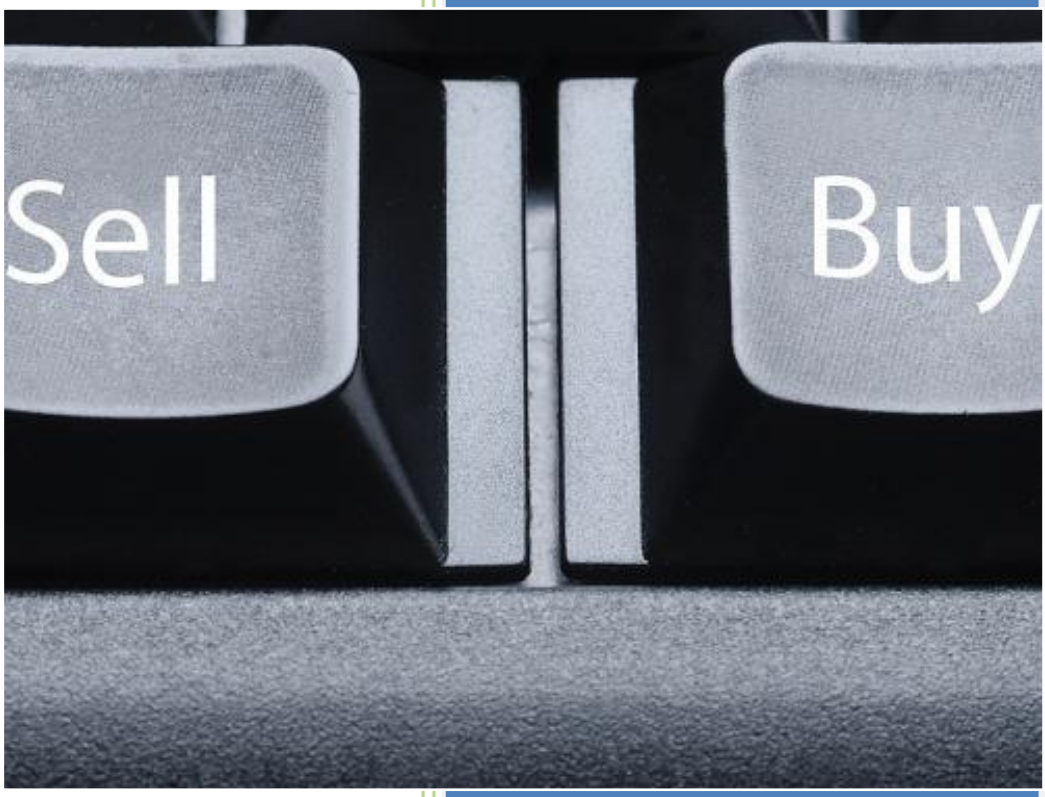
A Guide to Second-hand Software



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A Guide to Second-hand Software

Prologue

'A Guide to Second-hand Software' was written by Noel Unwin of Discount-Licensing Limited and was previously published as a three-part article within The ITAM Review during May and June 2012. It was entitled 'Quick Guide to Second-Hand Software' and the original three parts can be found using the links below to The ITAM Review website. The objective was to set out the facts surrounding the second-hand software industry in terms of structure and legalities. It also attempts to demystify the mist spread by individuals and companies that are motivated by means other than that of providing a true picture of the secondary software markets.

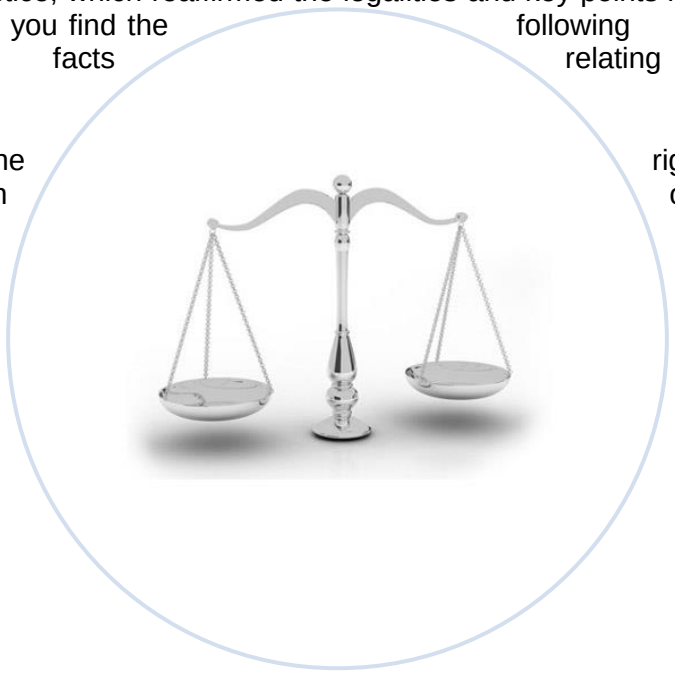
Part 1: Industry Dynamics (23rd May 2012)

Part 2: Demystifying the Mist (1st June 2012)

Part 3: The Legalities (19th June 2012)

Following the publication of the three-part article, a landmark decision was reached by the European Court of Justice, which reaffirmed the legalities and key points raised within the articles. As such, we trust that you find the following guide helpful in understanding the facts relating to secondary software licence industry.

Every business has the right to be armed with the correct information in order to make an informed decision when considering the purchase or disposal of disused software licence assets.



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Part 1: Industry Dynamics

Over the past decade, you may have come across articles relating to 'second hand software', otherwise referred to as 'pre-owned' or 'remarketed' software -- also sometimes known across the pond as the 'IT aftermarket'. These articles have originated from sources such as journalists within the IT arena, bloggers and legal eagles -- whilst the objectives of these opinion makers will be to try to paint a clear black and white picture of the development of the second hand software industry, some associated statements from the software vendors in this space may seek to cloud your judgement and paint a shady tone of grey.

For instance, your business may have been the lucky recipient of an invitation to audit and therefore received guidelines from a software vendor, which may have included statements relating to the use of pre-owned software licensing.

The mixed messages surrounding the industry do indeed add confusion to the mix, especially when businesses are faced with making proactive or reactive licence compliance decisions. So let's have a stab at aligning some of the truths and dispelling the myths surrounding the second hand software market.

Searching For Clarity

- The first part of this analysis will define the so-called "sub-market boundaries" of the second hand software industry and elaborate on their independency. We will then look at the interdependency of the tiers working within each market.

- The second part will go on to examine some of the myths that have evolved in terms of licence compliance and the business models / processes that are adopted by players within the secondary software industry.

- Finally, part three will consider the legalities of the industry, in terms of the software vendor's Licence Agreement (LA) terms (transfer provisions) as well as local and regional governing laws.

- Following the relevance of the landmark ruling by the European Court of Justice on 3rd July 2012, we decided that in the interest of completeness, we should elaborate upon the three part article published within The ITAM Review by including a summary of the court ruling, in layman's terms.

NOTE: *For the reader's transparency, my own secondary software experience began in 2003 and continues to this day with Discount-Licensing Limited, the business responsible for setting up the second hand market in Microsoft 'Volume' software licensing. However, to generalise the second hand software licence industry solely on Microsoft, volume licensing or my own company's business model would only contribute to the cloudiness already out there. Therefore, for*

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completeness, reference will be made to the secondary sub-markets, which includes Original Equipment Manufacturing (OEM) and Retail Boxed / Fully Packaged Product (FPP) whereby suppliers from these different secondary markets have been researched and/or conferred with.

Industry & Sub-Market Boundaries

Software Licence Programmes -- The second hand software industry can be broken down into three main sub-markets, defined by the software vendor's different licensing programmes: 'Volume', 'Original Equipment Manufacturer' (OEM) and 'Retail Boxed / Fully Packaged Product' (FPP). The distinct differences between these markets are the intangible characteristics of the volume licence programme as opposed to the tangible aspects of OEM / FPP. Tangibility and deployment do incur different issues in terms of legalities…and this will be covered in part three.

Partly due to the nature of the deployment, pre-owned volume licensing is aimed at small, medium and large organisations, whilst the latter two markets are primarily aimed at small to medium sized businesses as well as consumers.

Note that the second hand volume software market is restricted to trading in 'perpetual' software licence assets that have been paid for in full. As with any pre-owned market (cars, software, films etc), this excludes subscription (rented) software licences as clearly, a company cannot legitimately sell something that it does not own in the first place. Again, this will be elaborated upon in part three.

Software Vendors & Products -- Due to the distinct differences in product functionality, the software vendor's products themselves further define the boundaries of the sub-markets. Within the volume market, there are now established pre-owned suppliers of Microsoft and SAP products. The OEM and FPP markets offer a wider range of products including Microsoft, Adobe plus a host of anti-virus, security, audio and visual orientated software. The secondary suppliers within the volume market tend to work independently of the OEM and FPP markets although we do see an overlap between OEM / FPP.

It is notable that the pre-owned software licence baton has not been picked up again with Oracle products but as covered in part three, this is a software vendor that is known to be particularly unfriendly to the idea of secondary competition in a similar way that Cisco has been towards the secondary hardware / equipment market. Interestingly, Cisco's attitude has appeared to soften over the past year (CRN News: "Cisco comes around to used kit") although do not suddenly expect the software vendors to start advocating the second hand software markets.

Secondary Software Market Tiers -- In a similar way that most markets operate, secondary software licence suppliers (Tier 1) undertake the job of both distributing product to a network of resellers (Tier 2) as well as direct to end customers (Tier 3). The legal 'rights and title' to reassign the software licences can travel through numerous Tier 2 intermediaries before product arrives at the Tier 3 end customer; however, with second hand volume (as opposed to OEM / FPP) licensing, the actual transfer of the software licences will normally be facilitated directly from the original acquirer to the new end customer who is installing the software. This process should attempt to adhere to the transfer provision within the software manufacturer's LA Terms & Conditions and the model adopted by the secondary supplier but as covered in part 2, this is not always the case.

In contrast to the conventional software reseller channels, the secondary suppliers within the same tier do trade cooperatively with each other. For instance, Tier 1 players sell not only direct to Tier 2 resellers and Tier 3 customers, but also to other Tier 1 competitors. Likewise, the Tier 3 customers

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may ultimately provide a source of supply later down the line to Tier 1. This creates a "fairly unique" interdependency within the secondary software licence markets.

Trade Bodies / Protection

You may have stumbled across counterfeit-related newsfeeds from the anti-piracy bodies such as the UK's Federation Against Software Theft (FAST), the USA's 'Software and Information Industry Association' (SIIA) and the internationally known Business Software Alliance (BSA). You may have then surmised that software vendors would be in adulation at the thought of a trade body policing the secondary software licensing markets -- well, not quite - the second hand OEM, FPP and volume markets have yet to see a trade body emerge as we have seen with hardware markets such as America's UNEDA (United Network Equipment Dealer Association).

Whilst it is not surprising that the software vendors are not exactly queuing up to work more closely their secondary software market competition, the attempts to curtail the growth of the secondary markets have created a self perpetuating problem whereby the onus upon due diligence falls heavily upon the shoulders of the secondary software licensing supplier.

As we will visit in parts two and three, it may be that not every secondary supplier's business model operates neatly within the software vendor's transfer provisions or the local / regional governing laws. Therefore, customers need to be well informed and able to see that the secondary supplier is procuring from legitimate sources.

Specifically relating to OEM / FPP, the customer should know that the supplier is adhering to stringent ethical standards that eliminate the potential resale of a stolen or counterfeit product. Due to the stigma sometimes attached to secondary markets, there will be a vested interest by the secondary software supplier to be even more diligent and have even more stringent checks in place to eliminate the threat of counterfeit or stolen goods. It stands to reason that one wrong move could ultimately damage the reputation of that supplier and tarnish that of other sub-markets within the industry.

Unlike OEM / FPP products, the unique electronic licence numbers associated with volume software licences are manufactured by the software vendor and cannot be re-engineered, reproduced or found to be counterfeit. However, as with both 'new' and 'pre-owned' licence purchases, it is always plausible that a disgruntled employee with access to volume licence details could install elsewhere.

There is no evidence that pre-owned volume licences have ever been misused in this way although even the most innocent of businesses could have accidentally overused a Volume Licence Key (VLK) at one time or another when installing the software. Microsoft's Volume Licensing Service Centre (VLSC) web portal does now count the number of VLK installs and so there is a certain degree of policing by the software vendors.

While there is a distinct absence of trade bodies policing the second hand software industry, some secondary software licence suppliers and resellers carry what is known as 'Professional Indemnity' insurance. This is the currently the strongest known protection that a secondary supplier has to offer the channel against a mistake or invalid pre-owned licence transfer. It is therefore always worth checking whether the secondary (or conventional) software supplier / reseller has this protection is in place.

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Part 2: Demystifying the Mist

Having taken a look at the dynamics of the second hand software industry in Part 1, we can start to see how this market can play an important role in tackling licence compliance, but it is by no means an open and shut case. By addressing certain licence compliance scenarios that businesses face today and taking into account the business models adopted by the secondary software licence players, let's attempt sieve through some of the myths and seek out the truths that underpin our use of this technology.

Licence Compliance

So your business has received a software licence audit notification from either a representative of Microsoft's licence compliance team or perhaps a SAM auditor. You may have received a set of guidelines or a verbal / written statement that 'pre-owned' software licences are not an appropriate way to rectify your licence shortfall. Although these statements may not be "legally enforceable", the dominant software vendors and their representatives are not afraid to use intimidating as well as misleading language -- and unfortunately this thread is sometimes perpetuated through the auditors or resellers who are all eager to meet their targets.

Language Analysis & Breakdown

Let's look at some of the language currently being circulated by the software vendors and explore the rights and wrongs of each -- (NB: ***these are real extracts from software vendor's emails written to companies either prior, during or after a licence compliance audit***).

"A pre-owned software licence is not a suitable solution to rectify a non-compliant situation as it does not address historical usage". Both 'pre-owned' and 'new' software licence purchases can only rectify a non-licence compliant position on an on-going basis (from the point of purchase) and this is normally the key requirement set out by the software vendor prior to audit. Software vendors may often push the envelope with regards to their product development but they have yet to acquire the technology to travel back in time.

"Our (the software vendor's) position is that 'new' licences need to be purchased because the software vendor will not have received a licence fee when pre-owned licences are purchased to rectify a non-compliant position". Admittedly, neither the software vendor, SAM auditor, nor the authorised reseller will receive revenue when pre-owned software licences are purchased and this is of course the main objective; however, a loss of revenue does not constitute a legal argument for a company to purchase 'new' rather than 'pre-owned' software licences. A 'pre-owned' software licence option would have also been available at the time of the original deployment and so the software vendor may not have suffered any additional financial loss.

"The 'pre-owned' software licences would have been simultaneously in use by another company". Whether it is a 'new' or 'pre-owned' software licence purchase, it is of utmost importance that the 'new' end user has complete transparency with regards to legal ownership and documentation relating to de-installation back to the original customer and supplier. As long as such a model

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provides this basic documentation, you will be able to prove that you have the right to install / use the software. Web portals provided by the vendors are useful when combined with licence history reports, but ultimately the portals / licence reports cannot confirm the legal ownership of the software licence asset in the same way that a sales contract does or proof of payment can.

Business Models & Processes

Generic editorial (whether it be among the IT trade press or provided by industry analysts) that fails to pay sufficient reference to the differences between the sub-markets will always stop short of providing a well informed picture of the second hand software industry -- and so too will the negative software vendor statements (where they exist) aimed at misleading and sometimes intimidating potential clients.

However, under-researched editorial and the software vendors are not solely responsible for the mist that has formed over the second hand industry; indeed, scepticism is also fuelled by the actions of companies (or employees within) operating under dubious business models.

In the same way that a stolen or counterfeit piece of OEM / FPP software (pre-owned or 'new') can potentially be sold to an unsuspecting end user, questionable business models may be in operation that can ultimately tarnish the integrity of the software or hardware industries. However, as with any industry and its sub-markets, we are not about to see a mass exodus of customers from the market at the first sign of a rogue employee or dubious company business model.

A very recent example (ITAM News: Reseller Gone Bad) involved a number of rogue employees working for Bytes Software, Nettitude and Nisa Today; each linked to a fraudulent conspiracy worth £123,000 – but, despite this news, we are not all about to stop buying IT products or boycott each of these companies. If anything, it should make us more vigilant and cautious about our ongoing buying behaviour.

The secondary software licensing market is no different. Differing business models and processes exist across the second hand software sub-markets, which may not be deemed as being compliant with the software vendor's terms or the local / regional governing laws.

Notoriety in Notaries

A well-known supplier within the second hand Volume market that does not shy away from legal interludes when the software vendor is a German company called Usedsoft; and this company knows what the inside of a court room looks like as its business models appeared to conflict with the transfer provisions of Adobe and Oracle -- plus, it's business practices have also been called into question with regards to local and regional governing laws. Usedsoft's model was unique in that it hired the services of a 'Notary', which cloaked the fact that the company was sourcing 'new' educational software licences at rock bottom prices.

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The low cost Educational licences were then resold to unsuspecting businesses whom may have thought were purchasing Commercial or Government software licences (Heise Online - Frankfurt Court Prohibits Use of Notary). The Frankfurt court exposed Usedsoft's business model, which suggested that the company was not entirely operating as the secondary software licence supplier that it marketed itself to be. Even with this lucrative business model, Usedsoft GmbH & AG (Germany and Switzerland) was facing bankruptcy proceedings and has gone into administration (Heise Online – Usedsoft Insolvent).

There are further examples of software vendors being successful in obtaining injunctions against secondary suppliers, as we have recently seen between Microsoft and the court's ruling against German second hand OEM supplier, Softwarebilliger.de. The injunction against Softwarebillinger.de concerned a quantity of alleged counterfeit Microsoft OEM CDs and (whilst the ruling in the case is yet to be reached) Softwarebillinger.de has subsequently been successful in obtaining a 'gagging order' injunction against Microsoft who wrongly made claims that Softwarebillinger.de was continuing to sell counterfeit CD's.

So errors may occur within both the conventional and the pre-owned markets but this should not tarnish the integrity of the rest of the industry's sub-markets. In Part 3, we will take a closer look at a more widely publicised court case between Oracle v Usedsoft in an attempt to examine the legalities of the software vendors T&C's and local / regional governing laws.

A Closing Thought…

It is worth mentioning that the secondary software industry does operate outside of the software vendor's authorised channels and so secondary market players may not always have a formal relationship with the software vendor. This does not however prohibit direct support from the software vendor and whilst it is not a secret that the software vendors are not exactly advocates of the second hand markets, each is bound by the local governing laws that in some instances, take precedent over their own T&C's.

It is also important to highlight that 'new' & 'pre-owned' software licensing models normally operate in a very similar way across all the sub-markets. For instance, the legal rights and title of the software licence may travel through various intermediaries before ending up on the desktop of a end customer but the software licences will, as in the case of Volume licensing, should be transferred directly from the original customer to the 'new' end customer (the intermediaries will not of course be installing and using the software).

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Part 3: The Legalities

Whilst all secondary suppliers (in any marketplace) should always aim to operate in a legal manner, most second hand markets will always be labelled as 'grey' solely due to their unofficial status and the fact that these markets would not have been the originally intended first channel of sale of the manufacturer.

When it comes to recycling software, it is therefore imperative that the different software vendors' transfer terms are understood. Where a business model relies upon local/regional governing laws, we need to understand the precedents that are in place, specifically with regards to the Exhaustion Principle (First Sale Doctrine), the Software Directive and Competition law.

The industry's more dominant software vendors will often make good use of any 'grey' characteristics that the secondary technology markets may have i.e. the spread of 'fear, uncertainty and doubt' (FUD) is still the preferred weapon of choice by the major software vendors although some have chosen direct court action (rightly or wrongly), which as the following will attempt to summarise, appears to focus on the business model or processes adopted by the secondary supplier.

A Software Vendor's Licence Agreement (LA) / T&C's

With regards to volume, software vendors such as Oracle have always been very prohibitive towards resale, whilst the Microsoft and SAP contracts still contain restrictive transfer provisions that have tightened up since the birth of the secondary markets. As the changes have been restrictive rather than prohibitive, the net effect is on the process, by which the secondary market suppliers facilitate the sale and transfer of a pre-owned software licences. The second hand OEM and FPP markets are clearer in so far as a physical software boxed product/CD is capable of being bought and sold without a breach of the software manufacturer's T&C's, although one concern will always be the potential for re-produced, counterfeit or stolen product.

Different software vendor's activities and changing LA's make it impossible to make an in depth comment about each; however, the clauses concerning the ability to resell and to do so across regional boundaries require some air time:

(a) Cross Regional -- The legitimacy of buying a second hand Volume, OEM or FPP software licence from a different region (sometimes defined by continent) is another area that representatives of software vendors often circulate incorrectly. Despite statements to the contrary, not all software vendors and their respective LA's contain clauses that prevent cross regional sales and transfers. If a business is ever exposed to such a statement, it is always worth asking the software vendor representative to send evidence of such a clause within the respective LA, under which the licences were originally purchased.

(b) Resale -- Regarding the Volume LA's, the transfer provisions and notifications documents do permit transfers to affiliated and unaffiliated 3rd parties in connection with reasons such as

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divestiture or merger. In most circumstances, the transfer still does not require the software vendor's consent and only notifications need to be sent to software vendor to process internally - even if the T&C's do not require notification, it is always good practice to do so for transparency with the software vendor and customers. One consistent restriction across the LA's and the notification documents is that the actual software licence must be transferred directly between the original customer and the end customer. This is logical as the intermediaries / brokers / resellers are not installing or using the product and so software vendors will most likely want to minimise the chance of a breach of copyright taking place (prevent multiple copies of a single licence potentially being in use).

Contradictory Clauses

Whilst it would however be inconceivable for a motor company to print 'not for resale' on its cars, software vendors have tried to dissuade clients away from the secondary software markets by putting contradictory clauses into the LA's. It is worth noting though that if any prohibitive changes were ever made by a software vendor to its transfer provision, such changes could not retrospectively affect the trade of software licences purchased under the previous LA's transfer provision. Local and regional competition laws also make it highly unlikely that a software vendor will insert prohibitive clauses that could be legally enforced, which we will look at later in Part 3.

Exhaustion Principle & Software Directive

In the context of software, a software vendor's right to control the resale of its software is said to be exhausted once legal ownership has passed to the customer - the customer then has the right to resell the software to a 3rd party so long as there is no breach of copyright. In regards to the basic principle of software, where the distribution of computer software is by way of a sale, this is provided for in the EU Software Directive 2009/24/EC.

Article 4(2) states: *"the first sale in the Community of a copy of a program by the rightholder or with his consent shall exhaust the distribution right within the Community of that copy, with the exception of the right to control further rental of the program or a copy thereof".*

Admittedly, the strength of the Principle of Exhaustion (otherwise known as the 'First Sale Doctrine' across the pond) may impact differently upon the secondary software markets, dependant on the product tangibility and the business model(s) being adopted by the secondary software suppliers.

For instance, a second hand software supplier whose business model operates outside of the software vendor's transfer provision will need to rely upon the Principle of Exhaustion to legalise its trade. However, the Exhaustion Principle, as implemented via the EU Software Directive, was originally written for a tangible OEM and FPP era.

For example, in order to comply with Microsoft's T&C's, OEM versions would only be allowed to be sold along with a hardware item even though in many cases this item could be a simple inexpensive mouse etc. In a landmark ruling, the Bundesgerichtshof (BGH) (German court) decided in July 2001 that it was legal for the operating system to be sold separately from the computer / hardware, from which it was originally installed. This ruling helped open the floodgates for the secondary OEM markets – see: Case No.: I ZR 244 / 97 - OEM decision - judgment GRUR 2001, 153.

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Non-tangible Trials & Tribulations

With the emergence of a non-tangible 'digital' era over the past decade, secondary 'Volume' software licence suppliers may have felt the need to place more emphasis on operating within the software vendor's transfer provisions; otherwise, the secondary software supplier and its customers could be at risk because it was not clear how enforceable the principle of Exhaustion is within the context of the current version of the EU Software Directive (2009/24/EC).

As to the current strengths of the Exhaustion Principle and the Software Directive within the secondary Volume software licence markets, the most closely related case would be that of Oracle & the Administrators of Usedsoft. Here, the Court of Justice General Advocate, Mr Yves Bot, has very recently submitted his opinion to the European Court of Justice (ECJ), which the ECJ was likely to uphold in its final judgement of the case (**the actual ECJ ruling was made on 3rd July 2012 and a summary of the judgement is provided for at the end of this guide*).

The case firstly questioned the subject of whether an intangible software licence was even sold or, as Oracle argued, that it was simply licensing the right to use the Oracle software. The second key point related to the ability to reproduce and distribute the software.

On the first point, Bot stated that "The rightholder [Oracle] draws a somewhat artificial distinction between the making available of the copy of the computer programme and the grant of the right to use it; the assignment of a right of use over a copy of a computer program does indeed constitute a sale within the meaning of Article 4(2) of Directive 2009/24,".

In other words, the principle of Exhaustion applies to both the sale of tangible software as well as intangible software. This makes sense as the software vendors themselves make clear distinctions by offering both 'perpetual' and 'subscription' licence programmes. On the second point, 'Bot' further concludes that "the principle of exhaustion relates exclusively to the distribution of a copy of the computer program and cannot adversely affect the right of reproduction, which cannot be impaired without adversely affecting the very substance of the copyright".

In summary, whilst the secondary software supplier can resell either a tangible or intangible software product, this does not necessarily give the secondary supplier or 'new' end customer the right to make and resell illegal copies (deemed a breach of copyright laws). Whilst some of Bot's opinion may have been welcome news for the ex-Directors of Usedsoft, the final outcome of this case should not have an effect on the other secondary sub-markets whereby unlike Oracle, transfer provisions exist e.g.: Microsoft and SAP. What this case has demonstrated is that the current EU Software Directive (2009/24/EC) may not have adequately addressed today's intangible digital software environment and this may need to be considered in the next version.

Competition Law

Adding either restrictive or even prohibitive clauses within the transfer provision, coupled with the spread of misleading statements by the software vendors, could be considered to be in breach of both European and local governing competition laws. In the context of the underlying law found in the Software Directive 2009/24/EC, such actions by the software vendors could be deemed to be in breach of Articles 101 and 102 of the Treaty on the Functioning of the European Union ('TFEU') and in Chapter I (in particular, Section 2) and chapter II (in particular, Section 18) of the UK Competition Act 1998.

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In an attempt to eliminate the competition, the software vendor would appear to strengthen its own already dominant position in the market, thereby ensuring that consumers have no other option than to buy 'new' Volume, OEM or FPP software through the conventional software vendor's network of resellers.

This is plainly to the detriment of businesses and consumers whom are then deprived of choice and the discounts available through the pre-owned software licence markets. Businesses and consumers would also be deprived of the option to divest unwanted software licences and obtain a residual value for this asset. The consequence of this type of conduct simply results in the size of second hand software market being suppressed; however, whilst the past actions of some of the software vendors may be considered an abuse of a dominant position, the 'FUD' tactics adopted by some software vendors go largely unchallenged, at least in the public domain.

Summary & European Court Ruling...

Despite the independency between the different secondary software markets, the legalities of the entire second hand software licence industry can be brought into question as a result of an isolated action within one of the markets. This may be justified if a secondary supplier is found guilty of illegal practices but we also have to be aware of the 'FUD' tactics adopted by the software vendors and the inaccuracy of generic articles that form unnecessary black clouds over the second hand software industry.

Whether you are buying from or selling to a tier within the second hand Volume, OEM or FPP markets, the key will always be transparency, both in terms of legal ownership and the software vendor's transfer provision. The responsibility does falls upon the secondary supplier as well as the end customer to ensure that it is purchasing from a reliable source and that it can demonstrate the legal ownership all the way back to the original customer.

This particular step will at least keep your business within the local and regional governing laws but it is of equal importance to purchase from a secondary supplier that strives to operate within the vendor's transfer provision because the EU Software Directive 2009/24/EC may require a few tweaks in order to fully incorporate the modern digital software age.

European Court of Justice Ruling - Judgement Day: 3rd July 2012

Following the ITAM Review of our three part guide to second-hand software back in May / June, the Court of Justice of the EU (CJEU) upheld the General Advocate's opinion and went further by ruling that intangible software can be resold regardless of the vendor's transfer provision. See: Court Judgement of the CJEU (Case C-128/11 - 3rd July 2012) in the case between the administrators of UsedSoft GmbH v Oracle International Corp. This case was referred to the CJEU by The Bundesgerichtshof (Federal Court of Justice, Germany) who still has to make the final ruling but it is certain to follow the CJEU's judgement.

This ruling from the European Court of Justice has at least put a long awaited dent in the FUD (Fear, Uncertainty & Doubt) tactics employed by the software vendors. Whilst

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software vendors such as Microsoft may still have transfer provisions within its licence agreements, any restrictive or prohibitive changes from a software vendor would be futile.

The following highlights the key clauses from the ECJ ruling and offers a summary in laymen's terms:

> Clause 47: "it does not appear from Article 4(2) of Directive 2009/24 that the exhaustion of the right of distribution of copies of computer programs mentioned in that provision is limited to copies of programmes on a material medium such as a CD-ROM or DVD. On the contrary, that provision, by referring without further specification to the 'sale … of a copy of a program', makes no distinction according to the tangible or intangible form of the copy in question."

It is irrelevant as to whether the software is tangible or intangible (digitally downloaded). As long as the software licence is perpetual (unlimited life) and a form of payment has occurred, a sale (transfer of ownership) will have taken place and the software vendor (rights holder / author) thus exhausts its right to control subsequent distribution i.e.: of a secondary supplier.

> Clause 77: "It follows that, by virtue of that provision and notwithstanding the existence of contractual terms prohibiting a further transfer, the rightholder in question can no longer oppose the resale of that copy."

'By virtue' of the EU Software Directive, even if the licence agreement restricts or prohibits resale or transfers, the software vendor can no longer oppose the resale of that software licence copy.

> Clause 67 & 68: "..the conclusion of a maintenance agreement, such as those at issue in the main proceedings, on the occasion of the sale of an intangible copy of a computer program has the effect that the copy originally purchased is patched and updated. Even if the maintenance agreement is for a limited period, the functionalities corrected, altered or added on the basis of such an agreement form an integral part of the copy originally downloaded and can be used by the acquirer of the copy for an unlimited period, even in the event that the acquirer subsequently decides not to renew the maintenance agreement...In such circumstances, the exhaustion of the distribution right under Article 4(2) of Directive 2009/24 extends to the copy of the computer program sold as corrected and updated by the copyright holder."

Oracle offers a maintenance agreement with its products but even if the maintenance is for a limited period or is altered / updated, such an agreement forms an integral part of the software licence copy purchased and can therefore be used by the first acquirer / customer for an unlimited period.

> Clause 69: "...if the licence acquired by the first acquirer relates to a greater number of users than he needs, as stated in paragraphs 22 and 24 above, the acquirer is not authorised by the effect of the exhaustion of the distribution right under Article 4(2) of Directive 2009/24 to divide the licence and resell only the user right for the computer program concerned corresponding to a number of users determined by him."

This point needs elaborating on and could have been made clearer by the CJEU in its judgment. The ruling states that an Oracle "licence", which would be more appropriately defined as a minimum "block" of 25 CALs. A company that purchased 100 blocks (2500) CALs can sell off those 100 blocks to 100 different customers but it cannot break down the individual licence blocks i.e.: a 'licence' cannot be broken down into 5 x 5 user licence blocks. Let's transcend the ECJ ruling over to Microsoft Volume (Select / Enterprise) because Microsoft licences its software on a

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'per seat' basis, which is different to Oracle. Given the objective of the clause 69 in relation to the ECJ ruling is that the court does not want the original acquirer to still have a copy of the software installed on the machine from which the software is being disposed of, the only logical interpretation would be that the Microsoft LA or enrolment cannot be broken down past the 'licence' / 'SKU' level because Microsoft's licensing is structured generally on a 'per seat' basis. View the following examples in comparison to the Oracle / ECJ ruling to understand the ruling in relation to the way software is licensed by different vendors such as Microsoft.

[Example 1]: an Microsoft Enterprise LA containing 1000 x Office 2010 PRO can be broken down and sold off in smaller quantities to different clients e.g.: 50 + 100 + 350 + 500; however, you cannot break down past the individual Office 2010 PRO licence level and then sell off as individual components (Word, Excel, PowerPoint, Access etc) to different clients.

[Example 2]: Windows SBS CALs could be purchased in licence blocks of 5 or 20 CALs. A company may purchase 2 licence blocks: 1 licence block containing 20 CALs + another licence block containing 5 CALs. The ruling requires that you cannot break down the licence block of 20 CALs and sell off to two different customers in smaller quantities such as 10 + 10 CALs; however, you can resell the 2 originally acquired licence blocks to 2 different customers.

> Clause 78: "the original acquirer of a tangible or intangible copy of a computer program for which the copyright holder's distribution right is exhausted in accordance with Article 4(2) of Directive 2009/24 who resells that copy must, in order to avoid infringing that rightholder's exclusive right of reproduction of his computer program under Article 4(1)(a) of Directive 2009/24, make the copy downloaded onto his computer unusable at the time of its resale."

This follows on from clause 69 relating to the division of licences. From the point of resale, the first acquirer must ensure that the quantity of software licences being divested have been de-installed and not in use on its machines. For instance, if you are divesting 500 x Office 2010 PRO from a Select LA containing 1000 licences, you must de-install and not be using those 500 licences by the point of sale.

> Clause 81: "...in the event of a resale of the copy of the computer program by the first acquirer, the new acquirer will be able, in accordance with Article 5(1) of Directive 2009/24, to download onto his computer the copy sold to him by the first acquirer. Such a download must be regarded as a reproduction of a computer program that is necessary to enable the new acquirer to use the program in accordance with its intended purpose."

Whilst the exclusive right of *distribution is exhausted*, note that the exclusive right of *reproduction* is not exhausted by the first sale. However, any reproduction that is necessary for the use of the software by the lawful acquirer (such as Discount-Licensing) in accordance with its intended purpose of the computer programme, may not be prohibited by the vendor within the LA / contract. The lawful acquirer can download a copy of the software onto a computer and make a copy onto a carrier such as a DVD. Such a download / copy must be regarded as a reproduction that is necessary to enable the new acquirer use the program in accordance with its originally intended purpose.

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