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In the Matter of Notice of Inquiry: *Resale Royalty Right*	Docket No. 2012-10

COMMENTS OF CHRISTIE'S, INC. AND SOTHEBY'S, INC. REGARDING CONSTITUTIONAL AND STATUTORY ISSUES WITH A PROPOSED RESALE ROYALTY RIGHT

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December 5, 2012

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COMMENTS OF CHRISTIE'S AND SOTHEBY'S

I am writing on behalf of Sotheby's, Inc. and Christie's, Inc. (together, the "Auction Houses") in response to the Copyright Office's Notice of Inquiry dated September 13, 2012, published in the *Federal Register* September 19, 2012 ("Notice of Inquiry"), 77 Fed. Reg. 58,175. The Auction Houses welcome the opportunity to respond to the questions raised in the Notice of Inquiry.

Christie's, Inc. and Sotheby's Inc. welcome the opportunity to submit these comments regarding the legal difficulties with the proposed federal resale royalty right in response to the Notice of Inquiry. The Notice of Inquiry sought comment on "the means by which visual artists exploit their works under existing law as well as the issues and obstacles that may be encountered when considering a federal resale royalty right in the United States." *Id.* at 58,175.

The Auction Houses have separately commented to explain at length why a resale royalty right would make no sense as a matter of policy. Such a rule would give a windfall to already-successful artists and their heirs, would do nothing to help struggling artists or incentivize the creation of new works, and would likely drive art sales offshore or into the private market. It also reflects a fundamental misunderstanding of the art market, in which visual artists are able to fully capture the value of their work at the time of the first sale. Indeed, in addition to the proceeds of their initial sales, artists currently derive substantial benefits from

subsequent resales of their work, which increase the demand for (and price of) that artist's work. Put simply, the putative benefits of a resale royalty right would be far outweighed by its significant costs, and any such policy would likely fail to achieve its purported goals.

These comments complement those policy-based arguments by focusing primarily on the *legal* implications of a resale royalty right, which would be profound. Most notably, a resale royalty right would run directly counter to the long-established "first sale doctrine" and the even more deeply rooted common law tradition the first sale doctrine embodies. Courts in this country have recognized the first sale doctrine since the early 1800s, and Congress expressly codified the doctrine in the Copyright Act of 1909. The doctrine's roots can be traced to ancient common law principles disfavoring restraints on alienation of property.

The first sale doctrine provides that a copyright holder's rights in a work are extinguished after the first lawful sale of that work. Whatever rights an artist may maintain over subsequent works that embody the copyrighted material, the copyright owner's ability to control a particular physical embodiment of the work ends with the first sale. From that point, the copyright law cedes control over the physical object, which becomes governed by ordinary rules of property, which in the American tradition favor free alienability. A resale royalty stands in stark contrast to this long-standing American statutory and common law tradition. It

would impose a significant restraint on alienation by granting artists a permanent, irrevocable right to a portion of the proceeds from future sales of their works. It is also wholly unnecessary given that artists and purchasers generally remain free to contract around the first sale doctrine if they find such an arrangement to be mutually advantageous. In contrast, countries adopting a resale royalty right typically make the right non-waivable.

In addition to disrupting settled copyright jurisprudence, a new resale royalty right would raise constitutional concerns to the extent it applies to works of art that have already entered the stream of commerce. Retroactive legislation is disfavored under the Due Process Clause, and the extension of a resale royalty to already-sold works would disrupt the settled expectations of the parties to those completed transactions. Worse yet, those significant costs would do nothing to advance the goals of the copyright regime—that is, granting a retroactive windfall to the creators of already-sold works would not in any way incentivize the creation of new work. A resale royalty right would also raise serious concerns under the Takings Clause to the extent it merely confiscates the private property of select individuals (art sellers) and transfers it to other private individuals (copyright holders and their heirs), while bestowing no discernible benefit on the greater public.

Moreover, a resale royalty right would resemble a prohibited bill of attainder if it applied only to three or four large auction houses (either explicitly or implicitly through a gerrymandered definition that captured only a very few firms). The constitutional prohibition on bills of attainder was intended to ensure that parties had notice and fair warning of the regulations to which they would be subject, and to ensure that the costs of legislation were borne by society at large rather than by narrow, disfavored groups. A resale royalty that applied to large auction houses but did not apply to private transactions, gallery sales, the Internet, or sales by smaller auction houses would directly implicate these concerns.

ARGUMENT

I. A RESALE ROYALTY RIGHT WOULD UPEND THE DEEPLY ROOTED FIRST SALE DOCTRINE

A. The first sale doctrine is among the most deeply ingrained principles of American copyright jurisprudence. Section 109(a) of the Copyright Act provides that "the owner of a particular copy or phonorecord lawfully made under this title, or any person authorized by such owner, is entitled, *without the authority of the copyright owner*, to sell or otherwise dispose of the possession of that copy or phonorecord." 17 U.S.C. § 109(a) (emphasis added). In other words, a person who owns a lawful copy of a copyrighted work is free to resell that work without seeking the consent of the original creator or current copyright holder. *See*

American International Pictures v. Foreman, 576 F.2d 661, 664 (5th Cir. 1978) (the first sale "extinguishes the copyright holder's ability to control the course of copies placed in the stream of commerce").

This doctrine has a "venerable lineage." *Sebastian International v. Consumer Contacts, Ltd.*, 847 F.2d 1093, 1096 (3rd Cir. 1988). Courts have applied a first sale doctrine as a construction of the Copyright Act since at least the early 1800s. Although the Act granted authors the exclusive right to "vend" their works, *see* Act of May 31, 1790, ch. 15, § 1, 1 Stat. 124, courts have held that any such right is extinguished after the first sale of a work. *See Bobbs-Merrill Co. v. Straus*, 210 U.S. 339 (1908); *Quality King Distributors v. L'anza Research International*, 523 U.S. 135, 140-42 (1998) (tracing history of first sale doctrine). Congress formally codified the doctrine in 1909, and it has been retained in every subsequent iteration of the Copyright Act. *See* Copyright Act of 1909, ch. 320, 35 Stat. 1084, § 41 ("nothing in this Act shall be deemed to forbid, prevent, or restrict the transfer of any copy of a copyrighted work the possession of which has been lawfully obtained"); Copyright Act of 1947, ch. 391, 61 Stat. 660, § 27 (same).

The principle underlying the first sale doctrine is straightforward: the right of free alienation is a basic element of ownership, especially with respect to personal property or chattels. *See Sebastian*, 847 F.2d at 1096 (the statutory first sale doctrine "finds its origins in the common law aversion to limiting the

alienation of personal property"). As one court has explained, "[t]he right of alienation is one of the essential incidents of a right of general property in movables, and restraints upon alienation have been generally regarded as obnoxious to public policy, which is best subserved by great freedom of traffic in such things as pass from hand to hand." *John D. Park & Sons Co. v. Hartman*, 153 F. 24, 39 (6th Cir. 1907).

Law and Economics scholars have praised the common law rule as ensuring that goods find their highest and most efficient use and do not become stranded with an owner who does not value the good as highly as others, but is deterred from an efficient transfer by restraints on alienability or inefficiently high transaction costs. *See, e.g.*, Richard A. Posner, *Economic Analysis of Law* 31 (2d ed. 1977) ("If a property right cannot be transferred, resources will not be shifted from less to more valuable uses through voluntary exchange."); Richard Epstein, *Why Restrain Alienation?*, 85 Colum. L. Rev. 970, 971-72 (1985).

While the common law has recognized and enforced some restraints on the alienation of *real property*, even then there are long-recognized limits. As any law student ever compelled to master the rule against perpetuities can attest, there are limits on how long the "dead hand of the past" may control. But the rule against alienability applies with far great force to ordinary property: "A covenant which

may be valid and run with land will not run with or attach itself to a mere chattel." *Hartman*, 153 F. at 39.[1]

B. A statutorily mandated resale royalty would upend the first sale doctrine by allowing the "dead hand of the past" to take a government-imposed cut of each sale in the secondary market, thus restraining the alienability of existing works of art. That rule would prevent buyers from ever acquiring unencumbered title to a work of art, and would add an additional layer of complexity to all secondary transactions. It would also elevate visual artists above other types of creators—a painter would obtain a permanent right to a portion of the proceeds from resales of his paintings, while an author would have no similar rights in a rare first edition of a book.

Moreover, a resale royalty is entirely unnecessary in light of the fact that the first sale doctrine merely states a statutory *default* rule, which artists and art purchasers can contract around if they deem it mutually advantageous. As Professor Nimmer has explained, "nothing in the Copyright Act or in the doctrine of first sale prevents parties from agreeing, through a valid contract, to establish

[1] *See also* Zechariah Chafee, Jr., *The Music Goes Round and Round: Equitable Servitudes and Chattels*, 69 Harv. L. Rev. 1250, 1261 (1956) ("Where chattels are involved and not just land or a business, the policy in favor of mobility creates even stronger cause for courts to hesitate and scrutinize carefully factors of social desirability before imposing novel burdens on property in the hands of transferees.").

different use restrictions or privileges from those set out under copyright law."[2] Copyright law "does not preempt these contractual arrangements, nor do they disturb the balance set out in copyright law," and rights owners "may obtain economic benefits from their creative work by bringing those works to the market under economic terms of their choosing." *Id.*; *see, e.g.*, *Bowers v. Baystate Technologies*, 320 F.3d 1317, 1325-26 (Fed. Cir. 2003) (license agreement may prohibit "reverse engineering" even if such practices were allowed under the copyright laws); *id.* at 1336 (Dyk, J., dissenting) ("a state can permit parties to contract away a fair use defense or to agree not to engage in uses of copyrighted material that are permitted by the copyright law, if the contract is freely negotiated"). Thus, if current artists really believe that they will maximize their revenues by contractually relaxing the first sale doctrine, they are free to do so.

There are many different forms such an arrangement could take. The artist could agree to sell the work for a lower price in exchange for a fixed percentage of proceeds from a future resale of the work. Or, rather than transfer title to the work, the artist could lease or license the work for a fixed term of years. *See* 17 U.S.C. § 109(d) (first sale doctrine does not apply to "any person who has acquired possession of the copy . . . from the copyright owner, by rental, lease, loan, or

[2] Raymond T. Nimmer, *Copyright First Sale and the Over-Riding Role of Contract*, 51 Santa Clara L. Rev. 1311, 1345 (2011).

otherwise, without acquiring ownership of it"). Or the artist could acquire an option to repurchase the work at a fixed price, or a reversion interest that vests at the buyer's death. By contrast, most nations that have adopted a resale royalty right have made the right non-waivable, so that artists who believe they will maximize their revenues by selling pursuant to the traditional "American rule" (*i.e.*, with the first sale doctrine and without restraints on alienability) would be unable to contract for their preferred rule.[3] In that way, the resale royalty rights conflict not only with the first sale doctrine and the policy against restraints on alienability, but also with even more basic principles of freedom of contract.

In sum, the inconsistency between the resale royalty right and the long-entrenched first sale doctrine cannot be overstated. The two doctrines are fundamentally incompatible. While Congress may have the power to abandon the first sale doctrine, subject to the due process and bill of attainder concerns addressed next, it should hesitate in discarding a doctrine so central to the Copyright Act that courts inferred the doctrine's existence even before Congress expressly codified it. Simply put, the first sale doctrine has been central to the

[3] A bill introduced in 2011 similarly included a non-waivable resale royalty right. *See* Equity for Visual Artists Act of 2011 (S.2000), 112th Cong. 2011-2012, § 3 ("The right to receive such royalty . . . may not be waived by the artist or his successor as copyright owner.").

copyright regime for nearly 200 years, and a mandatory, government-established resale royalty would be anathema to the sound policies underlying that doctrine.

II. A RESALE ROYALTY RIGHT THAT APPLIES TO ALREADY-CREATED WORKS WOULD RAISE SERIOUS RETROACTIVITY, DUE PROCESS, AND TAKINGS CONCERNS

A. Retroactivity and Due Process Concerns

Along similar lines, "the presumption against retroactive legislation is deeply rooted in our jurisprudence, and embodies a legal doctrine centuries older than our Republic." *Landgraf v. USI Film Products*, 511 U.S. 244, 265 (1994). Retroactive legislation "raise[s] particular concerns," given that "[t]he Legislature's unmatched powers allow it to sweep away settled expectations suddenly and without individualized consideration." *Id.* at 266; *see also General Motors Corp. v. Romein*, 503 U.S. 181, 191 (1992) ("Retroactive legislation presents problems of unfairness that are more serious than those posed by prospective legislation, because it can deprive citizens of legitimate expectations and upset settled transactions."); *Weaver v. Graham*, 450 U.S. 24, 28-29 (1981) (prohibition on retroactive criminal legislation ensures that individuals have "fair warning" about prohibited conduct, and "restrain[s] arbitrary and potentially vindictive legislation").

As Justice Kennedy summarized the point, "for centuries our law has harbored a singular distrust for retroactive statutes." *Eastern Enterprises v. Apfel*,

524 U.S. 498, 547 (1998) (Kennedy, J., concurring in part and dissenting in part). The "largest category" of cases in which the Court has applied the presumption against retroactivity has involved "provisions affecting contractual or property rights, matters in which predictability and stability are of prime importance." *Landgraf*, 511 U.S. at 271 & n.25 (collecting cases).

The Due Process Clause also protects individuals' interests in fair notice and repose, both of which are likely to be compromised by retroactive legislation. It "does not follow" that "what Congress can legislate prospectively it can legislate retrospectively," and "the justifications for the latter may not suffice for the former." *Usery v. Turner Elkhorn Mining Co.*, 428 U.S. 1, 17 (1976). "If retroactive laws change the legal consequences of transactions long closed, the change can destroy the reasonable certainty and security which are the very objects of property ownership." *Eastern Enterprises*, 524 U.S. at 548-49 (Kennedy, J., concurring in part and dissenting in part).

Creating a new resale royalty right for works of art that are *already* in the stream of commerce, and were long ago sold free and clear pursuant to the first sale doctrine, would raise retroactivity concerns. Most obviously, such a rule would upset the settled expectations of art buyers by imposing a significant new limitation on their property that did not exist when the property was purchased. All past art sales in the United States took place against the backdrop of the first

sale doctrine: the artist believed that her rights to a work would be extinguished once it was sold, and the buyer believed that she was obtaining the work free and clear of any encumbrances. The price at which the work was sold necessarily reflected these default rules. *See Sebastian*, 847 F.2d at 1099 ("With respect to future distribution of those copies in this country, clearly the copyright owner already has received its reward through the purchase price."); *Denbicare U.S.A. Inc. v. Toys "R" Us, Inc.*, 84 F.3d 1143, 1151 (9th Cir. 1996) ("[T]here is no justification for reexamining the adequacy of the 'reward' received by the copyright owner in an alleged first sale where the owner has consented to that sale.").

Imposition of a resale royalty right for existing art would discard that bargain through government fiat by unilaterally increasing the value of the work to the artist and decreasing the value to the purchaser who has already paid the market price in a transaction governed by the first sale doctrine. Such a policy would raise serious retroactivity concerns in *any* context, but it is particularly misplaced as applied to intellectual property. Congress' power to confer patents and copyrights is certainly broad, but is not unlimited. Article I, section 8 of the Constitution empowers Congress: "[t]o promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries." While a resale royalty right

that attached only to newly created works could arguably be said to "promote the progress of ... useful arts," *but see* Auction Houses' Policy Comments, the same cannot be said of a resale royalty right that applies retroactively to *existing* works.[4] It would merely be a windfall to the holders of the copyrights on existing works—namely, already-successful living artists, wealthy heirs of successful artists, or well-endowed foundations—at the expense of those who purchased the art free and clear and subject to the first sale doctrine.

That latter point is critical for distinguishing other congressional efforts to extend copyright benefits to existing works. The Supreme Court has rejected challenges to congressional efforts to extend the term of existing copyrights, *see Eldred v. Ashcroft*, 537 U.S. 186 (2003), or even to restore copyrights for works that had come into the public domain, *see Golan v. Holder*, 132 S. Ct. 873 (2012). In those contexts, however, the extension of the copyright benefitted the copyright owner, but not at the direct expense of a purchaser's concrete reliance interest in a copy of the work.

To be sure, the general public had an abstract interest in works being freely available in the public domain. But all copyright protection comes at the expense

[4] The Notice of Inquiry requested comments about the "duration" of the term for a resale royalty right. 77 Fed. Reg. at 58,178. Any resale royalty that extended *beyond* the statutory copyright term would be plainly inconsistent with the goals of the Copyright Clause.

of such generalized public interests. In *Golan*, individuals with a desire to exploit particular works contended that this more discrete interest gave them a superior claim to the general public. But the Court emphasized in *Golan* that laws restoring protection for pre-existing works in the public domain could promote progress in the useful arts by "inducing *dissemination*." *Golan*, 132 S. Ct. at 888-89; *see id.* at 889 ("[a] well-functioning international copyright system would likely encourage the dissemination of existing and future works"). But that justification is wholly inapplicable to a resale royalty, which would directly *reduce* the current owner's incentive to disseminate the work by imposing a substantial levy on any further dissemination beyond the first sale. In this way, the resale royalty is antithetical not just to the first sale doctrine, but to one of the basic goals of the copyright laws.

B. Takings Concerns

The law at issue in *Golan* also included specific "reliance-party protections" to ameliorate the retroactive effect on particular users and eliminate Takings concerns. *Id.* at 883, 892 n.33. For example, the creator of a derivative work based on a work then in the public domain retained her full rights in the derivative work. *Id.* at 883, 896. Here, a royalty rate attaching to pre-existing works would have difficulty including such protections, because the whole point of applying the

law to pre-existing works would be to upset the current owner's settled expectation of a right to sell the property free and clear.[5]

Thus, a law that directly undermines that settled reliance interest raises constitutional concerns of a wholly different order. Indeed, the application of the royalty rate to pre-existing works implicates related concerns under the Takings Clause. *Cf. Golan*, 132 S. Ct. at 892, n. 33 (noting that it was concerns under the Takings Clause that prompted Congress to include the "reliance-party protections"). To be sure, the resale royalty right would not divest ownership of a work from someone who had purchased it free and clear under the first sale doctrine. But it would directly eliminate one of the specific property rights within the bundle of ownership rights—namely, the right to free alienation of the property.

While the royalty operates much the same way as a tax, which would not raise Takings concerns, there is one important difference—the royalty inures directly to the artist, not to the Treasury. *Cf. Kathrein v. City of Evanston*, 636 F.3d 906, 911 (7th Cir. 2011) ("The quintessential tax is imposed upon a broad population by a legislature to raise the revenue a government needs in order to function."). And the forcible transfer of an ownership interest from one private

[5] It makes little difference if the royalty is imposed on purchasers rather than current owners, because if the restriction applies to purchasers, this will directly reduce the amount that purchasers would be willing to pay the current owner.

citizen to another has been held to raise distinct Takings concerns in other contexts. *See, e.g.*, *Thompson v. Consolidated Gas Utilities Corp*., 300 U.S. 55, 80 (1937) ("[T]his Court has many times warned that one person's property may not be taken for the benefit of another private person without a justifying public purpose."); *Hairston v. Danville & Western Ry. Co.*, 208 U.S. 598, 606 (1908) ("[I]t is beyond the legislative power to take, against his will, the property of one and give it to another for what the court deems private uses."). And, of course such a takings concern is directly related to the more basic due process concern with retroactive legislation. *Compare Eastern Enterprises*, 524 U.S. at 538 (plurality op.) (invalidating Black Lung Benefits Act provision on takings grounds); *with id.* at 550 (Kennedy, J. concurring in the judgment in part and dissenting in part) (invalidating provision on due process/retroactivity grounds).

III. A RESALE ROYALTY RIGHT THAT APPLIES ONLY TO THE MAJOR AUCTION HOUSES WOULD RESEMBLE AN UNCONSTITUTIONAL BILL OF ATTAINDER

The Notice of Inquiry asks "whether the resale royalty should apply to some types of transactions and not others." Various parties have suggested in the past that any resale royalty should apply only to sales by auction houses that achieve a certain level of annual sales—*i.e.*, only to three or four large auction houses, including Christie's and Sotheby's. Any such proposal would raise serious

constitutional concerns, as it would closely resemble an impermissible bill of attainder.

Article I, section 9 of the Constitution provides that "No Bill of Attainder . . . shall be passed." In prohibiting bills of attainder, "the draftsmen of the Constitution sought to prohibit the ancient practice of the Parliament in England of punishing without trial 'specifically identified persons or groups.'" *Selective Serv. Sys. v. Minnesota Pub. Interest Research Grp.*, 468 U.S. 841, 47 (1984). The "singling out of an individual for legislatively prescribed punishments constitutes an attainder whether the individual is called by name or described in terms of conduct which, because of its past conduct, operates only as a designation of particular persons." *Id.* This protection was so central to the framing generation that the prohibition on bills of attainder is one of the very few individual rights enshrined in the *unamended* Constitution.

A resale royalty statute would directly implicate the bill of attainder prohibition if it were drawn to target a handful of large auction houses, while excluding large swaths of the art market, such as smaller auction houses, Internet-based sellers, galleries, and private sales. Those concerns would be especially strong if Congress deemed the resale royalty to be a form of punishment for purported "excess profits" or "exploitation" of artists by large auction houses. *See*

id. at 852 (congressional "intent to punish" is indicative of a bill of attainder); *Nixon v. Administrator of Gen. Servs.*, 433 U.S. 425, 474 (1977).

To be sure, a per-sale royalty equal to a percentage of the purchase price does not necessarily resemble the classic forms of legislative "punishment" that the bill of attainder clause was designed to prevent, such as imprisonment or outright confiscation of property. *See Selective Serv. Sys.*, 468 U.S. at 852; *Nixon*, 433 U.S. at 473-74. Nonetheless, the same concerns that underlie the bill of attainder clause—the need for notice and fair warning of prohibited conduct, and the importance of distributing the costs of legislation widely rather than upon only narrow groups—counsel against any rule limited only to large auction houses.

CONCLUSION

In addition to its many policy flaws, adoption of a resale royalty right would undermine the core principles embodied in the first sale doctrine, and would raise serious constitutional concerns under the Due Process, Takings, and Bill of Attainder Clauses.

Respectfully Submitted,

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December 5, 2012