

Scherer Smith & Kenny LLP serves mid-sized and fast-growing entrepreneurial companies. From complex litigation to business, real estate, intellectual property and employment law, our team brings strategic thinking, pragmatism and intense dedication to our clients' success.



When Do "Proposals" Become Binding Contracts?

How long or specific must a document be before it becomes a binding contract? The answer, perhaps surprisingly, is that the actions of the parties become more important the fewer the words that constitute the agreement under consideration. This issue was addressed recently in *First National Mortgage Company vs. Federal Realty Investment Trust*, 631 F. 3d 1058 (9th Cir. 2011), a case that addressed a ground lease between a landlord and property developer. The developer argued that the signed document between them was not binding, whereas the landlord sought to enforce it. Ultimately, the landlord was awarded \$15.9 million for the developer's anticipatory breach of a binding contract between the parties.

The document in question totaled just one page and nine paragraphs, entitled "Final Proposal," and succeeded several years of negotiations and several prior documents, including a "Counter Proposal" and a "Revised Proposal." Importantly, this Final Proposal stated at the end that it was accepted "...by the parties subject only to approval of the terms and conditions of a formal agreement."

Thereafter, the parties held protracted negotiations over the formal agreement's provisions, including the lease's term of years, which the developer later claimed in the suit to be an essential, disputed term. While the parties bickered, the 2008 financial meltdown broke, the ground lease's value declined, and the developer got cold feet and wanted out. Ultimately, the Federal court was asked to interpret the "Final Proposal."

The court determined the document was binding, and awarded the landlord damages, which award was affirmed by the 9th Circuit Court of Appeals. The court rejected any possibility that the Final Proposal was not binding, pointing out that it was conditioned "only to approval of the terms and conditions of a Formal Agreement." The court brushed aside arguments that the lease term, an essential term, had not been specifically agreed to, ruling that this provision could be determined by a jury:

"The mere fact the lease term is 'essential' does not mean that it has to be expressed in the contract. On the contrary, although extrinsic evidence cannot be used to supply an essential term, it can be used to 'explain essential terms that were understood by the parties but would otherwise be unintelligible to others.' [Citation omitted] Indeed, 'California courts have not hesitated to imply a term or of duration when the nature of the contract and surrounding circumstances afford a reasonable ground for such implication. [Citation omitted]'

Importantly, the court concluded that substantial evidence supported the jury's findings that the parties intended the Final Proposal to be enforceable and further that the parties intended the options in the Final Proposal to set a ground lease duration of ten years.

August 2011

In This Issue

[When Do "Proposals" Become Binding Contracts?](#)

[Vernor v. Autodesk Will Software have a Second Life?](#)

[ICANN Approves Historic Expansion of Top Level Domain Names](#)

[Partner Notes](#)



Bill Scherer

Welcome to the summer edition of *Perspectives*. It's always around this time of year that I most appreciate living in Northern California, with its warm weather, outside activities, beautiful, lazy weekend getaways, and outdoor entertaining. This is especially true this year after a winter that seemed to keep its wet, clammy grip on the region long, long after it had no reasonable reason to do so. Do you even remember more than one or two days of warm springtime weather? Sure, spring

What can be learned by this case, a one-page memorandum that cost the developer millions? First, that intent can be interpreted by conduct, regardless of a document's length, especially if it is not comprehensive. Second, it is imperative within any document that is not meant to be binding to state that it is, in fact, "nonbinding," and further that "no binding agreement shall exist until a substantive, definitive agreement has been mutually agreed to and executed by the parties."

If you have any questions concerning negotiations of commercial or real property transactions, please contact William Scherer at wms@sfcounsel.com.

- Written by Bill Scherer



Vernor v. Autodesk, Inc. Will Software have a Second Life?

Timothy S. Vernor sells stuff on eBay, a lot of stuff actually. Vernor purchased a few authentic used copies of Autodesk's AutoCAD Release 14 software from the original purchasers of the software. He then listed the software copies for sale on eBay. Actually, he listed copies for sale on three different occasions. Each time, Autodesk filed a Digital Millennium Copyright (DMCA) Takedown Notice with eBay, at which point eBay took down Vernor's auction. All three times, Vernor filed a counter-notice, resulting in eBay reinstating the auction. With the third takedown notice submission from eBay, however, eBay suspended Vernor's account.

Vernor filed suit in the Federal District Court for the Western District of Washington, seeking a ruling that the resale of the AutoCAD software did not violate Autodesk's copyright. The District Court granted summary judgment in favor of Vernor, concluding that Vernor's actions were covered by two Copyright Act "affirmative defenses" (defenses which apply even if the underlying allegations are proven): the first sale doctrine and the essential step defense.

The first sale doctrine (17 USC Section 14) allows an owner of a *particular* copy of a copyrighted work to sell his or her copy without the copyright owner's authorization. This applies, for example, to the sale of a book at a used book store. The essential step defense, codified at 17 USC Section 117(a)(1), allows the "*owner* of a copy" of software to make a copy of the program if the copy is "created as an essential step in the utilization of the computer program in conjunction with a machine and ... is used in no other manner." Thus, neither defense is available unless the person asserting the defense is an owner of a copy of the copyrighted work.^[1]

AutoCAD, like most retail software, is provided to the consumer pursuant to the terms of a "shrink wrap license agreement," to which the purchaser is bound by virtue of his or her purchase. This license contains significant limitations, including a prohibition on the transfer without the consent of Autodesk.^[2]

The Ninth Circuit employed a relatively straightforward analysis to conclude that Vernor did not own the AutoCAD copies. Thus, the Copyright Act affirmative defenses noted above were not available, and the Ninth Circuit reversed the District Court's grant of summary judgment to Vernor, and remanded for further proceedings. Vernor has now asked the Supreme Court of the United States to hear an appeal of the Ninth Circuit's decision.^[3]

We believe, the Supreme Court should grant review, as the implications of the Ninth Circuit's decision could be far-reaching. For example, consider for a moment the impact were "book wrap licenses" (or shrink wrap licenses applied to books) to become the norm. The exchange and sale of used books would certainly dwindle. And what of libraries? Already, libraries are paying more for e-book licenses than they would for traditional books. Moreover, HarperCollins has limited the number of checkouts per e-book license to 26, at which point the libraries would have to purchase another license.^[4] According to HarperCollins:

skiing is great, but on July 4th?

Perhaps it's this long, dark lead-in to the year that makes me so thankful for the summer weather that has finally arrived, and in anticipation of the indian summer that is still to come.

I feel largely the same way about my and my client's business prospects here in Northern California. We Northern Californians have all persevered through an equally dark period for business. In the commercial areas of my practice – business law, real estate, and software licensing – Northern California seems to be a bright spot in an otherwise dreary national economy.

Though it is hard to say the ultimate negative impact of the seven week debt ceiling impasse that just resolved, I can only say that people are getting more excited to do deals and take advantage of what they see as low prices of entry and a hopeful, profitable future. Restaurant and commercial spaces are leasing, companies are buying companies, and new, more efficient generations of software are finding eager customers. Growth is in the air. It is great to see people taking risks because they see tangible rewards, and it's been a long time coming. Some people I've talked to say this is simply another bubble, the so-called "social networking bubble." Certainly there is some truth to this, especially in home prices in the South Bay and Peninsula.

We have serious concerns that our previous e-book policy, selling e-books to libraries in perpetuity, if left unchanged, would undermine the emerging e-book eco-system, hurt the growing e-book channel, place additional pressure on physical bookstores, and in the end lead to a decrease in book sales and royalties paid to authors.[5]

There is a petition against HarperCollins policy being circulated, and some libraries are boycotting the publisher. It would not be a surprise if the HarperCollins policy somehow lands in court in the near future.

A thorough analysis of the potential implications of the decision is set forth in the Electronic Frontier Foundation's (EFF) amicus (friend of the court) brief to the Supreme Court.[6] As the EFF brief writers eloquently put it:

For more than a century, the first sale doctrine has been a critical part of the statutory balance struck by courts and Congress between the interest of copyright owners and the public. On the one hand, copyright's exclusive right of distribution gives the copyright owners control over the first vending of their works. On the other hand, individuals have the rights over the physical objects they have purchased and now own. After an individual copy has been sold, the first sale doctrine puts further dispositions of the copy beyond the reach of the copyright owner. The first sale doctrine thus ensures a "second life" for copyright works in libraries, archives, used bookstores, online auctions, and hand-to-hand exchanges.

On the other hand, in an increasingly digital world in which copyrighted works exist independent of "physical objects," doesn't it make some sense to limit the transfer of digital copyright, including software? It would represent a fundamental change indeed if we were able to sell our copy of the Angry Birds "app" for half the price after we got fed up with those stupid green pigs.

Whether the Supreme Court grants review or not, it is possible that Congress will react to the Ninth Circuit's decision in *Vernor v. Autodesk* with yet another amendment to the Copyright Act. In the meantime, be careful what you do with your old software products. And for you developers out there, be careful what goes into your development and license agreements.

Please contact Brandon Smith at bds@sfcounsel.com for more information.

[1] It is worth noting that Congress recently amended Section 117 to allow a computer owner to copy software for maintenance or repair purposes. (See 17 USC Section 117(c).)

[2] It should be noted that, irrespective of whether a Copyright Act violation occurred, Autodesk can raise a claim of breach of contract against the first owner for selling the software in violation of the license agreement.

[3] The case status is available on the Supreme Court's website at: <http://www.supremecourt.gov/>

[4] Libraries concerned over having to rebuy e-books, Sunday, April 17, 2011, Anya Sostek, Pittsburgh Post-Gazette (available at <http://www.post-gazette.com/pg/1107/1139998-53-0.stm#ixzz1S70hE1ug>)

[5] *Id*

[6] Available at: http://www.eff.org/files/efilenode/vernor_v_autodes/VernorCert.pdf



ICANN Approves Historic Expansion of Top Level Domain Names

Currently there are only a small number of top-level domains, such as .com, .net, .org, as well as country-specific domain names that are used on the Internet. While this has kept the universe of top level domain names contained, it also has restricted some companies' ability to grow their brand. Thanks to recent changes by ICANN (Internet Corporation for Assigned Names and Numbers), which is the international authority over top-level domain names, this is about to change beginning in 2012.

ICANN approved the expansion of generic top level domain names to allow organizations and companies to create domains for their brands (such

But from my perspective and based on the work I do, the base of this economic recovery is far wider, extending to clients in manufacturing, professional services, insurance, new initiatives, and mid-sized businesses. There is no doubt that challenges remain and the economy is still fragile, but if you live, work, or depend on the economy here in Northern California, the old saying remains true: "There's no place like here."

as .google or .apple). Applicants could also apply to create a generic top level domain name, such as .smartphone or .computers. Once an applicant obtains the top level domain they basically become the registrar of that domain and can determine who and who cannot register for the domain.

While this is an exciting new option for companies, the process will be both lengthy and expensive. The application fee will be approximately \$185,000 with an annual fee of \$25,000 and the application will likely be very detailed so that ICANN can determine that the applicant has the legal right to own such a top level domain name. However, ICANN is still determining the final application process and details so these fees may change. Despite the cost, this will likely result in significant interest, primarily, from larger, well-funded companies.

Applications for new generic top level domains will be accepted from January 12, 2012, to April 12, 2012. While new top level domains will likely begin appearing in approximately a year, it may take much longer to realize the full ramifications of this expansion on the domain registration industry.

Along with the possibilities of expanding brands, an increase in trademark disputes is likely, but remains to be seen.

If you have any questions concerning this new option or the process involved in applying for such a top level domain name, please contact Brandon Smith at bds@sfcounsel.com.

- Written by Brandon Smith

Areas of Practice

[Business: Real Estate: Intellectual Property and Employment Law:](#)

[Litigation and Dispute Resolution: Nonprofit: Estates and Trusts](#)

©2007-2011 Scherer Smith & Kenny LLP. All Rights Reserved.

[Disclaimer/Privacy Statement](#)

For more information: www.sfcounsel.com