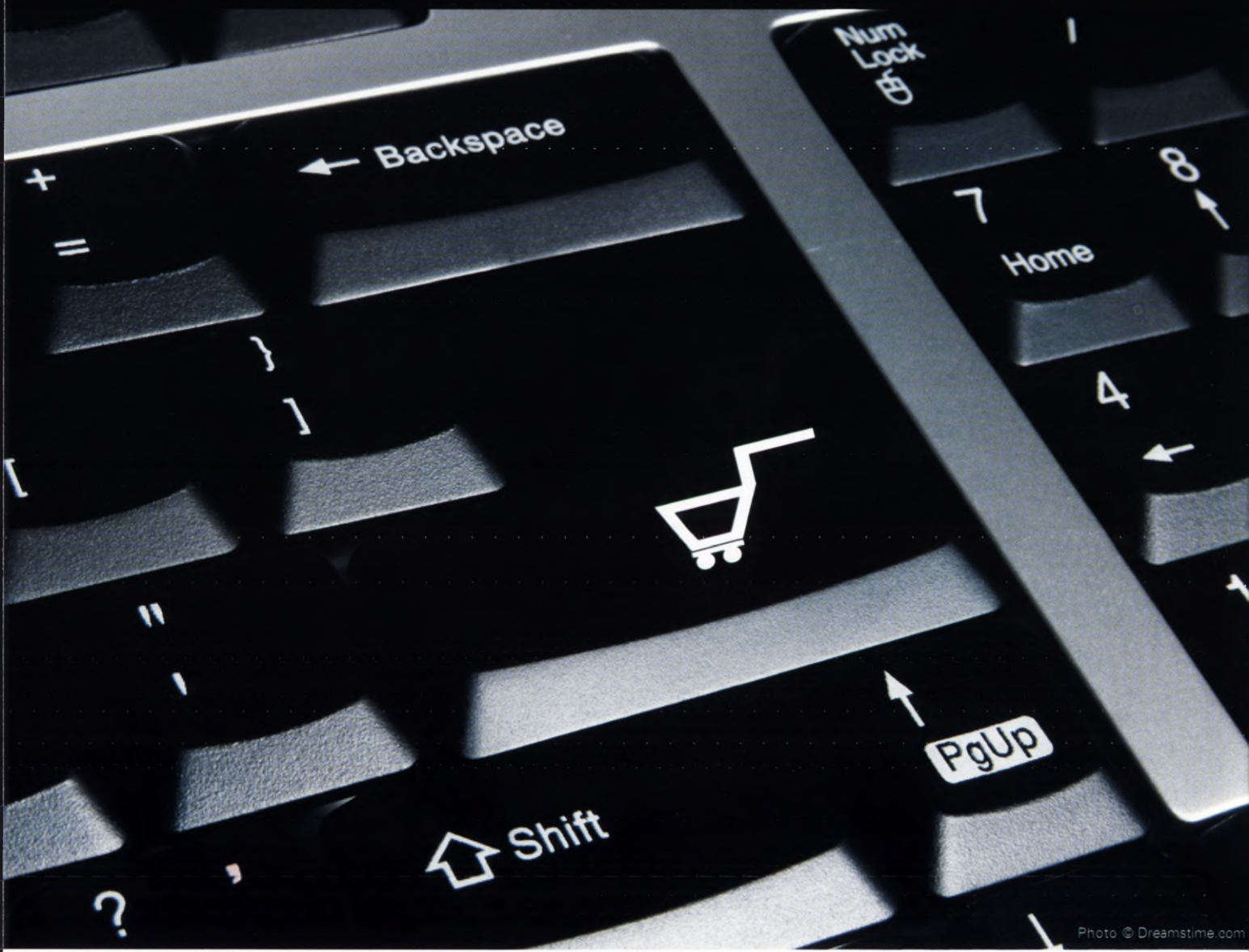
Shrink-wrap and click-wrap CONTRACTS

By David Bolton



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The increasing penetration of the personal computer (PC) into homes and businesses, along with its complementary technologies such as computer software and the internet, has led to changes in sale and distribution models. These changes have in turn led to transformations in the way that a contract is offered to the consumer. This article will examine these new contract methodologies, and will also consider some ramifications that have not yet been tested by the law.

In Australia, the first non-kit PCs sold through retailers were the Commodore PET, the Apple II and the RadioShack (Tandy) TRS-80 series in the late 1970s. Software for these PCs were purchased in two forms; the first being printed books of printed BASIC[1] that people could manually type into their PC; the second being programs saved on what were essentially audio-cassettes.[2]

As the first form required re-typing each time the computer was turned on and off, (unless it was saved to cassette, see below) the copyright owner's concern was generally limited to the photocopying of the pages. The second form (audio-cassette) could be copied using a tape-to-tape device (for example, a twin cassette deck), but it required a fair degree of fine-tuning to make a good reproduction, and suffered greatly when multi-generational copies were attempted.[3]

However, in the early 1980s the situation changed dramatically. In addition to the PC's increasing penetration of the consumer and small business markets, new technologies were introduced into the 'consumer/SOHO-space'[4] that, for the first time, allowed data (including computer programs) to be stored in a digital format (5 ¼ inch floppy disks)[5] rather than an analogue format (audio-cassettes).[6] For the first time, perfect copies could be made, and multi-generational copies could be made without error.

SOFTWARE: LICENSED NOT SOLD

It should be noted that in virtually every situation involving the purchase of packaged software, the nature of the contract is a licence to use the software rather than a 'sale' of the software. However, the physical component of the software package – for example, the disk (or CD/DVD) and manuals – are sold rather than licensed. So, in effect, when a person 'purchases' a software package, they own the disk, but not what is on it.

This kind of arrangement is neither new nor unique. Music or video, when sold as a physical product (for example, record, cassette, VHS cassette, CD, DVD or Blu-Ray), rather than as an electronic download, follows the same arrangement. The purchaser 'owns' the physical media, but is granted a licence to listen to the music or watch the video. This licence will usually contain conditions such as the prevention against public broadcast or reproduction of the contents. Generally speaking, anything involving the transference of copyrightable material via a physical medium is likely to have a similar sort of licence arrangement.

THE RISE OF SOFTWARE PIRACY

Once software could be digitally copied, it wasn't long before copyright infringement (in the form of 'software piracy') became more widespread. In order to combat the emerging practice of software piracy, software publishers and distributors tried various methods of protecting their intellectual property from unauthorised reproduction and distribution. Some of these copy protection methods were technological in nature (for example, encryption, use of dongles, bit-slip marks, etc); others were more prosaic (for example, a prompt to enter a word from a selected page/paragraph in the accompanying manual).

Typically, software purchasers 'own' the physical disk, but are only granted a licence to use the copyrightable material on it.

However, on its own, copy protection addressed only the reproduction and distribution concerns. It had no impact on the other restrictions that the publishers wished to impose on the 'users'. Furthermore, copy protection did not address the issue of communicating to the 'user' that they were being granted a limited licence rather than title to the contents of the medium. Thus, it became necessary to find a manner in which to:

- communicate the fact that the purchaser was entering into a licence agreement with the copyright-holder,
- communicate the terms and conditions of the agreement being offered to the purchaser by the copyright-holder or publisher; and

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- fulfil the general contractual requirement that the parties clearly communicate acceptance of the terms and conditions.

The first solution was the 'shrink-wrap' contract.

THE SHRINK-WRAP CONTRACT

In its simplest form, the shrink-wrap contract consists of three parts:

1. the box or package containing the software and manuals;
2. an external heat-treated shrink wrap of transparent plastic; and
3. a large sticker describing the terms and conditions of the licence.

The idea is that the potential purchaser has the opportunity to read the terms and conditions of the contract and indicates agreement to them by opening the package or breaking the seal.

The legality of shrink-wrap contracts

Despite the fact that millions of software packages are sold each year, there is very little case law and even less legislation addressing the legitimacy of the shrink-wrap contract. In Australia, legislation that addresses electronic transactions (see below), does not address shrink-wrap contracts.

As far as this writer has been able to determine, none of the world's common-law jurisdictions have enacted legislation that legitimises the shrink-wrap contract. An attempt was made in the US by the National Conference of Commissioners on Uniform State Laws (NCCUSL) and the American Law Institute (ALI) in 1999. Originally, it was an attempt to modify the Uniform Commercial Code (UCC).[7] However, after the ALI withdrew its support in 2002, the NCCUSL responded by renaming it the Uniform Computer Information Transactions Act (UCITA) and attempted to get it passed by all of the US states. To date, only two states – Virginia[8] and Maryland[9] – have ratified it. The main objections to the UCITA, raised by various attorneys-general and consumer groups, are that it weakens consumer protections and rights, and is too favourable towards the software publishers.[10]

The ALI made a more recent attempt (May 2009) to introduce uniformity, through its 'Principles of the Law of Software Contracts'. It is too early to tell if this effort will enjoy any more luck than previous attempts.[11]

Although there is no legislative support for shrink-wrap contracts, there have been cases dealing with the issue. However, almost all of them are US-based.

The leading case for supporting the enforceability of shrink-wrap contracts is *ProCD, Inc v Zeidenberg*, though strictly speaking it was not just a shrink-wrap contract.[12] Matthew Zeidenberg purchased, for $150, a single copy of ProCD's Select Phone, a database of phone numbers that had cost ProCD over $10 million to compile. The shrink-wrap licence stated that it was for personal use only and explicitly prohibited its use for commercial purposes. The terms were repeated on screen when the software was installed (thus it was both shrink-wrap and click-wrap). Zeidenberg developed his own search engine and started selling this, along with ProCD's data for a much cheaper price than ProCD did for commercial sales. He believed that as he was not using ProCD's program, he was not infringing copyright. ProCD sued and the US District Court found for Zeidenberg. However, an appeal to the US Court of Appeals for the Seventh Circuit found for ProCD, stating that unless the terms were unconscionable or otherwise disallowed by contract law (which these were not), a buyer was required to honour the terms of the shrink-wrap licence.

The decline of shrink-wrap contracts

The use of shrink-wrap contracts began to decline in the mid-1980s for a number of reasons, the two most important being:

1. the increasing length of the End User Licence Agreements (EULA); and
2. changes in the retail merchandising methods used to sell software.

The first reason is fairly self-explanatory. As software publishers/distributors added more and more terms and conditions to EULAs, the sticker required became larger and larger, to the point where it was the same size as the box. For a little while, the boxes became larger (mainly because of the increasing size of user manuals) and they could accommodate these very large stickers, but eventually a change became necessary. For a short while, the software publishers/distributors tried external stickers that merely said something like 'By opening this package you agree to the terms and conditions printed on the EULA enclosed in this package'. However, this was not a good solution because the user could easily claim that they had no way of knowing to what they were assenting.

At this point, the software publishers/distributors slightly modified their practice; instead of having a shrink-wrap contract on the outside of the box; they sealed the flaps of floppy disk envelopes with a sticker. This sticker usually said something along the lines of 'Please read the accompanying terms and conditions document. Breaking this seal indicates acceptance of the terms and conditions.'

This was the most frequently used solution until the

advent of the world wide web and the need to deal with downloaded software.[13]

The second reason for moving away from external shrink-wrap contracts arose because of the way that retail stores were selling software. When software is mentioned, the majority of readers think of business products, such as Microsoft Office. However, the reality is that in terms of unit sales, computer games outsell business products by at least a thousandfold.

Therefore, as PCs became increasingly mainstream, retailers started to carry an increasing number of computer games and were no longer content to keep the software locked away in glass cabinets because the customers wanted to be able to read the box for either a description of the game or for the required PC specifications. This also made attending to customers in the area very labour intensive (that is, opening and closing locked glass cabinets). The increasing number of games also put software publishers/distributors under pressure to decrease the packaging size, so that more variety could be displayed in a finite space.

By the mid-1980s, retailers decided that the best way to sell game software was to remove the contents and place the empty box on display (similar to video stores). This allowed the customer to read the box, while the contents (including the EULA) were kept secure. When the customer made their selection, the contents were retrieved and the sale made. Of course, this presented a problem with an external shrink-wrap contract, because the customer could no longer read the contract prior to purchase, nor indicate acceptance by opening the package. So sealing the floppy disks resolved this problem as well.

Interestingly, improvements in retail store security technology (for example, magnetic strips and tough plastic secure-cases) would have facilitated the return of the external shrink-wrap contract, but this is now unlikely to happen because click-wrap is so predominant.

THE CLICK-WRAP CONTRACT

The development of the world wide web in 1994[14] initially had little impact on the sale of computer software. However, when software publishers began to distribute their products via an internet download, it was necessary to find a new solution.

A click-wrap (also known as click-thru, click-through, click-and-accept, web-wrap) contract is one where the user is presented, usually during the installation of the program, with the question along the lines of 'Do you agree to be bound by the terms of this agreement?' There is usually a choice of two buttons; an affirmative button ('I agree', 'Yes') and a negative button ('I do not agree', 'No'). The terms of the EULA are usually presented either as a scrolling text-box, or sometimes a new window that opens automatically. Some software packages actually require that you scroll to the bottom of the terms text box before the affirmative button is selectable, others may require that the user clicks on a box that states something along the lines of 'I have read and understand the terms and conditions of the EULA' in addition to hitting the 'I agree' button.

If the user presses the affirmative button, the installation process progresses until the software is installed and ready to use. If the user presses the negative button, then the installation process stops and the user is usually returned to their PC desktop.

The click-wrap contract is now the most commonly used form of contract for computer software, whether it is purchased as a physical product or by download.

Disadvantages of click-wrap

Click-wrap contracts have two main disadvantages.

The first arises because there is no opportunity to read the terms and conditions and therefore 'accept' the contract before the product has been purchased. For example, a user purchases a software package at a retailer; they take the software home and open the product; they open the CD envelope and have the opportunity to see the unique CD-Key; they begin to install the software but realise they don't agree with one of the conditions; they then return to the store with the opened package and request a refund because they do not agree with the licence condition and therefore did not install the software. Now imagine how difficult this is to do.

Many retailers state that they will not refund software purchases, or that they will only exchange faulty products.[15] They usually display these signs very clearly because they wish to make it clear that this is a condition of the contract >>

Shrink-wrap contracts assume that the purchaser can read the terms and conditions and indicate agreement to them by opening the package or breaking the seal.

for the sale of the goods. So what can the user do?

In effect, there are two contracts for the software. There is a contract of sale between the retailer and the user for the purchase of the software, and there is a contract of licence between the software publisher and the user for the use of the software. So can these be reconciled?

One resolution would be to construct an implied term in the contract of sale that makes it dependent on the user agreeing to the terms of the licence agreement. In effect, the contract of sale is not fulfilled until the user indicates agreement with the licence conditions.

Alternatively, it may be possible to make use of the *Trade Practices Act* 1974 (Cth) (TPA).

Section 74A(4) of the TPA states that:

'the corporation shall be deemed, for the purposes of this Division, to have manufactured the goods.

(4) If:

(a) goods are imported into Australia by a corporation that was not the manufacturer of the goods; and

(b) at the time of the importation the manufacturer of the goods does not have a place of business in Australia.'

The problem is that the situation described does not appear to fulfil any of the grounds of action (for example, unsuitable goods, merchantable quality, false description, etc) described in Division 2A of the TPA.

Presuming that the retailer has refused to provide a refund, then perhaps the best course would be to seek out the Australian importer/distributor in its capacity as agent for the software publisher and seek compensation for the loss suffered in not being able to return the package to the retailer.

The second disadvantage with click-wrap contracts arises when there is an ongoing contractual relationship and the supplier unilaterally changes the terms and conditions. In July 2007, the virtual reality world of Second Life became headline news when it changed its terms of service so as to ban gambling. Some users were heavily invested in this area and lost considerable virtual money. While this might seem minor, the virtual money used in Second Life does have a fixed exchange rate for US dollars in the real world, so these users experienced a measurable real world loss.

The Massive Multi-player Online Role Playing Games (MMORPG) – such as World of Warcraft or Lord of the Rings Online – also periodically alter their terms of service. Users usually pay between one month to one year in advance, so the question arises – if you disagree with a new term in the agreement, are you entitled to get back the unused portion of the amount paid?

To date, there have been no reports of this kind of claim.

Browse-wrap

In recent years, a variant of the click-wrap (called 'browse-wrap') has developed, primarily for use on websites. Unlike click-wrap, the user is not presented with the terms and conditions before they can progress. Instead, there is usually a statement along the lines of 'By browsing this website you agree to the terms and conditions of use' or else a visible button labelled 'Conditions of Use'. This will normally be accompanied by a hyperlink connecting to the web page containing the terms and conditions. This means that it is possible to use the website without reading the terms and conditions first, if the user chooses to do so.

Understandably, this leads to difficulties in proving breach of contract.

Shrink-wrap, click-wrap and browse-wrap case law

Initially, US courts saw shrink-wrap licences as proposals for amending a contract of sale formed at the time when the customer purchased the shrink-wrapped package. Therefore, unless all the terms were completely visible at the time of purchase, they were held to be unenforceable on the basis that the purchaser could not have given their informed consent to them.[16] However, in the leading case of *ProCD Inc v Zeidenberg*,[17] it was held that the vendor of the shrink-wrapped software was making an offer, and could therefore dictate a reasonable method of conveying acceptance – in this case, a failure to return the software. As mentioned earlier, this is problematic when the retailers do their best to refuse returns.

ProCD Inc v Zeidenberg has been followed in several US courts,[18] though support for it has not been unanimous. Some cases have added conditions; for example, in *Hill v Gateway 2000* it was held that the terms were enforceable as long as a refund was offered if the terms were rejected by the purchaser.[19] Other cases have distinguished it – for example, in *Softman Products Co LLC v Adobe Systems Inc*, it was held that a software vendor (as opposed to the publisher) was not bound by the terms of the of the shrink-wrap EULA because there was no privity of contract between the vendor and licensor (publisher).[20] Further, at least one district court (Kansas) has rejected the *ProCD Inc v Zeidenberg* approach completely, and held that a term in a shrink-wrap licence was not enforceable because it did not constitute part of the contract.[21]

The enforceability of click-wrap licences appears to be supported by the history of shrink-wrap contracts and, in fact, presents a stronger case for enforcement because the purchaser has the opportunity to read all the terms and conditions of the contract prior to acceptance (by clicking >>

> The click-wrap contract effectively involves a contract of sale between the retailer and the user, and a contract of licence between the software publisher and the user.

on 'ok').[22] In contrast, browse-wrap is not as strongly accepted at the moment because these types of contract do not require clicking on a button to indicate express consent to be bound by the terms.[23]

THE FUTURE OF CLICK/SHRINK-WRAP CONTRACTS IN AUSTRALIA

During the late 1990s and early 2000s, the Commonwealth, the states and territories all enacted *Electronic Transactions Acts*.[24] These Acts do not specifically address click/shrink-wrap contracts but, rather, endorse the legality of the concept of electronic commerce and the use of electronic forms in situations where the law requires giving information in writing.

In June 2001, the Copyright Law Review Committee (CLRC) released an issues paper on the relationship between copyright and copyright law. Included in this paper was a section regarding mass-market agreements, with particular reference to shrink-wrap and click-wrap agreements.[25] Of the 36 submissions made by various bodies, 9 addressed the issue of shrink-wrap and/or click-wrap licence contracts:

1. Australian Consumers' Association (ACA)
2. Australian Copyright Council (ACC)
3. Australian Digital Alliance (ADA)
4. Australian Publishers' Association (APA)
5. Business Software Association of Australia (BSAA)
6. Copyright Agency Limited (CAL)
7. Dr Adam Gatt – RMIT University[26]
8. International Federation of Phonographic Industries (IFPI)
9. International Intellectual Property Alliance (IIPA)

The ACA's concerns regarding click/shrink-wrap formed part of its overall dissatisfaction with available '...remedies for one-sided contracts the contents of which the consumer has scant capacity and opportunity to negotiate'.[27]

In *contra*, the ACC claims that 'Individual consumers may not have the same ability to negotiate as institutional consumers, but they are not devoid of negotiating power.'[28] However, the only example it provides of a consumer negotiating such a contract is Monash University.[29]

The ADA expressed concern about the producers of EULAs' efforts to exclude copyright and trade practices laws. It recommended the use of a 'model licence', with official or semi-official endorsement.[30] It also provided several case studies, including a description of Microsoft Corporation's licence for the use of its version of Kerberos (a network authentication protocol), and the subsequent threats to sue the *Slashdot* website when users posted the specifications online.[31]

Unsurprisingly, the APA submitted that click/shrink-wrap contracts should continue to be enforceable because they are '...an efficient means to conduct certain types of transactions involving uniform terms on a mass-market basis. And not all limit the users' freedoms.'[32] Furthermore, it believes that 'Were non-negotiated licences to be used in the future in an unfair manner...' then consumer protection and fair trading regulations would be the most appropriate avenue for remedies rather than '...heavy-handed, blanket restrictions on intellectual property agreements'.[33] These views were also supported by the BSAA,[34] IFPI[35] and IIPA.[36] The CAL also supported the status quo and recommended '...that the CLRC should not make any recommendations that make the position in Australia different from might be called 'world standards', especially since most of the copyright material

in use in Australia comes originally from overseas'.[37] The consensus appears to be that the main reason for making click/shrink-wrap contracts enforceable in Australia is that US courts have declared them enforceable in the US.

In the seven years since the CLRC report was released, there has been no legislative action regarding click/shrink-wrap, nor have the courts had the opportunity to provide any guidance. In fact, the only 'official' mention of click/shrink-wrap is an Australian Tax Office: Goods and Services Tax Ruling on items that attract GST.[38]

If a case ever does make it to an Australian court, it is likely to involve an argument on an exclusion term that may be unconscionable, contrary to consumer protection laws or to copyright 'fair use' provisions. Whether in that situation the court will take the opportunity to officially endorse the enforceability of click/shrink-wrap contracts remains to be seen. ■

Notes: **1** Beginners All-purpose Symbolic Instruction Code – a very simple programming language. **2** Though there were 'special' computer tapes, most people used high-fidelity audio-cassettes because they were cheaper. **3** This is because the digital data was stored in an analogue format. **4** Small Office, Home Office. **5** Though floppy disk drives were available for some PCs in the late 1970s, their relatively high cost at the time meant that it wasn't really until the early 1980s that they became ubiquitous. **6** Digital storage is superior to analogue storage when it comes to long-term storage, retrieval, reproduction and reconstruction of missing data. **7** Proposed UCC, Article 2B. **8** http://leg1.state.va.us/cgi-bin/legp504.exe?001+ful+SB372ER. **9** http://mlis.state.md.us/2000rs/billfile/hb0019.htm. **10** David Toft, 'Opponents blast proposed US software law', *CNN.com*, http://www.cnn.com/TECH/computing/9907/12/ucita.idg/index.html. **11** http://www.ali.org/index.cfm?fuseaction=projects.proj_ip&projectid=9. **12** 86 F 3d 1447 (1996). **13** Why not the advent of the internet? The reality is that electronic consumer downloads really did not start until online shops appeared and these all came about after the introduction of the world wide web. **14** This date is based on the formation of the W3C consortium by Tim Burners-Less in October 1994. **15** There are exceptions – for example, some games retailers have a seven-day 'no questions asked' refund policy. **16** *Step-Saver Data Systems Inc v Wyse Technology and Software Link Inc* 939 F 2d 91 (1991). **17** 86 F 3d 1447 (7th Cir. 1996). **18** For example, *MA Mortenson Co, Inc v Timberline Software Corp* 998 P 2d 305 (2000), *Brower v Gateway 2000 Inc*, 86 F. 3d 1447, 1454 (7th Cir. 1996). **19** 1998 NY Slip Op. 07522, 1998 WL 481066 (NYAD 1 Dept.) Supreme Court Appellate Division, First Department, August 12, 1998. **20** *Softman Products Co LLC v Adobe Systems Inc* 171 F Supp. 2d 1975 (CD Cal, 2001). **21** *Klocek v Gateway Inc*, 104 F Supp 2d 1332 (D.Kan 2000). **22** *Compuserve v Patterson*, (6th Cir. July 22, 1996); *Hotmail Corp v Van$ Money Pie, Inc*, 1998 WL 388389 (ND Cal. April 16, 1998); *Groff v America Online Inc*, 1998 WL 307001 (RI Superior Ct, May 27, 1998); *In re Real Networks, Inc Privacy Litigation*, 00c1388,2000 WL 631341 (ND Ill. May 8, 2000). **23** *Pollstar v Gigmania Ltd*, 2000 WL 33266437 (ED Cal. Oct 17, 2000). **24** *Electronic Transactions Act* 1999 (Cth), *Electronic Transactions Act* 2000 (NSW), *Electronic Transactions Act (NT)* 2000, *Electronic Transactions Act* 2000 (SA), *Electronic Transactions Act* 2000 (Tas), *Electronic Transactions (Vic) Act* 2000, *Electronic Transactions Act* 2001 (ACT), *Electronic Transactions (Queensland) Act* 2001, *Electronic Transactions Act* 2003 (WA). **25** CLRC, *Copyright and Contract – Issues Paper June 2001*, p17. This document, the report, the discussion paper and the various submissions can be found at http://www.ag.gov.au/www/agd/agd.nsf/Page/Copyright_CopyrightLawReviewCommittee_CLRCReports_CopyrightandContract_CopyrightandContract as at 20 September 2009. **26** Dr Gatt's submission was the preliminary findings of a study he was conducting as part of a Masters degree in E-Business. It contained substantial information on case law and concluded by recommending better education of users. **27** Australian Consumers' Association, *Australian Consumers' Association Comment to the Copyright Law Review Committee Reference on the Relationship between Copyright and Contract Law*, 10 August 2001, p5. **28** Australian Copyright Council, *Second Submission to Copyright Law Review Committee on Copyright and Contracts*, October 2001, p7. **29** *Ibid* at p4, fn8. **30** Australian Digital Alliance / Australian Libraries Copyright Committee, *Australian Digital Alliance / Australian Libraries Copyright Committee Submission to the Copyright Law Review Committee on Copyright and Contract*, August 2001, p18. **31** *Ibid* at p27. **32** Australian Publishers Association, *Copyright and Contract Reference*, 10 August 2001, p4. **33** *Ibid* at p5. **34** Business Software Association of Australia, *Submission to the Copyright Law Review Committee Copyright and Contract Reference*, 2001, pp1-2. **35** International Federation of Phonographic Industries, *IFPI Comments on the Copyright Law Review Committee Issue Paper*, 1 August 2001, pp7-8. **36** International Intellectual Property Alliance, *Submission to CLRC*, 9/8/01, p6. **37** Copyright Agency Limited, *Copyright and Contract*, 13 August 2001, p6. **38** GSTR 2003/8 – Goods and services tax: supply of rights for use outside Australia – subsection 38-190(1), item 4, para (a) and subsection 38-190(2) (17 October 2007).

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