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# Too Clever by Half?: The Tension Between Section 203 of the Copyright Act and Freedom of Contract

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The authors question whether heirs inheriting copyrights under Section 203 will be denied contract options.


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Section 203 of the federal Copyright Act, 17 U.S.C. §203 provides for the termination and "recapture" of a grant of a copyright assignment or license that was executed by an author on or after Jan. 1, 1978. Specifically, Section 203 vests in authors or their heirs the right to terminate and renegotiate prior grants of copyright 35 years after their execution. [1]

[1] Pre-1978 copyright grants are governed by a parallel copyright recapture scheme under 17 U.S.C. §304 (hereinafter, "Section 304"). Notably, Section 203 does not apply to works made for hire. See 17 U.S.C. §203(a).

While intended to protect young authors and other content creators from usuristic agreements forced upon them by publishers or other content exploiters, now that some rights under Section 203 are beginning to vest, questions about unintended impacts on the rights of those creators, and especially their heirs, are beginning to arise. Unless courts choose to see function over form, the sweeping language of Section 203 may work to upset the wishes of the very creators the legislation was meant to protect.

## Second Bite at the Apple

Section 203 was designed to safeguard authors against "unremunerative transfers" due to "the unequal bargaining position of authors, resulting in part from the impossibility of determining a work's value until it has been exploited." [2] Accordingly, even if a young, unknown author granted a license to a publisher in 1980 for the life of a copyright, or for some other specified period of time, he or she nevertheless would possess a statutory right to terminate and "recapture" that license 35 years later (in 2015) in order to shop around for a better deal. [3] Essentially, Section 203 gives authors and their heirs a "second bite at the apple" to market their works, even after a transfer of rights has been made.

[2] H.R. Rep. No. 94-1476, at 124 (1976); *S.Rep. No. 94-473*, at 108 (1975), U.S. Code Cong. & Admin.News 1976, 5659, 5740.

[3] See 3 Melville B. Nimmer & David Nimmer, Nimmer on Copyrights §11.01 et seq. (Matthew Bender, Rev. Ed.) (hereafter, "Nimmer"); *Walth al v. Rusk*, 172 F.3d 481, 483-486, 50 USPQ2d 1311 (7th Cir. 1999).

As of 2013, the termination interests for copyright licenses granted in 1978 finally began to ripen. The vesting of these copyright "recapture" rights provides an opportunity to examine some of the inherent ambiguities in Section 203's statutory

scheme. We specifically focus on the potential for conflict between two of Section 203's provisions, described below.

**Section 203 Dictates the Percentage Termination Interests of a Deceased Author's Surviving Heirs—17 U.S.C. §203(a)(2)**

When an author passes away before the 35-year vesting of the rights subject to termination, Section 203 provides that the author's termination interest will automatically descend to the author's heirs pursuant to a detailed statutory formula. Specifically, under Section 203(a)(2), if the author is survived by a spouse and children, then 50 percent of an author's termination interest (including the right to vote on whether to terminate the copyright grant) belongs to the surviving spouse and the other 50 percent will be divided "per stirpes" among the children. If there is no widow or widower, then the termination interest is divided among the author's surviving children. The revenues flowing from any renegotiated license related to the same copyright will be divided in accordance with the heirs' respective percentage ownerships in the termination interest.

**Section 203 Applies to All Copyright Grants, "Notwithstanding Any Agreement to the Contrary"—17 U.S.C. §203(a)(5)**

Certain language in Section 203 suggests that the recapture statute is not simply a "default" manner of dividing up the author's termination and recapture interest. Rather, Section 203(a)(5), when read literally, indicates that an author's heirs are barred from attempting to contract around the statute at all. Specifically, Section 203 provides that its copyright recapture scheme "may be effected notwithstanding any agreement to the contrary." [4]

[4] See Section 203(a)(5) (emphasis added).

There is scant case law explaining what exactly constitutes an "agreement to the contrary" under Section 203(a)(5). Nimmer reads the phrase to mean that "one who holds a termination right may exercise that right notwithstanding any agreement that would stand in the way." [5] Under that reading, an express agreement between a publisher and an author's heirs not to terminate a copyright grant would constitute an "agreement to the contrary." [6] In that instance, the purported agreement with the publisher would be unenforceable and the heirs would retain the ability to pursue their statutory termination and recapture rights vis-a-vis the publisher.

[5] Nimmer, at §11.07[E][4][a].

[6] Id. at §11.07[E][2][b][i].

**Questions Raised**

However, Section 203(a)(5), when read together with Section 203(a)(2) (which dictates the manner in which an author's heirs inherit his or her termination rights), raises some important questions:

- May the statutory heirs agree amongst themselves to contract around Section 203's descendability scheme?
- To what extent will Section 203 be interpreted by courts to supersede private contracts between statutory heirs who inherit joint interests in a copyright?
- Does Section 203 permit an author's surviving heirs to contractually allocate the author's copyrights amongst themselves (including applicable termination and recapture rights), or would such contract be deemed an unenforceable "agreement to the contrary?"

Plainly, Section 203 was intended to override an early assignment of rights from an author to a publisher. Thus, its main purpose was to limit the freedom of contracts running between creators and exploiters on the theory that the class of creators needs to be protected from a class that would have unequal bargaining power over young creators.

There is no basis to suggest, however, that this section was ever intended to second guess how a given creator divvies up her rights in her own works or among her own family. Yet these bulleted questions illustrate the fundamental tension between Section 203 on the one hand and authors' (and their heirs') freedom of contract as among themselves on the other.

**Illustrative Scenario**

We illustrate the alternative ways in which the federal courts might answer these questions by applying them to the following fictitious scenario:

A prolific mystery writer ("W") created 30 works during her lifetime. Many of her novels have been licensed to various publishing houses and movie studios. Her most famous work, The Guest, was licensed to a literary publisher ("P") on Dec. 1,

1978, and was subsequently made into a trilogy of popular films. W died in 2012 and is survived by her spouse (“S”) and two children (“C1” and “C2”). C1 does not get along with S or C2. All of W's property—including the 30 pieces of intellectual property in W's portfolio—has been distributed to W's heirs pursuant to the instructions in W's trust document. The trust provided that S, C1 and C2 will each inherit equal 1/3 interests in each of W's works.

More than half of W's works have already been published or made into films, but certain parties to those licensing deals are interested in printing new editions or producing sequels. Some of those licensees require W's heirs to make decisions regarding publishing, film and e-book deals. Other works in W's portfolio were never commercially developed during W's lifetime and will require additional time and effort to guide them to market. With respect to decisions that need to be made regarding the re-publication or development of W's works, W's heirs are now deadlocked as to how to move forward on any of those projects because C1 is unwilling to agree to the same terms as S and C2.

In 2012, a settlement agreement (“Agreement”) was negotiated between S, C1 and C2. Per the Agreement, each of S, C1 and C2 became the 100 percent owner of the intellectual property rights in and to 10 of W's works apiece. The Agreement therefore provides each heir with the complete freedom to commercially exploit the works in his or her “pot,” without the need to consult the other, potentially adverse heirs. As part of the settlement, C1 becomes the 100 percent owner of intellectual property rights in The Guest, including the right to receive all revenues therefrom.

### Who Owns the Termination Interest?

As a preliminary matter, we must consider how the above-described parties can give proper notice of copyright termination. Specifically, Section 203 provides that a termination notice needs to be timely filed, by the appropriate person or persons. With regards to the question of when to file the notice, the termination of the author's prior grant of copyright may be effected any time during a five-year period beginning at the end of 35 years from the date that the author executed the grant. [7] The notice must be signed by a majority of the owners of the termination interest, [8] it must state the effective date of the copyright termination and it must be served not less than two or more than 10 years before that date. [9]

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[7] 17 U.S.C. §203(a)(3).

[8] 17 U.S.C. §203(a)(4).

[9] 17 U.S.C. §203(a)(4)(A).

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Using our scenario, based on the Dec. 1, 1978, license that W gave to P for the publication of The Guest, the 35-year copyright term in that work will end on Dec. 1, 2013. If the parties involved determine that the copyright termination will become effective on Dec. 1, 2017 (within the five-year window after the 35-year term expires), then the termination notice must be served on P between Dec. 1, 2007, and Dec. 1, 2015.

The more difficult question here is who owns the termination interest. Can C1 try to recapture the rights in The Guest, based on the Agreement's purported assignment of 100 percent of the same rights to C1? Or does the termination interest remain in the control of S and C2, since they hold a majority of the termination interest under the inheritance scheme set forth in Section 203(a)(2)? And, more difficult still, once the termination right is invoked, who will benefit from it?

Courts could potentially apply Section 203 to the above case in one of two ways:

**Scenario 1**: The termination and recapture rights will always revert back to the statutory allocation, notwithstanding the terms of the Agreement.

Under this very strict reading of Section 203(a)(5), a majority of W's statutory heirs will always remain in control over all of W's termination interests—notwithstanding their attempt to negotiate a private settlement with one another—because any attempt to assign away those future termination rights would constitute an “agreement to the contrary” under Section 203(a)(5). Stated another way, even if the parties agree that C1 will own 100 percent of the copyrights and all related rights in The Guest, when the 35-year copyright term expires in 2013, the right to recapture the copyright in the novel will nevertheless vest in S, C1 and C2 in the 50-25-25 proportion mandated by Section 203(a)(2). Accordingly, the parties' attempt to assign 100 percent of their prospective termination interests in The Guest to C1 would be void.

Mischief could occur in this scenario because S and C2 would silently retain the ability to exercise their rights as the holders of a majority of the termination interest, with the power to terminate the existing studio or publishing licenses and then re-grant such licenses to third parties of their choosing—over C1's objection. Thereafter, C1 would only retain a 25 percent interest in the revenues from The Guest (compared to the 100 percent interest he previously agreed to take pursuant to the settlement). This reading of Section 203 would arguably deprive an author's heirs of their freedom to make private contracts with one

another. Indeed, it is possible (albeit unclear) that C1 could bring a claim against S and C2 for interference with the terms of the license agreements that C1 assumed under the settlement (or with C1's prospective advantage thereunder).

Scenario 2: The statutory heirs may enter into an enforceable contract that will avoid the 50-25-25 allocation of the termination interest dictated by Section 203(a)(2)(A), and C1 will continue to hold 100 percent of the termination interest in The Guest.

Under this scenario, a court would honor and enforce the private allocation of copyrights among S, C1 and C2, since those individuals constitute all of W's statutory heirs under Section 203(a)(2). Therefore, an assignment to C1 of 100 percent of the copyright in The Guest would include 100 percent of the associated termination rights under Section 203. S and C2 would have no further rights to interfere with C1's ownership of The Guest. This liberal—but arguably more practical—interpretation of Section 203 is based on the assumption that Section 203 was never intended to prevent the author's statutory heirs from striking a deal among themselves regarding the allocation of the author's various copyrights. Such a reading would also remain consistent with Congress' stated goal—to protect authors against “unremunerative transfers.”

**Related Case Law**

Although Scenario 2 above is based on a pragmatic reading of Section 203, the statute currently remains subject to the stricter, literal reading described in Scenario 1 above. At stake is the ability of an author's heirs to contract among themselves so as to freely allocate and to exploit their inherited copyrights, without fear that their settlement will be invalidated by a court.

We are not aware of any case law that directly addresses this problem. However, some cases that have interpreted Section 203 provide valuable insight into the extent to which authors or their heirs enjoy the freedom to make or break their own contracts.

The U.S. Court of Appeals for the Ninth Circuit in *Rano v. Sipa Press* interpreted Section 203 to provide that licensing agreements are not terminable at will from the moment of creation, but instead are terminable at the will of the author “only during a five year period beginning at the end of thirty-five years from the date of execution of the license unless they explicitly specify an earlier termination date.” [10] The *Rano* court went on to hold that Section 203's termination and recapture mechanism preempts a California common-law rule that permits the unilateral termination at will of an agreement that has a non-specified duration. [11] Based on this reasoning, the court found that a professional photographer was essentially “locked in” to a license agreement that he had made with a photograph distribution syndicate, for 35 years. [12]

[10] Section 203(a). In *Rano v. Sipa Press, Inc.*, 987 F.2d 580, 585, 26 U.S.P.Q.2d 1051 (9th Cir. 1993) (emphasis added).

[11] 987 F.2d at 585-86.

[12] Id. at 585-86.

*Rano* “has been called into serious question by courts as well as commentators.” [13] As the Seventh Circuit colorfully put it in *Walthal v. Rusk*, “If the *Rano* decision were a Broadway show, bad reviews would have forced it to close after opening night.” [14] Nevertheless, *Rano* is still the law in the Ninth Circuit.

[13] *Scholastic Entm't, Inc. v. Fox Entm't Group, Inc.*, 336 F.3d 982, 988 n. 2, 67 U.S.P.Q.2d 1464 (9th Cir. 2003).

[14] *Walthal*, 172 F.3d at 484. See also Nimmer, §11.01 (observing that the 35-year period in Section 203 is a maximum period that a contract can be enforced, not a minimum as *Rano* holds); Mark F. Radcliffe , “Copyright Ownership Issues,” 411 PLI/Pat at 243, 300 (Practicing Law Institute, “Patents, Copyrights, Trademarks, and Literary Property Course Handbook Series,” 1995) (calling *Rano* a “ridiculously incorrect interpretation of the statute. It takes a provision meant to protect the author and turns it into a straitjacket.”).

In contrast, the Seventh Circuit rejected *Rano*'s interpretation of Section 203. [15] Specifically, the Seventh Circuit held that Section 203 does not impose a mandatory 35-year minimum term on license agreements, and that state contract law is automatically incorporated into any contract pertaining to a transfer of copyright interests. [16] The Eleventh Circuit in *Korman v. HBC* [17] adopted the *Walthal* court's interpretation of Section 203 and also criticized *Rano*.

[15] See Walthal, 172 F.3d at 483-86.

[16] Id. at 485-86.

[17] *Korman v. HBC Fla., Inc.*, 182 F.3d 1291, 1295, 51 U.S.P.Q.2d 1672 (11th Cir. 1999).

**Conclusion**

The circuit split described above illustrates the inherent tension arising under Section 203, and the consequences of reading

the statute too literally. Whereas Congress intended the recapture provision to preserve authors' rights to negotiate favorable deals for themselves, some of Section 203's provisions can be interpreted so as to "straightjacket" the same authors (or their heirs) by limiting their freedom to terminate unfavorable contracts with third parties. Indeed, *Rano*'s interpretation of Section 203 would seem to turn the very purpose of the statute on its head.

Which solution will the federal courts adopt with respect to agreements made between an author's heirs? Only time will tell. What is certain is that the way in which courts construe Section 203 will have important and long lasting consequences for every single copyright license or assignment granted since 1978, particularly when the original author has died prior to the vesting of recapture rights, and her heirs have attempted to allocate copyrights among themselves.