Digital Transmissions: To Boldly Go Where No First Sale Doctrine Has Gone Before

Brian Mencher*

> "Because the underlying purpose of the first sale doctrine is to ensure the free circulation of tangible copies, it simply cannot be said that a transformation of section 109 to cover digital transmissions furthers that purpose."[1]

I. INTRODUCTION

Over the years, society has grown comfortable with the notion that the purchasers of musical works may sell or relinquish those works at their discretion. This notion has been supported by nearly 100 years of judicial opinions and legislative mandates, and currently is codified in §109(a) of the 1976 Copyright Act - the first sale doctrine.[2] Society's traditional application of the first sale doctrine, however, has been limited to physical copies of copyrighted works.

The advancement of technology is testing the first sale doctrine in new ways. No longer are copyrighted works contained in a singular physical object, such as a painting on canvas or a song on a compact disc. Technology has enabled society to appreciate these artistic expressions in digital formats , arguably in an intangible format. These advancements have changed the way we store artistic expression, although they have not changed the meaning of the artistic expression itself. Instead of purchasing a vinyl record, cassette tape, or compact

* Brian Mencher graduated from the University of Florida Levin College of Law with high honors in December 2002. Special thanks to Professor Bill Chamberlin for his guidance and dedication.

[1] U.S. Copyright Office's Digital Millennium Copyright Act, §104 Report (August 29, 2001).

[2] Copyright Act of 1976, 17 U.S.C. §109(a) (2001).

disc, consumers can purchase music in other formats, including the very popular MP3 format.[3]

These storage formats provide for two distinct styles of property ownership – physical tangible works and intangible digitally formatted works. Traditional physical works include, analog formats, such as vinyl records and cassette tapes and digital formats, such as compact discs. The newest style of property ownership, and the focus of this paper, is digitally formatted works that have no physical elements and are only transferable by a digital transmission.[4] What separates the traditional notions of ownership from digital ownership are the ways in which particular copies may be disposed of. With traditional ownership, once the physical copy is sold, the initial consumer no longer has possession over that particular copy. With current digital ownership if a copy is obtained through a digital transfer[5], the original owner still retains a copy of the work. In essence, the original owner of the work reproduces it – a clear violation of the Copyright Act.[6]

"Forward and delete" technology is being developed that will allow the digital transfer of a digitally formatted copyrighted work without implicating the reproduction right. Notwithstanding the ability to separate the distribution right with the reproduction right through such technology, it remains unclear whether digital transfers conform to the language of §109(a).[7] This paper seeks to determine whether 17 U.S.C. § 109(a) [First Sale Doctrine] grants the purchaser of a digitally formatted musical work (musical composition and sound recording) the right to sell or otherwise dispose of the possession of that work by means of a digital transfer.

This research area is important for many reasons. First, there is no legal commentary on the application of the first sale doctrine as it applies to digitally formatted works.[8] Second, the U.S. Copyright Office's

---

[3] *E.g.* B.J. Richards, *The Times they are A-Changin': A Legal Perspective on how the Internet is Changing the Way we Buy, Sell, and Steal Music*, 7 J. INTELL. PROP. L. 421 (2000) ("MP3 shrinks digital audio files to less than one tenth of their original size. . . MP3 enables users to duplicate audio files from CDs or other sources and post them on the Internet, e-mail them to others, or store them on computer hard-drive or other playback devices.").

[4] 17 U.S.C. §101 "A 'digital transmission' is a transmission in whole or in part in a digital or other non-analog format."

[5] A digital transfer includes the use of a computer to transfer the material via the Internet.

[6] 17 U.S.C. §106(1).

[7] See *infra* Part IV.

[8] But see Richards, *supra* note 3; Stephen Summer, *Music on the Internet: Can the Present Laws and Treaties Protect Music Copyright in Cyberspace?*, 8 CURRENTS INT'L TRADE L.J. 31 (1999); Adam P. Segal, *Dissemination of Digitized Music on the Internet: A Challenge to the Copyright Act*, 12 COMPUTER & HIGH TECH. L.J. 97 (1996) for examples of legal scholarship dealing with copyright and the Internet.

recent report, analyzing the effect of the Digital Millennium Copyright Act on the first sale doctrine, raises concern about how copyright law will govern and be governed on the Internet. Third, the music industry, and its collective lobbyist, the Recording Industry Association of America (RIAA), has recently been active in pursuing high-profile cases invoking copyright protection of music on the Internet.[9] 'Finally, the Internet's architecture continues to allow potentially infringing activities to occur, which questions what constitutes copyright infringement in the digital landscape.

Part II of this paper will introduce the first sale doctrine. Part III discusses how copyright law and economics drive the music industry, with particular attention given to music on the Internet. Part IV presents two critical issues that lay the foundation for Part V of this paper: 1) the meaning and technology of a digitally formatted musical work and 2) the U.S. Copyright Office's §104 report examining the first sale doctrine to music online. Part V examines the merits of the Copyright Office's report and analyzes whether a digitally formatted musical work remains consistent with the language of the first sale doctrine. In the case that the first sale doctrine does not apply to digitally formatted musical works, Part VI offers a business model for facilitating a digital first sale doctrine that considers the balanced interests of music purchasers and music businesses.[10] Part VII will conclude this paper.

II. THE FIRST SALE DOCTRINE §109(a)

The first sale doctrine is codified in the Copyright Act of 1976 under Title 17 of the United States Code, section 109(a).[11] It states, "notwithstanding the provisions of §106(3) [distribution right], the owner of a particular copy or phonorecord lawfully made under this title. . .is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord."[12] Thus, one who purchases a compact disc has the right to dispose of that copy in any fashion the purchaser wishes, with one statutory exception. Section 109(b) prohibits the owner of a compact disc to rent, lease, or lend that copy of the sound recording.[13]

---

[9] *See e.g* A & M Records v. Napster, Inc., 239 F.3d 1004 (9th Cir. 2001); Recording Industry. Ass'n v. Diamond Multimedia Systems, Inc., 180 F.3d 1072 (9th Cir. 1999). These interests will undoubtedly drive the current debate on §109(a)'s scope.

[10] The digital first sale doctrine is based on the reality that currently, a digital transmission implicates both the distribution right and the reproduction right.

[11] 17 U.S.C. §109(a) (2001).

[12] *Id.*

[13] §109(b).

A. *Judicial Creation*

The first sale doctrine was created through judicial interpretation. As early as 1790, the United States granted authors of maps, charts, and books the "sole right and liberty of printing, reprinting, publishing and vending[14]."[15] The Act prohibited any person other than the author of the copyrighted work to publish or sell the work.[16] Not until 1908 was the U.S. Supreme Court called upon to interpret the scope of a copyright owner's vending right.[17]

In *Bobbs-Merrill v. Macy & Co*, the Court was faced with the issue of whether a copyright owner's sole right to vend enables the copyright owner to restrict subsequent sales of the copyrighted work.[18] Appellant, Bobbs-Merrill, owned the copyright in a book. Appellant attempted to restrict subsequent sales of its book through a notice inside the work that stated, "The price of this book at retail is one dollar net. No dealer is licensed to sell it at a less price, and a sale at a less price will be treated as an infringement of the copyright."[19]

Appellee, R.H. Macy & Co. [Macy & Co.], purchased Bobbs-Merrill's book from a wholesale dealer and knowingly disregarded appellants retail restriction. Macy & Co. subsequently sold the books for 89 cents each.[20] Lacking a contractual relationship with Macy & Co., the Bobbs-Merrill claimed that it's right to vend its copyrighted works extended to subsequent sales of particular copies of the work.[21] The U.S. Court of Appeals for the Second Circuit disagreed with appellant's interpretation of it's vending right. The Supreme Court affirmed the lower court's ruling.[22]

The Supreme Court held that the vending right did not extend beyond the first sale of the copyrighted work.[23] Such a reading, the Court claimed, would extend the copyright owner's right beyond the statute's

---

[14] As will be gleaned from the *Bobbs-Merrill* case, *infra* note 17, the purpose of the vending right was to give effect to the reproduction right granted copyright owners. The present day distribution right is analogous to this vending right, with respect to first sale doctrine jurisprudence.

[15] First United States Copyright Act, 1 Stat. 124 §1; 1st Cong., 2d Sess., c. 15 (1790) (dealing with maps, charts, and books).

[16] *Id.* at § 2.

[17] *Bobbs-Merrill Co. v. R.H. Macy & Co.*, 210 U.S. 339 (1908); see also *Harrison v. Maynard, Merrill & Co.*, 61 F. 689 (2d Cir, 1894).

[18] *Id.* at 351.

[19] *Id.* at 341.

[20] *Id.* at 342.

[21] *Id.* at 343.

[22] *Id.* at 351.

[23] *Id.*

meaning.[24] Thus, a purchaser of a book sold under the authority of the copyright owner may subsequently dispose of that copy of the book. The Court was clear to point out, however, that such a right did not permit the purchaser of a book to "publish a new edition of it."[25] Nevertheless, the Court left open the issue of whether contractual restrictions could preempt a purchaser's right to dispose of a particular copy.[26]

One year later, the U.S. Congress codified the first sale doctrine under the Copyright Act of 1909.[27] Section 109(a) is the current codification of this judicial doctrine. The underlying policy driving the first sale doctrine was concern "against restraints on the alienation of tangible property."[28] Thus, the copyright owner's vending right[29] was limited to first sale.

B. *Case Law Interpretation*

Although many court opinions have applied the first sale doctrine, case law interpreting its scope remains scarce. This scarcity may be caused by a number of factors. First, the statutory language may leave little to be interpreted. Second, because interpretation of the language has not been needed, many cases likely never reached the appellate level. Finally, enforcing violations of the doctrine are difficult. Policing all sales of a copyrighted work, by someone other than the copyright owner, is not feasible. There has been one case interpreting §109(a) thoroughly and provides some insight.

In *Independent News Co. v. Williams*, the U.S. Court of Appeals for the Third Circuit held that a copyright owner's control over his or her work ended when a lawful transfer was made to a first purchaser.[30] A second-hand comic book dealer lawfully purchased copies of outdated comics from a wholesaler ordered to destroy them.[31] Unknown to the purchaser, the wholesale dealer was under contract with the comic publisher to destroy all comic books unsold after a certain period.[32] The issue before the court was whether a second-hand purchaser of comic books could sell those copies when the comic books

---

[24] *Id.*

[25] *See* id at 350.

[26] *Id.* ("[T]his is purely a question of statutory construction. There is no claim in this case of contract limitation, nor license agreement controlling the subsequent sales of the book.").

[27] 17 U.S.C. § 27 (1977).

[28] S. Rep. No. 162, 98th Congress., 1st Sess. 4 (1983).

[29] The vending right is currently codified under 17 U.S.C. §106(3) – the distribution right.

[30] Independent News Co. v. Williams, 293 F.2d 510 (3d Cir. 1961).

[31] *Id.*

[32] *Id.*

were purchased from a wholesale dealer under contract to destroy all copies.

The court gave no weight to the contractual relationship between the publisher and wholesale dealer, holding:

> where the publisher has parted with the title to the copyrighted work and despite that fact that as between the immediate parties there is a contractual restriction on it use, this restriction does not bar subsequent purchasers from vending the periodical as a literary work free of the restriction.[33]

The court's holding maintains the consistent interpretation of §109(a) granting the owner of a lawfully obtained copy or phonorecord with the right to dispose of that copy.

C. *First Sale Doctrine in Perspective*

Section 106 of the Copyright Act of 1976 grants the copyright owner a bundle of rights.[34] They include the right to: 1) reproduce the work, 2) prepare derivative works, 3) distribute copies or phonorecords of the work, 4) perform the work, and 5) display the work. The *Bobbs-Merrill* Court suggested that the vending/distribution right was granted to give the copyright owner's reproduction right effect – drawing distinction between the reproduction and vending/distribution rights.[35] The first sale doctrine solely limits a copyright owner's vending/distribution right.[36] The first sale doctrine, therefore, has never granted the owner of a particular copy or phonorecord the right to reproduce that copy and subsequently distribute the reproductions.[37] This distinction is paramount to understanding the debate surrounding the application of the first sale doctrine to digital transmissions on the Internet.

III. The Music Industry Online – Copyright and Economics

The music industry relies heavily on copyright protections to generate revenue. Every right granted to musical works through the Copyright Act creates an exclusionary and exploitable right[38], to a limited

---

[33] *Id.* at 517.

[34] §106.

[35] Bobbs-Merrill, 210 U.S. at 350.

[36] §109(a) ("Notwithstanding the provisions of §106(3). . .").

[37] Bobbs-Merrill, 210 U.S. at 350 ("The purchaser of a book, once sold by the authority of the owner of the copyright, may sell it again, although he could not publish a new edition of it.").

[38] The term "exploit" is not to be construed negatively. Rather, in the music industry, the term "exploit" describes the process by which music is utilized in the various mediums, such as for compact discs, television commercials, and movie synchronizations.

extent.[39] The business of music revolves around these rights and shapes the corporate structure for generating profitability. This business structure, however, depends on the medium of distribution involved – physical or digital distribution.

A. *Copyright Protection*

The Copyright Act recognizes two types of fixed musical expression – musical compositions and sound recordings.[40] The musical composition generally consists of sheet music and written lyrics (i.e. the underlying song).[41] The sound recording is one rendition of that song usually recorded by a particular musician or band.[42] The author of the musical composition and the author of the sound recording are sometimes different people or entities. For instance, Dolly Parton wrote the song "I Will Always Love You" and Whitney Houston created a sound recording of that song. This leads to two separate copyright owners, one for the musical composition and one for the sound recording.[43]

B. *Economics*

Copyright law drives the economics of the industry. In the music industry, every right granted under §106 of the Copyright Act is licensed out to a music entity and exploited.[44] A digital sale of a digitally formatted musical work, like a traditional sale of a compact disc, creates numerous royalties for the copyright owners of the underlying works. Generally, two royalties are generated through the sale of a musical work in a sound recording – a musical composition or mechanical royalty[45] and the performing artist royalty.[46]

---

[39] The bundle of rights are limited mainly by the fair use doctrine, codified under 17 U.S.C. §107.

[40] §102(a) ("Works of authorship include the following categories. . .musical works. . . sound recordings").

[41] Robert Merges, Peter Menell, and Mark Lemley, INTELLECTUAL PROPERTY IN THE NEW TECHNOLOGICAL AGE 405 (2nd ed., Aspen Law & Business 1997) (2000).

[42] §101 ("Sound recordings are works that result from the fixation of a series of musical, spoken, or other sounds. . ."); *See also* Merges, Menell, and Lemley, Intellectual Property in the New Technological Age 405.

[43] This is easy to understand when you think of a Beethoven composition performed by the New York Philharmonic. The author of the musical composition is Beethoven, while the author of the Sound Recording is the New York Philharmonic. Both are entitled to a copyright.

[44] Music entities include American Society of Composers, Authors, and Publishers (ASCAP), BMI, Inc., Sesac, music publishing companies, record labels, and the Harry Fox agency, to name a few.

[45] *See generally* Donald S. Passman, ALL YOU NEED TO KNOW ABOUT THE MUSIC BUSINESS 211 (2000) (The royalty became known as a "mechanical" for the action that was taken when the musical sounds were mechanically molded into the vinyl album.).

1. Mechanical Royalty

The copyright owner in a musical composition generates revenue in many ways. The musical works can be used in a television commercial, a feature film, or a musical toy.[47] The work can also be used in a sound recording, as exemplified in the Whitney Houston example above. When the musical composition is used in a sound recording, the Copyright Act grants the copyright owner in the musical composition a statutory per-use royalty known as a mechanical royalty.[48] Currently, the royalty rate determined by the U.S. Congress is eight cents per musical composition used, per sound recording distributed.[49]

When one considers the money potentiality generated through the use of one musical composition, the economics of copyright protection become clear. For example, assume one songwriter produces three songs that are used in a sound recording. Assuming two million copies of the sound recording are distributed in the United States, the mechanical royalty due to the copyright owner in the musical composition would be $480,000 dollars.

2. Performing Artist Royalty

The performing artist, generally signed to a record label, is also paid a royalty. As compensation for recording music exclusively with one label and signing over the copyright in the sound recording, the performing artist is paid a royalty based on the number of sound recordings sold.[50] While the royalty rate fluctuates with the medium used (i.e. cassette, compact disc, new media), an average royalty is about 15% of listed retail price.[51] In dollars and cents, this averages out to a $1.10 royalty for each sound recording sold.[52] Thus, for the sound recording that sells two million copies, the performing artist receives roughly $2.2 million dollars.

---

[46] *Id.* at 176.

[47] See Jeffrey Brabec and Todd Brabec, MUSIC MONEY AND SUCCESS, The Insider's Guide to Making Money in the Music Industry (2000) for the many ways to exploit musical compositions and the revenue generated from such use.

[48] §115(c).

[49] 37 C.F.R. § 255.3 (2002) (For every phonorecord made and distributed on or after January 1, 2002, the royalty rate payable with respect to each work embodied in the phonorecord shall be either 8.0 cents, or 1.55 cents per minute of playing time or fraction thereof, whichever amount is larger, subject to further adjustment pursuant to paragraphs (l) through (m) of this section.) *Id.* Sections (l) & (m) set the royalty rate to 8.5 cents, or 1.65 cents per minute beginning in 2004 and 9.1 cents, or 1.75 cents per minute beginning in 2006, respectively.

[50] *See* Passman, *supra* note 45 at 90.

[51] *Id.* at 90.

[52] *Id.*

In cases where the copyright owner in the musical composition and the sound recording are the same person or band, the total monies received are greatly increased. Rather than three musical compositions as discussed above, assume the songwriter produces twelve songs and records them. If two million copies of the sound recording were sold in the United States, the artist would receive $4,120,000 - $2.2 million dollars in performing artist royalties and $1,920,000 dollars in mechanical royalties for the use of the twelve musical compositions.[53]

C. *The Interests Involved – Copyright and Economics*

Musical composers and performing artists make a majority of their revenues from mechanical and performing artist royalties, respectively. These artistic people, however, are generally not the "powers that be." It is very common in the music industry for a composer to grant the rights in the musical composition to a musical publishing company in exchange for 50% of the revenue made from use of the work.[54] Thus, the composer only receives a four-cent mechanical royalty per musical composition sold in a sound recording, while the music publisher receives the other four cents.[55] When a music publisher's entire catalog is taken into account, the sale of sound recordings generates millions of dollars in mechanical royalties every year.

The same can be said about performing artists and their relationships to record labels. Record labels require that their contracted performing artists sign over the copyrights in the sound recordings.[56] Performing artists generally receives a 15% royalty for each sound recording sold, while the record label collects the remaining 85% due from sales.[57] Thus, music entities, rather than songwriters and performing artists, stand to profit the most from the sale of sound recordings and their underlying musical compositions.

D. *Shaping Legislation and Governance*

The money generated by the music industry is a product of copyright protection. Without copyright law, there would be no legal re-

---

[53] The mechanical royalty would actually be less due to the controlled composition clause required by record labels.

[54] *See* Brabec, *supra* note 47.

[55] In a co-publisher deal, the musical composer as publisher will receive half of the publishing percentage, or 25% of the 50% publishing royalty. Thus, the music composer receives 75% of publishing revenues.

[56] *See generally* Passman, *supra* note 45.

[57] *See generally* Passman, *supra* note 45.

quirement to pay for music. The music industry, as can be expected, is heavily involved in shaping how copyright laws are administered.

For example, the first sale doctrine limits the royalties to the first sale of each compact disc. Thus, re-sell and trade stores do not generate any royalties to the interests discussed above.[58] The industry, however, lobbied for a statutory prohibition against lending and renting of sound recordings.[59] In the digital paradigm, music-trading programs[60] usurp first sales, thus diminishing the profits gained from mechanical and performing artist royalties.[61] If the first sale doctrine applies to digital transmissions, music entities would be precluded from claiming copyright protection for lawful subsequent sales of a particular digitally formatted musical work – consisting of the musical composition and sound recording.[62]

Economic considerations by these entities are beginning to shape the extent to which the first sale doctrine will apply to digitally formatted musical works that are transferred by digital transmission. Although a first sale doctrine on the Internet could potentially be applied similarly to the first sale doctrine in the traditional market, the lobbying of composers, music publishers, performing artists, and record labels create compelling arguments against an extension of the doctrine. It is with this in mind that an analysis of the first sale doctrine as it applies to digital transfers is presented.

IV. THE U.S. COPYRIGHT OFFICE'S §104 REPORT

On August 29, 2001, the United States Copyright Office issued its §104 Report as mandated by the Digital Millennium Copyright Act [DMCA].[63] Section 104 of the DMCA required the Copyright Office to

---

[58] But see Carla M. Miller, *New Technology and Old Protection: The Case for Resale Royalties on the Retail Sale of Used CDs*, 46 HASTINGS L.J. 217, 240 (1994) (advocating that "Congress should amend the Copyright Act to exempt the commercial sale of used CDs from first sale protection.").

[59] Congress passed The Record Rental Act §109(b) preventing the rental, lease, or lending of a sound recording.

[60] The infamous Napster program allowed peer-to-peer file sharing of musical works. The host Napster computer did not store any music files in its database. Rather, it served as the conduit. Napster would allow third party users to access the system and transfer copies of digitally formatted musical works with other third party users that also accessed the system.

[61] Jim Griffin, The Ethical Dilemma of Digital Development, 8 No. 2 NARAS J. 64, 65 (1999) ("Aside from the financial issues involved, there was a very real loss to [performing artists] in airplay, tours, and other support that are generated through movement on the sales charts. . .").

[62] Presuming subsequent sales did not implicate the reproduction right of the Copyright Act of 1976.

[63] U.S. Copyright Office's Digital Millennium Copyright Act, §104 Report (August 29, 2001).

examine the "development of electronic commerce and associated technology on the operation of section 109. . . of the U.S. Copyright Act."[64] In so doing, the Office drew a distinction between transferring of digital physical copies and digital copies that are transferred by digital transmission. This distinction is an important factor in the U.S. Copyright Office's analysis.

A. *Digitally Formatted Musical Works*

Technology has had an undeniably significant impact on the music business. Rather than music being stored on physical cassettes and compact discs, it can now be stored in a digital format on computer hard drives.[65] The digitally formatted musical work can be purchased online and freely transferred to other computer users.[66] Unlike a cassette or compact disc, the digitally formatted musical work cannot be viewed without the assistance of a computer. Nevertheless, the hard drive or memory storage, such as a floppy disc, can be removed and treated similarly to a cassette or compact disc.

With current technological restrictions, a digital transfer of a digitally formatted musical work creates a result inconsistent with the traditional application of the first sale doctrine. Currently, when a digitally formatted musical work is transferred from one computer to another, two rights under the Copyright Act are implicated. First, the distribution right is implicated because a transmission from one source to another qualifies as a distribution. Second, the reproduction right is utilized because the digitally formatted musical work remains on the computer, while the digital transmission sends a copy of the work to the other source. Thus, the file at the computer of origin is different than the copy at the computer of reception.

The first sale doctrine has never been a defense to reproducing copyrighted works.[67] Therefore, one could conclude that §109(a) does not apply to transmissions of digitally formatted musical works. To comply with the first sale doctrine, one of two steps must take place. Either, the party transferring the digitally formatted musical work must voluntarily delete the file from the computer hard drive. Or, "forward and delete" technology would have to be developed that ensures automatic deletion from the transmitting computer immediately at trans-

---

[64] Digital Millennium Copyright Act of 1998, Pub. L. No. 105-304, §104, 105th Cong. (1998).

[65] *See, e.g.*, Paul Veravanich, *Rio Grande: The MP3 Showdown at Highnoon in Cyberspace*, 10 MEDIA & ENT. L.J. 433 (2000).

[66] *See, e.g.*, www.pressplay.com for one example of an online music provider.

[67] Bobbs-Merrill, 210 U.S. at 350.

mission. Development of the latter technology is underway.[68] In light of these developments, the issue of whether the first sale doctrine applies to digital works transferred by digital transmission has surfaced.The U.S. Copyright Office, when asked to analyze this issue by Congress, recommended that §109(a) not be extended to include such a transmission.

B. *Analysis of the §104 Report*

After months of public comment, both for and against the application of the first sale doctrine to digital transmissions, the U.S. Copyright Office found that the doctrine did not apply to this type of disposition. While the Office's report is not binding on any court or the U.S. Congress, concerns raised by the report could bolster judicial and legislative action.[69] The report focused on a few key issues in making its determination.

1. Digital Content Disposed Of vs. Digital Transmission

The report claimed that "[t]he application of section 109 to digital content is not a question of whether the provision applies to works in digital form – it does."[70] Rather, the issue was whether section 109 applied to digital content that was transmitted digitally.[71] As to the former issue, the report analogized a digital format contained in a compact disc to a physical copy of the work in analog form, such as a cassette tape.[72] Because of the physical nature of the above formats that are entirely relinquished once disposed of, the report found that they were subject to the first sale doctrine.[73] A digital transmission, however, was found to be different.

2. Implicating the Reproduction Right

Absent technological capabilities, a digital transmission not only distributes the copyrighted work, but also reproduces it. This enables

---

[68] §104 Report at 46.

[69] Paul Sweeting, *Virtually Revisiting First Sale*, 12 VIDEO BUSINESS 33, Aug. 14, 2000, at 12 ("any concerns the report reflects about the weakening of the first-sale doctrine at the hands of the DMCA could become the basis for court challenges to the act somewhere down the line.").

[70] §104 Report at 78.

[71] *Id.*

[72] *Id*; *See also* §104 Report at 100 ("Of course, a lawfully made and owned copy of a work on a floppy disk, Zip disk, CD-ROM or similar removable storage medium can easily be transferred by physical transfer of the item and that activity is within the current reach of section 109").

[73] §104 Report at 78.

the transmitting party to retain the original copy of the work, while a second and new copy is created.[74] Because the first sale doctrine never served as a defense to the reproduction right granted under the Copyright Act, the report found that "section 109 does not apply to the digital transmission of works."[75] This finding, however, do not account for the availability of "forward and delete" technology.

3. Technology Is Not Viable at This Time

Public comment offered two mechanisms to prevent implication of the reproduction right – voluntary deletion or "forward and delete" programs. The report quickly dismissed voluntary deletion as "an open invitation to virtually undetectable cheating."[76] The report also criticized "forward and delete" technology as not being a viable option in preventing the reproduction of a digitally transferred digital work, as the technology has not yet been developed. The U.S. Copyright Office suggested that once such technology becomes available, it would have to be "robust, persistent, and fairly easy to use."[77] The Copyright Office also claimed that the technology would likely not be 100% foolproof.[78] Finally, it would come at great expense to either the copyright owners or consumers through cost spreading.[79] The report found that copyright owners would not undertake such an expense because technology that gives effect to the first sale doctrine would usurp otherwise retail sales.[80]

4. Distinguishing from Physical Copies

Even assuming the technology was viable, the U.S. Copyright Office was hesitant to extend the first sale doctrine to digital transmissions of digital works. The basis for this analysis was "whether the differences between the circulation of physical copies and electronic 'transfers' [were] more significant than the similarities."[81] The report considered physical evidence, economics, and policy to find that the first sale doctrine should not apply to digital transfers.

---

[74] *Id.*

[75] *Id.* at 79.

[76] *Id.* at 97.

[77] *Id.* at 98; *See also* id. at 84 ("Technological measures can be hacked, they are expensive, and they often encounter resistance in the marketplace.").

[78] *Id.* at 98.

[79] Cost spreading is an economic term of art. Rather than a business invest millions of dollars in a technology and keep consumer prices stable, the business is better off developing the technology and applying the costs to the purchase price – thus cost spreading among consumers.

[80] §104 Report at 98.

[81] *See* §104 Report at 82.

First, the quality of a physical copy, unlike digital formats digitally transferred, degrades overtime.[82] This, the report finds, makes the physical copy less desirable to consumers. In contrast, a digital transfer creates a perfect replica of the original copy.[83] Second, without barriers in time and space for digital transfers, the ability for computer users "to compete for market share with the new copies is thus far greater in the digital world."[84] This market competition decreases the revenue generated by the music industry. Finally, the first sale doctrine was premised on the free alienability[85] of tangible property. The report suggests that applying the first sale doctrine to digital transmissions does not further this premise.[86] For these reasons, the U.S. Copyright Office recommended that the doctrine should not be extended to digital transmissions of digitally formatted copyrighted works.

V. Applying the First Sale Doctrine to Digital Transmissions

Irrespective of the U.S. Copyright Office's §104 report, the law remains unsettled as to whether the first sale doctrine applies to digital transmissions of digitally formatted works, particularly musical works. This section attempts to settle the issue. The analysis requires a two-step approach. The conclusions presented by the U.S. Copyright Office must first be critiqued. Then, the statutory language of § 109(a) must be examined to determine whether a digital transmission of a digitally formatted copyrighted work could conform to its mandates.

A. *U.S. Copyright Office's §104 Report*

The report raised four issues regarding the applicability of digitally formatted copyrighted works to the first sale doctrine. Each of them lacks foresight and thorough legal analysis. The Copyright Office based its recommendation solely on the current state of technological capabilities on the Internet. Because "forward and delete" technology did not exist at the time of the report, the Copyright Office found that the first sale doctrine did not apply in the digital landscape of the Internet.

---

[82] *Id.* at 82.

[83] *Id.*

[84] *See Id.* at 83.

[85] Alienability is "[t]he quality or attribute of being transferable; *e.g.*, interest in property. Blacks Law Dictionary 72 (6th ed. 1990).

[86] §104 Report at 87, 88.

The report's treatment of digital content in a tangible format is simply form over substance.[87] A computer hard drive is just as tangible as a compact disc or DVD. It can be viewed, removed, and can be sold separate from the rest of the computer. In many respects, it is similar to a compact disc, albeit in a format that is harder to transfer. Where the report concedes that the transfer of a tangible compact disc that stores digital content is within the reach of the first sale doctrine, it fails to realize that a computer hard drive is also a tangible format that stores digital content. Although a digital transfer does not involve disposing of the hard drive itself, the concern raised by the Copyright Office is more form over substance. Substantively, a digital transfer, with "forward and delete" technology in place, is no different than disposal of the physical copy.

When "forward and delete" technology finally becomes "robust, persistent, and fairly easy to use," digital transmissions will no longer implicate the reproduction right of copyrighted works. The report's concern over this area fails to account for a time when such technology is readily available.

It is clear that technology is being developed to allow the simultaneous transfer and deletion of a digital work.[88] Thus, concern over its availability should not interfere with a thorough analysis. The fact that technology is not foolproof comes as no surprise and is a meritorious concern. Although every system has its glitches, there is an underlying policy reason for why it should be given more leniency in the first sale doctrine context – free alienability of property is a cornerstone of American jurisprudence. To find that digital property falls outside the application of the first sale doctrine requires that many years of jurisprudence be ignored. The final concern dealing with economics, however, is more problematic.

The issue of whether there is economic incentive to create technology capable of forwarding and deleting digital works is the framework for which this paper relies on, at least on a practical level. Whether there is an incentive or not, however, is an extra-legal concern that should not interfere with an interpretation of §109(a). Clearly, the interests in the music business will not voluntarily create technology that allows millions of online music collectors to freely sell and trade music. The online music collectors are likely not in a position, economically or technologically, to devote resources for creating the "forward and delete" programs. There remains one option – third party businesses. If

[87] *See generally*, Bobby Rosenbloum, *An Analysis of the DMCA Section 104 Report as it Pertains to the Music Industry*, ABA (2001).

[88] §104 Report at 46.

the first sale doctrine were found to apply to digital transmissions, requiring the music industry to conform, numerous programming companies would quickly begin developing the technology necessary to give effect to the first sale doctrine. Although further economic analysis is needed, the report's suggestion that no economic incentive exists is self-serving.

The U.S. Copyright Office's best argument, and likely the simplest, is that digital transfers do not degrade the subsequent copy. This finding, however, is inconsistent with the spirit of the first sale doctrine. There is no reason to believe that consumers of second-hand copyrighted works are less selective than consumers purchasing first retail sales. Further, the first sale doctrine was premised on the alienability of property, not the alienability of degraded property. Thus, the incidental increase in quality of a transferred digital file over delivery of a physical copy should not preclude a finding that the first sale doctrine applies to digital transmissions.

Because of the ease and quality of the transfer, digital transmissions do increase market competition between individual computer users and music businesses.[89] Increased market competition should not hinder the application of the first sale doctrine. It should facilitate it. If nothing else has been gleaned from the current situation in online music, the music industry should realize that it has millions of worker bees at its disposal.[90] Part VI of this paper discuses one business model that the music industry could adopt to facilitate its economic growth.

B. *Judicial Intervention*

The U.S. Copyright Office's §104 Report raised many issues in determining whether and to what extent the first sale doctrine applies to digital transmissions. It failed, however, to apply a pure statutory analysis of §109(a) to digital transfers. When a case finally becomes ripe for judicial intervention, a court may likely determine whether §109(a) of the 1976 Copyright Act grants an owner of a particular phonorecord[91] of a digitally formatted musical work the right to sell or otherwise dis-

---

[89] Assuming the competition is lawful through a digital transmission that implicates the first sale doctrine.

[90] Paul Sweeting, *The Lowdown on Download*, 20 Video Business 51 Dec. 18, 2000, at 12 *quoting* Yair Landau, President of Sony Pictures Digital (if the studios don't cooperate among themselves, "you're opening it up to someone else to aggregate the services.").

[91] 17 U.S.C. §101 Phonorecord means "a material object in which sounds. . . are fixed by any method now known or later developed, and from which the sounds can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device."

pose of the possession of that phonorecord by means of a digital transmission. A statutory analysis may yield an affirmative decision.

Three elements must be met to satisfy the disposal of a copyrighted work under the first sale doctrine: 1) the owner must have a particular copy or phonorecord of a copyrighted work, 2) the particular copy or phonorecord must have been lawfully made, and 3) implicitly, notwithstanding the distribution right, the owner of the copy or phonorecord must not implicate any other rights granted to copyright owners.[92] In the digital landscape of the Internet, a court's decision will likely rest on satisfying the first element – that of owning a particular copy or phonorecord of the copyrighted work. The other two elements can easily be satisfied.

1. Particular Copy or Phonorecord

Arguably, a digitally formatted musical work is not a copy or phonorecord within the language of §109(a). The Copyright Act of 1976 defines phonorecord as "a material object in which sounds. . . are fixed by any method now known or later developed, and from which the sounds can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device."[93] A computer hard drive, which contains the digitally formatted musical works, likely is a phonorecord.

A computer hard drive is a material object that fixes the sounds of the digitally formatted musical works. The statutory language "now known or later developed," suggests that the U.S. Congress envisioned times when new technologies would replace traditional applications. There is no better example than the progression of vinyl albums to 8-tracks, cassette tapes to compact discs. Furthermore, while the sound cannot be perceived directly, it can be perceived through the "aid of a machine or device." For these reasons, it is clear that a computer hard drive qualifies as a phonorecord.

This finding, however, would still require a leap to justify the transfer of a digitally formatted musical work, rather than the computer hard drive itself. The format of the digital work, such as a .wav or .mp3 file, is not the material object that fixes the sounds. Thus the format is not the phonorecord. This concern was implicitly raised in the §104 report.[94] As discussed above, this concern is more form over substance. Rather than removing the hard drive, or phonorecord, from the com-

[92] §109(a) in combination with §106; See §106 for the bundle of rights granted copyright owners. They are reproduction, derivative, distribution, performance, and display.

[93] §101.

[94] *See* supra text at Part V.A.

puter, a transfer between two computers that deletes the file upon transmission would ensure the same result. This result is not only more practical, but is consistent with the spirit of the first sale doctrine. Because of the lack of case law dealing with the doctrine, it is unclear whether a court would be willing to make such a leap.[95]

2. Not Implicate §106 Rights

Presuming a court does make the leap and the technology is in place, a digital transfer will only implicate the distribution right. Upon transfer, the original copy will be deleted. The remaining rights of a copyright owner – display, derivative, and performance – will not have been implicated.[96] Currently, however, technology is not available to assure simultaneous deletion with the transfer. Strictly construed based on current technological capabilities, the first sale doctrine should not apply because it does implicate the reproduction right.

3. Lawfully Made

So long as the owner of the particular copy or phonorecord receives the digitally formatted musical work through a lawful distributor, the copy will be possessed and lawfully made.[97] If the file were received through a Napster-like program, the copy likely would not be lawfully made. Thus, subsequent transfers of the copy would fail to satisfy the first sale doctrine. In the business models that are being developed by the music industry for online distribution, the digitally formatted musical works would be lawfully made and received.[98]

---

[95] Another compelling argument is that a digitally formatted musical work is a copy rather than a phonorecord. The Copyright Act, defines copies as "material objects, other than phonorecords, in which a work is fixed by any method now known are later developed, and from which the work can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device." §101. Because the definition of phonorecord and copy is nearly identical, the analysis in the text would be the same.

[96] *But see* §104 Report; *See also* Bobby Rosenbloum, *An Analysis of the DMCA Section 104 Report as it Pertains to the Music Industry*, ABA (2001) (suggesting that a digital transfer of a digitally formatted musical work incidentally implicates the performance right.).

[97] *See supra* note 66.

[98] *Id.* ("pressplay is an online music service company led by an executive team with deep music, programming, technology and business experience with offices in Los Angeles and New York City. Pressplay is an equally held venture of Sony Music Entertainment and Universal Music Group.").

VI. BUSINESS MODEL FOR FACILITATING A DIGITAL FIRST SALE DOCTRINE

In the music business, economics drive technological advances.[99] The most prevalent technology being developed, rights management regimes, is reactive and preventative. They are created to preclude the exploitation of music online.[100] Through the Digital Millennium Copyright Act, Congress granted protection to security measures that protect underlying copyrighted works.[101] The Serial Copy Management System [SCMS] is a code that prevents music files from subsequently being recorded digitally.[102] Other programs in place are known as "tethered works", where the digital file is locked to one device. The file can then be limited in a number of ways – 1) prevent further distribution of the music file, 2) automatically delete after a certain number of plays, or 3) automatically delete after a certain number of days ("time out").[103] The music industry utilized these protection methods to prevent online music collectors from further disseminating music files. If the first sale doctrine applied to digital transfers, however, a logical conclusion would warrant a review of the legality of these programs.[104]

The music industry's utilization of preventative technology is the product of reactionary decision-making. The industry should begin to develop digital structures that allow open access, while enabling a tracking system to collect revenue [rights-management containers][105]. This container technology can be structured in an infinite number of

---

[99] *Internet Regulation Through Architectural Modification: The Property Rule Structure of Code Solutions*, 112 HARV. L. REV. 1634, 1653 (1999) ("The market, however, is likely to be the most effective regulator of [technology] regimes. Having brought [ ] technology into existence, the market is likely to play a major role in shaping the future development of [ ] technologies.").

[100] *Id.* at 1634 ("Rights-management containers change the nature of the copyright entitlement by granting copyright owners extra-legal and absolute control over their material, thus reversing the Internet trend toward access rights and resetting the copyright balance in favor of exclusion.").

[101] Circumvention of Copyright Protection Systems, 17 U.S.C. §1201.

[102] 17 U.S.C. §1002.

[103] Bobby Rosenbloum, *An Analysis of the DMCA Section 104 Report as it Pertains to the Music Industry*, ABA (2001)

[104] This issue is the basis for another research paper. If the first sale doctrine applies to digital transmissions, but the Copyright Act grants protection against circumventing security measures, further analysis would be required to reconcile this contradiction.

[105] *See supra* note 99 at 1653 (1999) ("Although technological efforts to protect intellectual property online have taken many forms, the most comprehensive code solution to the problem of online copyright infringement is the development of rights-management containers, which not only protect copyrighted materials, but also strengthen the content provider's rights allocation.").

ways. The structure controls access and tracks the distribution of digitally formatted musical works. While the access is limited only to those who chose to accept the container's parameters, access to the container would be available to all. The tracking of digital transfers can be accomplished through metered usage, requiring a per unit charge for each distribution that is metered.

The technology costs to create a container would be minimized through long-term savings in transaction costs, such as distribution and packing.[106] Ultimately, the container could prevent no-cost file sharing and create a "superdistribution" model.[107] As one article described it, "[i]n this way, a popular single could spread instantly across the digital community, as friends send copies to friends, who send copies to their friends, and so on. The content provider would reap substantial rewards from such a phenomenon because rights-management containers would ensure payment for every end-use."[108] This structure maintains security protection for copyrighted works, but also is flexible to either give the first sale doctrine effect or provide the music industry with an economically advantageous distribution model.

A. *An Applied Business Model*

The structure can be designed in many ways. The following is just one viable design. Because security measures, such as SCMS, are in place, all digitally formatted musical files should be encrypted to prevent subsequent reproduction and distribution. The musical works can then be sold to online music collectors for a fee established by the record labels (taking into account the mechanical and performing artist royalties). Each online collector must be granted access to the container that enables distribution of the music. And then, the technology must provide: 1) a metered tracking system to measure the number of distributions, and 2) a digital payment system that automatically transfers funds to online music banking accounts.

Economic incentives exist for both the music business and music purchasers and sellers. Through this structure, the music industry could require a minimum sales price per each digitally formatted musical file sold to compensate for mechanical royalties, performing artist royalties, and profit. Online music purchasers can then sell copies of their lawfully purchased musical files to other music purchasers through the container. The music purchasers would be in competition with each

---

[106] *Id.* at 1653.
[107] *Id.*
[108] *Id.* at 1653-54 (1999).

other, attempting to offer the closest price to the minimum sales price established by the music business. Any money in excess of the minimum price would be transferred into the purchaser/seller's online music banking account and applied against other purchases or converted into cash. Eventually, the music industry generates revenue off the millions of users trading through the container.

While this model may illustrate the technological and economic capabilities of the music industry, there is reason for concern. If each music entity creates its own structure, digitally formatted musical works will not be compatible with each container. Being user-unfriendly, this business model would deter widespread acceptance. For this reason, the music businesses must cooperate through self-regulation or the U.S. Congress may have to require a uniform business model. Self-regulation would clearly be more advantageous to the music industry.

VII. Conclusion

Exploitation of music on the Internet is pervasive and likely to remain for many years, at least until another medium is created. The state of copyright law as it applies to the Internet is unclear. The traditional reproduction and distribution models of the music industry are not the same as the reproduction and distribution models on the Internet. No longer does corporate music entities solely own the means of exploitation. Because of the accessibility of computers and the Internet, anyone can exploit music online, albeit unlawfully.

Congress and the courts are just beginning to develop parameters for copyright protection on the Internet. From safe-harbor statutes for Internet service providers (ISP)[109] to liability for catalysts of peer-to-peer file sharing,[110] some conception of copyright protection in the digital age has begun to form. One area where legal interpretation and academic theory still lacks is on the application of the first sale doctrine to digital works on the Internet, specifically digitally formatted musical works.

Less than seven months ago, the U.S. Copyright Office offered its recommendations on whether the development of electronic commerce and associated technology affected the operation of the first sale doctrine in the digital landscape. The Office's report clearly stated that the doctrine did not extend to digital transmissions. The recommendations were not binding, and thus far the U.S. Congress has not acted on them.

---

[109] § 512(c).

[110] A & M Records v. Napster, Inc., 239 F.3d 1004 (9th Cir. 2001).

In the meantime, online music collectors, the music industry, and third party businesses are left to determine the fate of digitally formatted musical works. It remains unclear whether a court would find that a digital transfer of a digitally formatted work satisfies the requirements of §109(a). Compelling arguments have been made for both sides.[111] Regardless of the outcome, the music industry is in a great position to create business models that provide inexpensive production costs, while generating consistent royalties. One such business model was proposed in this paper.

Ultimately, the battle of copyright protection and free access to copyrighted works will live on. Copyright law provides millions of dollars in revenue streams each year to the music industry. The battle over the scope of the first sale doctrine has just begun. In the end, the party that can create a distribution model that is inexpensive and can be utilized with ease will shape copyright law on the Internet.

[111] It is likely that the courts or the legislature will intervene in this issue in the near future because of the pervasive alleged infringement of music online.