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The Licensing of Intellectual Property

Until not too long ago, commercial property trading was accomplished primarily through either sale or lease, usually of tangible assets. If you wanted more rights in an asset, you bought it. Otherwise, you leased it. But with the rise of digital media as an important class of assets, and, more fundamentally, with the growing share of information products in the economy, the mechanics of trade have changed. Information is neither sold nor leased; it is now licensed under terms whose richness matches the complexity of the new bundle of rights. You can still buy a book, or a music CD, or even a patent. But increasingly common is the acquisition of only a subset of intellectual rights—a license to enjoy digital content, to use a technology, or to brand a good. From the standard end user license agreement attached to all consumer software, to the assemblage of negotiated licenses underlying every new technological product, the license transaction has taken over intellectual property (IP) commerce.

On June 19 and 20, 2010, the John M. Olin Center for Law and Economics at The University of Chicago and *The University of Chicago Law Review* hosted a conference, The Licensing of Intellectual Property. The title for our conference was not chosen by accident. The law of intellectual property has three distinct components: registration of various forms of intellectual property, protection of that property against infringement, and disposition of intellectual property in a variety of business, professional, and consumer markets. The first component involves the acquisition of IP rights in an invention, a literary work, or a trademark, which includes trade names. In these areas, the differences among the various branches IP are evident, for examination of patents is a far more complex affair than the registration of either copyrights or trademarks. These differences in IP types persist in the second component, which involves litigation over infringement of the protected IP

rights, as supplemented by the backstop doctrines of contributory infringement and inducement of infringement.

Yet the third topic, rights of disposition, is characterized by substantial similarities across classes of intellectual property. In many cases, owners, users, and consumers of patented technologies, copyrighted works, and trademarks are faced with similar issues when deciding whether to license IP rights or to opt for an alternative such as sale or infringement. Here, the legal rules differentiating licensing from other types of transactions can be highly significant. For example, IP rights are often sold in order to facilitate their assertion in infringement proceedings by parties with greater litigation expertise and resources. IP sales also allow for the creation of complementary IP pools, which increase the overall value of the patents to buyers and sellers alike. In licensing cases, by contrast, the end in view is rarely litigation. Licensing's typical use is to facilitate either the development of new products or their commercialization to end users in a variety of consumer and commercial markets. In some cases, the line between license and sale matters given the general view that it is easier to attach conditions on use to licenses than it is to attach them to sale. For example, under many circumstances only the latter is subject to the first-sale or exhaustion rules that operate for both copyrights and patents.

In many licensing transactions, moreover, the licensee pays some fee based on the intensity of its use of the licensed product. In general, this approach is used when pervasive market uncertainties make it difficult to attach a lump sum value to an IP right, especially when its future value could easily depend on cooperation between licensor and licensee. This uncertainty makes the topic of licensing far more difficult to organize because of the need to develop a comprehensive theory that can explain this wide variety of licensing transactions. Some licenses are exclusive to one licensee, while others are nonexclusive; some licenses are among merchants and professionals, while others are with consumers; some licenses are offered on a take-it-or-leave-it basis, while others are complex negotiated agreements; most licenses are voluntary, but some licenses are compulsory; some licenses are freestanding arrangements, but often parties use cross-licensing or pooling agreements; some licenses are part of standard-setting arrangements, but most are not; some licenses use open-source arrangements, but others remain strictly proprietary.

Regardless of their individual pedigrees, all licenses are vulnerable to the usual attacks that can be leveled against all types of contracts. Thus they can be attacked on the grounds that their mode of creation leaves it uncertain whether an agreement has been formed, and, if it has, on what terms. Likewise, licenses can be attacked for

fraud in the inducement, or even for insufficient disclosure of relevant information, and for creating collusive arrangements under the antitrust laws. And they can be attacked on grounds that are specific to license or user type, as with clickwrap contracts and consumer transactions. Positioned at the interface between contract law and IP law, licenses are also vulnerable to a wide variety of collateral attacks. One such common claim is that the ostensible license must be recharacterized as a sale, which would make it subject to the limitations of the first-sale rule. At this point, the parties and courts face the same challenges in deciding whether a given transaction is a sale or lease for tax or tort liability purposes. What the parties say always matters, but it is never conclusive.

The articles in this Issue address the numerous legal and market structures that can facilitate or impede licensing activity across all types of intellectual property. The diversity of issues brings with it a diversity of views. Often these articles take opposing views on such key questions as the required disclosures in consumer transactions, the desirability of allowing parties to vary via contractual arrangements the bundle of rights that licensing agreements leave with the owner and transfer to the licensee, or the relationship between property-based and contractual remedies. But the articles are unified in their treatment of IP licensing as an area of law embodying specific concerns and warranting particular attention.

The flavors of the collected contributions in this Issue can be captured through a common metaphor. Consider the copy (hard or digital) of the Symposium Issue you are presently reading. Someone else owns the copyright to it, but through a chain of transactions—mostly if not solely licenses—you are now enjoying this content. Your rights in the copy are limited by these licenses, but do you know the exact scope of such limitations? Two articles in this Issue debate whether better precontractual disclosure of license terms would help end users. Robert Hillman and Maureen O'Rourke, the Reporters of the American Law Institute's recent *Principles of the Law of Software Contracts*, advocate more disclosure, whereas Florencia Marotta-Wurgler presents empirical evidence that such disclosure would be pointless.

What if some readers of this Issue accessed it without a license? Rebecca Eisenberg argues that rightholders sometimes turn a blind eye to unlicensed uses (even of patents), especially those made for limited research purposes, which might in the long run improve the value of their creations. It is also possible that some readers had to pay more than others for the license. Indeed, the practice of licensing makes it quite easy to tailor different prices and terms to different users. Guy Rub's article critiques Judge Frank Easterbrook's well-known decision in *ProCD, Inc v Zeidenberg*, which enabled and

rationalized such tailoring. He argues that the resulting price discrimination may be less efficient than is commonly thought because it may result in less, rather than more, readership. In contrast, David McGowan argues that allowing authors strong licensing control over downstream modifications of their work may in the long run encourage creativity by increasing both the number and quality of artistic works protected by these licensing terms.

What if the unlicensed use of the content of this Issue is committed by a user who is either hard to detect or judgment proof? Jonathan Masur explores how the presence of liable third parties (here, perhaps, the university that negotiated a group license or the publisher who distributes unlicensed derivative work) incentivizes search for infringement. He shows that sometimes licenses can be written to induce socially inefficient levels of search.

Or what if the copyright holders refuse to license this *Law Review* Issue to high-value users who cannot afford to pay for the license? IP laws recognize some grounds for “compulsory licensing,” and in some places compulsory licenses are available at regulated prices below marginal cost. Richard Epstein and F. Scott Kieff attack such practices and show that they go beyond the settled injunctive and remedial rules.

Your license allows you some uses of the articles in this Issue, but not others. What remedies would the copyright holder have if you commit unlicensed uses? Some unlicensed uses (for example, distributing free photocopies to an entire class) might give rise only to breach of contract remedies, while other unlicensed uses (for example, modifying the content of the articles or selling them online) might give rise to IP remedies. Omri Ben-Shahar’s article addresses the relationship between remedies for breach of contract and infringement of IP rights, demonstrating the boundary issues and analyzing how they can be manipulated by IP owners to increase overall compensation beyond what the law intended to accord them.

While quite uncommon in the context of law review content, other copyrights and patents are sometimes sold in a secondary market. Anne Kelley, associate general counsel at Microsoft, explains how such sales create value. Buyers are not always the better users of the rights, but are instead better suited to litigate the infringement suits, or more generally have superior abilities to overcome information obstacles and friction in utilizing the rights.

Many authors of law review articles are known to value their creations more than other users of the content do. Is this a version of an endowment effect, extended to the IP context, whereby people attach more value to property they own than do potential buyers? Christopher Buccafusco and Christopher Sprigman provide experimental

evidence of what they label a “creativity effect”: owners of IP who originally created a work attach a higher value to it than owners who acquire the work by purchase only.

Many authors of academic work distribute it through open-source licenses. Mark Lemley and Ziv Shafir ask more generally who uses open-source software licenses. They present survey data that explore the differences between academic users and private firms and find that the former are somewhat more likely to adopt the open-source format than the latter.

A well-known pricing strategy, also prevalent in the licensing area, is “razors and blades” pricing, whereby a producer sells one product (the razor) at a loss in order to command profits from the sale of a second product (the blades). For instance, the owner of a law review database might charge a small fee for general access to its content, with additional fees for each article that the user reads or copies. Randal Picker explains the flaws in the conventional account from both a historical and analytical perspective. Because it is impossible to lock in customers with free razors without patent or technological protection, the razor company can charge high prices for its razors only during its period of patent protection. He argues that Gillette, the supposed inventor of the strategy, did not actually play razors and blades—or at least not when it would have been most advantageous to do so.

We think that the rich diversity of topics and approaches makes this Issue of the *Law Review* a timely contribution to the rapidly evolving field of intellectual property licensing that sheds light on a wide range of business and litigation practices. We are proud to commend to your attention this licensed copy of the *Law Review*’s Licensing of Intellectual Property Symposium.

Richard A. Epstein
Omri Ben-Shahar
Jonathan S. Masur

