

COMMENT

IHACK, THEREFORE IBRICK: CELLULAR CONTRACT LAW, THE APPLE IPHONE, AND APPLE’S EXTRAORDINARY REMEDY FOR BREACH

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Apple’s release of the iPhone was a highly anticipated event, promising to revolutionize the cellular phone industry as the iPod had previously done for the music industry. Like most cell phones though, the iPhone was tied to one carrier: AT&T. This restriction was untenable to some enthusiasts, who promptly “unlocked” the device for use on other carrier networks. Because doing so meant that customers could circumvent an AT&T service contract entirely, the situation threatened to undermine the Apple-AT&T business relationship. In response, Apple released a software update that crippled unlocked iPhones, and AT&T threatened purveyors of unlocking software with copyright lawsuits. This comment argues that the contractual provisions that portend to prohibit unlocking and justify Apple’s conduct are likely unenforceable as unconscionable under California law, and that AT&T’s threats based on copyright law are legally unsound and a misuse of copyright law. If nothing else, the iPhone “bricking” fiasco has put an exclamation point on consumer discontent with the anticompetitive U.S. cell-phone industry, and ultimately may serve as the harbinger of true cellular freedom.

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INTRODUCTION

Few companies enjoy the fiercely loyal following and resounding market success of Apple, which recently dropped “Computer” from its name in a nod to its looming ascendancy into the broader consumer-electronics realm.¹ With the release of the original iPod in 2001,² Apple revolutionized the music industry. The device, coupled with the launch of the iTunes Music Store in 2003,³ dragged the major record labels kicking and screaming into the twenty-first century. Steve Jobs⁴ and his cadre of engineers and designers at Apple next turned their sights to the cell phone industry, and in 2007 released another revolutionary, groundbreaking, game-changing product: the iPhone.⁵

1. The name change was announced January 9, 2007, at the Macworld Conference and Expo in San Francisco. Mathew Honan, *Apple Drops ‘Computer’ from Name*, MACWORLD.COM, Jan. 9, 2007, <http://www.macworld.com/article/54770/2007/01/applename.html>; see also Apple Inc., Report of Unscheduled Material Events or Corporate Changes (Form 8-K) (Jan. 9, 2007).

2. The original iPod was released October 23, 2001. See Press Release, Apple Inc., Apple Presents iPod (Oct. 23, 2001), available at <http://www.apple.com/pr/library/2001/oct/23ipod.html>.

3. Press Release, Apple Inc., Apple Launches the iTunes Music Store (Apr. 28, 2003), available at <http://www.apple.com/pr/library/2003/apr/28musicstore.html>.

4. Steve Jobs is the CEO and cofounder of Apple Inc. Apple.com, Bios – Steve Jobs, <http://www.apple.com/pr/bios/jobs.html> (last visited Sept. 21, 2008).

5. Press Release, Apple Inc., iPhone Premieres this Friday Night at Apple Retail Stores (June 28, 2007), available at <http://www.apple.com/pr/library/2007/06/28iphone.html>.

The response was incendiary. Having announced the product a full six months earlier during his annual “reality distortion field”⁶ Macworld keynote speech, Steve Jobs gave consumers, commentators and technophiles plenty of time to salivate over the latest offering.⁷ Fans literally camped out overnight at Apple and AT&T retail stores,⁸ AT&T being Apple’s exclusive partner in the iPhone venture,⁹ hoping to be the first to get their hands on the coveted new device.

While there were some minor complaints and noticeable omissions,¹⁰ in general the iPhone delivered. Its combination of features was compelling—cell phone, iPod, video player, personal organizer, wireless e-mail, Web browser—and all of it in a sleek, stylish handheld device with a gorgeous, high-resolution, touch-sensitive display.¹¹ iPhones flew off the shelves so fast that less than three months later, Apple celebrated its one-millionth unit sold,¹² despite a relatively high

6. “Reality distortion field” is a humorous reference to Steve Jobs’s unusual combination of charisma and salesmanship, often used to great effect at Macworld keynote speeches to induce excitement and anticipation in Apple’s latest products. *See, e.g.,* Jessica Guynn, *Questions Swirl Around Jobs as Macworld Opens*, S.F. CHRON., Jan. 9, 2007, at E1 (explaining how Apple employees borrowed the term from the “Star Trek” television series to describe Jobs); *see also* Jack Shafer, *The Apple Polishers: Explaining the Press Corps’ Crush on Steve Jobs and Company*, SLATE.COM, Oct. 13, 2005, <http://www.slate.com/id/2127924> (“Another thing that sets Apple product launches apart from those of its competition is cofounder Jobs’s psychological savvy. From the beginning, Jobs flexed his powerful reality-distortion field to bend employees to his will, so pushing the most susceptible customers and the press around with the same psi power only comes naturally.”).

7. *See* Press Release, Apple Inc., Apple Reinvents the Phone with iPhone (Jan. 9, 2007), available at <http://www.apple.com/pr/library/2007/01/09iphone.html>.

8. *See* David Pogue, *The iPhone Matches Most of Its Hype*, N.Y. TIMES, June 27, 2007, at C1.

9. Press Release, Apple Inc., Apple Chooses Cingular as Exclusive US Carrier for Its Revolutionary iPhone (Jan. 9, 2007), available at <http://www.apple.com/pr/library/2007/01/09cingular.html>. Cingular is now known as AT&T Wireless. Stuart Elliot, *AT&T Aims to Put Its Mark on Mobility*, NYTIMES.COM, Sept. 11, 2007, <http://www.nytimes.com/2007/09/11/business/media/11at-web.html?pagewanted=print> (“AT&T previously owned 60 percent of Cingular and acquired the rest when it took over the BellSouth Corporation. The Cingular brand has vanished; the cellular operations are now referred to as the AT&T wireless group.”).

10. At the time of release, the iPhone had no memory card, no instant messaging program, lacked a user-replaceable battery, could not capture video with the built-in camera, and did not support voice-commands or picture-messaging (known as MMS). Pogue, *supra* note 8.

11. *Id.*

12. Press Release, Apple Inc., Apple Sells One Millionth iPhone (Sept. 10, 2007), available at <http://www.apple.com/pr/library/2007/09/10iphone.html>.

initial price tag of \$499 to \$599.¹³ The device even garnered *Time* magazine's award for the best invention of 2007.¹⁴

The early adopters were not just buying a nifty new gadget, though. Due to an exclusive partnership between Apple and AT&T, they were also agreeing to a wireless service contract.¹⁵ Anyone who wanted to “reach out and touch someone”¹⁶ with the iPhone could only do so on AT&T's network, and only after agreeing to a full two years of service.¹⁷ Furthermore, the closed nature of the iPhone's software meant users could not write their own applications for the device.¹⁸ For a company that once encouraged its customers to “think different,”¹⁹ the situation was both intolerable to many Apple enthusiasts and an open invitation to hackers.²⁰ Terms of service, software-license agreements and contracts of adhesion²¹ aside, the hackers set to work breaking the iPhone free.²²

13. See Press Release, Apple Inc., *supra* note 7. Initially both a 4GB and 8GB models were offered, for \$499 and \$599, respectively. *Id.* The price has since been lowered to \$399 for the 8GB model and the 4GB model is discontinued. See Press Release, Apple Inc., Apple Sets iPhone Price at \$399 for this Holiday Season (Sept. 5, 2007), available at <http://www.apple.com/pr/library/2007/09/05iphone.html>.

14. Lev Grossman, *Invention of the Year: The iPhone*, TIME, Nov. 12, 2007, at 60.

15. See Press Release, Apple Inc., *supra* note 9; see also Press Release, Apple Inc., AT&T and Apple Announce Simple, Affordable Service Plans for iPhone (June 26, 2007), available at <http://www.apple.com/pr/library/2007/06/26plans.html> (discussing service contract options).

16. “Reach out and touch someone” was an advertising slogan used by AT&T in the early 1980's. Eric Zeman, *Reach Out And Touch Something*, INFORMATIONWEEK.COM, Sept. 26, 2007, 12:03 EST, http://www.informationweek.com/blog/main/archives/2007/09/reach_out_and_t_1.html.

17. See Press Release, Apple Inc., AT&T and Apple Announce Simple, Affordable Service Plans for iPhone, *supra* note 15.

18. See Pogue, *supra* note 8 (“You can't install new programs [on the iPhone] from anyone but Apple; other companies can create only iPhone-tailored mini-programs on the Web.”).

19. “Think Different” was the slogan for an Apple advertising campaign launched in September 1997. Charles Jade, *10 Years After “Think Different.”*, ARSTECHNICA.COM, Sept. 29, 2007, <http://arstechnica.com/journals/apple.ars/2007/09/29/10-years-of-think-different>.

20. See Li Yuan, *Hackers Bypass iPhone Limits*, ONLINE.WSJ.COM, July 6, 2007, http://online.wsj.com/article_email/SB118368127325158660-.html.

21. BLACK'S LAW DICTIONARY 342 (8th ed. 2004) (defining “adhesion contract” as “[a] standard-form contract prepared by one party, to be signed by the party in a weaker position, usually a consumer, who adheres to the contract with little choice about the terms”).

22. See Sumner Lemon, *Hackers Race to Unlock iPhone*, INFOWORLD.COM, July 2, 2007, <http://www.infoworld.com/article/07/07/02/Hackers-race-to-unlock-iphone1.html>.

Within a week, the hackers had succeeded in bypassing²³ the iPhone activation process.²⁴ This meant that the iPhone could be used as a Web browser and iPod without signing up for AT&T wireless service.²⁵ Progress was steady,²⁶ and the hackers soon unlocked the phone's file system to allow the execution of homemade programs, a process they coined "jail breaking."²⁷ Because the hackers shared their work online, third-party developers were now free to write their own programs for the iPhone.²⁸ However, the holy grail of wresting it free from AT&T's network remained elusive.

No hacking tale would be complete without a precocious teenage whiz-kid, and this one is no exception. Seventeen-year-old George Hotz in New Jersey made the first major breakthrough regarding the iPhone's cellular connectivity in late August 2007.²⁹ Using a combination of programming and a soldering iron, he unlocked his iPhone for use on T-Mobile's network.³⁰ Meanwhile, other groups of hackers were pursuing a more user-friendly method that would unlock the iPhone via software alone and succeeded in this effort only days later.³¹

23. See Yuan, *supra* note 20. One of the hackers involved was none other than "DVD Jon," the Norwegian hacker who figured out how to break the encryption on DVDs so they could be copied to computer hard drives. *Id.*

24. Unlike most cell phones, which are activated at the point of sale, the original iPhone activation process was completed at home by the customer using Apple's iTunes software. *Id.* ("New iPhone users are required to activate their handset using the latest version of iTunes, released on Friday, before they can use the phone."). See also Press Release, Apple Inc., Apple and AT&T Announce iTunes Activation and Sync for iPhone (June 26, 2007), available at <http://www.apple.com/pr/library/2007/06/26activate.html>.

25. See Yuan, *supra* note 20.

26. See *Apple iPhone: More Has Happened*, ONLINEREPORTER.COM, July 21, 2007, http://www.onlinereporter.com/article.php?article_id=10053; *Hackers Close to Cracking iPhone*, EWEEK.COM, July 16, 2007, <http://www.baselinemag.com/c/a/Security/Hackers-Close-to-Cracking-iPhone>.

27. See Arik Hesseldahl, *The Hackers' First Hello on the iPhone*, BUSINESSWEEK.COM, Aug. 3, 2007, http://www.businessweek.com/technology/content/aug2007/tc2007081_895247.htm; see also Mike Musgrove, *Introducing the New and Improved iPhone -- by Hackers*, WASH. POST, Aug. 23, 2007, at F1.

28. See Hesseldahl, *supra* note 27.

29. See Brad Stone, *With Software and Soldering, AT&T's Lock on iPhone Is Undone*, N.Y. TIMES, Aug. 25, 2007, at C1.

30. *Id.*

31. See Ryan Block, *iPhone Unlocked: AT&T Loses iPhone Exclusivity*, ENGADGET.COM, Aug. 24, 2007, 12:00 EST, <http://www.engadget.com/2007/08/24/iphone-unlocked-atandt-loses-iphone-exclusivity-august-24-2007>. The software-only method was developed by iPhoneSIMFree.com and demonstrated for the editors of Engadget.com. *Id.*

With the iPhone now doubly unlocked—open to third-party developers and functional on competing cellular networks—Apple and AT&T’s symbiotic business model and consumer-electronics coup was in serious jeopardy. These developments threatened Apple’s control over their proprietary technology and AT&T’s revenue from iPhone wireless service. In addition, the Apple-AT&T agreement involved an unprecedented revenue sharing of monthly service charges by AT&T with Apple.³² That revenue came along with a contractual obligation for Apple to prevent users from decoupling the iPhone from AT&T’s network.³³ If Apple turned a blind eye to widespread unlocking of the iPhone, it ran the risk of losing their exclusive deal with AT&T and the significant revenue that came with it.³⁴

The response was two-pronged: AT&T unleashed lawyers;³⁵ Apple unleashed software. On September 24, 2007, Apple issued a statement in advance of the release of their version 1.1.1 update for the iPhone: “Apple has discovered that many of the unauthorized iPhone unlocking programs available on the Internet cause irreparable damage to the iPhone’s software, which will likely result in the modified iPhone becoming *permanently inoperable* when a future Apple-supplied iPhone software update is installed.”³⁶ Furthermore, Apple noted that making “unauthorized modifications” to the software on the iPhone violates the software-license agreement and voids the warranty,³⁷ and added “[t]he

32. See Saul Hansell, *The \$831 iPhone*, NYTIMES.COM, Oct. 25, 2007, 12:41 EST, <http://bits.blogs.nytimes.com/2007/10/25/the-831-iphone>.

33. See Leslie Cauley, *iWeapon: AT&T Plans to Use Its Exclusive iPhone Rights to Gain the Upper Hand in the Battle for Wireless Supremacy*, USA TODAY, May 22, 2007, at 1B.

34. Even with the deal, Apple loses money on each unlocked phone because, unless iPhone purchasers actually sign up for wireless service with AT&T, there is no monthly revenue to share with Apple. See John Markoff, *Record Mac Sales Help Apple Earnings Climb 67% in Quarter*, N.Y. TIMES, Oct. 23, 2007, at C3.

35. A company planning on commercially releasing a software iPhone unlock held off when threatened with a copyright infringement and illegal software dissemination by AT&T lawyers. See Jacqui Cheng, *AT&T Legal Hits the Brakes on (Commercial) iPhone Unlocks*, ARSTECHNICA.COM, Aug. 27, 2007, <http://arstechnica.com/journals/apple.ars/2007/08/27/att-legal-hits-the-brakes-on-commercial-iphone-unlocks>.

36. Mark Hachman, *Update: Apple Issues Warning on iPhone Hacking*, PCMAGAZINE.COM, Sept. 24, 2007, <http://www.pcmag.com/article2/0,2817,2188296,00.asp> (emphasis added); David Zeiler, *Tinkering with iPhone Software Voids Apple Warranty*, BALT. SUN, Sept. 27, 2007, at 5D.

37. The author remains curious how modifying *software* violates a *hardware* warranty.

permanent inability to use an iPhone due to installing unlocking software is not covered under the iPhone's warranty."³⁸

When the update was released on September 27, 2007, the warnings proved true.³⁹ Reports began trickling in on the Internet from users whose iPhones were disabled entirely, or "bricked."⁴⁰ Those proud new owners of "iBricks" who took their crippled devices to Apple Stores for help were turned away, and an Apple spokeswoman offered an amusingly callous solution: "If the damage was due to use of an unauthorized software application, voiding their warranty, they should purchase a new iPhone."⁴¹

Refusing to service under warranty a product that has been tampered with by the customer is both reasonable and expected, but affirmatively disabling an expensive piece of consumer electronics for doing so is another issue altogether, and unprecedented. Apple had already drawn customers' ire, including iPhone-related lawsuits (regarding international roaming charges⁴² and lack of user-replaceable batteries⁴³) and backlash against a dramatic price drop only two months after the iPhone's release.⁴⁴ For some, "iBricking" was seen as the last straw and the source of legitimate legal complaint.

The hackers did find a way to "unbrick" some of the crippled iPhones,⁴⁵ but it was a complex, nineteen-step process⁴⁶ that only worked for iPhones unlocked with certain software.⁴⁷ Therefore, just over a week

38. Hachman, *supra* note 36.

39. See Katie Hafner, *Altered iPhones Freeze Up*, N.Y. TIMES, Sept. 29, 2007, at C1.

40. *Id.*

41. *Id.*

42. See Jacqui Cheng, *Class Action Suit Filed over iPhone Locking*, ARSTECHNICA.COM, Aug. 28, 2007, <http://arstechnica.com/journals/apple.ars/2007/08/28/class-action-suit-filed-over-iphone-locking>.

43. *iPhone Battery Design Leads to Lawsuit in U.S.*, INT'L HERALD TRIB., Aug 2, 2007, at 12.

44. See Katie Hafner & Brad Stone, *iPhone Owners Crying Foul Over Price Cut*, N.Y. TIMES, Sept. 7, 2007, at C1.

45. See Jacqui Cheng, *iPhoneSIMFree Issues Commercial iPhone 1.1.1 Unlock*, ARSTECHNICA.COM, Oct. 11, 2007, <http://arstechnica.com/journals/apple.ars/2007/10/11/iphonesimfree-issues-commercial-iphone-1-1-1-unlock> ("Not only does the newest unlock allow you to unlock your iPhones running the new firmware, it also lets you 'unbrick' anySIM or iUnlock unlocked iPhones (the two solutions released by the iPhone Dev Team).").

46. See Jacqui Cheng, *"iPhone Elite" Team Posts Free iPhone Unbricking Instructions*, ARSTECHNICA.COM, Oct. 12, 2007, <http://arstechnica.com/journals/apple.ars/2007/10/12/iphone-elite-team-posts-free-iphone-unbricking-instructions> ("19- (or 20, if you count step zero) step procedure might be a little bit of a pain.").

47. See *id.*

after the “bricking” occurred, Apple and AT&T were hit with two class-action lawsuits in both state⁴⁸ and federal⁴⁹ court in California, alleging, inter alia, antitrust violations, unfair competition, and breach of express and implied warranties.⁵⁰ The complaints sought monetary and injunctive relief.⁵¹

This Comment will address the legality of unlocking the iPhone under both California contract doctrine⁵² and federal copyright law. Part I provides some necessary background on basic cellular phone technology, the major U.S. carriers, and standard wireless industry practices. Part II describes the nature of the Apple-AT&T deal and briefly summarizes the class-action lawsuits. Part III discusses California contract doctrine, the relevance of copyright law, and congressional responses to consumer discontent with the wireless industry. Part III also introduces the iPhone contracts, while Part IV analyzes their validity under California law, arguing that Apple and AT&T’s attempts to prevent unlocking the iPhone via contract law are misguided and the contracts likely unenforceable. Part IV further argues that Apple grossly overreached by creating its own extra-legal remedy for breach in the form of “bricking” unlocked iPhones, and that AT&T’s legal threats based on copyright law are legally unsound, a misuse of copyright law and contrary to public policy. Finally, this Comment concludes that the inability of Apple and AT&T to leverage the law to protect their exclusive business model may

48. Complaint for Treble Damages and Permanent Injunctive Relief, *Smith v. Apple Inc.*, No. 1-07-CV-095781 (Super. Ct. Cal., Santa Clara County filed Oct. 5, 2007). The case was removed to federal court on Apple’s motion, Defendant Apple Inc.’s Notice of Removal, *Smith v. Apple Inc.*, No. C 07-05662 (N.D. Cal. filed Nov. 7, 2007), and consolidated with the other iPhone case. See Order Relating Cases; Consolidating Cases; and Setting Case Management Conference, *In re Apple & AT&TM Anti-Trust Litigation*, No. C 07-05152 JW, No. C 07-05662 RMW (N.D. Cal. Nov. 30, 2007).

49. Class Action Complaint for Damages, Injunctive Relief and Restitution, *Holman v. Apple Inc.*, No. C 07-05152 (N.D. Cal. filed Oct. 5, 2007); see Order Relating Cases; Consolidating Cases; and Setting Case Management Conference, *supra* note 48.

50. First Amended Complaint for Damages and Permanent Injunctive Relief, *Smith v. Apple Inc.*, No. 1-07-CV-095781 (Super. Ct. Cal., Santa Clara County filed Nov. 7, 2007) [hereinafter *Smith Amended Complaint*]; Class Action Complaint for Damages, Injunctive Relief and Restitution, *Holman v. Apple Inc.*, No. C 07-05152 (N.D. Cal. filed Oct. 5, 2007) [hereinafter *Holman Complaint*].

51. See *Smith Amended Complaint*, *supra* note 50, at 53; *Holman Complaint*, *supra* note 50, at 23–24.

52. The iPhone Software License Agreement explicitly states that California law will govern “as applied to agreements entered into and to be performed entirely within California between California residents.” Apple Inc., iPhone Software License Agreement, § 12, available at <http://images.apple.com/legal/sla/docs/iphone.pdf>.

ultimately sound the death knell of business as usual in the wireless industry.

I. OVERVIEW OF CELL PHONE TECHNOLOGY AND WIRELESS INDUSTRY PRACTICES

An explanation of the legal issues surrounding iPhone unlocking necessarily requires a brief overview of cellular technology and the business practices common among the large wireless carriers. This Part will explain the two dominant cellular communication standards, how “locking” is achieved with both of them, and how the wireless carriers use locked phones, lengthy contracts, and early-termination fees to enforce customer loyalty.

The majority of modern cell phones operate on one of two competing wireless standards: Code Division Multiple Access (CDMA) and Global System for Mobile Communication (GSM).⁵³ GSM is more widely used worldwide, accounting for approximately 85 percent of the global market.⁵⁴ CDMA is used primarily in the United States, South America, and Korea.⁵⁵

The technical details of the two standards are beyond the scope of this Comment, but it is sufficient to note that they are not compatible.⁵⁶ This means a phone designed for a GSM network cannot be used on a CDMA network, and vice versa.⁵⁷ Dual-mode phones that can function on both types of networks do exist, but they are intended primarily for international travelers.⁵⁸ Therefore, for purposes of economy and simplicity, the major wireless carriers in the United States⁵⁹ employ one

53. Tim Wu, *Wireless Carterfone*, 1 INT. J. OF COMM. 389, 399 (2007), available at <http://ijoc.org/ojs/index.php/ijoc/article/view/152/96>.

54. GSM WORLD, 20 FACTS FOR 20 YEARS OF MOBILE COMMUNICATIONS (2008), available at http://www.gsmworld.com/documents/20_year_factsheet.pdf.

55. Wu, *supra* note 53, at 425 n.25.

56. Cauley, *supra* note 33 (“AT&T uses GSM, a global standard incompatible with CDMA.”); see also Walt Mossberg, *Free My Phone*, ALLTHINGS.COM, Oct. 21, 2007, 21:31 EST, <http://mossblog.allthingsd.com/20071021/free-my-phone>.

57. See Mossberg, *supra* note 56 (“[W]e have two major, incompatible cell phone technologies in the U.S. . . . Except for a couple of oddball models, phones built for one of these technologies can’t work on the other.”).

58. See James Derk, *New World Phone Is Not Without Its Shortcomings*, INTELLIGENCER (Wheeling, WV), July 10, 2007, at D2 (noting that the Blackberry 8830 is a “World Phone” because “its dual-mode CDMA/GSM capability . . . allows it to be used in more than 150 countries with your same phone number”).

59. Cauley, *supra* note 33, at 1B tbl.1. AT&T is the leading wireless provider in the United States with 27.1% of the market, followed by Verizon (26.3%), Sprint Nextel

standard throughout their network. In the United States, AT&T and T-Mobile operate GSM networks; Verizon and Sprint Nextel use CDMA.⁶⁰

GSM phones and networks are particularly attractive to those who travel internationally. This is due to the standard's global dominance,⁶¹ as well as its support for exchangeable memory cards called subscriber identity module (SIM) cards.⁶² Because SIM cards identify the user and store contact information, upgrading or changing phones is as simple as swapping the card into a new GSM-compatible phone.⁶³ Conversely, new SIM cards can be swapped into an existing phone.⁶⁴ This is important because it allows GSM-phone owners traveling abroad to avoid international roaming charges,⁶⁵ which can be extremely expensive.⁶⁶ Swapping in a local carrier's prepaid SIM card makes the phone function as a local device on the foreign network, so calls are billed at relatively cheap local rates.⁶⁷

Replacing a SIM card is only possible with an "unlocked" GSM phone.⁶⁸ While most phones are sold unlocked worldwide, the wireless industry in the United States differs by locking cell phones to a particular carrier.⁶⁹ The method differs based on the underlying network technology. CDMA devices each have a unique ID number that the carriers can use to make sure only "approved" phones are allowed to connect to their network.⁷⁰ Those phones not on the approved list are

(23.6%), and T-Mobile (11.1%). *Id.* Other smaller carriers comprise the remaining 11.9% of the market. *Id.*

60. Wu, *supra* note 53, at 425.

61. See GSM WORLD, *supra* note 54.

62. Wu, *supra* note 53, at 426; see also *Gatton v. T-Mobile USA, Inc.*, 61 Cal. Rptr. 3d 344, 349 (Cal. Ct. App. 2007), *cert. denied*, *T-Mobile USA, Inc. v. Gatton*, No. 07-1036, 128 S. Ct. 2501, 2502 (May 27, 2008) (describing the allegations in plaintiff's complaint regarding T-Mobile's sale of handsets containing removable SIM cards).

63. Wu, *supra* note 53, at 426.

64. *Id.*

65. See Cyrus Farivar, *Locked vs. Unlocked: Opening Up Choice*, N.Y. TIMES, Nov. 1, 2007, at C9 ("[T]he advantage of having an unlocked GSM phone is that the phone can easily be used in other countries at a fraction of the usual charge by buying a local prepaid SIM card, the microchip that contains the telephone number and other data. Otherwise, consumers are left paying exorbitant international roaming fees.").

66. See, e.g., Katie Hafner, *Fun, Tours and a \$3,000 Bill for Hardly Using an iPhone*, N.Y. TIMES, Sept. 10, 2007, at C8.

67. See Farivar, *supra* note 65.

68. See Wu, *supra* note 53, at 426.

69. See John C. Dvorak, *Apple Bricking the iPhone*, PCMAGAZINE.COM, Oct. 1, 2007, <http://www.pcmag.com/article2/0,2817,2190855,00.asp>.

70. Wu, *supra* note 53, at 425–26. The CDMA identifier is called an electronic serial number (ESN), or mobile equipment ID (MEID). *Id.*

effectively locked out.⁷¹ GSM locks work differently and operate by programming the phone to reject SIM cards from a competing service provider.⁷² In that way, locked GSM phones are deprived of one of their primary benefits: the ability to operate on multiple networks.

The locks exist because typically, carriers heavily subsidize the cost of new cell phones, hoping to recover the cost of the phone over the life of a one- or two-year service agreement.⁷³ If consumers could purchase a steeply discounted phone and then promptly switch to a competing carrier, the carrier that subsidized the phone would incur a loss. This is also the reason that carriers have traditionally charged large fees if a customer terminates his service agreement early.⁷⁴

Cell phone locks can be undone, however, and the carriers hold the key. AT&T and Sprint Nextel will issue an unlock code to a customer on request, provided that customer has completed their service contract.⁷⁵

71. *Id.* at 426. However, Verizon, the largest U.S. CDMA carrier, recently announced plans to abandon its “whitelist” in 2008 and allow any device capable of connecting to operate on its network. See Nate Anderson, *Verizon Opens Up, Will Support Any Device, Any App on Its Network*, ARSTECHNICA.COM, Nov. 27, 2007, <http://arstechnica.com/news.ars/post/20071127-verizon-opens-up-will-support-any-device-any-app-on-its-network.html>. AT&T soon followed suit, announcing that customers could use any device by any manufacturer on AT&T’s network. See Leslie Cauley, *AT&T Flings Cellphone Network Wide Open*, USATODAY.COM, Dec. 5, 2007, http://usatoday.com/tech/wireless/phones/2007-12-05-att_N.htm. However, at least one commentator noticed that the announcement was somewhat disingenuous, because AT&T’s GSM network has always allowed any GSM-compatible device. See Tom Krazit, *AT&T Reopens Its Open Network*, CNET.COM, Dec. 6, 2007, http://news.cnet.com/8301-13579_3-9830094-37.html.

72. See Wu, *supra* note 53, at 426; see also *Gatton v. T-Mobile USA, Inc.*, 61 Cal. Rptr. 3d 344, 349 (Cal. Ct. App. 2007), *cert. denied*, *T-Mobile USA, Inc. v. Gatton*, No. 07-1036, 128 S. Ct. 2501, 2502 (May 27, 2008) (“T-Mobile employs a SIM lock to prevent its handsets from operating with a SIM card programmed for any other network.”).

73. See Wu, *supra* note 53, at 425. For example, AT&T currently offers a Blackberry Curve 8310 for a list price of \$349, but if purchased with a two-year service agreement the price is reduced to \$199. Wireless.att.com, Blackberry Curve 8310 – Titanium, http://www.wireless.att.com/cell-phone-service/cell-phone-details/?q_sku=sku1070078 (last visited Sept. 21, 2008).

74. Lisa Vaas, *Hackers Close to Cracking iPhone*, EWEK.COM, July 16, 2007, <http://www.eweek.com/c/a/Security/Hackers-Close-to-Cracking-iPhone> (“Wireless carriers impose early termination fees purportedly to recoup lost revenues from discounted or free phones they use to lure in new customers . . .”). However, both AT&T and Verizon announced plans in 2007 to prorate those fees based on the length of the remaining contract. See Jacqui Cheng, *AT&T Tries to Preempt Congress with Prorated Termination Fees*, ARSTECHNICA.COM, Oct. 16, 2007, <http://arstechnica.com/news.ars/post/20071016-att-tries-to-preempt-congress-with-prorated-termination-fees.html>.

75. Farivar, *supra* note 65.

But AT&T specifically excludes the iPhone,⁷⁶ and Sprint Nextel only agreed to unlock its phones in order to settle a class-action lawsuit.⁷⁷ T-Mobile will unlock a customer's phone after an account has been active for ninety days, and, while Verizon will not unlock phones at all,⁷⁸ it recently announced an ambitious open-access plan for its network starting in 2008.⁷⁹ The carriers are not eager to provide unlock codes because doing so only frees up their customers for the competition.⁸⁰ Therefore, as the iPhone situation demonstrates, the carriers use a combination of technology and contract law to enforce customer loyalty.

II. THE APPLE-AT&T PARTNERSHIP AND THE CLASS-ACTION LAWSUITS

The business relationship between Apple and AT&T is a first in many respects for the wireless industry. This Part describes what makes the agreement so unusual and also provides a brief overview of the class-action lawsuits filed against both Apple and AT&T in California. The merits of the lawsuits are not addressed; rather they are summarized as a means of introducing the underlying legal issues, as well as demonstrating how strongly Apple's actions and policies regarding the iPhone have resonated with the general public.

A. The Apple-AT&T Partnership

If the iPhone is Apple's baby, then AT&T is the godfather. Unlike the iPod, which was essentially a stand-alone cash-cow for Apple,⁸¹ the nature of the iPhone as a cellular device meant that Apple either had to become a wireless-service provider itself or make the iPhone a joint venture by partnering with one.⁸² Apple chose the latter approach.

76. According to Apple spokeswoman Jennifer Bowcock, "Neither [Apple nor AT&T] will provide an unlock code for the iPhone." Phuong Cat Le, *Want Your iPhone Unlocked? Too Bad*, SEATTLE POST-INTELLIGENCER, July 3, 2007, at C1.

77. Farivar, *supra* note 65; *see also Sprint Nextel to Unlock Phone Software*, SAN JOSE MERCURY NEWS, Oct. 27, 2007, at 3C.

78. Farivar, *supra* note 65.

79. *See* Anderson, *supra* note 71.

80. This follows from the fact that the cellular communication standards are not carrier specific. *See supra* text accompanying notes 56–60.

81. *See* Laurie Flynn, *Apple's Profit Quadruples, Thanks to iPod*, N.Y. TIMES, Jan. 13, 2005, at C1.

82. *See* Fred Vogelstein, *Weapon of Mass Disruption*, WIRED, Jan. 9, 2008, at 124, available at http://www.wired.com/gadgets/wireless/magazine/16-02/ff_iphone ("Apple was prepared to consider an exclusive arrangement to get [the iPhone] deal done.

The exact details of the business relationship between Apple and AT&T have not been disclosed, but some provisions are generally known. The five-year deal makes AT&T the exclusive wireless-service provider for the iPhone in the United States.⁸³ Apple and AT&T comarketed the device and originally offered it for sale in both their retail and online stores.⁸⁴ Perhaps most significantly, it is widely believed that AT&T shares monthly subscriber revenue with Apple,⁸⁵ a provision unprecedented in the wireless industry.⁸⁶ In fact, Apple's first choice for a wireless partner, Verizon, balked when Apple demanded (among other things)⁸⁷ a share of monthly service revenues from iPhone subscribers.⁸⁸

In another departure from business-as-usual in the wireless industry, AT&T did not subsidize the cost of the first-generation iPhone.⁸⁹ This is why the original asking price of \$499 to \$599 seemed quite high for those used to getting a phone for "free" or relatively cheaply when signing up for new cellular service. But this point begs the question: if AT&T did not need the monthly service fees to recoup the price of the

But Apple was also prepared to buy wireless minutes wholesale and become a de facto carrier itself.").

83. Le, *supra* note 76.

84. Press Release, Apple Inc., AT&T and Apple Announce Simple, Affordable Service Plans for iPhone (June 26, 2007), available at <http://www.apple.com/pr/library/2007/06/26plans.html>.

85. See Michelle Kessler, *Apple Tries to Crack Down on iPhone Abusers*, USA TODAY, Nov. 5, 2007, at 2B ("[Apple] . . . is widely believed to have a revenue-sharing deal with AT&T."); see also Hansell, *supra* note 32 ("AT&T appears to be paying \$18 a month, on average, to Apple for each iPhone activated on its network.").

86. See John Cox, *Apple to Release Unlocked iPhone in France*, NETWORKWORLD.COM, Oct. 17, 2007, <http://www.networkworld.com/news/2007/101707-apple-to-release-unlocked.html> (quoting a wireless executive who said that having handset manufacturers demand a share of revenues is a significant change for the industry).

87. See Robert W. Hahn et al., *The Economics of "Wireless Net Neutrality,"* 3 J. COMPETITION L. & ECON. 399, 430–31 (2007).

88. Ryan Kim, *Competitors Wrestling with iPhone*, S.F. CHRON., Nov. 5, 2007, at E1 ("Verizon Wireless famously passed on the iPhone after taking a look at the customer service, retail and revenue sharing arrangements required by Apple.").

89. Peter Svensson, *Lockdown on the iPhone*, INTELLIGENCER (Wheeling, WV), Aug. 30, 2007, at C8 ("Most U.S. phones are locked to their carrier when sold, since the carrier subsidizes the cost of the phone. The iPhone, however, is apparently not subsidized by AT&T."). In contrast to the original iPhone, the new iPhone 3G, released July 11, 2008, is subsidized by AT&T, starting at \$199 for the 8-GB model. See Peter Svensson, *"Unlockers" Face Apple's Obstacles with New iPhone*, SEATTLE TIMES, June 11, 2008, at C4.

iPhone, then why did it insist on locking the iPhone to its network?⁹⁰ The answer of course is business, pure and simple. With ownership of cell phones reaching the saturation point among consumers,⁹¹ the carriers now focus less on adding new customers than stealing existing ones.⁹² With the iPhone in its arsenal, AT&T has been doing just that.⁹³

B. The Class-Action Lawsuits

Two iPhone-related class-action lawsuits were filed against Apple in 2007⁹⁴ and subsequently consolidated in federal district court under the caption *In Re Apple & AT&TM Anti-Trust Litigation*.⁹⁵ The first suit, *Smith v. Apple Inc.*,⁹⁶ was originally filed in California state court but removed to federal court on Apple's motion.⁹⁷ The amended complaint named both Apple and AT&T as defendants⁹⁸ and asserted fourteen causes of action, including antitrust violations,⁹⁹ unfair competition,¹⁰⁰ common-law monopolization,¹⁰¹ and breach of express and implied

90. Not to mention, it also continued to charge a \$175 early-termination fee. AT&T Knowledge Ventures, AT&T Postpaid Terms of Service, available at http://www.apple.com/legal/iphone/us/terms/service_att.html.

91. See Cauley, *supra* note 33 (noting that “78% of U.S. households have a mobile phone,” and “[f]or the most part . . . anybody who wants a cell phone has one”).

92. *Id.* (explaining that because Wall Street values the carriers based on how many new subscribers they add each month, carriers are increasingly trying to steal their competitors' customers instead of adding entirely new customers).

93. See Kim, *supra* note 88 (“The success of the iPhone, which sold 1.4 million units in its first 90 days, has come at the expense of Palm and T-Mobile, which both lost customers after the iPhone came out, according to the NPD Group research firm.”).

94. See *supra* text accompanying notes 48–49.

95. Order Relating Cases; Consolidating Cases; and Setting Case Management Conference, *In re Apple & AT&TM Anti-Trust Litigation*, No. C 07-05152 JW, No. C 07-05662 RMW (N.D. Cal. Nov. 30, 2007).

96. No. 1-07-CV-095781 (Super. Ct. Cal., Santa Clara County filed Oct. 5, 2007).

97. Defendant Apple Inc.'s Notice Of Filing Of Removal To Federal Court, *Smith v. Apple Inc.*, No. 1-07-CV-095781 (Super. Ct. Cal., Santa Clara County filed Nov. 7, 2007).

98. *Smith Amended Complaint*, *supra* note 50, at 1.

99. The complaint asserts violations of the California Cartwright Act for unlawful trusts and unlawful tying agreements, CAL. BUS. & PROF. CODE §§ 16720, 16727 (West 2008), as well as violations of the Sherman Antitrust Act for unlawful tying and monopolization, 15 U.S.C. §§ 1, 2. *Smith Amended Complaint*, *supra* note 50, at 3–4.

100. The unfair-competition claims are based on a violation of section 17200 of the California Business & Professions Code. *Smith Amended Complaint*, *supra* note 50, at 4.

101. *Id.*

warranties,¹⁰² among others.¹⁰³ The complaint demanded a jury trial and sought relief in the form of treble damages,¹⁰⁴ disgorgement of profits, permanent injunctive relief, costs, and attorney's fees.¹⁰⁵

The second complaint, *Holman v. Apple Inc.*,¹⁰⁶ also named both Apple and AT&T as defendants.¹⁰⁷ It asserted similar causes of action (antitrust and unfair competition),¹⁰⁸ but also added a computer trespass/trespass to chattels claim¹⁰⁹ and demanded an accounting.¹¹⁰ The complaint also demanded a jury trial¹¹¹ and sought restitution; actual, compensatory and punitive damages; injunctive and declaratory relief; costs; and attorney fees.¹¹²

Both complaints alleged that Apple and AT&T illegally conspired to restrain competition and lock customers into using AT&T's wireless services.¹¹³ Furthermore, the complaints alleged that once customers began unlocking their iPhones, Apple deliberately punished them by releasing the software update designed to "brick" the devices,¹¹⁴ then refused to service the iPhones under warranty. The antitrust and warranty¹¹⁵ claims are beyond the scope of this Comment, but contract

102. *Id.*

103. The remaining causes of action were for breach of the Song-Beverly Consumer Warranty Act, CAL. CIV. CODE §§ 1790–1795.7 (West 2007), violation of the Consumer Legal Remedies Act, *id.* § 1750, violation of the Computer Fraud Abuse Act, 18 U.S.C. § 1030, violation of the California Penal Code, CAL. PENAL CODE § 502 (West 1999), and violation of the Racketeer Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. §§ 1961–1968. *Smith Amended Complaint*, *supra* note 50, at 4.

104. Under federal law, a jury trial is generally available in antitrust treble damages suits, provided a timely demand is made and "the issues are not so complex as to unduly confuse a jury." 54 AM. JUR. 2D *Monopolies and Restraints of Trade* § 635 (2008). Because both complaints allege violations of the Sherman Antitrust Act, the demand for a jury trial contained in the complaints will likely be granted if the case goes to trial.

105. *Smith Amended Complaint*, *supra* note 50, at 52–54.

106. *Holman Complaint*, *supra* note 50, at 1.

107. *Id.*

108. *Id.* at 18–22.

109. *Id.* at 22–23.

110. *Id.* at 23.

111. *Id.* at 1.

112. *Id.* at 23–24.

113. *Id.* at 9–12; *Smith Amended Complaint*, *supra* note 50, at 5–6.

114. *Holman Complaint*, *supra* note 50, at 11–12; *Smith Amended Complaint*, *supra* note 50, at 19–20.

115. This Comment does not contend that Apple is unjustified in refusing to service iPhones under warranty that were unlocked by means of a hardware modification. The limited hardware warranty explicitly does not apply "to damage caused by operating the product outside the permitted or intended uses described by Apple," or "to a product

and copyright issues related to the iPhone unlocking are addressed below.

III. CONTRACT, CONGRESS AND COPYRIGHT

This Part describes California contract doctrine, particularly “click-wrap” contracts of adhesion and unconscionability. The focus is on California because Apple’s iPhone software-license agreement specifically states that California law will control how the agreement is governed and construed.¹¹⁶ The relevance of copyright law to the iPhone locking issue is explained, as is the congressional response to consumer discontent in the wireless industry. Lastly, the substantive provisions of both Apple’s and AT&T’s contracts are summarized.

A. California Contract Law

California has adopted many provisions of the Uniform Commercial Code as embodied in the California Commercial Code.¹¹⁷ Sections of the California Civil Code also pertain to unlawful and unconscionable contracts,¹¹⁸ as well as consumer warranties.¹¹⁹

1. SHRINK- AND CLICK-WRAP CONTRACTS

Shrink-wrap contracts are contracts of adhesion contained inside retail software packages sealed with plastic or cellophane.¹²⁰ These

or part that has been modified to alter functionality or capability without the written permission of Apple.” See Apple Inc., Apple One (1) Year Limited Warranty, available at <http://images.apple.com/legal/warranty/iphone.pdf>. Apple likely bases its decision not to service unlocked iPhones on the “altered functionality” clause, as it is unclear how a *software only* method of unlocking the phone could actually damage the device’s hardware.

116. See iPhone Software License Agreement, *supra* note 52, § 12. This choice of law provision would likely be upheld by courts. See *infra* note 202.

117. See generally CAL. COM. CODE (West 2002). California has adopted “2001 Revision of Article 1, Article 2A (Leases), 1990 Revision of Article 3, 1990 Amendments to Article 4, Article 4A (Funds Transfers), 1995 Revision of Article 5, 1989 Revision of Article 6, 2003 Revision of Article 7, 1994 Revision of Article 8, and 2000 Revision of Article 9.” *Id.*, annot. However, the adoption was not verbatim. Charles J. Williams, *California Legislative Changes in Uniform Commercial Code Subsequent to Adoption*, in CAL. COM. CODE 26 (“California made over 120 changes from the Official Text, more than any other state.”).

118. CAL. CIV. CODE §§ 1667–1670.6 (West 2007).

119. *Id.* §§ 1790–1795.7.

120. See *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447, 1449 (7th Cir. 1996).

contracts are called software or end-user license agreements,¹²¹ and stipulate terms of use which the consumer can either accept by using the software or reject by returning the package to the store.¹²² The enforceability of such contracts was upheld in the well-known case of *ProCD v. Zeidenberg*.¹²³ However, shrink-wrap contracts remain vulnerable to challenges based on generally applicable contract defenses, such as fraud, duress or unconscionability.¹²⁴

Click-wrap contracts are similar to shrink-wrap contracts, but derive their name from the fact that the contract is displayed on a computer screen and accepted when the consumer clicks a button indicating agreement.¹²⁵ With the rapid growth of the Internet, click-wrap contracts have become especially useful for conducting business online.¹²⁶ They have also become ubiquitous in mass-market software distribution, with a consumer being required to click through one or more agreements

121. See *infra* Part III.C (discussing software-license agreements).

122. *ProCD, Inc.*, 86 F.3d at 1452. The *ProCD* decision has been widely followed. See, e.g., *Register.com, Inc. v. Verio, Inc.*, 356 F.3d 393, 428 (2d Cir. 2004); *Hill v. Gateway 2000, Inc.*, 105 F.3d 1147, 1148 (7th Cir. 1997); *Static Control Components, Inc. v. Lexmark Int'l, Inc.*, 487 F. Supp. 2d 830, 844–47 (E.D. Ky. 2007); *Meridian Project Sys., Inc. v. Hardin Const. Co.*, 426 F. Supp. 2d 1101, 1106–07 (E.D. Cal. 2006); *Schultz v. AT&T Wireless Servs., Inc.*, 376 F. Supp. 2d 685, 692 (N.D. W.Va. 2005); *I.Lan Sys., Inc. v. NetScout Serv. Level Corp.*, 183 F. Supp. 2d 328, 338 (D. Mass. 2002); *Pollstar v. Gigmania Ltd.*, 170 F. Supp. 2d 974, 981 (E.D. Cal. 2000); *Brower v. Gateway 2000, Inc.*, 676 N.Y.S.2d 569, 572 (N.Y. App. Div. 1998). But see *Step-Saver Data Sys., Inc. v. Wyse Tech.*, 939 F.2d 91 (3d Cir. 1991); *Vault Corp. v. Quaid Software Ltd.*, 847 F.2d 255 (5th Cir. 1988).

123. 86 F.3d at 1449.

124. See *id.* This follows from the fact that shrink-wrap contracts represent simply a different method of contract formation, and are not a qualitatively different legal obligation from traditionally formed contracts. Indeed, as the court in *ProCD* noted, using the software after reading the terms constituted acceptance by conduct under UCC section 2-204(1). *Id.* at 1452. A common defense with regard to shrink- and click-wrap contracts is inadequate notice of the terms. See, e.g., *Softman Products Co. v. Adobe Sys., Inc.*, 171 F. Supp. 2d 1075, 1087–88 (C.D. Cal. 2001) (determining that the software reseller was not bound by end-user license agreement because the agreement was only displayed when installing the software, something the reseller did not itself do).

125. *Stomp, Inc. v. NeatO, LLC*, 61 F. Supp. 2d 1074, 1081 n.11 (C.D. Cal. 1999) (“A ‘clickwrap agreement’ allows the consumer to manifest its assent to the terms of a contract by ‘clicking’ on an acceptance button on the [computer] The term ‘clickwrap agreement’ is borrowed from the idea of ‘shrinkwrap agreements,’ which are generally license agreements placed inside the cellophane ‘shrinkwrap’ of computer software boxes.”); see also BLACK’S LAW DICTIONARY 1195 (8th ed. 2004) (defining point-and-click agreement).

126. See, e.g., *Comb v. PayPal, Inc.*, 218 F. Supp. 2d 1165, 1169 (N.D. Cal. 2002) (explaining that PayPal’s user agreement is a click-wrap contract formed when the user clicks on an “I Agree” button or submits payment through the service).

before installing or updating software.¹²⁷ As with their shrink-wrap brethren, click-wrap contracts are generally enforceable, but subject to standard contract defenses.¹²⁸

2. UNCONSCIONABILITY

A contractual defense implicated by the iPhone contracts is unconscionability. Contractual unconscionability under California law is comprised of both procedural and substantive elements.¹²⁹ The procedural element “focus[es] on oppression or surprise due to unequal bargaining power”¹³⁰ Substantive unconscionability is found in overly harsh or one-sided results.¹³¹ While both elements are required for a finding that a particular contract provision is unconscionable, California courts apply a “sliding scale,” so that a greater degree of procedural unconscionability will compensate for a lesser degree of substantive unconscionability, and vice versa.¹³²

Procedural unconscionability is often found in a contract of adhesion, which is defined as “a standardized contract, imposed upon the subscribing party without an opportunity to negotiate the terms.”¹³³ Contracts of adhesion can be oppressive because they are drafted by parties of superior bargaining power and leave the consumer with “an

127. For this reason they are sometimes also referred to as click-through contracts. See *Brazil v. Dell Inc.*, No. C-07-01700 RMW, 2007 WL 2255296, at *1–2 (N.D. Cal. Aug. 3, 2007). However, that can lead to confusion because click-through is a term of art in Internet advertising used to describe when a Web user clicks “through” an online advertisement to reach the sponsoring site. See, e.g., *Coremetrics, Inc. v. AtomicPark.com, LLC*, 370 F. Supp. 2d 1013, 1018 (N.D. Cal. 2005). For this reason this Comment will use the less ambiguous click-wrap to refer to these contracts.

128. See generally, Kevin W. Grierson, Annotation, *Enforceability of “Clickwrap” or “Shrinkwrap” Agreements Common in Computer Software, Hardware, and Internet Transactions*, 106 A.L.R. 5TH 309, § 4[a]–[d] (2003).

129. See *Shroyer v. New Cingular Wireless Servs., Inc.*, 498 F.3d 976, 981 (9th Cir. 2007) (citing *Discover Bank v. Superior Court*, 113 P.3d 1100 (Cal. 2005)). In *Discover Bank*, the California Supreme Court set forth the test for unconscionability in holding unenforceable a class arbitration waiver included in a consumer credit card agreement. 113 P.3d at 1108–10.

130. *Shroyer*, 498 F.3d at 982 (quoting *Discover Bank*, 113 P.3d at 1108).

131. *Id.*

132. *Id.* at 981–82 (quoting *Armendariz v. Found. Health Psychcare Servs., Inc.*, 6 P.3d 669, 690 (Cal. 2000)).

133. *Id.* at 983 (quoting *Nagrampa v. MailCoups, Inc.*, 469 F.3d 1257, 1281 (9th Cir. 2006) (en banc)).

absence of meaningful choice.”¹³⁴ Surprise can exist if such contracts contain language in the “fine print” that contradicts the consumer’s understanding of the terms.¹³⁵ Therefore, “a finding of a contract of adhesion is essentially a finding of procedural unconscionability.”¹³⁶

The nature of substantive unconscionability was illustrated in a pair of recent cases where the California unconscionability doctrine was applied.¹³⁷ Tellingly, both were class-action lawsuits that challenged provisions included in wireless-service agreements.¹³⁸

In the first case, *Gatton v. T-Mobile USA, Inc.*,¹³⁹ the plaintiffs alleged unfair business practices regarding T-Mobile’s early-termination fees and practice of locking cell phones to their network.¹⁴⁰ T-Mobile moved to compel arbitration, invoking the mandatory arbitration and class-action-waiver provisions of its service agreement.¹⁴¹ The trial court denied the motion and the Court of Appeal affirmed, finding the class-action waiver unconscionable and, therefore, the arbitration clause unenforceable.¹⁴²

Similarly, the United States Court of Appeals for the Ninth Circuit found a class-arbitration waiver in a standard contract for cellular-phone service unconscionable in *Shroyer v. New Cingular Wireless Services, Inc.*¹⁴³ The plaintiffs in *Shroyer* asserted a variety of claims under California law, including, inter alia, untrue and misleading advertising, fraud and deceit, and unjust enrichment with regard to Cingular’s business practices following its merger with AT&T Wireless in 2004.¹⁴⁴ After removal to federal court,¹⁴⁵ Cingular’s motion to compel arbitration was granted and the case dismissed without prejudice.¹⁴⁶ The Ninth

134. *Gatton v. T-Mobile USA, Inc.*, 61 Cal. Rptr. 3d 344, 352 (Cal. Ct. App. 2007) (quoting *Flores v. Transamerica HomeFirst, Inc.*, 113 Cal. Rptr. 2d 376, 381 (Cal. Ct. App. 2001)), *cert. denied*, No. 07-1036, 128 S. Ct. 2501, 2502 (May 27, 2008).

135. *Id.* (quoting *Stirlen v. Supercuts, Inc.*, 60 Cal. Rptr. 2d 138, 145 (Cal. Ct. App. 1997)).

136. *Id.* at 353 (quoting *Flores*, 113 Cal. Rptr. 2d at 382).

137. *See Shroyer*, 498 F.3d at 976; *Gatton*, 61 Cal. Rptr. 3d at 356–58.

138. *Shroyer*, 498 F.3d at 979; *Gatton*, 61 Cal. Rptr. 3d at 348.

139. 61 Cal. Rptr. 3d at 344.

140. *Id.* at 346. Since T-Mobile is a GSM carrier, the lock employed was the SIM-lock discussed earlier in Part I.

141. *Id.* at 349.

142. *Id.* at 358.

143. 498 F.3d at 978.

144. *Id.* at 979.

145. The case was removed to the United States District Court for the Central District of California. *Id.* at 980.

146. *Id.* at 981.

Circuit reversed and remanded, holding the class-arbitration waiver unconscionable under California law.¹⁴⁷

In both cases, the procedural element of unconscionability was met because the standardized consumer contracts at issue were contracts of adhesion.¹⁴⁸ The availability of market alternatives as a factor mitigating procedural unconscionability was expressly considered and rejected by both courts.¹⁴⁹ The class-action waivers were found substantively unconscionable because they were indistinguishable from the class-action waiver held unenforceable in *Discover Bank v. Superior Court of Los Angeles*.¹⁵⁰ In *Discover Bank*, the California Supreme Court explained that such waivers are inherently one-sided because large companies “typically do not sue their customers in class-action lawsuits.”¹⁵¹ Furthermore, waivers are fundamentally unfair because absent class actions or arbitration, consumers may be denied vindication of substantive rights.¹⁵² Lastly, to the extent that such waivers allow companies to shield themselves from wrongful conduct, they are contrary to public policy, which provides an independent statutory basis for denying their enforcement.¹⁵³

In summary, contract formation via click-wrap is generally accepted under California law. However, such contracts of adhesion can usually be classified as procedurally unconscionable by definition; a finding of substantive unconscionability is a more fact-intensive inquiry. An

147. *Id.* at 993.

148. *Id.* at 983; *Gatton v. T-Mobile USA, Inc.*, 61 Cal. Rptr. 3d 344, 353 (Cal. Ct. App. 2007), *cert. denied*, *T-Mobile USA, Inc. v. Gatton*, No. 07-1036, 128 S. Ct. 2501, 2502 (May 27, 2008).

149. *Shroyer*, 498 F.3d at 985 (“California has rejected the notion that the availability . . . of substitute . . . services *alone* can defeat a claim of procedural unconscionability.” (alteration in original) (citations omitted)); *Gatton*, 61 Cal. Rptr. 3d at 353 (“[W]e reject the contention that the existence of market choice altogether negates the oppression aspect of procedural unconscionability.”).

150. *Shroyer*, 498 F.3d at 983; *Gatton*, 61 Cal. Rptr. 3d at 358.

151. *Discover Bank v. Superior Court*, 113 P.3d 1100, 1109 (Cal. 2005) (quoting *Szetela v. Discover Bank*, 118 Cal. Rptr. 2d 862, 867 (Cal. Ct. App. 2002)).

152. *Id.* at 1109.

153. *Id.* at 1108 (“All contracts which have for their object, directly or indirectly, to exempt anyone from responsibility for his own fraud, or willful injury to the person or property of another, or violation of law, whether willful or negligent, are against the policy of the law.” (quoting CAL. CIV. CODE § 1668 (West 1985))). While *Discover Bank* articulated the general rule of unconscionability in California, on remand the Court of Appeals held that the class-action waivers in the case were nonetheless enforceable because a choice-of-law analysis dictated that the law of Delaware, *Discover Bank*’s place of business, should apply. See *Discover Bank v. Superior Court*, 36 Cal. Rptr. 3d 456, 459 (Cal. Ct. App. 2005).

application of California contract doctrine to the iPhone contracts is discussed in Part IV.

B. Congressional Reaction & The Relevance of Copyright Law

The restrictions surrounding cell phones in general, and the iPhone in particular, have not escaped the attention of the federal government. In 2006, the Librarian of Congress determined that unlocking cell phones for the purpose of connecting to a wireless network is a legal activity, at least insofar as copyright law is concerned.¹⁵⁴ Copyright law is relevant because the Digital Millennium Copyright Act (DMCA)¹⁵⁵ makes it illegal to “circumvent a technological measure that effectively controls access to a [copyrighted] work”¹⁵⁶ Broadly construed, this provision would include the software locks that control access to cell phones’ copyrighted operating software.¹⁵⁷

The Librarian of Congress’s decision came as part of the triennial rule-making process required by the DMCA.¹⁵⁸ The Act authorizes the Register of Copyrights to recommend the exemption of certain classes of copyrighted works from the DMCA’s anticircumvention provisions.¹⁵⁹ These exemptions¹⁶⁰ are warranted where technological access controls

154. Exemption to Prohibition on Circumvention of Copyright Protection Systems for Access Control Technologies, 71 Fed. Reg. 68,472, 68,476 (Nov. 27, 2006) (codified at Patent, Trademarks, and Copyrights, 37 C.F.R. § 201.40 (2007)). Specifically, the exemption covers “[c]omputer programs in the form of firmware that enable wireless telephone handsets to connect to a wireless telephone communication network, when circumvention is accomplished for the sole purpose of lawfully connecting to a wireless telephone communication network.” *Id.*

155. 17 U.S.C. §§ 1201–1205 (West 2000).

156. *Id.* § 1201(a)(1)(A).

157. *See, e.g.*, Marybeth Peters, Recommendation of the Register of Copyrights, U.S. Copyright Office, at 48 (Nov. 17, 2006), http://www.copyright.gov/1201/docs/1201_recommendation.pdf (“Generally, [cellular-phone] software locks prevent customers from using their handsets on a competitor’s network by controlling access to the software that operates the mobile phones (*e.g.*, the mobile firmware).”).

158. *See* 17 U.S.C. § 1201(a)(1)(C) (“[D]uring each succeeding 3-year period, the Librarian of Congress, upon the recommendation of the Register of Copyrights . . . shall make the determination in a rule-making proceeding . . . whether persons who are users of a copyrighted work are, or are likely to be in the succeeding 3-year period, adversely affected by the [anticircumvention] prohibition . . . in their ability to make noninfringing uses under this title of a particular class of copyrighted works.”).

159. *Id.* § 1201(a)(1)(B)-(C).

160. *Id.* § 1201(a)(1)(B). The exemptions last for three years, until the next rule-making proceeding. *Id.* § 1201(a)(1)(D).

would adversely affect the ability of individuals to make otherwise lawful noninfringing uses of copyrighted works.¹⁶¹

At issue during the 2006 DMCA rule-making proceeding was whether unlocking cell phones constituted a circumvention of a technological access control in violation of the DMCA.¹⁶² The Register of Copyrights found that the software locks used in cell phones were not intended to protect copyrighted works, but rather prevent consumers from switching to another wireless carrier, “a business decision that has nothing whatsoever to do with the interests protected by copyright.”¹⁶³ Therefore the Register’s recommendation¹⁶⁴ to exempt such locks from the anticircumvention provisions of the DMCA was adopted by the Librarian of Congress.¹⁶⁵ The exemption means that, provided a consumer circumvents the software lock on a cell phone “for the sole purpose of lawfully connecting to a wireless . . . network,” he or she is immune from liability under the DMCA.¹⁶⁶

The DMCA exemption for unlocking cell phones is significant for three reasons. First, it clearly indicates that unlocking cell phones for use on other carrier networks is a legitimate consumer activity. Second, the Register of Copyrights’ conclusion confirms that existence of locks is simply a business decision, not a technological necessity. Finally, as discussed in Part IV, the exemption means that AT&T’s attempts to use legal threats based on the DMCA to prevent iPhone owners from unlocking their phones should be unsuccessful.

While the Register of Copyrights considered the cell phone locking issue in response to specific consumer requests,¹⁶⁷ Congress took notice *sua sponte* in a July 2007 hearing on the state of the wireless industry.¹⁶⁸

161. See Peters, *supra* note 157, at 5 (“The primary responsibility of the Register and the Librarian in this rule-making proceeding is to assess whether the implementation of access control measures is diminishing the ability of individuals to use copyrighted works in ways that are otherwise lawful.” (citing H.R. REP. NO. 105-551, pt. 2, at 37 (1998))).

162. 17 U.S.C. § 1201(a)(1)(A).

163. Peters, *supra* note 157, at 52.

164. *Id.* at 53.

165. Patents, Trademarks, and Copyrights, 37 C.F.R. § 201.40 (2007). Effective Nov. 27, 2006, the exemption will last for three years. *Id.* § 201.40(b).

166. *Id.*

167. See Jennifer Granick, *Cell Phones Freed! Poor Suffer?*, WIRED.COM, Dec. 6, 2006, <http://www.wired.com/politics/law/commentary/circuitcourt/2006/12/72241>.

168. See *Wireless Innovation and Consumer Protection: Hearing Before H. Subcomm. on Telecommunications and the Internet of the H. Comm. on Energy and Commerce*, 110th Cong. (2007) [hereinafter *Wireless Hearing*]; see also Randall Stross, *When Mobile Phones Aren't Truly Mobile*, N.Y. TIMES, July 22, 2007, at Bus-3.

In his opening statement, House Subcommittee on Telecommunications and the Internet chairman Edward J. Markey used the iPhone as an example of the industry's anticonsumer tendencies:

The iPhone highlights both the promise and the problems with the wireless industry today [E]ven though consumers must buy an iPhone for the full price for [\$]500 or [\$]600 . . . , AT&T Wireless reportedly still charges an early termination fee of apparently \$175 for ending the service contract early, even though the phone cost wasn't subsidized and a consumer can't even take it to use with another network provider.¹⁶⁹

A bill introduced in the Senate¹⁷⁰ would remedy some of the most vexing industry practices—though not cell-phone locking—by eliminating hidden charges, requiring termination fees to be prorated, and more strictly regulating how cellular service contracts are marketed, sold, and renewed.¹⁷¹ Predictably, the wireless industry is opposing the bill.¹⁷²

The fact that the federal government has begun taking an active role in addressing consumer discontent with the wireless industry is an encouraging sign. While the congressional action so far is not relevant for a legal analysis of unlocking the iPhone, the Register of Copyrights' DMCA exemption is directly on point, and will be addressed later.¹⁷³

C. The iPhone Contracts

As the product of a business partnership between two large corporations, it is not surprising that the iPhone comes complete with a suite of prolix contracts. There are three high-level agreements: the Apple iPhone Terms of Service,¹⁷⁴ the Apple One Year Limited

169. *Wireless Hearing*, *supra* note 168.

170. Cell Phone Consumer Empowerment Act of 2007, S. 2033, 110th Cong. (2007).

171. See Press Release, Sen. Klobuchar, Klobuchar and Rockefeller Announce Cell Phone Consumer Empowerment Act of 2007 (Sept. 7, 2007), *available at* http://klobuchar.senate.gov/newsreleases_detail.cfm?id=281970.

172. Eric Bangeman, *Cellular Freedom: Bill Would Cut Early Termination Fees, Hidden Charges*, ARSTECHNICA.COM, Sept. 10, 2007, <http://arstechnica.com/news.ars/post/20070910-cellular-freedom-bill-would-cut-early-termination-fees-hidden-charges.html>.

173. See *infra* Part IV.B.

174. Apple Inc., iPhone Terms of Service, *available at* http://www.apple.com/legal/iphone/us/terms/service_all.html.

Warranty,¹⁷⁵ and AT&T's Terms of Service.¹⁷⁶ The warranty issues are not relevant, but this Section describes important details of the Apple and AT&T terms of service.

1. APPLE'S IPHONE TERMS OF SERVICE

The terms of service for the iPhone is a composite document that includes five separate contracts.¹⁷⁷ Most relevant for the purposes of this Comment is the iPhone Software License Agreement.¹⁷⁸

Software-license agreements are used frequently as a means of distributing software while protecting the developer's intellectual property.¹⁷⁹ The agreements grant licensees usage rights while specifically reserving ownership of the software itself in the grantor.¹⁸⁰ This is important because typically the physical object on which the software is distributed—a CD, DVD, even an iPhone—is considerably less valuable than the software itself.¹⁸¹ Therefore, license agreements are used to prevent the consumer from assuming he or she obtains ownership of the intellectual property by purchasing the copy.¹⁸²

Many software-license agreements carefully circumscribe the conditions of the grant by dictating acceptable and prohibited uses of the software.¹⁸³ License agreements can be “self-executing” in that they

175. Apple One (1) Year Limited Warranty, *supra* note 115.

176. AT&T Postpaid Terms of Service, *supra* note 90.

177. The separate contracts are: (1) Apple iPhone Software License Agreement, (2) Apple iTunes Store Terms of Service, (3) Google Maps Terms and Conditions, (4) YouTube Terms of Use, and (5) Notices From Apple. *See* iPhone Terms of Service, *supra* note 174. The iTunes Store, Google and YouTube conditions are included because features of those sites are available via the iPhone's internet capabilities. The “Notices From Apple” is a simple statement that e-mail from Apple will satisfy legal communication requirements. *Id.*

178. *See* iPhone Software License Agreement, *supra* note 52.

179. Stephen J. Sand, Annotation, *Validity, Construction, and Application of Computer Software Licensing Agreements*, 38 A.L.R. 5TH 1, § 2 (1996).

180. *Id.*

181. *See* Michael J. Madison, *Reconstructing the Software License*, 35 LOY. U. CHI. L.J. 275, 307 (2003) (explaining that the economic value of the media on which copies of software are distributed is negligible, and that customers pay for the content, not the copy).

182. *See* 17 U.S.C. § 202 (West 2000) (“Ownership of a copyright, or of any of the exclusive rights under a copyright, is distinct from ownership of any material object in which the work is embodied.”); *see also* RAYMOND T. NIMMER, *THE LAW OF COMPUTER TECHNOLOGY* § 7:66 (3d ed. 2008) (“A transfer of ownership of tangible property does not transfer ownership of intellectual property or other information-related interests.”).

183. *See* NIMMER, *supra* note 182, § 7:101.

immediately terminate usage rights for violation of the license's conditions.¹⁸⁴ Any consumer that uses the software outside the scope of the agreement has breached contract, and technically can be held legally liable for so doing.¹⁸⁵

The terms of the Apple license are typical.¹⁸⁶ The iPhone software is licensed, not sold, so Apple retains ownership of the underlying intellectual property.¹⁸⁷ Reverse engineering or modification of the iPhone software is expressly prohibited, with violations subjecting the consumer to "prosecution and damages."¹⁸⁸ Furthermore, the rights under the license terminate immediately for a failure to comply with any of the terms.¹⁸⁹ This does not mean that the software suddenly stops working. Rather, the consumer is simply no longer legally permitted to *use* the software,¹⁹⁰ which effectively rescinds the consumer's right to use the iPhone at all.¹⁹¹ Warranties of any kind are disclaimed,¹⁹² liability is limited,¹⁹³ and Apple reserves the right to collect technical "information about your iPhone, computer, system and application software, and peripherals" to facilitate software updates, support, and onerously, "to verify compliance with the terms of this License."¹⁹⁴ Finally, the license states that California law, as applied to California residents, will govern the agreement.¹⁹⁵

184. *See id.* ("Many contracts contain a specified duration or number of permitted uses. In such cases, termination occurs automatically when the stated criteria is passed.")

185. *Id.* §§ 7:177, 7:184. Breach of a software-license agreement may also constitute copyright infringement, based on either direct or contributory theories. Sand, *supra* note 179, § 10; *see also id.* § 7:99 ("Once a license terminates, subsequent use of the intellectual property infringes the intellectual property right.")

186. *See* iPhone Software License Agreement, *supra* note 52.

187. *Id.* § 1 ("General").

188. *Id.* § 2(c) ("Permitted License Uses and Restrictions").

189. *Id.* § 6 ("Termination").

190. *Id.*

191. However, the consumer could still use the iPhone as a stylish paperweight.

192. Express, implied and statutory warranties are disclaimed, including but not limited to implied warranties and/or conditions of merchantability and of fitness for a particular purpose. iPhone Software License Agreement, *supra* note 52, § 7 ("Disclaimer of Warranties").

193. Liability for personal injury, incidental, special, indirect or consequential damages is disclaimed. *Id.* § 8 ("Limitation of Liability").

194. *Id.* § 4 ("Consent to Use of Non-Personal Data").

195. *Id.* § 12 ("Controlling Law and Severability"). A discussion of choice of law principles is beyond the scope of this Comment, but it suffices to note that the application of California law is reasonable given that Apple is headquartered in the state and members of the plaintiff class in the pending suit are domiciled there. *See also infra* note 202.

2. AT&T'S SERVICE AGREEMENT

The AT&T service agreement¹⁹⁶ contains provisions common to the major carriers, including an early-termination fee,¹⁹⁷ mandatory binding arbitration,¹⁹⁸ and a prohibition against class-action lawsuits.¹⁹⁹ The agreement specifies that the law of the state of the customer's billing address will govern the agreement.²⁰⁰ However, since the class-action lawsuits were brought in California, Apple is headquartered there,²⁰¹ and Apple's agreement explicitly specifies California law as controlling, it is likely courts would apply California law to both agreements.²⁰²

Particularly relevant for this Comment is the equipment clause.²⁰³ This provision states: "Equipment purchased for use on AT&T's system is designed for use exclusively on AT&T's system. You agree that you will not make any modifications to the Equipment or programming to enable the Equipment to operate on any other system."²⁰⁴ While this clause is not specific to the iPhone, it demonstrates that those iPhone owners who have unlocked their phones for use on other GSM networks are in material breach of their contracts with AT&T. Unlike the Apple

196. AT&T Postpaid Terms of Service, *supra* note 90.

197. *Id.* The early-termination fee is \$175. *Id.* ("Service Commitment; Early Termination Fee").

198. *Id.* ("Arbitration Agreement").

199. *Id.* ("Dispute Resolution by Binding by Arbitration").

200. *Id.* ("Miscellaneous").

201. Apple's corporate headquarters are located in Cupertino, California. Apple.com, Contacting Apple, <http://www.apple.com/contact> (last visited Aug. 20, 2008).

202. The resolution of the issue will require application of choice-of-law principles. Generally, federal courts exercising diversity jurisdiction "apply the substantive law of the forum in which the court is located, including the forum's choice of law rules." *Downing v. Abercrombie & Fitch*, 265 F.3d 994, 1005 (9th Cir. 2001) (quoting *Ins. Co. of North Am. v. Fed. Express Corp.*, 189 F.3d 914, 919 (9th Cir. 1999)). Therefore the United States District Court for the Northern District of California, where the iPhone lawsuits were filed, would apply California's "governmental interest" choice-of-law method. See 12 CAL. JUR. 3D *Conflict of Laws* § 29 (2008); see also *Downing*, 265 F.3d at 1005 ("California applies a three-step 'governmental interest' analysis to choice-of-law questions: (1) 'the court examines the substantive laws of each jurisdiction to determine whether the laws differ as applied to the relevant transaction,' (2) 'if the laws do differ, the court must determine whether a true conflict exists in that each of the relevant jurisdictions has an interest in having its law applied,' and (3) 'if more than one jurisdiction has a legitimate interest . . . the court [must] identify and apply the law of the state whose interest would be more impaired if its law were not applied.'" (quoting *Abogados v. AT&T, Inc.*, 223 F.3d 932, 934 (9th Cir. 2000); *Liew v. Official Receiver & Liquidator*, 685 F.2d 1192, 1196 (9th Cir. 1982))).

203. See AT&T Postpaid Terms of Service, *supra* note 90 ("Equipment").

204. *Id.*

software license, the AT&T agreement does not specify a penalty for breach.²⁰⁵ However, this may be immaterial because those who unlocked their phones would already be in violation of Apple's software license and therefore would be legally forbidden from using their phones, period.²⁰⁶

IV. ANALYSIS OF IPHONE UNLOCKING UNDER CONTRACT AND COPYRIGHT LAW

There are two aspects to analyzing the legality of iPhone unlocking. On one side are consumers who may unlock their phones without violating copyright law,²⁰⁷ but promised not to do so when they accepted the iPhone contracts.²⁰⁸ On the other side are commercial software vendors with no such contractual constraints,²⁰⁹ but who may violate copyright law by distributing unlocking software.²¹⁰ In this context, the Apple-AT&T response to iPhone unlocking is two-pronged, and aligned along the consumer-contract-commercial-copyright axis. Apple's software updates disable unlocked iPhones, thereby "remedying" the consumer's breach of contract, while AT&T mounts legal attacks on the software vendors based on copyright law.²¹¹ Ultimately, both tactics are indefensible.

This Comment argues that the contractual restrictions prohibiting unlocking iPhones may be susceptible to a finding of unconscionability under California law.²¹² At the same time, a careful analysis of the

205. *See id.*

206. *See supra* text accompanying notes 188–90.

207. *See supra* text accompanying notes 162–66.

208. Apple's iPhone software-license agreement prohibits reverse engineering or modification of the iPhone software, both of which are necessary in order to unlock the phone. *See* iPhone Software License Agreement, *supra* note 52, § 2(c) ("Permitted License Uses and Restrictions").

209. Assuming that the software developers are not also consumer iPhone owners, there is no privity of contract between them and Apple-AT&T. Therefore, the contractual restrictions cannot be enforced against them.

210. The violation would be of the Digital Millennium Copyright Act's provisions prohibiting the *trafficking* in anticircumvention technology, which is distinct from the prohibition against actual circumvention itself. *See* 17 U.S.C. § 1201(a)(2)(A) (West 2000) ("No person shall manufacture, import, offer to the public, provide, or otherwise traffic in any technology, product, service, device, component, or part thereof, that is primarily designed or produced for the purpose of circumventing a technological measure that effectively controls access to a work . . .").

211. *See, e.g., supra* note 35.

212. In addition, Apple's self-help remedy for consumer breach of the iPhone agreements is arguably a violation of its obligation of good faith performance and

DMCA provisions at issue demonstrates that while wireless-service providers may succeed in temporarily intimidating software vendors by threatening legal action, their theory of liability under the DMCA's antitrafficking provisions is fundamentally flawed and unsustainable in court.

A. Of Consumers and Contract

Under the *ProCD v. Zeidenberg*²¹³ theory of contract formation, the iPhone agreements were arguably accepted and are binding on iPhone owners. However, the terms that prohibit unlocking may be unconscionable under California law. Even if legally valid, enforcing those restrictions in practice is unrealistic and counterproductive. Finally, there may be significant social benefits to consumers simply disregarding the restrictions, making their breach akin to a quasi-efficient breach of contract.

1. ACCEPTANCE

The original iPhone contracts were click-wrap contracts of adhesion²¹⁴ which the consumer accepted by activating and using the iPhone.²¹⁵ As such, they were a classic example of the “money now, terms later” principle of contract formation upheld in *ProCD*.²¹⁶ Notice of the terms was established because they were displayed on the user's

enforcement of the contract. *See* CAL. COM. CODE § 1304 (West Supp. 2008) (“Every contract or duty within this code imposes an obligation of good faith in its performance and enforcement.”).

213. 86 F.3d 1447 (7th Cir. 1996).

214. The iPhone software-license agreement, along with the other Apple terms of service and the AT&T service agreement were presented within iTunes during the iPhone activation process. The user was required to check a checkbox indicating he or she read and understood the agreements before the software would continue the activation process. *See* Apple Inc., *Activating and Setting Up iPhone*, IPHONE USER'S GUIDE at 4–5 (on file with author); *see also* Video: Apple - iPhone - How to Activate iPhone (on file with author).

215. The agreement begins with the following language: “Please read this software license agreement (“License”) carefully before using your iPhone *By using your iPhone . . . you are agreeing to be bound by the terms of this License* If you do not agree to the terms of this License, do not use the iPhone if you do not agree to the terms of the License, you may return the iPhone within the return period to the Apple store or authorized distributor where you obtained it for a refund” iPhone Software License Agreement, *supra* note 52 (emphasis added).

216. *See generally ProCD v. Zeidenberg*, 86 F.3d 1447 (7th Cir. 1996).

computer.²¹⁷ Consent was voluntary because the customer was required to affirmatively click a button labeled “I agree” in order to proceed with activation.²¹⁸ The customer was free to reject the contract and return the product if the terms were objectionable.²¹⁹ Therefore, under *ProCD*, there is no question that the iPhone contracts were accepted by customers that activated their phones.²²⁰

However, “activation” in this context means that the user went through the normal iPhone activation process using iTunes.²²¹ Users that bypassed this activation sequence using unlocking software designed for that purpose would not have seen the contracts, and therefore may argue they neither accepted nor are bound by them. For example, part of the rationale of the United States Court of Appeals for the Seventh Circuit’s holding in *ProCD* was that an enforceable contract was formed because the software “splashed the license on the screen” which required acceptance in order to use the product.²²² The implication is that, had the software at issue in that case *not* required explicit acceptance by conduct, a binding agreement may not have been formed.

Apple’s novel approach of selling iPhones without requiring activation at the point of sale,²²³ as is the usual practice in the wireless industry,²²⁴ certainly helped them move inventory as fast as possible.²²⁵ It

217. At least one court has held that the amount of the agreement that appears on screen at any given time—for example in a very small scroll-box—does not render the notice of the terms inadequate. See *Forrest v. Verizon Commc’ns., Inc.*, 805 A.2d 1007, 1010–11 (D.C. 2002).

218. See *supra* note 212 and accompanying text.

219. See *supra* note 214 and accompanying text.

220. See 86 F.3d at 1449.

221. See *supra* note 212 and accompanying text.

222. 86 F.3d at 1452.

223. Apple abandoned this novel do-it-yourself activation process with the release of the updated iPhone 3G in July 2008. See Svensson, “*Unlockers*” Face Apple’s Obstacles with New iPhone Revised Strategy, *supra* note 89. Customers must now sign up for AT&T wireless services and activate their iPhones before leaving the Apple or AT&T retail stores. *Id.* Furthermore, iPhone 3Gs can no longer be purchased online. See Apple.com, iPhone - Where to Buy, <http://www.apple.com/iphone/buy> (last visited Sept. 22, 2008).

224. Olga Kharif & Peter Burrows, *On the Trail of the Missing iPhones*, BUS. WK., Feb. 11, 2008, at 25 (“Most phones from Nokia, Motorola, and others are sold through the wireless carriers themselves or authorized dealers, and you sign up for a service contract at the same time you buy the phone.”); see also Fred Vogelstein, *The Untold Story: How the iPhone Blew Up the Wireless Industry*, WIRED.COM, Jan. 9, 2008, http://www.wired.com/gadgets/wireless/magazine/16-02/ff_iphone (noting that Apple convinced AT&T to “reinvent the time-consuming in-store sign-up process”).

may also have had the unintended side effect of giving credence to the unlockers' argument that they were not bound by the contractual restrictions. After all, Apple and AT&T let the customers leave the store with an inactive phone. If the customer was clever enough to unlock and use the device while avoiding the click-wrap contracts, it would seem that Apple and AT&T had been beaten at their own contract of adhesion game.²²⁶

This argument is seductive, but unsustainable for several reasons. First, the fine print on the backside of the iPhone package states that a service contract with AT&T is required to use the phone,²²⁷ and that use is subject to Apple and third-party software licenses. Second, the iPhone product information guide included in the retail box contains a notice that use of the iPhone is subject to the software-license agreement.²²⁸ Finally, courts may simply view bypassing the activation process as ignoring the contracts instead of never being presented with them.

Even if the notice on the box or in the product guide was overlooked, any consumer savvy enough to use the unlocking software must have known that (1) the iPhone came with built-in technical and contractual restrictions, and (2) the whole purpose of the unlocking software was to avoid them. For that reason, any claim that a consumer did not accept the terms due to lack of notice is probably unconvincing. In addition to the *actual* notices provided, a court may simply impute constructive notice²²⁹ of the terms to unlockers because of the

225. See *Unlocked iPhones May Total 250,000*, SEATTLE POST-INTELLIGENCER, Oct. 24, 2007, at F2 (“Apple had sold 270,000 iPhones in the first two days after the product’s June 29 debut.”).

226. An added wrinkle to this argument would be that even if the Apple software-license agreement may still apply with a nonactivated iPhone, the AT&T service agreement, and its equipment clause that prevents modifying the device for use on another network, *never* would. This is because the unlockers never sign up for AT&T wireless service, and so the AT&T service agreement is simply irrelevant.

227. Apple Inc., Requirements for iPhone on 2007 iPhone packaging (on file with author). Under the “Requirements” section, the exact language is: “Minimum new two-year wireless service plan with AT&T required to activate all iPhone features, including iPod features.” *Id.* The original iPhone could also be purchased at the online Apple Store, but the product page clearly indicated that an AT&T service agreement was required.

228. Apple Inc., iPhone Important Product Information Guide, at 16, http://manuals.info.apple.com/en/iPhone_Product_Info_Guide.pdf. The entire agreement is not printed in the manual. Instead, the notice is a rather easy to miss three lines: “Software License: Use of iPhone is subject to the iPhone Software License Agreement found at: www.apple.com/legal/sla.” *Id.* Interestingly, the one-year limited warranty is reproduced in full, taking up five pages of the small guide. *Id.* at 16–20.

229. CAL. CIV. CODE § 19 (West 2007).

widespread publicity regarding the Apple-AT&T exclusive deal, as well as the ready availability of the various agreements online.²³⁰ In short, whether users activated their iPhones as intended by Apple or not, the contracts can probably be considered binding.

The UCC, as embodied in the California Commercial Code, applies to the iPhone because it is a “good”²³¹ within the meaning of Article 2.²³² While its purchase requires an AT&T service contract, it is clear from the public response that it is the iPhone itself, and not the AT&T wireless service, that is the consumer’s principal motivation for the transaction. Therefore, under the predominant element test,²³³ the AT&T service would be only incidental to the sale of the iPhone and so the UCC applies. However, because this Comment does not contend that there was any defect in acceptance or any defect in the iPhone itself, and does not address the warranty issues, the UCC is of minor importance to this Comment.

2. ENFORCEABILITY

Under a liberal application of California’s unconscionability doctrine, the provisions of the iPhone contracts prohibiting unlocking can be found both procedurally and substantively unconscionable.²³⁴ While there is a conflict between public copyright and private contract law, this Comment does not find an issue of preemption,²³⁵ nor does it suggest that

230. See iPhone Terms of Service, *supra* note 174.

231. CAL. COM. CODE § 2105(1) (West 2002).

232. *Id.* § 2101.

233. See *Bonebrake v. Cox*, 499 F.2d 951, 960 (8th Cir. 1974) (explaining that in mixed contracts involving both goods and services, the predominant factor or purpose of the contract will characterize the whole).

234. In addition, the class-arbitration and class-action waivers in the AT&T service agreement are unenforceable under California law because they are indistinguishable from the waivers found unconscionable in *Gatton* and *Shroyer*. See generally *Shroyer v. New Cingular Wireless Servs. Inc.*, 498 F.3d 976 (9th Cir. 2007); *Gatton v. T-Mobile USA, Inc.*, 61 Cal. Rptr. 3d 344 (Cal. Ct. App. 2007), *cert. denied*, *T-Mobile USA, Inc. v. Gatton*, No. 07-1036, 128 S. Ct. 2501, 2502 (May 27, 2008). Therefore, the antitrust class-action lawsuit should be allowed to proceed. See *supra* note 96.

235. Federal copyright law preempts state law to the extent that it creates rights “equivalent to any of the exclusive rights within the general scope of copyright” 17 U.S.C. § 301(a) (West 2000). However, numerous courts have held that contractual agreements provide an “extra element” that makes the contractual right asserted “qualitatively different from those protected by the copyright act.” See, e.g., *Meridian Project Sys., Inc., v. Hardin Constr. Co.*, 426 F. Supp. 2d 1101, 1108 (E.D. Cal. 2006).

private contracting parties should never be able to waive certain rights.²³⁶ Rather, the specific situation of cell phone unlocking in the context of current wireless industry practices supports a strong policy argument that the unconscionability doctrine could be expanded to render the iPhone's unlocking provisions unenforceable.

The iPhone contracts satisfy the procedural element of unconscionability because they are contracts of adhesion like the contracts at issue in *Gatton v. T-Mobile USA, Inc.*²³⁷ As with most mass-market contracts of adhesion, oppression exists due to the superior bargaining power of the corporate parties and the unique nature of the iPhone.²³⁸ Consumers were surprised because the iPhone was marketed as a “world” GSM phone, implying that it could be used on other GSM networks worldwide.²³⁹ However, Apple's exclusive relationship with AT&T, and the software that locked the iPhones to AT&T's network, meant the iPhone was not a “world” phone but rather only a “U.S.” phone. The oppression, surprise, and mass-market form contract all sustain a finding of procedural unconscionability.

The contractual restrictions that prevent iPhone unlocking can also be found substantively unconscionable. This finding could be based on one of two legal theories. First, by serving as a pretext for punishing consumers who unlocked iPhones, as well as the means of restraining competition in the wireless industry, the restrictions shield Apple from wrongful conduct, which is contrary to public policy under California law.²⁴⁰ Second, like the class-action waivers in *Gatton*²⁴¹ and *Shroyer*,²⁴²

236. An argument can be made that customers willingly waive any “right” to unlock their phone for use on another carrier's network as part of their service agreement, but most carriers will issue unlock codes to customers eventually. *See supra* Part IV.A.1. AT&T however, has stated that it will *never* allow customers to unlock the iPhone, even after customers' two-year contracts have ended. *See supra* note 76 and accompanying text.

237. 61 Cal. Rptr. 3d at 353.

238. *See, e.g.*, Anna Marie Kukec, *Yep, Looks Like Apple's iPhone Phenomenon Is For Real*, DAILY HERALD (Arlington Heights, IL), June 30, 2007, at 1 (noting the availability of alternatives, but explaining how the design, large touch-screen, functionality, and user-friendliness all distinguished the iPhone from Blackberries and Treos).

239. Steve Jobs himself even described the iPhone as a “world phone with quad-band GSM technology that works great in the U.S., Europe and most of Asia.” Walt Mossberg, *Steve Jobs Answers My iPhone Questions*, ALLTHINGS.COM, June 26, 2007, 15:01 PST, <http://mossblog.allthingsd.com/20070626/jobs-qa>.

240. *See* CAL. CIV. CODE § 1668 (West 1985).

241. *See Gatton*, 61 Cal. Rptr. 3d at 358.

242. *See Shroyer v. New Cingular Wireless Servs., Inc.*, 498 F.3d 976, 984 (9th Cir. 2007).

the contractual restrictions are fundamentally unfair because they prevent consumers from vindicating their substantive legal “right” to a carrier-agnostic phone.

To the extent that the iPhone contracts provide Apple with an excuse or justification for “bricking” unlocked phones, they essentially shield Apple from wrongful conduct, and so would be unenforceable under California law. Remember that before releasing the software update that disabled unlocked iPhones, Apple made sure to state that (1) unauthorized modifications of the iPhone software violated the software-license agreement and voided the warranty, (2) unlocking programs irreparably damaged the iPhone’s software,²⁴³ and (3) applying the software update to unlocked phones could result in permanent inoperability.²⁴⁴ With that notice given, Apple was free to release its iPhone-crippling update with a clean corporate conscience. Apple could plausibly argue that any iPhones bricked by the update were not the result of its punitive and extralegal remedy for breach of contract, but simply an unavoidable result of the “damage” caused to the iPhone’s software by the unauthorized locking programs.

It’s worth recalling at this point that the iPhone software-license agreement explicitly reserves to Apple the right to collect technical information about consumer iPhones to “verify compliance with the terms of [the] License.”²⁴⁵ It does not take a dramatic leap of intuition to surmise that Apple’s iPhone software update was designed to do exactly that—and brick any iPhones found to be noncompliant. Insofar as Apple interprets their software-license agreement to permit that vigilante action, the restrictions are so overly harsh and one-sided as to be substantively unconscionable. Furthermore, while Apple did politely warn iPhone owners in advance of the potentially disastrous effects of the iPhone update, nowhere does the software-license agreement specify iPhone bricking as a penalty for breach; only “prosecution and damages” are mentioned.²⁴⁶ This is undoubtedly no accident. Including an explicit “bricking” clause in the agreement would not only be patently unconscionable, but would deprive Apple of the plausible deniability that so far has allowed it to sell its iPhone and brick it, too.

The effect of the iPhone contract in shielding Apple from wrongful conduct can be compared to the class-action waivers at issue in *Gatton*

243. While the author is not prepared to definitively refute the claim with respect to the iPhone, it is a highly dubious contention that *software* can be irreparably damaged.

244. See *supra* text accompanying notes 36–38.

245. iPhone Software License Agreement, *supra* note 52, § 4.

246. *Id.* § 2(c).

and *Shroyer*. In those cases, the courts found the waivers unconscionable because they made it impractical and economically wasteful for consumers to pursue a legal remedy, just like the waivers at issue in *Discover Bank*.²⁴⁷ Deprived of an effective legal remedy, consumers were prevented from holding the wireless companies accountable for their wrongful conduct.²⁴⁸ Achieving that result via contract is expressly contrary to public policy under California law,²⁴⁹ and so the waivers were unenforceable. By similar reasoning, the unlocking prohibition in Apple's iPhone agreement could be as well.

The second legal theory that could possibly support a finding of substantive unconscionability requires an aggressive interpretation of the 2006 DMCA exemption permitting cell-phone unlocking.²⁵⁰ The argument is that the exemption did not simply acknowledge a noninfringing use of the copyrighted cell-phone operating software, but instead recognized a new consumer right *to* unlock. Provided that the unlocking is done for the sole purpose of "lawfully connecting to a wireless . . . network,"²⁵¹ the contractual provisions that prohibited doing so would, like the class-action waivers in *Gatton*²⁵² and *Shroyer*,²⁵³ be fundamentally unfair because they prevent consumers from vindicating substantive rights.

This theory is likely unpersuasive, as there is a significant difference from being *able* to unlock an iPhone, and having the legal *right* to do so. In contrast to the "important"²⁵⁴ and "well-accepted"²⁵⁵ role of class-action remedies in California law, the right to unlock, even if California courts are prepared to recognize it, does not enjoy such a firm grounding in the contemporary legal landscape.

Perhaps a bigger problem with the iPhone's contractual restrictions is that the iPhone is both more "good" than "service," and more computer than cell phone. This has two important consequences. First, consumers are likely to feel strongly that having purchased the iPhone, they own it and can do with it whatever they like. By attempting to dramatically constrain what consumers can do with their lawfully purchased property, the contractual restrictions can appear so overly one-

247. *Shroyer*, 498 F.3d at 983–84; *Gatton*, 61 Cal. Rptr. 3d at 356–58.

248. *Supra* note 241.

249. CAL. CIV. CODE § 1668 (West 1985).

250. Patents, Trademarks, and Copyrights, 37 C.F.R. § 201.40 (2007).

251. *Id.* § 201.40(b)(5).

252. *Gatton*, 61 Cal. Rptr. 3d at 358.

253. *Shroyer*, 498 F.3d at 983.

254. *Discover Bank v. Superior Court*, 113 P.3d 1100, 1106 (Cal. 2005).

255. *Id.* at 1103.

sided and draconian as to be unconscionable.²⁵⁶ Secondly, because the iPhone is basically a handheld computer, the restrictions that originally made it technically difficult and contractually forbidden to unlock the phone for the purpose of running third-party applications seemed inexplicable.

At least Apple has come around on the latter point, releasing a software-development kit in March 2008.²⁵⁷ The kit allows developers to create custom programs for the iPhone without first having to breach the software-license agreement by unlocking the device.²⁵⁸ Therefore, the potential unconscionability of the iPhone software-license agreement as it pertains to writing custom software is effectively moot.

While this Comment argues that the contractual terms that prohibit unlocking may not be enforceable as a matter of law, there are also significant problems with attempting to enforce them in practice. Apple's own estimates indicated that approximately one out of every six iPhones sold in the U.S. was purchased with the intent to unlock: approximately 250,000 devices as of October 2007.²⁵⁹ Analysts later estimated that by the end of 2007, between 800,000 and 1 million iPhones had been unlocked worldwide: about one-fourth of all units sold.²⁶⁰ Apple's apparent enforcement mechanism for keeping the devices locked, bricking, is not only highly invasive, but also ineffective.²⁶¹ Steve Jobs

256. Concededly, the traditional restrictions on *all* cell phones are arguably one-sided, not just iPhones. However, the capabilities and popularity of the iPhone mean that the contractual restrictions are that much more likely to come before the courts.

257. See Press Release, Apple Inc., Apple Announces iPhone 2.0 Software Beta (Mar. 6, 2008), *available at* <http://www.apple.com/pr/library/2008/03/06iphone.html> ("The iPhone SDK provides developers with a rich set of Application Programming Interfaces (APIs) and tools to create innovative applications for iPhone and iPod® touch."). The delay in releasing development tools was ostensibly because Apple wanted to ensure third-party development would not subject the iPhone or AT&T's network to viruses or malicious software. See Michelle Quinn, *Apple to Open Up the iPhone*, L.A. TIMES, Oct. 18, 2007, at 3.

258. See Press Release, Apple Inc., *supra* note 257. Indeed, the new iPhone applications marketplace that Apple launched with the release of the iPhone 3G has so far been a resounding success. See Press Release, Apple Inc., iPhone App Store Downloads Top 10 Million in First Weekend (July 14, 2008), *available at* <http://www.apple.com/pr/library/2008/07/14appstore.html>.

259. *Unlocked iPhones May Total 250,000*, *supra* note 225. Many of these unlocked iPhones were destined for grey markets overseas before Apple had officially released the iPhone outside of the U.S. *Id.*

260. See Kharif & Burrows, *supra* note 224, at 26.

261. See Cheng, *supra* note 46. There were also anecdotal reports of sympathetic Apple retail store employees resurrecting "bricked" iPhones, demonstrating both the futility of Apple's policy and belying its claims that unlocked iPhones were irreparably damaged. See Rob Beschizza, *How To Unbrick an iPhone: Let Apple Do It For You*,

famously referred to the battle with iPhone hackers as a “cat and mouse game,”²⁶² and indeed hackers continued to find ways around Apple’s iPhone patches.²⁶³

This is likely why, with the release of the second-generation iPhone 3G in July 2008, Apple backpedaled on its innovative online-activation process, instead requiring customers to sign up for AT&T service at the point of sale.²⁶⁴ Apple and AT&T also do not sell the iPhone 3G online.²⁶⁵ While this move may not prevent unlocking entirely, it certainly makes it much more difficult and irksome for hackers because they have to surrender their personal information and a credit card to open an account with AT&T before Apple lets them get their hands on the hardware. However, because AT&T now subsidizes the iPhone 3G,²⁶⁶ Apple was able to effectively cut the price of the low-end model in half to \$199.²⁶⁷ This means a customer can buy an iPhone, sign up for service, then promptly cancel it and pay the termination fees all for about what it cost to buy a first-generation iPhone.²⁶⁸ Free and clear of the AT&T contract, the customer could then unlock with impunity.²⁶⁹ Therefore Apple’s change in tactics does not entirely moot the unlocking conundrum.

Loopholes aside, more important for Apple is that punishing unlockers threatens to drive away customers who are otherwise snapping

WIRED.COM, Sep. 28, 2007, 7:29 EST, <http://blog.wired.com/gadgets/2007/09/how-to-unbrick-.html>.

262. Brad Reed, *Apple’s Options for Stopping Open Source iPhone Use*, NETWORKWORLD.COM, Sept. 20, 2007, <http://www.networkworld.com/news/2007/09/2007-apple-stop-open-source-iphone.html>.

263. See Cheng, *supra* note 46.

264. See Svensson, “*Unlockers*” *Face Apple’s Obstacles with New iPhone Revised Strategy*, *supra* note 89.

265. Apple.com, iPhone - Where to Buy, <http://www.apple.com/iphone/buy/> (last visited Sept. 22, 2008).

266. See Svensson, “*Unlockers*” *Face Apple’s Obstacles with New iPhone Revised Strategy*, *supra* note 89 (“Analysts estimate AT&T will subsidize [iPhone 3Gs] by more than \$200 each.”).

267. See Press Release, Apple Inc., Apple Introduces the New iPhone 3G (June 9, 2008), available at <http://www.apple.com/pr/library/2008/06/09iphone.html>.

268. Svensson, “*Unlockers*” *Face Apple’s Obstacles with New iPhone Revised Strategy*, *supra* note 89 (“AT&T charges customers who break a two-year contract within the first month a \$175 early-termination fee plus the \$36 activation fee. That would bring the cost of the new iPhone to \$411 for an unlocker, slightly more than the old model’s \$399 price.”).

269. An individual unlocker could likely get away with this tactic. However, because customers must submit personally identifying information to AT&T when creating an account, any large-scale unlocking efforts would likely fail; AT&T could simply refuse to provide service to a known “unlocker.” See *id.*

up the gadget at a frenetic pace. Even worse, Apple and AT&T could take a cue from the major record labels and begin suing their customers en masse.²⁷⁰ Not only would that also be ineffective, but it would further tarnish Apple's otherwise enviable reputation among consumers. Thus, even if the restrictions were enforceable as a matter of general contract law, doing so would remain cumbersome and counterproductive in practice. Nonetheless, Apple may have a significant motivation in the form of shared revenues from AT&T for at least attempting or appearing to enforce the iPhone restrictions, but in the long run this is bound to fail.

The consideration of market forces begs the question whether the courts need get involved at all. In other words, is not a legal analysis of the iPhone contracts purely an academic endeavor, given that sufficient consumer discontent and market pressure would surely cause Apple to change its ways? Imagine if Apple suddenly required consumers purchasing a new Apple computer to sign a two-year service agreement with Apple's exclusive Internet-service-provider.²⁷¹ In that situation, Apple would likely watch as its customers tripped over themselves to buy computers elsewhere. Yet iPhone sales show no signs of slowing.²⁷² In a sense, this hypothetical helps underscore two important points about the wireless industry: (1) consumers have become so accustomed to restrictive contracts that they accept them without question, and (2) there is no reasonable choice of alternatives. Perhaps the relative ease with which the original iPhones could be unlocked explains why the market's invisible hand did not reach for a pen and strike the offensive language from Apple's contracts.

270. See Scott Mervis, *Artists Seek New Ways To Sell Their Music*, PITTSBURGH POST-GAZETTE, Feb. 5, 2008, at A1 (“[T]he Recording Industry Association of America, or RIAA, which represents the major labels, has tried to stem the tide [of illegal music downloads], filing 20,000 lawsuits against consumers over the past four years . . .”).

271. It's interesting to note that the prohibition on reverse engineering contained in the Software License Agreement for Apple's OS X operating software is almost identical to that in the iPhone agreement. See Apple Inc., Software License Agreement for Mac OS X, at 2F, <http://images.apple.com/legal/sla/docs/macosx105.pdf> (last visited Sept. 22, 2008). However, this Comment does not contend that the OS X agreement is also potentially unconscionable, precisely because there is no requirement that consumers use only one Apple-approved internet-service-provider.

272. See Press Release, Apple Inc., Apple Reports First Quarter Results (Jan. 22, 2008), available at <http://www.apple.com/pr/library/2008/01/22results.html> (noting that 2,315,000 iPhones were sold in Apple's fiscal 2008 first quarter). Even more impressive was the consumer response to the iPhone 3G. Consumers worldwide purchased 1 million of the devices in the first weekend it was released. See Press Release, Apple Inc., Apple Sells One Million iPhone 3Gs in First Weekend (July 14, 2008), available at <http://www.apple.com/pr/library/2008/07/14iphone.html>.

In summary, because the iPhone contracts are contracts of adhesion, and because the restrictions in the iPhone agreement can serve to shield Apple from wrongful conduct and prevent customers from lawfully unlocking their phones, the restrictions are vulnerable to a finding of unconscionability under California law.

3. IPHONE UNLOCKING AS QUASI-EFFICIENT BREACH

Unlocking the iPhone in violation of its click-wrap contracts can also be viewed as similar to an efficient breach of contract. The theory of efficient breach posits that when the promisor's gains from breach exceed the promisee's losses, breach of contract is not only acceptable, but encouraged.²⁷³ The idea is that the promisor can afford to pay the promisee's expectation damages²⁷⁴ for breach, while still coming out ahead.²⁷⁵ Therefore, breaching leaves both parties better off and is more economically efficient than performing under the contract.²⁷⁶

While there is no suggestion that the iPhone hackers are paying Apple and AT&T's expectation damages,²⁷⁷ a broader view of efficient-breach theory—one more akin to general public interest—could support a conclusion that unlocking iPhones is acceptable despite the pecuniary loss to Apple and AT&T. Instead of a purely economic analysis using dollars as the sole measure of efficiency, this approach would

273. See Melvin A. Eisenberg, *Actual and Virtual Specific Performance, the Theory of Efficient Breach, and the Indifference Principle in Contract Law*, 93 CAL L. REV. 975, 997 (2005); Frank Menetrez, *Consequentialism, Promissory Obligation, and the Theory of Efficient Breach*, 47 UCLA L. REV. 859, 861 (2000) (“[B]ecause efficient breaches . . . yield net benefits to society (by moving goods and services to their most highly valued use), they should be encouraged.”).

274. In contract law, expectation damages aim to put the aggrieved party in the economic condition they would have been had the contract been performed. See BLACK'S LAW DICTIONARY 417 (8th ed. 2004) (defining damages).

275. See Menetrez, *supra* note 273, at 861 (“[T]he way to encourage such breaches is to award the promisee only expectation damages, because the promisor thus gets to pocket the added profits from the breach.”).

276. *Id.* at 860 (“An efficient breach of contract is a breach that will, in some economically defined sense, make society better off—it will lead to a more efficient use or allocation of resources.”).

277. Indeed for many the whole point of unlocking the phone is specifically to avoid having to sign up for AT&T wireless service. However, it is worth noting that Apple's exclusive iPhone partner in Germany offered to sell the phone with no service agreement for €999 (about \$1,477), instead of the regular €399 price (about \$590) with a two-year contract. Kenneth Wong, *T-Mobile Changes iPhone Sale Terms After Court Ruling*, BLOOMBERG.COM, Nov. 21, 2007, <http://www.bloomberg.com/apps/news?pid=20601087&sid=a7wsGa9Xbyr4>. Interestingly, the standalone option came in response to a legal challenge by a competitor in the German wireless market. *Id.*

characterize the promisor not as an individual consumer, but as the class of consumers in general. In so doing, it would take into consideration unquantifiable benefits such as increased competition and innovation in the wireless industry.

Also on the benefit side of the equation would be restraining the anticompetitive behavior exhibited by Apple and AT&T in tying the iPhone to AT&T wireless service. Measured this way, the gains to be realized by consumer breach may exceed the losses to Apple and AT&T. Furthermore, if the arrangement between Apple and AT&T is in violation of antitrust laws, then their expectation of profits is illicit to begin with and a breach by consumers even more justified.

Support for the theory of a quasi-efficient breach in this context can be drawn from the history of the telecommunications industry. As Professor Tim Wu noted in a recent article, the constraints that wireless carriers place on cell phones and their customers are very similar to those formerly employed by AT&T when it had a monopoly in the landline telephone business.²⁷⁸ Back then, AT&T used this power to prevent customers from using non-AT&T equipment, insisting that total control over all equipment on the network was necessary to ensure it functioned properly.²⁷⁹

In a pivotal 1968 ruling, the FCC rejected that argument and mandated that consumers be able to attach any device compatible with the standard telephone interface to AT&T's network.²⁸⁰ Wu argues that this "right of attachment" resulted in the creation of new markets for telecommunications equipment, increased competition, and enabled innovation that eventually led to the modem and the growth of the internet.²⁸¹ Therefore, to the extent that history is repeating itself regarding the wireless carrier's stranglehold on both consumers and cell phones, iPhone owners breaching their contracts could prove to be very efficient indeed.

Some may argue that creating new markets, increasing competition, and sparking innovation are the domain of antitrust law, and that wielding the contract doctrine of unconscionability is a clumsy and misguided way to achieve such results. That is likely why the lawsuits filed against Apple in response to the iPhone "bricking" rely on antitrust

278. Wu, *supra* note 53, at 421–24.

279. *Id.* at 423.

280. *Id.* (citing *In re Of Use Of The Carterfone Device In Message Toll Telephone Service*, 13 F.C.C.2d 420 (1968)).

281. *Id.*

and unfair-competition claims instead of contract law.²⁸² Ultimately, courts holding the contractual restrictions unenforceable, in this limited situation where the corporate party uses the “lock-in” clause as an excuse for unilateral enforcement, may serve as a stepping stone to a more robust and effective remedy under an antitrust theory. The quasi-efficient-breach theory adds support to expanding the unconscionability doctrine in that manner.

B. Of Commerce and Copyright

Leveraging copyright law in an attempt to protect questionable business practices and restrain competition is not a new tactic, and the anticircumvention and antitrafficking provisions included in the DMCA have provided even more opportunities for abuse.²⁸³ Indeed, at least two companies have been unsuccessful in litigation alleging violations of the DMCA where no legitimate copyright issues were involved.²⁸⁴ Rather, the suits were attempts to prevent unwelcome competition in consumer markets.²⁸⁵ The threats AT&T has made against purveyors of iPhone-unlocking software are strikingly similar.²⁸⁶ Reviewing the precedent set in *Chamberlain Group Inc. v. Skylink Technologies Inc.*²⁸⁷ helps explain why AT&T’s legal theories under the DMCA are fatally flawed, will not stand up in court, and are simply transparent efforts to intimidate developers.

1. THE *CHAMBERLAIN* CASE: CIRCUMVENTING COMPETITION?

In *Chamberlain*, the plaintiff garage-door-opener manufacturer brought suit under the DMCA, alleging defendant’s universal garage-

282. See *supra* Part II.B.

283. See, e.g., Dan L. Burk, *Anticircumvention Misuse*, 50 UCLA L. REV. 1095 (2003) (arguing that the doctrine of misuse in copyright and patent law should be adapted and applied to the DMCA’s anticircumvention provisions to avoid anticompetitive overreaching).

284. See, e.g., *Chamberlain Group, Inc. v. Skylink Tech. Inc.*, 381 F.3d 1178 (Fed. Cir. 2004) (relating to a garage door opener manufacturer who brought suit under the DMCA to prevent competitor from manufacturing compatible garage door opener remote controls); *Lexmark Int’l, Inc. v. Static Control Components, Inc.*, 387 F.3d 522 (6th Cir. 2004) (rejecting Ink Jet printer manufacturer’s suit under the DMCA targeting a competitor that developed microchips that could be used to produce recycled ink cartridges compatible with Lexmark printers).

285. *Chamberlain*, 381 F.3d at 1183–84; *Lexmark*, 387 F.3d at 529.

286. See *supra* note 35.

287. 381 F.3d at 1178.

door-opener remote control violated the Act's antitrafficking provisions.²⁸⁸ Chamberlain claimed Skylink's remote was a circumvention device because it simulated the effect of a copyrighted software code emitted by Chamberlain's remote so Skylink remotes could be used with Chamberlain's garage-door openers.²⁸⁹ Key to the Federal Circuit's decision affirming the district court's grant of summary judgment in favor of Skylink was the fact that "Chamberlain neither alleged copyright infringement nor explained how the access provided by [Skylink's remote] facilitates . . . infringement . . ." ²⁹⁰ In other words, Chamberlain's reading of the DMCA would make access *alone* illegal, regardless of any connection between that access and copyright protection,²⁹¹ and even if the access at issue "enabled only rights that the Copyright Act grants to the public."²⁹² The court determined Congress could not have intended that result,²⁹³ nor would it have been a rational exercise of its Copyright Clause authority.²⁹⁴ Therefore, Chamberlain had no cause of action under the DMCA because it failed to establish "the critical nexus between access and protection."²⁹⁵

Chamberlain's understanding of the DMCA was flawed for other reasons as well. Because "circumvention" within the meaning of the DMCA is defined as being unauthorized by the copyright owner,²⁹⁶ Chamberlain argued that the anticircumvention provisions²⁹⁷ meant that consumers could *never* legally access copyrighted-embedded software without explicit authorization when the purpose of that access was to use the software with a competitor's products.²⁹⁸ However, the court reasoned that Chamberlain had implicitly authorized its customers to access the software because it sold the product free of any explicit terms or conditions.²⁹⁹ Even absent implicit authorization, copyright law itself authorized the consumers' access to the software.³⁰⁰ Particularly relevant to the iPhone unlocking situation, the court stated that "[c]onsumers who

288. *Id.* at 1183 (citing 17 U.S.C. § 1201(a)(2)).

289. *Id.* at 1184–85.

290. *Id.* at 1204.

291. *Id.* at 1197.

292. *Id.* at 1200.

293. *Id.* at 1197.

294. *Id.* at 1200 (quoting *Eldred v. Ashcroft*, 537 U.S. 186, 205 n.10 (2003)).

295. *Id.* at 1204.

296. 17 U.S.C. § 1201(a)(3)(A) (West 2000).

297. *Id.* § 1201(a)(1).

298. *Chamberlain*, 381 F.3d at 1193.

299. *Id.* at 1187.

300. *Id.* at 1202.

purchase a product containing a copy of embedded software have the inherent legal right to use that copy of the software.”³⁰¹ Finally, the court noted that adopting Chamberlain’s interpretation of the anticircumvention provisions would result in manufacturers being able to use the DMCA to create aftermarket monopolies in their products, violating both antitrust laws and the doctrine of copyright misuse.³⁰²

2. AT&T’S IDLE DMCA THREATS

AT&T has threatened at least two software development companies that were planning on releasing a commercial iPhone-unlock with legal action.³⁰³ Specifically, the AT&T threats reportedly alleged copyright infringement and illegal software distribution³⁰⁴ based on the anticircumvention³⁰⁵ and antitrafficking³⁰⁶ provisions of the DMCA.

The copyright infringement claim is presumably based on a secondary theory of liability. The unlocking software (the circumvention technology) provides access to the copyrighted software that operates the phone. Therefore, to the extent an end user (1) unlocks an iPhone, and (2) subsequently infringes the copyright, the company that sold the unlocking software could be held vicariously or contributorily liable.³⁰⁷

Illegal software dissemination, on the other hand, would be based on the DMCA’s antitrafficking provisions, which prohibit trafficking in technology designed to circumvent “a technological measure that

301. *Id.* The court left open the question of “whether a consumer who circumvents a technological measure controlling access to a copyrighted work in a manner that enables uses permitted under the Copyright Act but prohibited by contract can be subject to liability under the DMCA.” *Id.* at 1202 n.17. This is exactly the issue addressed by this Comment, which concludes there is no such liability.

302. *Id.* at 1193, 1201.

303. *See supra* note 35.

304. *Id.*

305. 17 U.S.C. § 1201(a)(1)(A) (West 2000).

306. *Id.* § 1201(a)(2), (b)(1).

307. Vicarious and contributory copyright infringement are secondary theories of liability, meaning the defendant is being held liable for alleged acts of infringement committed by another. MELVILLE B. NIMMER & DAVID NIMMER, 3 NIMMER ON COPYRIGHT § 12.04[A] (2008). Vicarious liability requires that the defendant (1) possess the right and ability to supervise the infringing conduct, and (2) have an obvious and direct financial interest in the exploitation of copyrighted materials. *Id.* § 12.04[A][2]. Contributory liability requires either knowingly and materially contributing to the infringing conduct of another, or knowingly providing the means to infringe. *Id.* § 12.04[A][3].

effectively controls access to a work”³⁰⁸ or “a technological measure that effectively protects a right of a copyright owner.”³⁰⁹ AT&T uses a software lock to restrict access to the iPhone’s operating software³¹⁰ that would technically constitute an access control within the meaning of the antitrafficking provisions, and therefore software designed to defeat that lock is illegal, or so the argument would go.

Despite its initial plausibility, the argument is fundamentally flawed. As *Chamberlain* squarely held, a valid cause of action under the DMCA must allege more than simply *access*, there must also be a nexus between that access and a right protected by copyright.³¹¹ But the Register of Copyrights determined that the locks on cell phones have nothing to do with any interest protected by copyright.³¹² Therefore, AT&T’s legal claim would fail for the same reason *Chamberlain*’s did: the inability to establish the connection between access and copyright protection. Furthermore, the *Chamberlain* court explicitly noted that “[f]or obvious reasons, § 1201(a)(2) trafficking liability cannot exist in the absence of § 1201(a)(1) violations”³¹³ This means that trafficking liability³¹⁴ can *never* exist with regard to cell phone unlocking software³¹⁵ because the Librarian of Congress has specifically exempted consumers from liability³¹⁶ for the very circumvention that software enables.³¹⁷

The only possible complication is that the cell-phone anti-circumvention exemption only applies “when circumvention is accomplished for the sole purpose of lawfully connecting to a wireless telephone communications network.”³¹⁸ In this vein, the contractual provisions that expressly prohibit doing so may be an attempt to “patch” the exemption (and the holding of *Chamberlain*) by making carrier-agnostic network access a violation not of copyright but of contract law. In other words, AT&T could argue that the exemption does not apply

308. 17 U.S.C. § 1201(a)(2)(C).

309. *Id.* § 1201(b)(1)(C).

310. *See generally supra* Part II.

311. *Chamberlain Group, Inc. v. Skylink Tech. Inc.*, 381 F.3d 1178, 1204 (Fed. Cir. 2004).

312. *See supra* text accompanying notes 162–66.

313. *Chamberlain*, 381 F.3d at 1196 n.13.

314. 17 U.S.C. § 1201(a)(2).

315. Rather, trafficking liability cannot exist before Oct. 27, 2009, when the exemption expires. *See Patents, Trademarks, and Copyrights*, 37 C.F.R. § 201.40(b) (2007).

316. 17 U.S.C. § 1201(a)(1)(A).

317. *See supra* text accompanying note 154.

318. 37 C.F.R. § 201.40(b)(5).

because the consumers who used the unlocking software did not connect “lawfully.”³¹⁹ With no exemption, there is a violation of the anticircumvention provision,³²⁰ and the software vendors can be liable under the antitrafficking section.³²¹ Therefore, for the same reasons courts should hesitate to enforce the iPhone’s contractual restrictions against consumers, they should refuse to allow the wireless carriers to use those contracts to bootstrap a theory of liability against the developers of unlocking software under the DMCA.

In summary, Apple’s attempts to use contract law as a justification for disabling unlocked phones, and AT&T’s reliance on copyright law to stifle unlocking software, are both indefensible tactics to enforce the anticompetitive tie between the iPhone and AT&T wireless service. While consumers accepted the click-wrap contracts of both companies, the unlocking restrictions could be found unconscionable under California contract law, violating those agreements as quasi-efficient breach, or both. In terms of copyright law, the DMCA was never intended to be used as a means of protecting monopolies, and so AT&T should be prevented from misusing the statute towards that end.

CONCLUSION

The iPhone lawsuit continues to slowly work its way through the court. Recently the court ruled favorably for the plaintiff class, denying AT&T and Apple’s motions to compel arbitration and dismiss many of

319. At least one court has parsed the meaning of the word “lawfully” to hold a commercial reseller of unlocked phones did not benefit from the exemption, and so was liable under the DMCA. See *Tracfone Wireless, Inc. v. Dixon*, 475 F. Supp. 2d 1236 (M.D. Fla. 2007). The court in that case found that the defendants’ conduct was not within the scope of the exemption because the defendants’ “misconduct and involvement in unlocking TracFone handsets was for the purpose of reselling those handsets for a profit, and not ‘for the sole purpose of lawfully connecting to a wireless telephone communication network.’” *Id.* at 1238 (quoting 37 C.F.R. § 201.40(b)). The holding can reasonably be limited to its facts, and so distinguished from iPhone unlocking. TracFone’s business involved selling heavily subsidized cell phones with no contract, and then selling minutes directly to customers to recoup the price of the phone. Granick, *supra* note 167. The defendants purchased TracFone phones in bulk, unlocked them for use on any wireless network, and then resold them for a substantial profit. *Tracfone*, 475 F. Supp. 2d at 1237. However, unlike the iPhone situation, the defendants did not unlock the phones for their own use as consumers, but rather strictly to resell them. *Id.* Furthermore, since the iPhone itself is not subsidized, a similar pecuniary loss is not incurred, at least on the initial purchase.

320. 17 U.S.C. § 1201(a)(1)(A).

321. *Id.* § 1201(a)(2).

the claims.³²² While Apple has taken a less aggressive stance regarding unlockers lately, if the case proceeds to trial it is possible that the court may award some modicum of damages for those whose phones were disabled by the September 2007 software update. The cost of purchasing a new iPhone would be one remedy, or perhaps a smaller amount for those who were not left with an “iBrick,” but rather only inconvenienced. Absent evidence of malicious intent on the part of Apple in disabling the unlocked phones, punitive damages are unlikely.

The antitrust claims are more difficult to assess. If the case ever goes to trial, the market in iPhone-like devices may have matured to the point where the issues are effectively moot. In other words, if other manufacturers and wireless carriers introduce products with similar features, there would no longer be a lack of alternatives that would support anticompetitive claims. There is also anecdotal evidence that Apple may eventually offer the iPhone without requiring a specific wireless carrier, perhaps after the five-year exclusive AT&T deal has expired.³²³

Regardless of the outcome of the iPhone lawsuits, consumer discontent with the wireless industry has been growing for some time. Change is already underway. Consumers won the right to take their phone number with them when switching carriers years ago.³²⁴ Congress has taken notice of continuing complaints about industry practices, as evidenced by the iPhone hearing and the Cell Phone Consumer Empowerment Act of 2007.³²⁵ Carriers have begun prorating early-

322. Order Denying Defendant AT&TM’s Motion to Compel Arbitration and to Dismiss; Denying Defendant AT&TM’s Motion to Stay Discovery; Granting in Part and Denying in Part Defendant Apple’s Motion to Dismiss, *In re Apple & AT&TM Anti-Trust Litigation*, No. C 07-05152 JW (N.D. Cal. Oct. 1, 2008).

323. See Arnold Kim, *Apple COO Discusses iPhone Exclusivity, SDK, and Unlocking*, MACRUMORS.COM, Feb. 28, 2008, 7:07 EST, <http://www.macrumors.com/2008/02/28/apple-coo-discusses-iphone-exclusivity-sdk-and-unlocking> (noting that Apple’s chief operating officer Timothy Cook stated at a Goldman Sachs investment symposium that the reason the iPhone was exclusive to AT&T was that Apple felt it was impractical to make both a CDMA and GSM version of the phone that would support multiple carriers for the initial release).

324. See generally FCC.gov, *Wireless Local Number Portability Frequently Asked Questions*, <http://www.fcc.gov/cgb/NumberPortability> (last visited Sept. 23, 2008).

325. See *supra* Part III.B.

termination fees³²⁶ and opening their networks to third-party devices and applications.³²⁷

Apple's vigilante action did little to stem the tide of iPhone unlocking, and if anything, has only put an exclamation point on consumer discontent with the anticompetitive U.S. cell-phone industry. The original contractual restrictions were easily ignored and arguably unenforceable, both in court because of possible unconscionability and in practice because absent another round of bricking, Apple is left with no reasonable means of enforcement short of suing their customers one-by-one. The reversion to in-store activation with the iPhone 3G means the contracts can no longer be ignored, but does not remedy the contracts' underlying enforceability problems. AT&T may continue wielding the DMCA in an effort to scare developers of unlocking software, but as explained above, their legal theory is only a paper tiger. Therefore, the massively popular iPhone may ultimately prove to be the harbinger of true cellular freedom. In that vein, Apple may find success in failure: losing an exclusive business partner in AT&T, but once again revolutionizing an entire industry. Think different indeed.³²⁸

326. *See supra* text accompanying note 74.

327. *See supra* text accompanying note 71.

328. *See supra* text accompanying note 19.