacy to the contract. This was not the case with a copyright article. Any terms which should be implied must be limited to those necessary to lend business efficacy to a contract, and that did not extend to implied consent to copying the program in order to make a competing product.

1 *Critique*

This case, like *North American Systemshops Ltd v King,* illustrates the black letter problem with shrink-wrap licences. Shrink-wrap licences are not enforceable because they are not brought to the attention of the purchaser until the contract is concluded. It also provides an interesting discussion of the extension of the patent implied licence principle to copyright works. Given that it is necessary for a software user to copy the copyrighted computer program in order to use the product, an implied licence to copy seems justified, at least to the extent required to make ordinary uses of the program. Whether this extends to an implied licence to make a competing product seems to depends on the court's attitude to the role of innovation in copyright policy.

[39] *Creative Technology Ltd v Aztech Systems Pte Ltd* [1997] 1 SLR 621 (CA).

C USA

The earliest cases in the USA held that purchasers could not be bound by shrink-wrap licences. Mass market software transactions were treated as sales, effective at the point of purchase, not licences, and the "licence" in the box as an attempt to alter the terms of the contract without meaningful consent from the purchaser.[40] The Louisiana courts treated shrink-wrap licences as contracts of adhesion and therefore invalid.[41] Thus, the only rights the software producer retained in the software were those available under copyright law. However, in a recent 7th circuit decision, *Pro-CD v Zeidenburg*,[42] this trend has been reversed.

Pro-CD produced a software telephone directory which it offered to the public for two different prices, the higher price allowing commercial use and the lower price allowing personal use. The defendant purchased a copy with a personal use licence for the lower price. He read the shrink-wrap licence and also had to proceed through an on-line version of the licence before accessing the software. The licence asked the user to return the software for a refund if he or she did not assent to the terms of the licence.

Although aware that the terms of his licence forbade commercial use, the defendant proceeded make his copy available to the public on his website for a fee. He did not believe that the licence was enforceable and the telephone directory was not protected by copyright under United States law.[43] The Judge at first instance found for the defendant on the grounds that the licence was unenforceable as it was presented to the defendant after the formation of the contract. However, this decision was reversed on appeal.

---

[40] *Step-Saver Data Systems Inc. v Wyse Technology* (1991) 939 F 2d 91 (3d Cir); *Arizona Retail Sys v Software Link* (1993) 831 F Supp 759 (D Ariz).

[41] *Vault Corp v Quaid Software Ltd* (1987) 655 F Supp 750 (ED La), aff'd (1998) 847 F 2d 255 (5th Cir).

[42] *Pro-CD v Zeidenburg* (1996) 86 F 3d 1447 (7th Cir) [*Pro-CD v Zeidenburg*].

[43] *Feist Publications v Rural Telephone Service Co* (1990) 499 US 340.

1 *Commercial importance of shrink-wrap licences*

The Court of Appeals held that computer software shrink-wrap licences are enforceable unless their terms are objectionable on grounds applicable to contracts in general.[44] In coming to this conclusion, the Court emphasised the commercial importance of the shrink-wrap licence. The telephone database was expensive to produce and maintain. The licence allowed the vendor to use price discrimination, selling the product for personal use at a low price and for commercial use at a much higher price. If the vendor could not limit use by contract, then it would have to sell at one price allowing for all uses. This would be bad for consumers as it would eliminate buying for personal use and, also, raise the single price above that currently charged for commercial use in order to make up for the lost personal use sales.

The Court considered that standardisation of agreements was essential to a system of mass production and distribution. While the terms of an agreement must be known before the contract is concluded, the Court thought that this requirement had been met. The terms of the licence allowed the purchaser to return the software for a refund if he or she did not accept the terms. This allowed the Court to hold that the contract was not formed until the purchaser had had an opportunity to read the licence and indicate assent by using the software. The Court concluded that, as it was not practical to put the agreement on the outside of the box, then, notice on the outside, terms on the inside and a right of refund if the terms are unacceptable may be a means of doing business that is valuable to buyers and sellers alike.

2 *Private intellectual property rights*

The Court also had to consider whether the licence created rights equivalent to those created by the federal Copyright Act. If this was the case, then the rights created by the licence would be pre-empted by the Copyright Act and would be ineffective.[45] The Court noted that a copyright is a right against the world. Contracts, in contrast, generally only affect their parties, and so do not create exclusive rights. Someone who found a copy of the software on the street would not be bound by the shrink-wrap licence, but they would be by the law of copyright.

The Court considered that terms and conditions offered by contract generally reflected private ordering, essential to the efficient functioning of markets. The point of the rule forbidding state law from pre-empting federal copyright law was to prevent States from substituting their own regulatory systems for those of the national government. It was not to interfere with private transactions in intellectual property. The Court did not think it prudent to adopt a rule that anything with the label "contract" was outside the pre-emption clause. However, the general enforcement of shrink-wrap licences of the kind in *Pro-CD* did not pre-empt federal copyright law.

3 *Critique*

The judgment is valuable for the recognition it gives to the commercial importance of standard form contracts in the mass production and distribution of software. While it may be a legal fiction to say that the consumer agrees to the licence if he or she has an opportunity to read it (because consumers generally ignore them), this is no less true than for other products sold with standard form contracts. In particular, the judgment recognises that licensing gives software producers the ability to tailor their product to different users, to the benefit of both producers and consumers.

However, the Court failed to recognise the possibility of producers using shrink-wrap licences to expand their rights in information to the detriment of public access to information. The argument that such contracts only bind the parties is

---

[44] *Pro-CD v Zeidenburg* above n 42, 1449.

[45] Copyright Act 17 USC s 301(a) (1998).

erroneous. As was pointed out above, shrink-wrap licences enable the licensor to control the access of third parties to their software. Third parties must copy the software to "read it". The copyright status of the software means they cannot do this without the authorisation of the software producer. The licensee is invariably bound by the contract not to allow others to use his or her copy of the software. Thus, an enforceable shrink-wrap licence is, indeed, a right enforceable against the world. The Court's example of a stranger finding a copy of the software in the street and not being bound by the licence is unconvincing. People who find software lying in the street are a very small section of the world's population.[46]

The Court considered that the purpose of the copyright pre-emption section was to prevent the States from substituting their own regulatory systems for those of the national government, not to interfere in private contractual arrangements. However, if policy precludes the States from doing this, surely industry groups should also be precluded from effectively creating private de facto intellectual property rights in substitution for those of the national government.

The ability of software producers to use licensing to create de facto intellectual property rights can be demonstrated by comparing *Pro-CD* to another American copyright case, *Feist Publications v Rural Telephone Service Co*.[47] *Feist* also concerned a telephone directory, however, the *Feist* directory was a tangible, paper directory. The defendant in *Feist* had copied a telephone directory produced by the plaintiff in order to include the information in its own telephone directory. The plaintiff alleged that this was an infringement of its copyright. The Supreme Court held that the plaintiff's telephone directory was not sufficiently original to attract copyright. Therefore, the defendant (and others) could freely copy it.

---

[46] Perhaps shrink-wrap licences could be described as creating a property right good against all the world except strangers who find the software lying in the street!

[47] *Feist Publications v Rural Telephone Service Co* above n 43.

The database of electronic telephone directories in *Pro-CD* was also assumed not to be subject to copyright.[48] Nevertheless, the Court found for the plaintiff as it considered the licence an effective limitation on the defendant's ability to use the database. Thus, a change in the method of contracting has effectively given a property right in electronic telephone directories where a similar right does not exist with regard to the tangible paper equivalent.[49]

D Scotland

The effectiveness of shrink wrap licences was considered in the Scottish case of *Beta Computers (Europe) Ltd v Adobe Systems (Europe) Ltd*.[50] *Beta v Adobe* involved a retail transaction. The defender (the end user) had ordered software off the pursuers (the retailer) by telephone. The software was delivered, however the defender decided it did not want it and returned it unopened. The software was packaged so as to indicate that it was subject to a strict end-user licence to the copyright owner (a third party). The packaging bore the words "opening the ... software package indicates your acceptance of these terms and conditions".[51] The defenders contended that this gave them an absolute right to reject the package until they opened it. The pursuers contended that the contract for the supply of the software had been concluded and that the defenders were obliged to pay them the price of the software.

1 A single complex product

Lord Penrose began his analysis by identifying what it was the defenders sought to have supplied by the pursuers, that is, what was the subject of the contract?

[48] Of course, the computer program that enabled users to see the directory on the screen was copyrighted.

[49] On 9 October 1997, a bill was introduced into Congress which would create a property right in such collections of information: HR 2652 "Collections of Information Antipiracy Act". The bill was passed by the House of Representatives 8 May 1998 and is currently before the Senate.

[50] *Beta Computers (Europe) Ltd v Adobe Systems (Europe) Ltd* (1996) 5 FSR 367 (Scottish Court of Session, Outer House) [*Beta v Adobe*].

[51] *Beta v Adobe* above n 50, 370.

He found that the subject of the contract was access to the third party's intellectual property in a medium which the defenders could use, and from which they could copy program material electronically into their hardware system. The order was not an order for the supply of disks or an order for the supply of information: "The subject of the contract was a complex product comprising the medium and the manifestation within it ... of the intellectual property of the author... in the form of the program material contained".[52]

2 *Not a sale - a sui generis contract*

A contract for the sale of software must, if it is to have business efficacy, make available to the purchaser both the medium and the right to access and use the software. However, the scheme of the Copyright, Designs and Patents Act 1988 (UK) makes it impossible to legitimately supply the medium with the facility to access program material contained in it, independently of the authority of the owner of the copyright. Lord Penrose rejected an analogy with the sale of a printed book, as a book merely needs to be read, not copied. With a book there are no limitations on accessing the information which affect readers generally and which are inherent in the medium. However, with software there is no possibility of accessing the information without copyright infringement. He concludes that: [53]

> the supply of proprietary software for a price is a contract *sui generis* which may involve elements of nominate contracts such as sale, but would be inadequately understood if expressed wholly in terms of any of the nominate contracts.

[52] *Beta v Adobe* above n 50, 375.

[53] *Beta v Adobe* above n 50, 377.

3 *A single contract*

Lord Penrose rejected the idea that the transaction consisted of two contracts, one between the purchaser and supplier and one between the purchaser and the copyright owner. He considered that there was a single contract between the supplier and the purchaser and that it was an essential feature of the contract that the supplier undertake to make available to the purchaser both the medium and the right of access to the copyright material.

He did not think that it was possible to hold that a second contract came into existence between the copyright owner and the end user when the product was unwrapped. This was because the supplier would not be bound by such a contract, which would mean that the supplier's only obligation would be to supply the disk. This would leave purchasers with a product they could not use unless they accepted the copyright owner's conditions. Or, if the copyright owner could not enforce the restrictions, would undermine the ability of the copyright owner to control the permitted use of his or her intellectual property. Neither of these results pleased the judge. He thought that the interests of the industry as a whole in the efficient and sensible management of transactions required that effect should be given to the licence conditions if possible.

Lord Penrose concludes that, given the importance of the purchaser's ability to legitimately use the software, the contract could not be properly analysed without acknowledging the need to ensure the consent of the copyright owner to the intended use of his property. Where the conditions of such use were not within the control of the supplier but must be granted by the owner, and where there were well-established routines for determining what those requirements were, consensus could not be achieved the until the conditions were produced and accepted by the parties. That point could not come earlier in this case than the stage at which the supplier, deriving the material from the owner, tendered to the purchaser an expression of those conditions which the purchaser might accept or reject before becoming bound to the contract.

Lord Penrose's analysis leaves one black letter contract problem. The licensor is a third party to the contract between the supplier and the purchaser and therefore has no standing to enforce the terms of the licence. The Judge solves the problem by applying the Scottish law doctrine of *ius quaesitium tertio*. This doctrine protects third party interests in a contract if the terms of the contract indicate that it was an object of the contract to benefit the third party.

4 *Critique*

Lord Penrose recognised the unique nature of software transactions and the necessity of focusing on the "thing of value" to the parties when analysing the transaction. His conclusion that mass market retail software transactions are *sui generis* contracts for a complex product enables him to avoid the trap of squeezing the transaction into familiar, but unsuitable, contractual forms. Nevertheless, he still has to fit the transaction into the general rules of contract law; that is, the licence terms must be known before the contract is concluded and there must be privity of contract.

His analysis of the contract of supply as being a contract for *useable* software neatly solves the timing problem. Further reasons for finding the licence to be part of the contract between the user and supplier are that it is easier for a user to obtain a refund off the retailer and the difficulty of finding consideration for a contract between user and producer.[54]

However, the Judge does not refer to these factors. His reasoning centres around the fact that if the licence was to form a new contract between software producer and user, the supplier's only obligation would be to supply the disk. Then either the user would be obliged to accept and pay for a disk it could not use, or, if the licence was ineffective, the copyright owners' ability to control their intellectual property would be undermined. Oddly, Lord Penrose does not

[54] Several commentators have pointed out that purchasing the software would be past consideration at this point. See, for example, Gary Lea "The Impossible Intangible: Shrinkwrap Software Revisited" (1996) 1 Communications Law 238, 240.

refer to the patent cases, discussed above, which hold that the sale of patented items (and by analogy copyright items) without restriction grants all uses that are part of the exercise of ownership.

The mechanism whereby Lord Penrose validates the licence is rather idiosyncratic, *ius quaesitium tertio* being a civil law doctrine which is not available at common law. The problem with using this doctrine is that, while it would enable the licensor to enforce the licence terms against the licensee, it would not permit the licensee to enforce licence terms, for example warrantee provisions, against the licensor. The doctrine has been introduced into New Zealand by the Contracts (Privity) Act 1982. However, the same difficulty would arise if the Act were to be used to validate a shrink-wrap licence. Under the Act, a beneficiary of a contract can sue to enforce the terms made for its benefit.[55] However, the beneficiary itself cannot be sued.

The Judge was aware of the commercial importance of shrink-wrap licences. Indeed, he states that he considers that the interests of the industry as a whole in the efficient and sensible management of transactions required that effect should be given to the conditions if possible.

However, he does not consider the effect of shrink-wrap licences on the public information domain. That is not surprising as the case was limited to asking if the purchaser can return the software without payment. Yet, by finding that the licence terms form part of the contract between the supplier and the user and that they are enforceable by the software producer against the user, the judgment implicitly raises the question of what sort of licence terms should be enforceable.

[55] Contracts (Privity) Act 1982, s 4.

V THE SOFTWARE ENFORCEMENT ACTS OF LOUISIANA AND ILLINOIS

The cases that recognise shrink-wrap licences have had to fit them within the confines of classical contact law. As was demonstrated in *Beta v Adobe*, traditional doctrines may have to be stretched to accommodate transactions in intangible goods. The legislatures of Louisiana and Illinois have attempted to address the need for a specific contractual regime designed for mass market software sold with shrink-wrap licences. These States both enacted statutes which validated shrink-wrap licences.[56] These statutes provide an example of one form of legislative enforcement of shrink-wrap licences. It should be noted at this point that the Illinois statute has subsequently been repealed, as have several provisions of the Louisiana statute.

The statutes were based on the same model bill and provided very similar schemes for enforceable shrink-wrap licences. Under these schemes, the shrink-wrap packaging must include a conspicuously visible notice, stating that use of the software or opening the sealed packages will constitute acceptance of the terms of the accompanying licence agreement.[57] The purchaser must have the option of returning the unopened software for a refund.[58]

The statutes also provided a list of specific provisions that would be enforceable in conforming licences.[59] Under these provisions, the licensor may retain title in the copy. If the licensor retains title, purchasers are conclusively presumed to accept licence terms prohibiting any copying, limiting the purposes for which copies may be made, prohibiting the right to modify, adopt, translate, reverse engineer, decompile, disassemble, or create derivative works from the software,

[56] Louisiana Software License Enforcement Act above n 30; Illinois Software Enforcement Act, (repealed) above n 30.

[57] Louisiana Software License Enforcement Act above n 30, §§ 51: 1963(1); Illinois Software Enforcement Act (repealed) above n 30, para 803, s 3(1).

[58] Louisiana Software License Enforcement Act above n 30, §§ 51: 1963(4); Illinois Software Enforcement Act (repealed) above n 30, para 803, s 3(4).

[59] Louisiana Software License Enforcement Act above n 30, §§ 51: 1964; Illinois Software Enforcement Act (repealed) above n 30, para 804, s 4.

prohibitions on the subsequent transfer, assignment, sale or other disposition of the copy, and prohibitions on the use of the software on more than one computer or by more than one user at the same time.[60]

These statutes were intended to provide certainty as to the enforceability of shrink-wrap licences. This would have had the benefit of ensuring that software providers could introduce rivalry into the market and practice price discrimination. However, the statutes would also have allowed the contractual extension of the software producers intellectual property rights to a considerable degree. Many of the terms that were specifically validated covered activities for which there was no apparent commercial need, such as prohibitions on subsequent sale of the copy. Other possible restrictions, such as the prohibition on reverse engineering, could have had anti-competitive effects. Although such restrictions might have been commercially necessary in some circumstances, there was no onus on the producer to demonstrate that this was the case.

As noted above, these statutes were not successful. Several provisions of the Louisiana statute were struck down by because they were found to pre-empt federal copyright law.[61] The Illinois statute, which would have been subject to the same criticisms, has subsequently been repealed.

VI ARTICLE 2B OF THE UNIFORM COMMERCIAL CODE

A General

Shrink-wrap licences are part of a larger revolution in commercial transactions in digital information. The United States has responded to this revolution by seeking to develop the Uniform Commercial Code (UCC) to provide a suitable framework for such transactions. The UCC is not a statute. It is a model

[60] Louisiana Software License Enforcement Act above n 30, §§ 51: 1964; Illinois Software Enforcement Act (repealed) above n 30, para 804, s 4.

[61] *Vault Corp v Quaid Software Ltd* above n 41.

commercial code which the state legislatures may adopt or not, as they wish. The UCC has been adopted, with some minor variations, by all the 50 states, thus providing uniformity in state commercial law. The UCC strongly supports the concept of freedom of contract. However, in order to facilitate commercial transactions, it provides a set of default rules to apply in the absence of contractual agreement. It also provides a small number of mandatory rules.

The UCC was created in the 1950's. It is based on the sale of goods which was the foundation of the economy of that time. However, transactions in digital information are based on rights to use information. A new Article 2B is being drafted which will apply to transactions in digital information.[62]

B The "licensing" of "information"

Article 2B applies to any transaction that creates a software contract,[63] computer database access contract or licence of rights in information.[64] It also applies to any agreement to provide support for, maintain, or modify information related to such a contact.[65] It does not apply to the licensing of patents, trade marks or similar types of information, which have their own fields of law.[66]

The paradigmatic transaction of Article 2B is licensing, which allows the information producer to control the licensee's access to the information. Article 2B defines "license" as:[67]

> a contract that authorizes access to or use of information or of informational rights and expressly limits the contractual rights or

---

[62] National Conference of Commissioners on Uniform State Laws "Uniform Commercial Code Article 2B: Licenses" draft of 1 August 1998, 6-7, which can be found at <http://www.law.upenn.edu/bll/ucl/ucc2b/2b898.htm> ["Article 2B"].

[63] Except where the software is contained in another product and is incidental to the transaction.

[64] "Article 2B" above n 62, s 103.

[65] "Article 2B" above n 62, s 103.

[66] "Article 2B" above n 62, s 104.

[67] "Article 2B" above n 62, s 102(28).

> permissions granted, expressly prohibits, limits, or controls uses, or expressly grants less than all informational rights in the information. A contract may be a license ... whether or not the contract transfers title to a copy. ...

Any law regulating information will have significant free speech implications. In recognition of this, Article 2B distinguishes between information, "data, text, images, sounds, mask works or works of authorship",[68] and informational content, which refers to the information that the user perceives when using the information. For example, with regard to an encyclopaedia software product, the computer program running it would be information while the information displayed on the computer screen would be informational content.

Article 2B also distinguishes between rights to information created by contract and rights created by law, which it terms "informational rights".[69]

The Article covers the formation and terms of contracts, the formation of contracts electronically, construction of contracts, interpretation, warranties, transfer of interests and rights, performance and remedies. As part of their project, the drafters have tackled the issue of shrink-wrap licences. They endorse shrink-wrap licences as long as a certain procedure is followed.

C Shrink-Wrap Licences Validated

1 Mass market transactions

Article 2B has developed a new concept of the "mass market transaction".[70] The purpose of the mass market classification is to provide a suitable regime for low value, routine and anonymous transactions for information in pre-packaged

[68] "Article 2B" above n 62, s 102(24).

[69] "Article 2B" above n 62, s 102(27).

[70] "Article 2B" above n 62, s 102(32).

form, that occur in a retail market open to the general public. Consumer transactions on the Internet are also included.

A mass market transaction means a consumer transaction or any other transaction in information or informational rights directed to the general public as a whole under substantially the same terms for the same information with an end-user licensee. A transaction other than a consumer transaction is a mass-market transaction only if the licensee acquires the information or informational rights in a retail market transaction under terms and in a quantity consistent with an ordinary transaction in that market. A transaction other than a consumer transaction is not a mass-market transaction if it is:

- a contract for redistribution
- a contract for public performance or public display of a copyrighted work
- a transaction in which the information is customised or otherwise specially prepared by the licensor for the licensee other than minor customisation using a capability of the information intended for that purpose
- a site licence
- an access contract

2 Mass market licences

Mass market transactions are accompanied by mass market licences. A mass-market licence is defined as "a standard form that is prepared for and used in a mass-market transaction".[71]

[71] "Article 2B" above n 62, s 102(31).

3 *Manifesting assent*

Contracts may be formed by the manifestation of assent.[72] A person manifests assent if they intentionally engage in conduct that they know, or have reason to know, will indicate acceptance to the other party. The person must have had knowledge of the licence or term they are assenting to, or had an opportunity to review it before engaging in the affirmative conduct.

4 *Opportunity to review*

A person has an opportunity to review a licence or term only if it is made available in a manner that ought to call it to the attention of a reasonable person, and that permits review.[73] An example would be a click-wrap software licence which asks the licensee to indicate acceptance of the licence by clicking on an assent button, while giving the licensee an opportunity to review the licence via a hypertext link. As the licensee has an opportunity to review the licence, he or she can indicate assent by clicking on the assent button, regardless of whether they review the licence or not.

A manifestation of assent may be proved in any manner. This includes showing that a procedure existed by which a person must have engaged in conduct that manifested assent in order to proceed further in the use he or she made of the information. For example, a licensor could show that it was not possible to access their software without going through a series of screens that required the licensee to click assent to the terms of the licence.

[72] "Article 2B" above n 62, s 111.

[73] "Article 2B" above n 62, s 112.

5 *Adoption of mass market licence terms*

A party can adopt the terms of a mass market licence by manifesting assent to them either before or during the initial performance, use of, or access to the information.[74]

6 *Licensee protections*

Article 2B provides a number of protections for mass market licensees. A term does not become part of the contract if it is unconscionable or if it conflicts with terms to which the parties have expressly agreed.[75] If there is a legal requirement of assent to a particular term, there must be an opportunity to review the term and the manifestation of assent must relate specifically to the term.[76]

Further, the potential licensee has a right to back out of the transaction without loss (other than inconvenience) if he or she does not like the terms of the licence once they are known. If a party does not have an opportunity to review a mass market licence before having to pay for it, they have a right to a refund on returning all copies of the information or destroying them pursuant to instructions.[77] They also have a right to reimbursement for reasonable expenses associated with returning or destroying the information.[78] If the information had to be installed on a computer to review the licence and the installation damages the computer or information on the computer, the purchaser is entitled to compensation for any foreseeable loss caused by the installation, including any reasonable expenses incurred in restoring the computer to its previous condition.[79]

---

[74] "Article 2B" above n 62, s 208.

[75] "Article 2B" above n 62, s 208(a).

[76] "Article 2B" above n 62, s 111.

[77] "Article 2B" above n 62, s 208(b)(1).

[78] "Article 2B" above n 62, s 208(b)(2).

[79] "Article 2B" above n 62, s 208(b)(3).

7 *Contracts involving publishers, distributors and end users*

One topic that had concerned commentators on shrink-wrap licences was the issue of privity of contract in situations where there was a producer, a distributor and an end user. If the contract for the sale of the software was between the suppler and the end user, how could the producer be a party? Article 2B deals with the three party relationship typical to shrink-wrap licensing by providing for three separate but linked relationships.[80]

The contract between the end user and the distributor is conditional on the end user's agreement to the publisher's licence.[81] If the end user does not agree to the terms of the publisher's licence, the end user has a right to a refund on return of the information to the distributor.[82] The distributor is not bound by the terms of, and does not receive the benefits of, an agreement between the publisher and the end user unless the distributor and end user adopt those terms as part of their agreement.[83] If an agreement provides for distribution of copies on a physical medium provided by the publisher, a distributor shall distribute the copies and documentation received from the publisher in the form as received and subject to any contractual term that the publisher provides for end users.[84] A distributor that enters into a licence or software contract with an end user is a licensor of the end user for all purposes under the Article, including warranties, other performance obligations and remedies.[85]

---

80 "Article 2B" above n 62, s 617.

81 "Article 2B" above n 62, s 617(b)(1). This follows the reasoning in *Beta v Adobe*.

82 "Article 2B" above n 62, s 617(b)(2).

83 "Article 2B" above n 62, s 617(b)(3).

84 "Article 2B" above n 62, s 617(c).

85 "Article 2B" above n 62, s 617(d).

D Are All Terms Validated?

Thus, Article 2B provides a scheme whereby software producers can ensure that their shrink-wrap licences will be valid as long as a certain procedure is followed. However, it is possible that certain terms in an otherwise valid shrink-wrap licence will not be enforceable. As was noted above, a term does not become part of the contract if it is unconscionable or if it conflicts with terms to which the parties have expressly agreed. There are also more specific limitations. A term that provides for an exclusive judicial forum will not be enforced if the choice is unreasonable and unjust.[86] Article 2B also provides a number of consumer protections that would extend to the majority of shrink-wrap licence transactions.

However, the larger question of whether, or to what extent, terms that extend the rights of licensors in information are permissible, is left in the air. The drafters of 2B claim that the article is neutral when it comes to policy questions regarding the relationship between contract law and intellectual property law.[87] They consider that article 2B merely provides a generic contract law framework to bring to modern form the existing network of United States common law, statute and general industry practice. It does not change the law with regard to copyright.

However, this argument ignores the fact that the interaction of copyright with intangible forms of intellectual property has the potential to change the law of copyright in a de facto manner. The drafters distinguish between a contract, which defines rights between parties to the agreement, and a property right, which creates rights against all the world. This distinction was discussed in part IV above, and shown to be invalid with regard to intangible intellectual property.

---

[86] "Article 2B" above n 62, s 108.

[87] "Article 2B" above n 62, Introduction.

Article 2B further strengthens the licensor's hand by permitting the licensor to enforce contractual restrictions with electronic self help. A licensor may use an electronic restraint[88] if the licence agreement includes a term authorising its use, or the restraint merely restricts uses that have not been contracted for, or the restraint prevents use when the contract terminates.[89] The licensor is also entitled to prevent continued use of the licensed information upon cancellation of the contract for breach.[90] It is not clear if this extends to electronic self help.

Article 2B has been heavily criticised for its validation of mass market licences.[91] Critics suggest that anti-competitive and anti-social effects are likely to ensue when the heightened technological power of intellectual property licensors to control access to information and to impose restrictions on end-users of software is combined with the validation of non-negotiated mass market licences.[92] Indeed, the history of software protection indicates that when companies with market power use shrink-wrap or other mass market licences, they are strongly tempted to impose anti-competitive conditions.[93]

As a result of these criticisms, the National Conference of Commissioners on Uniform State Laws (NCCUSL) has proposed a motion which would allow a court to refuse to enforce licence terms which were contrary to public policies relating to innovation, competition and free expression.[94] The motion would insert a new section 110:

---

[88] A "restraint" means as a program, code, device, or similar electronic or physical limitation that restricts use of information.

[89] "Article 2B" above n 62, s 310.

[90] "Article 2B" above n 62, s 715.

[91] See, for example, J.H. Reichman and Jonathan A. Franklin "Privately Legislated Intellectual Property Rights: The Limits of Article 2B of the UCC" Final Draft, last revised 10/4/98, Presented at: Intellectual Property & Contract Law in the Information Age: The Impact of Article 2B of the UCC on the Future of Transactions in Information & Electronic Commerce, April 23-25, 1998, Berkeley, CA, which can be found at <http://www.vanderbilt.edu/Law/faculty/reichman.html> (last modified 24 August 1998) ["Privately Legislated Intellectual Property Rights"].

[92] "Privately Legislated Intellectual Property Rights" above n 91,

[93] "Privately Legislated Intellectual Property Rights" above n 91, 28.

[94] The NCCUSL and the American Law Institute must both approve the final draft of the Article.

Section 2B-110 IMPERMISSIBLE CONTRACT OR TERM.

(a) If a court as a matter of law finds the contract or any term of the contract to have been unconscionable or contrary to public policies relating to innovation, competition, and free expression at the time it was made, the court may refuse to enforce the contract, or it may enforce the contract without the impermissible term, or it may so limit the application of any impermissible term as to avoid any unconscionable or otherwise impermissible result.

(b) When it is claimed or appears to the court that the contract or any term thereof may be unconscionable or impermissible under this section the parties shall be afforded a reasonable opportunity to present evidence as to the contract's or term's commercial setting, purpose and effect and the extent to which the contract or term resulted from the actual informed affirmative negotiations of the parties to aid the court in making the determination.

If this proposal is accepted, it will enable Article 2B to capture the benefits of standardised licensing but avoid placing too much power in the hands of the software producers. Copyright owners will be able to tailor their product to particular markets, but will have to justify any extension of their rights in information beyond those granted by intellectual property law. The courts will be able to balance the public benefits of mass market licensing against the public interest in education, science, research, technological development and the preservation of competition.

E Does 2B Treat Software as a Good?

As well as validating mass market licences, Article 2B provides default rules for the contract from formation through to cancellation. The particular rule that is applied to a particular type of transaction depends, in a large part, on whether the transaction looks more like a service, a good, or a pure licence.[95] The rules that Article 2B would apply to mass market transactions are, to a large extent, based on rules for the sale of goods. This is appropriate, given the similarity between the transactions. However, Article 2B also allows for variation where necessary; for example, the rules for transfer of title depend on whether a physical or electronic copy is delivered.

1 *Duration of contract*

The general default rule on duration of contract is that the contract is subject to termination at will on reasonable notice.[96] However, duration is perpetual in a software contract that transfers ownership of a copy or delivery of a copy for a fee which is fixed at or before delivery of the copy.[97] Thus, shrink-wrap licences are perpetual, unless they explicitly state otherwise. This makes them look very much like a sale, with the licence a device to control use of the information.

2 *Warranties*

Warranty rules also depend very much on whether a transaction looks like a sale of goods or a service contract or a pure licensing of information. Mass market computer programs resemble functional products and so an implied warranty which focuses on result and merchantabilty is appropriate. Section 403 provides for an implied warrantee that a delivered computer program and any physical medium on which it is delivered are merchantable[98] if the licensor is a merchant

---

[95] However, the drafters of 2B reject an approach strictly based on whether the court characterises a transaction as involving a good or not. The drafters consider that distinction to be unreliable in relation to information transactions.

[96] "Article 2B" above n 62, s 308(1).

[97] "Article 2B" above n 62, s 308(2).

[98] To be merchantable, a computer program and any physical medium on which it is delivered must: (1) pass without objection in the trade under the contract description; (2) be fit for the ordinary purposes for which it is distributed; (3) in the case of multiple copies, consist of copies that are, within the variations permitted by the agreement, of even kind, quality, and quantity, within each unit and among all units involved; (4) be adequately contained,

with respect to computer programs of that kind. Implied warrantees may be disclaimed or modified in the contract; however, in a mass market transaction, language that disclaims or modifies an implied warranty must be conspicuous.[99]

Modifying a copy of a computer program, other than by using a capability of the program intended for that purpose in the ordinary course, invalidates any warrantees regarding the performance of the modified copy.[100] A modification occurs if a licensee alters code in, deletes code from, or adds code to, the computer program. Because of the complexity of software systems, changes may cause unanticipated results. It would not be fair to burden the licensor with liability for these results.

Mass market software may also contain informational content. The supply of informational content to the public is not subject to any warranty of accuracy.[101] Such a warranty would chill the free flow of information. This parallels the treatment of informational content in tangible information goods such as newspapers, books etc. However, where there is a special relationship of reliance (not the case with mass market software), an implied warrantee of reasonable care in compiling the information is created.[102]

3 *Transfer of rights and interests*

Title to a copy depends on the contract. In the absence of a contractual specification, title to a copy on disk passes with physical delivery, while title to an electronically delivered copy passes at the time and place at which the licensor completed its obligations with respect to delivery of the copy.[103]

packaged, and labelled as the agreement may require; and (5) conform to the promises or affirmations of fact made on the container or label, if any.

[99] "Article 2B" above n 62, s 406(b)(6).

[100] "Article 2B" above n 62, s 407.

[101] "Article 2B" above n 62, s 404(b)(2).

[102] "Article 2B" above n 62, s 404(a).

[103] "Article 2B" above n 62, s 501.

Information transactions often raises issues of confidentiality. Section 502 specifies that transfers of contractual interests are subject to protecting any confidential information that may be involved in the transaction. Likewise, to protect the licensor's interest in the information, financiers interests may not be enforced without the licensors permission.[104] These obligations survive the contract. However, confidentiality issues are not likely to arise in relation to mass market software.

4 Performance

Tender of performance entitles a party to acceptance of performance. Many licences for information create a continuing relationship with on-going commitments. This makes the perfect performance rule associated with the sale of goods unsuitable. Thus, the general rule is that a party may refuse performance only for a material breach. The delivery of a non conforming copy only requires the party in breach to promptly and in good faith make an effort to cure.[105] However, delivery of a non-conforming copy in a mass market transaction entitles the licensee to cancel.[106] Rules for tender of delivery of a copy are based on whether a physical medium is involved or whether delivery is electronic.[107] Risk of loss of copies also varies according to how a copy is delivered.[108] A concept of transfer of possession or control is used as the general standard for when risk of loss passes.

---

[104] "Article 2B" above n 62, s 503.

[105] "Article 2B" above n 62, s 606.

[106] "Article 2B" above n 62, s 609(b).

[107] "Article 2B" above n 62, s 607.

[108] "Article 2B" above n 62, s 623.

VII SHRINK-WRAP LICENCES IN NEW ZEALAND

A Shrink-Wrap Licences Probably Not Enforceable

Contract law in New Zealand is not codified as it has been in the United States. Contracts are subject to a number of general statutes that apply regardless of subject matter or type of transaction. These include the Consumer Guarantees Act 1993, Contracts (Privity) Act 1982, Contractual Mistakes Act 1977, Contractual Remedies Act 1979, Fair Trading Act 1986 and Illegal Contracts Act 1970. In addition, contracts for the sale of goods are subject to the Sale of Goods Act 1908. Contracts are also governed by a wealth of case law.

There are no New Zealand cases on the validity of shrink-wrap licences. However, it is likely that they would be held to be invalid. While shrink-wrap licences vary, generally the purchaser only has an opportunity to read the terms of the licence after purchasing the software. A New Zealand court is likely to apply black letter contract law and say that the terms come to late too be part of the contract.[109] In retail transactions, which constitute the majority of shrink-wrap sales, there is the additional problem of privity of contract.

B Would a New Zealand Court Treat Shrink-Wrap Software as a Sale of Goods?

I consider that it is likely that a New Zealand court would treat a mass market software transaction as a sale of goods with an implied licence from the copyright owner to copy the software to the extent necessary to use the product. However, the only New Zealand case to consider whether software is a good has taken a different view. In *Case T28*,[110] Judge Barber had to consider whether the sale of a business package, which included computer programs and software, was the sale of a good or goods, for the purposes of the Goods and Services Tax

[109] An analogy may be drawn with cases such as *Thornton v Shoe Lane Parking Ltd* [1971] 2 QB 163 and *Olley v Marlborough Court Ltd* [1949] 1 KB 532.

[110] *Case T28* (1997) 18 NZTC 8,197 (DC).

Act 1985. The Act states that: "Goods means all kinds of personal or real property; but does not include choses in action or money".[111]

The computer programs in *Case T28* were originally written by one of the vendors for use in his pharmacy business. They had been adapted by the vendor for the diagnosis of soil, using the vendor's extensive knowledge of soil properties. In his analysis, Judge Barber distinguished between the software medium (the hard drive), the computer programs and the information on soil properties.[112] He noted that it was not disputed that any physical item on which information is stored is a good. However, the consideration in the case was not for the physical medium, but for the knowledge and information stored on the physical medium.

The sale of the computer programs and information on soil properties did not involve the transfer of any physical item. The computer programs were transferred as electrical impulses down a cable from the hard disk of one computer to another. The information on soil properties existed only in the vendors' heads at the time of sale. As the vendors were selling to a company which they owned, no transfer of the information was required. (The information appears to have been added to the computer programs at some later date).

The Judge held that the computer programs and software were not goods because they were intellectual property in the form of "know-how".[113] The Judge did not define "know-how" but seemed to be referring to trade secrets. "Know-how" was a form of information and there is no property in information.[114] The information on soil properties was also not a good for this reason.

[111] Goods and Services Tax Act 1985, s 12(2).

[112] *Case T28* (1997) above n 110, 8,203. Judge Barber's distinction between the computer programs and the data parallel the Article 2B definitions of information and informational content.

[113] *Case T28* (1997) above n 110, 8,207.

[114] *Case T28* (1997) above n 110, 8,207.

The agreement between the vendors and the company had transferred the copyright in the programs to the company. Judge Barber held that copyright is a chose in action and not a good.[115] He came to this conclusion on the basis of the description of "choses in action" in several authoritative texts.[116] However, he did not outline his reasoning. The Judge considered what the situation would be if the vendors did not claim copyright in the software or the data stored on the software medium. In this case, payment would be for the vendors' services in compiling the information. Thus, Judge Barber seems to consider that software consists of pure information in the form of know-how and (possibly) copyright.

The Judge's conception of the computer programs and informational content as separate objects of sale seems to me incorrect in general, but understandable in these unusual circumstances, where they were, in fact, separate at the time of the sale. However, clearly his analysis would not apply to mass market software. A buyer who purchases an encyclopaedia on CD-ROM does not enter into two transactions. He or she is buying a single product. It would be impractical to treat the computer program and the informational content as separate objects of sale as they are inextricably bound together. A customer dissatisfied with the informational content could not return the information and keep the software.

The Judge's finding that the computer program was a chose in action and not a good was based on his characterisation of the program as information in the form of "know-how" or a trade secret. However, a computer program is *functioning* know-how. This matters. When users buy a software product, they are not interested in the information, which they probably cannot comprehend; they expect to buy a product that *does* a particular thing. The sale of a written copy of the source code of the program would not be the same as the sale of a

[115] *Case T28* (1997) above n 110, 8,207.

[116] *Halsbury's Laws of England,* Volume 6, para 1; *The Laws of New Zealand*, in the Chapter "Choses in Action" Butterworths 1993; *Personal Property* by J Crossley Vaines, 4th Edition, Butterworths, 1967 pp 11-13; Garrow and Gray *Law Of Property in New Zealand* 5th Edition, Butterworths 1968 242 (as cited by the Judge).

copy of the program. Yet, under Judge Barber's analysis, it is. *Case T28* suggests that New Zealand courts are likely to find that shrink-wrap software transactions are indeed merely licences to use information. However, because of the level of the court and weaknesses in the Judge's reasoning, the case is not a strong authority.

The English courts have also addressed the issue of whether licensed software is a good. In *St Albans City and District Council v International Computers Ltd*,[117] the defendant supplied the plaintiff with customised software licensed for the plaintiff's use. The software was defective and caused the plaintiff loss. The contract contained a clause limiting the defendant's liability in the event of such loss. However, the clause was not permissible under the Sale of Goods Act 1979. The defendant argued that the contract fell outside the provisions of the Act as the software did not constitute goods.

Scott Baker J, at first instance, found that software was goods within the Sale of Goods Act as, otherwise, it would be difficult to see what it could be. The definition of "good" in the Sale of Goods Act is practically identical to that in the New Zealand Act; "all personal chattels other than things in action and money".[118]

On appeal, it was not considered necessary to decide if software was goods in order to decide the case. However, Glidewell J considered the question obiter. He drew an analogy between an instruction manual and software on a physical medium such as a disk. He concluded that, as the instructions in a manual could not be separated into the intangible information and the tangible ink and paper, neither should the tangible disk and the software in it be so separated; together, they constituted goods. However, while the disk and program together were within the definition of goods in the Sale of Goods Act 1979, a computer program, of itself, was not. Thus the program in question, which had been

[117] *St Albans City and District Council v International Computers Ltd* [1996] 4 All ER 481 (CA).

[118] Sale of Goods Act 1979 (UK), s 62.

placed directly onto the plaintiff's computer by an employee of the defendant, was not a "good". Therefore, there was no statutory implication of terms as to quality or fitness for purpose.[119]

The Supreme Court of New South Wales has also held that software embodied in a tangible medium is a good.[120] The sale of a computer system comprising both hardware and software was found to constitute a sale of goods within the New South Wales Sale of Goods Act 1923 under a definition practically identical to that in the New Zealand Act.[121]

The courts in the United States have also, in the main, rejected the argument that the physical medium may be severed from the intangible program with only the medium treated as a good.[122] Since 1983, American courts have tended to treat software as a good for sales, use and property tax purposes.[123] Draft Article 2B has also, in the main, devised rules for mass market software based on rules for the sale of goods. Although the drafters do not consider that licensing mass market software is the same thing as the sale of a good, they recognise that there are many similarities, particularly where the software is on a disk.

Thus, a number of influential jurisdictions have come to the conclusion that software is a good, at least where it is embodied in a tangible physical medium. The New Zealand courts are likely to follow these cases. The finding in *Case T28* may be distinguished because it did not involve software on a tangible medium. In any case, Judge Barber's reasoning is open to criticism.

---

[119] This finding was of no benefit to the defendant, however, as the judge proceeded to apply similar implied terms under the common law.

[120] *Toby Constructions Products Pty Ltd v Computer/Sales Pty Ltd* [1983] 2 NSWLR 48.

[121] Sale of Goods Act 1923 (NSW), s 5(1) states that "goods" includes (unless the context or subject matter otherwise require) all chattels personal other than things in actions and money.

[122] These cases are discussed in: Peter Dengate-Thrush "Can Bad Software be Goods?" (1997) NZIPJ 206 ["Can Bad Software be Goods?"].

[123] *Comptroller of the Treasury v Equitable Trust Company* (1983) 464 A 2d 248 (Md CA) cited in "Can Bad Software be Goods?" above n 122, 207.

I consider that mass market software transactions are also likely to be treated as sales. The licence is usually of perpetual duration, a single payment is made, and there is no further contact between the parties. Thus, the transaction looks, in most respects, very much like the sale of a good. Mass market transactions where the software is embodied in a disk would therefore be subject to the Sale of Goods Act 1908 and the Consumers Guarantees Act 1993. The Consumers Guarantees Act in particular will provide strong protects for purchasers, the majority of whom will be consumers.

However, mass market software delivered directly over a wire without delivery of a physical medium would probably not be treated as the sale of a good. Scott-Baker J, at first instance in *St Albans*, seems to be the only judge for whom the lack of a physical medium for the information appears not to be an insurmountable obstacle. However, as Lord Penrose pointed out in *Beta v Adobe*, legal analysis of contracts should focus on matters of importance to parties, that is the software and the ability to use it, rather than matters of no significance to them, such as method of delivery. There is no significant reason for treating a transaction in which mass market software is delivered over a wire any differently from a transaction in which it is delivered in a physical medium. The only exception would be that different default rules concerning delivery may be appropriate.

Transactions for mass market software that do not involve a physical medium are likely to be conducted electronically; that is, the offer, acceptance and delivery will take place over the Internet. Such electronic transactions raise many issues that are not dealt with by current contract law. However, this is an issue of general concern and is not limited to the purchase of mass market software. The development of rules for electronic commerce is currently being investigated by national and international bodies.[124]

---

[124] A report by the Law Commission on electronic commerce is due to be published in early October, 1998.

VIII WHAT SHOULD NEW ZEALAND DO?

Shrink-wrap licences are beneficial in that they allow software producers to create rivalry with regard to their products. As *Pro-CD* demonstrated, enforceable restrictions on the uses a software user may make of a product allows price discrimination which is beneficial to producer and consumer alike. Further, standardisation of agreements is common with respect to standardised goods, offering the benefits of reduced transaction costs and increased efficiency. I suggest that New Zealand should adopt some means of legitimising shrink-wrap licences. An examination of the limited case law on software contracts may indicate whether this should be in the context of a general codification of transactions in intangible information, similar to article 2B of the UCC.

A Should NZ Follow Article 2B of the UCC?

Andas Finance Ltd v Te Kaha Hotel Ltd[125] concerned a contract for the supply of a computer, software and training. The computer was delivered but most of the software and the training were never supplied. After unsuccessfully attempting to get the supplier to perform, the defendant concluded that the contract was not going to be fulfilled and stopped making payments. Applying the Contractual Remedies Act 1979, the Judge decided that the contract had been rightfully cancelled due to misrepresentations as to the ability of the of the supplier to provide the software and training.

Under the UCC, the contract would have been dealt with under Article 2 (which deals with the sale of goods) as regards the computer and draft Article 2B as regards the software and support training. Cancellation would be allowed if there had been a material breach of the entire contract which had not be cured or

[125] *Andas Finance Ltd v Te Kaha Hotel Ltd* (4 July 1989) unreported, High Court, Rotorua, CP 194/87, Smellie J.

waived. Clearly, failure to supply both the majority of the software or the training was a material breach of the entire contract and it had not been either cured or waived. Thus, under the UCC, the defendant would have been entitled to cancel. At that point, all executory obligations would have been discharged (as under the Contractual Remedies Act). However, the cancellation would also have ended any right the defendant had under the contract to use the information or copies supplied (i.e. the software that had been delivered).[126] Under the Contractual Remedies Act the defendant would not, merely by reason of the cancellation, have been divested of any property transferred pursuant to the contract.[127]

Progeni Systems Ltd v Hampton Studios Ltd[128] also concerned the cancellation of a contract on the grounds of misrepresentation. The defendant had engaged the plaintiff as a consultant to advise it on the availability of "off-the-shelf" software that would suit its business needs. On being advised that no suitable packages were available, the defendant hired the plaintiff to create customised software for it. Later, the defendant discovered that a suitable software package had been available and purported to cancel the contract for the customised software on the grounds of misrepresentation.

The Judge found that the defendant had rightfully cancelled under section 7 of the Contractual Remedies Act as the parties had impliedly agreed that the representation was essential to the defendant. The defendant asked for damages under section 9 of the Contractual Remedies Act, which gives the court very broad powers to grant relief to either party. This is so broad it can easily encompass the special requirement of intangible goods. The section does not preclude further action for damages for misrepresentation, repudiation or breach. However, any relief given under section 9 must be taken into account in granting such damages.

---

126 "Article 2B" above n 62, s 702.

127 Contractual Remedies Act 1979, s8(3).

128 *Progeni Systems Ltd v Hampton Studios Ltd* (11 August 1987) unreported, High Court, Christchurch, CP 105/86, Tipping J.

Under Article 2B, the licensee is entitled to direct, incidental and consequential damages.[129] The section sets out in some detail several methods of calculating the damages. The licensee is given a choice between various methods, subject to a ban on double recovery. The main difference is that there is no general discretion, such as section 9 provides, whereby the judge can grant any relief he or she thinks appropriate applying general principles applicable to any contract.

In *Works Civil Construction Ltd v Does Not Compute Ltd*,[130] a term in a contract to supply hardware, software and system support services forbade assignment of the contract without consent. The court held that the plaintiff was entitled to decline consent to the assignment of the agreement and that the law did not imply a condition that the consent should not be unreasonably withheld. A similar result would have been reached under draft article 2B which places great emphasis on freedom of contract.

These judgments suggest that the general nature of New Zealand contract law enables it to respond in a flexible manner to the issues posed by intangible information products. Lacking a detailed codified commercial law like the UCC, we have no need to "update" in the same sense. Broadly worded statutes of general applicability seem able to cope with new technological developments through the extension of case law.

B A Specific Statute Validating Shrink-Wrap Licences?

Although our contract law is flexible and seems well able to deal with issues that arise where a valid contract is present, the problem with mass market shrink-wrap licence transactions is their lack of validity under black letter contract law. Thus, a specific statute is necessary to legitimate shrink-wrap licences. Drawing

129 "Article 2B" above n 62, s 709.

130 *Works Civil Construction Ltd v Does Not Compute Ltd* (22 July 1992) unreported, High Court, Wellington, CP 46/92, Master Williams.

upon the case law and Article 2B, such a statute could provide a regime which the licensor could follow to ensure a valid licence.

A purchaser should be able to assent to a shrink-wrap licence by conduct, as long as he or she was aware of the terms of the licence or had an opportunity to review them. A manifestation of assent would consist of conduct which the purchaser knew or reasonably ought to have known, would indicate assent to the other party. Where the purchaser does not have an opportunity to review the licence before paying, there must be a right to a refund if the purchaser does not wish to accept the terms of the licence once they became known. The purchaser must also be entitled to payment of reasonable expenses incurred in returning the product and compensation for any damage caused to the users computer if it were necessary to view the licence on-line.

Article 2B also offers a guide for determining the relationship between the several parties in retail transactions. The statute should determine that the user has a right of refund directly off the retailer and the retailer should be bound to distribute the material as packaged by the licensor.

The statute should state that mass market software supplied on a physical medium was a good for the purposes of the Sale of Goods Act 1908 and the Consumers Guarantee Act 1993. Where software is delivered without a physical medium, it should be deemed a good for the purposes of these Acts, except with regard to delivery. Specific rules would be necessary to regulate delivery. Again, Article 2B may provide guidance. This should provide adequate consumer protection to shrink-wrap licensees.

However, it is also important to ensure that software producers do not use shrink-wrap licences to illegitimately extend their rights in information. New Zealand is a net importer of intellectual property. As such, it should look hard at allowing stronger intellectual property rights than are required, either under international agreements or to satisfy its major trading partners. The benefit of such rights would largely flow out of New Zealand. New Zealand's small software industry may be disadvantaged by such laws, if they result in a less competitive environment. This seems likely, as a ban on any form of reverse engineering is very common in shrink-wrap licences.

C Guarding Against De Facto Intellectual Property Rights

In the United States, the response to the prospect of valid shrink-wrap licences under Article 2B has been a proposal that judges be empowered to refuse to enforce contracts or terms which are contrary to public policies relating to innovation, competition, and free expression.[131] It is tempting to borrow from the United States again, but unfortunately, due to differences in our intellectual property law, such a solution may not be effective in New Zealand.

Intellectual property law in the United States is based on a constitutional requirement to "promote the Progress of Science and the useful Arts".[132] The Copyright Act is interpreted in light of this underlying purpose. The Act grants free-wheeling fair use rights for purposes *such as* criticism, comment, news reporting, teaching, scholarship or research. The non-specific nature of the fair use provision requires judges to consider the policy behind protecting these particular uses. The constitutional guarantee of free speech[133] influences the interpretation of copyright law, particularly with regard to fair use. Because of these factors, the United States has developed broad public policies with regard to innovation, competition and free expression in the context of intellectual property rights.

In contrast, New Zealand intellectual property law is not overtly based on the promotion of knowledge and science. What policy we have with regard to innovation, competition and free expression, vis a vis copyright, is completely

[131] Proposed article 2B-110, discussed above in part *IV D*.

[132] US Const art I, s 8, cl 8.

[133] US Const 1st amendment.

embodied in the Copyright Act 1994. These policies are expressed in the idea/expression dichotomy[134] and the exceptions to copyright infringement such as fair dealing,[135] copying for educational purposes,[136] and replacement copying by libraries and archivists.[137] However, these are not affirmative rights but are merely not copyright infringements. Nor are the fair use exceptions free wheeling as in the United States; they are limited to specific exceptions.

Thus, if we permit shrink-wrap licensing, subject to public policies with regard to innovation, competition, and free expression, we would run the risk of legitimating the creation of de facto rights by contract. If the Copyright Act does not grant positive rights to users, there is no public policy reason why software producers should not be able to restrict such uses by contract.

A solution may be to import public policy factors, with regard to innovation, competition and free speech, into the Copyright Act. This could be achieved by inserting a suitable purpose clause into the Act. Such a purpose clause could draw upon the preamble of the WIPO Copyright Treaty 1996, which New Zealand intends to sign.[138] The preamble emphasises the significance of copyright protection as an incentive for literary and artistic creation and recognises the need to maintain a balance between the rights of authors and the larger public interest, particularly education, research and access to information.

However, such a provision would create a significant change in New Zealand copyright policy. It may be argued that such a change is not justified merely to solve the problems associated with shrink-wrap licensing. I would suggest that it is time to re-examine the basis of New Zealand copyright law. The

---

[134] In *Television New Zealand Ltd v Newsmonitor Services Ltd* [1994] 2 NZLR 91, Blanchard J found that s 14 of the New Zealand Bill of Rights Act, which affirms the right to freedom of expression, did not require any change in the interpretation of the Copyright Act. Effectively, the Copyright Act contained within itself the definitive policy on freedom of expression in the form of the ideas/expression dichotomy.

[135] Copyright Act 1994, ss 42 and 43.

[136] Copyright Act 1994, ss 44, 46 and 49.

[137] Copyright Act 1994, s 55.

[138] Information supplied by the Ministry of Commerce, telephone conversation, 23 September 1998.

development of the digital information industry prompts such re-examination as it exposes the problems with an intellectual property law that is not overtly based on the encouragement of innovation and knowledge. Such a law lacks the guidance necessary for case law to respond flexibly to new developments in technology.

Nor can the problem of de facto intellectual property rights in digital information be avoided by not validating shrink-wrap licences. There is growing use of Internet delivery of mass market software using click-wrap licences.[139] These licences present the terms to the purchaser before the contract is formed. As they usually do not involve a supplier, there are no problems with privity of contract. Thus, there is no reason why the contracts may not be valid under black letter contract law.

However, importing an intention to encourage innovation and knowledge into the Copyright Act may well be considered too radical. A more restrained means of protecting the public interest in information would be the creation of inalienable rights for software users. These could be limited rights, which apply to all software users, or more expansive rights, granted to shrink-wrap licensees only.

The European Union has provided certain basic user rights for software licensees which cannot be contracted out of.[140] These rights include the right to decompile to achieve interoperability with independently created programs and the right to use a device or means which observes, studies or tests the functioning or the program in order to understand the underlying ideas or principles.

This approach has the advantage of certainty. However, it is not very flexible. It is difficult to say that a particular use should always be permitted and so

[139] Mark A Lemley "Shrinkwraps in Cyberspace" (1995) Jurimetrics Journal 311, 320.

[140] The European Council Directive on the Legal Protection of Computer Programs (Directive 91/250).

inalienable rights will always be very limited, even when restricted to shrink-wrap licensees.

Inalienable rights are a blunt tool. It is preferable, in my view, to empower judges to weigh the public interest in allowing particular contractual restrictions against the public interest in maintaining the boundaries of the public information domain.

IX CONCLUSION

Shrink-wrap licences are part of the modern, mass production economy and, like all standard form licences, offer benefits of cost reduction and efficiency. In addition, shrink-wrap licences allow software producers the ability to tailor software products so that the price paid is commensurate with the use made. Without the ability to do this, software producers would have to charge a single price to cover all uses, which would be to the detriment of consumers and the software industry alike.

Shrink-wrap licences are probably unenforceable under black letter contract law. Therefore, it would be necessary to give them contractual validity by statute. Such a statute could draw upon the provisions of the UCC draft Article 2B, which establishes a regime for mass market software transactions which are accompanied by mass market licences.

However, while shrink-wrap licences are beneficial, they are also problematic. Because of the intangible nature of software, they may enable the software producer to extend his or her rights in the information in a manner that is not possible with tangible information products. Any validation of shrink-wrap licensing must guard against allowing the licence to be used in this way. One means of preventing such use would be to allow the court to refuse to enforce terms which were contrary to public policies relating to innovation, competition, and free expression. The software producer would be able defend such a term by showing that it was commercially necessary.

Such an approach would require changes to the Copyright Act 1994. Currently, the Act is not based upon any conception of copyright as a right granted to promote science and the arts, as is the United States Copyright Act. Hence, we have not developed public policy doctrines with regard to innovation, competition and free expression in relation to copyright law. However, it would be possible to provide guidance to the interpretation of copyright law in a manner that took account of these factors by providing a suitable purpose provision for the Act.

Enacting such a provision would represent a major change in New Zealand's intellectual property law. A less radical solution to the problem of de facto intellectual property rights would be the creation of inalienable user rights for software buyers, as has occurred in the European Union. Limited rights could be granted to all software licensees. Or, more expansive rights could be granted to shrink-wrap licensees only.

BIBLIOGRAPHY

TEXTS

David Bainbridge *Software Copyright Law* (2 ed, Butterworths, London, 1994)

James Boyle *Shamans, Software & Spleens: Law and the Construction of the Information Society* (Harvard University Press, Massachusetts, 1996)

Dennis Campbell and Susan Cotter (eds) *International Information Technology Law* (John Wiley, Chichester, 1997)

Computer Law (Loose Leaf ed, Matthew Bender, New York, 1979)

ARTICLES

"Are Shrink-wrap Licences Legally Effective?" (1997) 10 Australian Intellectual Property Law Bulletin 91

Amelia H Boss and Jane Kaufman Winn "The Emerging Law of Electronic Commerce" (1997) 52 The Business Lawyer 1469

Connie Carnabuci & Caroline Ives "Maximising Legal Protection of Packaged Software" (June 1993) 23 Computers & Law 20

Michael Chissick "Software Contracts After St Albans" (1996) 1 Communications Law 190

Alan M Christenfeld & Shephard W Melzer "Security Interests in Software: Proposed Article 2B" The New York Law Journal 7 August 1997 http://www.ljx.com/internet/0807ucc2b.html (accessed 10 July 1998)

Clive Davies "An Introduction to Computer Contracts" (1992) 8 Computer Law and Practice 54

Stephen Davidson "Scope of Use Provisions in Software Licence Agreements" (1995) 11 Computer Law and Security Report 74

J Bradford De Long & A Michael Froomkin "The Next Economy?" draft April 6, 1997 Version B17
http://www.law.miami.edu/^froomkin/articles/newecon.htm (accessed 2 May 1998)

Peter Dengate-Thrush "Can Bad Software Be Goods?" (1997) 1 New Zealand Intellectual Property Journal 206

Mary Jo Howard Dively and Donald A Cohn "Treatment Of Consumers Under Proposed UCC Article 2B Licenses" (1997) 15 Journal of Computer and Information Law 315

"The Draft Copyright (Computer Programs) Regulations 1992 - UK Implementation of EC Software Directive" (1992) 8 Computer Law and Practice 124

Linda Fazzani and Adam Rose "Shrink-Wrapped Software: Do the Licence Terms Apply?" (1996) 4 Computer and Telecommunications Law Review 164

A Michael Froomkin "Comment: 2B as Legal Software for Electronic Contracting: Operating System of Trojan Horse?" preliminary draft. Version 0.9f
http://www.law.miami.edu/^froomkin/articles/2b.htm (accessed 2 May 1998)

Paul Gardner "Shrink-Wrap Licences: *Beta v Adobe*" (April/May 1996) Computers and Law 5

Robert W Gomulkiewicz "The Implied Warranty of Merchantability in Software Contracts: A Warranty No One Dares to Give and How to Change That" (1997) 15 Journal of Computer and Information Law 393

George L Gretton "Software: Binding the End User" (1996) Journal of Business Law 524

Sunny Handa "Reverse Engineering Computer Programs Under Canadian Copyright Law (1995) 40 McGill Law Journal 621

David L Hayes "The Enforceability of Shrinkwrap License Agreement On-Line and Off-line"
http://www.fenwick.com/pub/shrnkwrp.html (accessed 25 July 1998)

David L Hayes "Shrinkwrap Licence Agreements: New Light on a Vexing Problem"
http://www.fenwick.com/pub/shrink.html (accessed 25 July 1998)

Gail Hillebrand "The Uniform Commercial Code Drafting Process - Will Articles 2, 2B, and 9 Be Fair to Consumers?" (1997) 75 Washington University Law Quarterly 69

Meredith D Jackson "Article 2B Financing Provisions" (1997) 10 (2) Technology and Intellectual Property Law Bulletin (Special Article 2B Issue) http://wsgrgate.wsgr.com/Whats-new/Newsletters/tl_news.htm (accessed 25 May 1998)

Page M Kaufman "The Enforceability of State 'Shrink-Wrap' License Statutes in Light of *Vault Corp v Quaid Software Ltd*" (1988) 74 Cornell Law Review 222

Gary Lea "The Impossible Intangible: Shrinkwrap Software Revisited" (1996) 1 Communications Law 238

Mark A Lemley "Intellectual Property and Shrinkwrap Licenses" (1995) 68 Southern California Law Review 1239

Mark A Lemley "Shrinkwraps in Cyberspace" (1995) Jurimetrics Journal 311

Raymond T Nimmer "Article 2B Preface: Meeting the Information Age" http://www.lawlib.uh.edu/ucc2b/pref1201.html (accessed 29 June 1998)

Ng-Loy Wee Loon "Copyright Protection for Computer Programs in Singapore: *Creative Technology Ltd v Aztech Systems Pte Ltd*" (1997) 4 Computer and Telecommunictions Law Review 182

Clifford Miller "Shrink-Wraps are Enforceable - An Opinion" (1992) 8 Computer Law and Practice 52

Jeremy Morton "When the Software Hits the Fan: *St Albans City and District Council v International Computers Ltd*" (1996) 6 Computer and Telecommunications Law Review 242

Raymond T Nimmer "Article 2B: An Introduction" (1997) 15 Journal of Computer and Information Law 211

Raymond T Nimmer "Breaking Barriers: The Relationship Between Contract and Intellectual Property Law" http://www.softwareindustry.org/issues/guide/docs/rncontract-new.html (accessed 22 July 1998)

Raymond T Nimmer "Electronic Contracting: Legal Issues" (1996) 14 Journal of Computer and Information Law 211

Robert L Oakley "UCC Article 2B: Some Preliminary Comments on a New Issue for the Library Community" prepared for presentation at the annual meeting of the Association of Research Libraries October 16, 1997. Http://www.arl.org/info/frn/copy.uccspeech.html (accessed 30 June 1998)

Maureen A O'Rourke "Copyright Pre-emption After the Pro-CD Case: A Market Based Approach" (1997) 12 Berkeley Technology Law Journal. Http://www.law.berkeley.edu/btlj/articles/12-1/orourke.html (accessed 10 July 1998)

Maureen A O'Rourke "Fencing Cyberspace" (1998) 82 Minnesota Law Review 609

Maureen A O'Rourke "Rethinking Remedies at the Intersection of Intellectual Property Law and Contract: Toward a Unified Body of Law" (1997) 82 Iowa Law Review 1137

J H Reichman & Jonathan A Franklin "Privately Legislated Intellectual Property Rights: The Limits of Article 2B of the UCC" Presented at: Intellectual Property & Contract Law in the Information Age: The Impact of Article 2B of the UCC on the Future of Transactions in Information & Electronic Commerce, April 23-25, 1998, Berkeley, CA

David A Rice, A letter dated 28 October 1996, to the UCC Article 2B Drafting Committee, Chair, Reporter and Advisors NCCUSL and ALI officials involved with Project http://www.softwareindustry.org/issues/guide/docs/dricsali.html (accessed 27 May 1998)

Michael L Rustad "Commercial Law Infrastructure for the Age of Information" (1997) 15 Journal of Computer and Information Law 255

Pamela Samuelson "Legally Speaking: Does Information Really Want To Be Licensed?", unedited copy, scheduled to be published in September 1998 issue of *Communications of the ACM*
http://sims.berkeley.edu/^pam/papers/acm_2B.html (accessed 30 June 1998)

Pamela Samuelson "The Never-Ending Struggle for Balance" (1997) 40 Communications of the ACM 17

Stephanie Sharron and Vivian Distler "An Overview of Proposed Article 2B" (1997) 10 (2) Technology and Intellectual Property Law Bulletin (Special Article 2B Issue) no page numbering
http://wsgrgate.wsgr.com/Whats-new/Newsletters/tl_news.htm (accessed 25 May 1998)

Mark Sherwood-Edwards "Seven Degrees of Separation: the Software Directive and UK Implementation" (1993) 9 Computer Law & practice 169

Craig Sinclair "Shrinkwrap Licences: the New Zealand Position" (October 1989) Computers and Law Newsletter 24

Susan Singleton "Computer Software Agreements and the Implementation of the EC Directive" (1993) 9 Computer Law & Practice 50

Susan Singleton "Product Liability, Computer Software and Insurance Issues - the St Albans and Salvage Association Cases" (1994) 10 Computer Law and Practice 167

Graham P Smith "Shrink-Wrap Licences in Europe After the EC Software Directive" (1992) 11 Computer Law Journal 597

Joseph P Verdon "Article 2B: Transactions in Software and "Information"" The New York Law Journal 13 August 1997 http://www.ljx.com/internet/0813ucc2b.html (accessed 10 July 1998)

Joseph C Wang "*ProCD, Inc v Zeidenberg* and Article 2B: Finally, the Validation of Shrink-Wrap Licenses" (1997) 15 Journal of Computer and Information Law 439

Conor Ward and Lovell White Durrant "Shrink Wrapped Licences Revisited" (1996) 1 Communications Law 174

8

220