

1-1-2013

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## Recommended Citation

Clark D. Asay, *Kirtsaeng and the First-Sale Doctrine's Digital Problem*, 66 *Stan. L. Rev. Online* 17, 17 (2013).  
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## KIR TSAENG AND THE FIRST-SALE DOCTRINE'S DIGITAL PROBLEM

Clark D. Asay\*

### INTRODUCTION

On March 19, 2013, the Supreme Court issued its highly anticipated<sup>1</sup> decision in *Kirtsaeng v. John Wiley & Sons, Inc.*<sup>2</sup> At issue was the geographic scope of copyright law's first-sale doctrine. Historically, this doctrine has functioned as a significant limitation on the rights of copyright holders by allowing lawful owners of copyrighted works to distribute them without violating a copyright holder's exclusive distribution right.<sup>3</sup>

Significantly, the Court held six to three that the first-sale doctrine allows importing physical books, lawfully made and acquired abroad, into the United States for resale without violating a copyright owner's distribution right.<sup>4</sup> The Court previously held in *Quality King Distributors, Inc. v. L'anza Research International, Inc.* that first-sale rights allow for copyrighted works originally and lawfully made in the United States to be reimported,<sup>5</sup> and in *Kirtsaeng* the Court completed the circle. In short, the first-

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1. Commentators, for instance, analyzed the significant issues in the case prior to the decision. See, e.g., Guy A. Rub, *The Economics of Kirtsaeng v. John Wiley & Sons, Inc.: The Efficiency of a Balanced Approach to the First Sale Doctrine*, 81 *FORDHAM L. REV. RES GESTAE* 41, 44-47 (2013) (assessing the potential economic effects of the ruling, including the possible detriment to copyright owners as they lose the ability to price discriminate and the potential chilling of valuable secondary markets).

2. 133 S. Ct. 1351 (2013).

3. Without the first-sale doctrine, for instance, library lending, gifting of books and CDs, video rentals, and other secondary markets for copyrighted works would violate a copyright holder's exclusive distribution right.

4. *Kirtsaeng*, 133 S. Ct. at 1357, 1371.

5. 523 U.S. 135, 138-40, 154 (1998).

sale doctrine includes no geographic limitations, so long as the copyrighted work was lawfully made somewhere.<sup>6</sup>

Many have lauded the Court's decision as a significant pro-consumer decision,<sup>7</sup> but how significant will *Kirtsaeng* prove? After all, more and more copyrighted works have moved into digital format, and the pace of digitization is only accelerating. And in that context, copyright holders can more easily argue that first-sale rights do not apply because the recipient of the copyrighted work is merely a "licensee" of the work, not an "owner." Furthermore, some courts have recently held that first-sale rights do not apply to transfers of digital works when the transferred file is a copy of the original one, which is generally the case since the transferred file resides on a different hard drive than the original.<sup>8</sup> Consequently, while *Kirtsaeng* may be a step in the right direction, its ultimate effect in the increasingly important digital context relies on resolving these issues in a manner that preserves first-sale rights rather than eviscerates them.

This Essay argues that the history and purpose of the first-sale doctrine provide good reasons to abandon the licensee/owner dichotomy as well as the formalistic approach to interpreting the doctrine's applicability to digital transfers. Doing so, furthermore, is unlikely to undermine markets for copyrighted works, but instead will help preserve the appropriate balance between the rights of copyright holders and consumers that first-sale rights have historically helped maintain.

#### THE LICENSEE VERSUS OWNER CONUNDRUM

Federal courts have held that when a recipient of a copyrighted work is a "licensee" and not an "owner" of a copy of the work, first-sale rights do not apply.<sup>9</sup> In such cases, copyright holders can prevent any subsequent distribution of the copyrighted work, including by way of importation.

What are the key factors in determining whether someone is a "licensee" or an "owner?" Different circuits employ a variety of tests to answer this question. But one important variant is reflected in the Ninth Circuit's approach, which was elaborated on in a series of cases in 2010. According to the Ninth Circuit, one significant factor, ironically, is simply whether the

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6. Consequently, a native of Thailand studying in the United States who profited from textbook arbitrage was not liable for copyright infringement. *Kirtsaeng*, 133 S. Ct. at 1358.

7. See, e.g., Joe Mullin, *Supreme Court Upholds First-Sale Doctrine in Textbook Resale Case*, ARS TECHNICA (Mar. 19, 2013, 8:44 AM PDT), <http://arstechnica.com/tech-policy/2013/03/thai-student-protected-by-first-sale-supreme-court-rules>.

8. See, e.g., *Capitol Records, LLC v. ReDigi Inc.*, No. 12 Civ. 95(RJS), 2013 WL 1286134, at \*5 (S.D.N.Y. Mar. 30, 2013).

9. See, e.g., *Vernor v. Autodesk, Inc.*, 621 F.3d 1102, 1103-04 (9th Cir. 2010). For an overview of the variety of approaches courts have taken to making this determination, see Brian W. Carver, *Why License Agreements Do Not Control Copy Ownership: First Sales and Essential Copies*, 25 BERKELEY TECH. L.J. 1887 (2010).

copyright holder labels the agreement with the purchaser a license agreement.<sup>10</sup> The other two factors concern whether the copyright holder imposes (1) significant restrictions on the recipient's ability to transfer the copyrighted work, and (2) other notable use restrictions.<sup>11</sup> In other words, a copyright owner can eliminate first-sale rights by specifying, essentially, that they do not apply.

Doing so becomes increasingly simple with the digitization of copyrighted works. With physical products it may be more difficult to impose such terms on users.<sup>12</sup> But with digital content there is no such difficulty. Consequently, eliminating first-sale rights—including the effects of the *Kirtsaeng* decision—is generally only a clickthrough agreement away.

But courts err in focusing on the licensee/owner distinction. First, purchasers of copyrighted works are by definition licensees of the copyright in the work. They do not become, by virtue of the purchase, owners of the copyright in the work or even licensees of all the rights available under copyright. A purchase constitutes a limited license to use the work for personal benefit, subject to statutory exceptions such as fair use and first-sale rights.

Consequently, the strained legal analysis that focuses on determining whether someone is a “licensee” or an “owner” is a moot point. It has already been answered. It then becomes all the more illogical that a copyright holder, by designating purchasers as licensees and restricting them from transferring the work, can eliminate first-sale rights and the effects of *Kirtsaeng*.

This seems even clearer when considering certain exceptions to first-sale rights specified in the Copyright Act. For instance, despite first-sale rights, purchasers of software or phonorecords cannot rent either to subsequent parties.<sup>13</sup> The obvious concern underlying these exceptions is that

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10. *Vernor*, 621 F.3d at 1110.

11. Some “notable use restrictions” that the Ninth Circuit referenced include “limit[ing] user[s] to making one working and one backup copy of the” copyrighted work; forbidding “examination, disclosure, copying, modification, adaptation, and visual display” of the work; “prohibit[ing] . . . duplication and third-party use”; limiting use to a single computer; “prohibit[ing] multicomputer and multi-user arrangements[;] and permit[ing] transfer to another computer no more than once every thirty days.” *Id.* at 1110, 1111 & n.11.

12. For instance, courts have found that placing such terms inside a book cover or including them on a CD sent to consumers without solicitation did not result in binding terms on the consumers. *See, e.g.*, *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339, 350-51 (1908) (holding that a copyright owner's inclusion of restrictive conditions on the inside flap of its book were not binding because no contract had formed between the purchaser and the copyright owner); *UMG Recordings, Inc. v. Augusto*, 628 F.3d 1175, 1180 (9th Cir. 2011) (holding that restrictive conditions included with promotional CDs sent to consumers were not binding on the consumers because under all circumstances of the CDs' distribution, the consumers were free to do with the CDs as they wished and no consensual license agreement had been entered into).

13. 17 U.S.C. § 109(b)(1)(A) (2011).

with the widespread availability of copying technology, renters could easily copy these media and thereby undermine the copyrighted works' market.

But these exceptions are unnecessary if the same result could have been achieved by relying on the licensee/owner distinction. One might argue that, historically, it was more difficult to render someone a licensee because software and phonorecords were distributed as physical products. And so one logical interpretation is that Congress provided the exceptions because limiting a consumer's rights through binding terms was difficult.

But elements of the first-sale doctrine's legislative history suggest otherwise. For instance, the House Report to the 1976 Copyright Act specifies that the first-sale doctrine does not mean that copyright holders cannot impose conditions on the future disposition of their copyrighted works, but it does mean that violation of those conditions is a breach of contract rather than a copyright violation.<sup>14</sup> In short, first-sale rights were meant to limit copyright outright; copyright owners should not be able to circumvent them through semantics. And because of this prohibition against circumventing first-sale rights through contract, the specific software and phonorecord exceptions were provided. Otherwise, the recipient of software or phonorecords could still distribute either by renting them without violating copyright law, even if doing so was a breach of contract.

To some extent, the statute mandates the licensee/owner analysis. After all, the statute indicates that first-sale rights only apply to "owners" of a copy of a copyrighted work.<sup>15</sup> But for all intents and purposes, purchasers of digital works "own" their copies of the work, regardless of what the license agreement may say. Purchasers are generally not expected to return the works, and in most cases there is no expectation of recurring payments for continued access. The examples of non-ownership listed in the statute all envision only temporary possession of the work. This line of reasoning—where the focus is on the realities of possession rather than semantics of the license agreement—shows up other circuits,<sup>16</sup> as well as in Europe.<sup>17</sup> And this is the line of reasoning that the Supreme Court and Congress should adopt. Otherwise, a historically important limitation on copyright—as bolstered by *Kirtsaeng*—will likely become history.

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14. H.R. REP. NO. 94-1476, at 79 (1976).

15. 17 U.S.C. § 109(a). The statute later specifically indicates that leasing, lending, renting, or providing a copy of the work to users in any way such that the user does not "own" the copy means that first-sale rights are inapplicable. *Id.* § 109(d).

16. *See, e.g.*, *Krause v. Titleserv, Inc.*, 402 F.3d 119, 123-24 (2d Cir. 2005).

17. *Cf.* Claus Färber & Ralf Weisser, McDermott Will & Emery, *CJEU Rules First Sale Doctrine Applies to Digital Copies of Software in Europe*, JD SUPRA LAW NEWS (July 16, 2012), <http://www.jdsupra.com/legalnews/cjeu-rules-first-sale-doctrine-applies-t-32547> (noting that there is still uncertainty as to the status of the first-sale doctrine with regards to certain subscription models of software distribution).

## DIGITALLY TRANSFERRING FIRST-SALE RIGHTS AWAY

Some courts have also recently held that first-sale rights do not apply to digital transfers of copyrighted works because the transferred file does not bear the same properties as the original file.<sup>18</sup> In essence, such courts reason that because the transferred file is fixed on a different hard drive, the transferred file is a new copy of the original file, not the original file itself. And first-sale rights only apply to the original.<sup>19</sup>

But such a conclusion defies the simple purpose of the first-sale doctrine, which is to allow an owner of a work to transfer it. If such a transfer can occur while also ensuring that the original owner does not retain his copy, good reasons for eliminating first-sale rights in the digital transfer context vanish.

To analogize to the physical world: concluding that first-sale rights do not apply if the work can be accessed from somewhere other than the original purchaser's home would seem absurd to most. But that is precisely the effect of a formalistic interpretation of the first-sale doctrine's statutory text in the digital transfer context. Such an interpretation thus effectively eliminates first-sale rights—including the effects of *Kirtsaeng*—for much digital content.

## THE EFFECTS OF A DIGITAL FIRST-SALE RIGHT

If courts abandoned the licensee/owner distinction and accepted first-sale rights for digital transfers, would the sky fall on copyright holders? There are certainly significant issues to consider. For instance, the ease with which copies can be made and retained, all without degradation, may mean that digital first-sale rights would lead to increased piracy and thereby undermine markets for copyrighted works. Furthermore, a digital first-sale right may prevent copyright holders from being able to price discriminate in different jurisdictions. Consequently, consumers—particularly, perhaps, in poorer countries—may suffer as copyright holders raise prices in order to compensate both for increased piracy and an inability to price discriminate. And society may suffer as copyright holders lose their incentives to create at all.

But each of these issues is addressable. First, the Copyright Act does not guarantee copyright holders a right to price discriminate. And preserving such a benefit at the expense of a statutorily enshrined limitation, with

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18. *See supra* note 8 and accompanying text.

19. The legislative history of the Digital Millennium Copyright Act supports this interpretation of the Copyright Act. *See* U.S. COPYRIGHT OFFICE, LIBRARY OF CONG., DMCA SECTION 104 REPORT 22-24 (2001) (discussing the legislative history of the Digital Millennium Copyright Act).

its “impeccable historic pedigree,”<sup>20</sup> is unjustified. The same issue was relevant in *Kirtsaeng*.<sup>21</sup> Presumably, the majority believed that copyright holders would continue to find ways to effectively monetize their works as they have done, for instance, in the domestic marketplace. Price discrimination may enable copyright holders to obtain higher revenues than they otherwise would. But the primary purpose of copyright is to enrich society, not copyright holders.

But will copyright holders continue to enrich society with their works if a digital first-sale right were reality? If history is any guide, the answer is yes. Copyright holders have raised the specter of technology gutting their markets with each new innovation. But often the new technology has actually proved a boon for them.<sup>22</sup>

In the case of digital first-sale rights, copyright holders would almost certainly respond by working with device manufacturers to ensure that when a file is transferred, it no longer resides with the transferor. Certainly some cases of piracy would still occur—as they do today when consumers burn their CDs onto their devices before giving the CDs away—but the possibility of piracy in the physical world has never been justification enough to eliminate first-sale rights there. Nor should it be in the digital world.

A digital first-sale doctrine might also reduce piracy as consumers rely on legitimate secondary markets instead of piracy. Secondary markets might also result in increased sales of other copyrighted works because secondary markets expose consumers to a broader spectrum of copyrighted works, which often leads them to purchase complementary goods.<sup>23</sup>

Last, some argue that the lack of degradation in digital works and the ease of transferring them should make first-sale rights inapplicable to such works. But it is hard to see why. The first-sale doctrine does not require that physical books be tattered before the doctrine applies. Neither does it require that access to such works include significant barriers; anyone can buy a new CD or book today and give it to the first person she sees. It might be argued that eventually such physical products wear away, and so the doctrine implies some limitation on the number of transfers. But that is an ar-

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20. See *Kirtsaeng v. John Wiley & Sons, Inc.*, 133 S. Ct. 1351, 1363 (2013).

21. See *id.* at 1374 (Ginsburg, J., dissenting).

22. For instance, copyright holders argued when the VCR first came to market that it would undermine their ability to generate revenues. See *Sony Corp. of Am. v. Universal City Studios, Inc.*, 464 U.S. 417, 459 (1984). Instead, sales of cassette tapes provided them with significant new sources of revenue. See R. Anthony Reese, *The Problems of Judging Young Technologies: A Comment on Sony, Tort Doctrines, and the Puzzle of Peer-to-Peer*, 55 CASE W. RES. L. REV. 877, 884 (2005).

23. There is some evidence, for instance, that those who illegally download music via peer-to-peer networks purchase significantly more music than the average consumer. See, e.g., *Does Piracy Increase Sales?*, POLLSTAR, (Apr. 23, 2009, 2:01 PM), [http://www.pollstar.com/news\\_article.aspx?ID=663094](http://www.pollstar.com/news_article.aspx?ID=663094).

gument for adjusting first-sale rights in the digital context, not eliminating them altogether.

#### CONCLUSION

The *Kirtsaeng* decision helped further cement the first-sale doctrine as an important limitation on the rights of copyright holders. But more cement is needed. Specifically, as the digitization of copyrighted works increases, first-sale rights face increasing peril as copyright holders subject consumers to click-through agreements that eviscerate first-sale rights in effect if not in theory. Furthermore, some courts have recently employed a formalistic approach to the statutory text that renders first-sale rights simply inapplicable to digital transfers. If *Kirtsaeng* is to avoid becoming the first-sale doctrine's "swan song," courts and Congress must respond to save it.

Doing so will help maintain the proper balance between the rights of consumers and copyright holders that is vital to a just copyright law. Concerns about increased piracy and undermining creative incentives are certainly legitimate. But history suggests copyright holders are up to the task and may, in fact, benefit both themselves and consumers by performing it.



