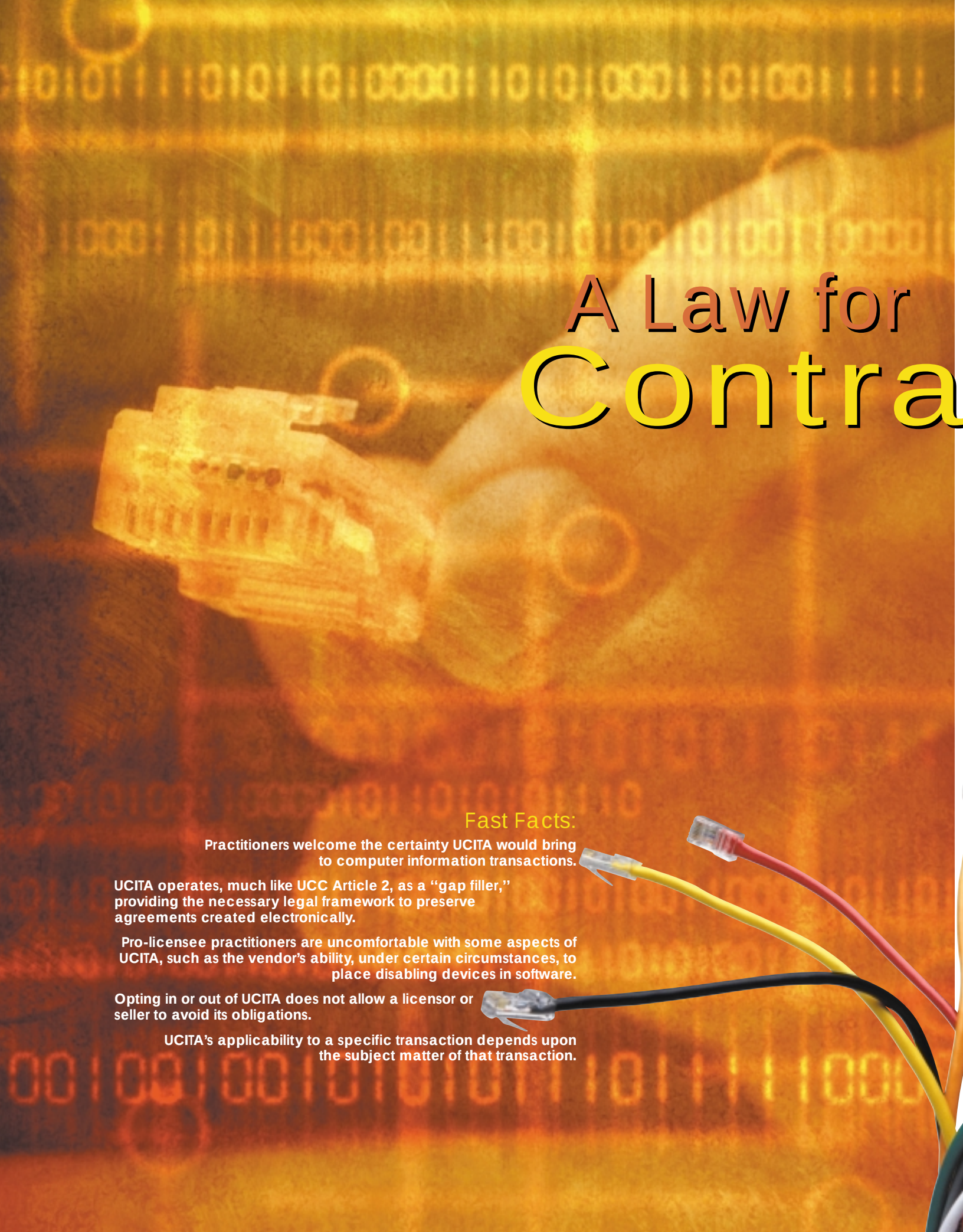
A Law for Contra



Fast Facts:

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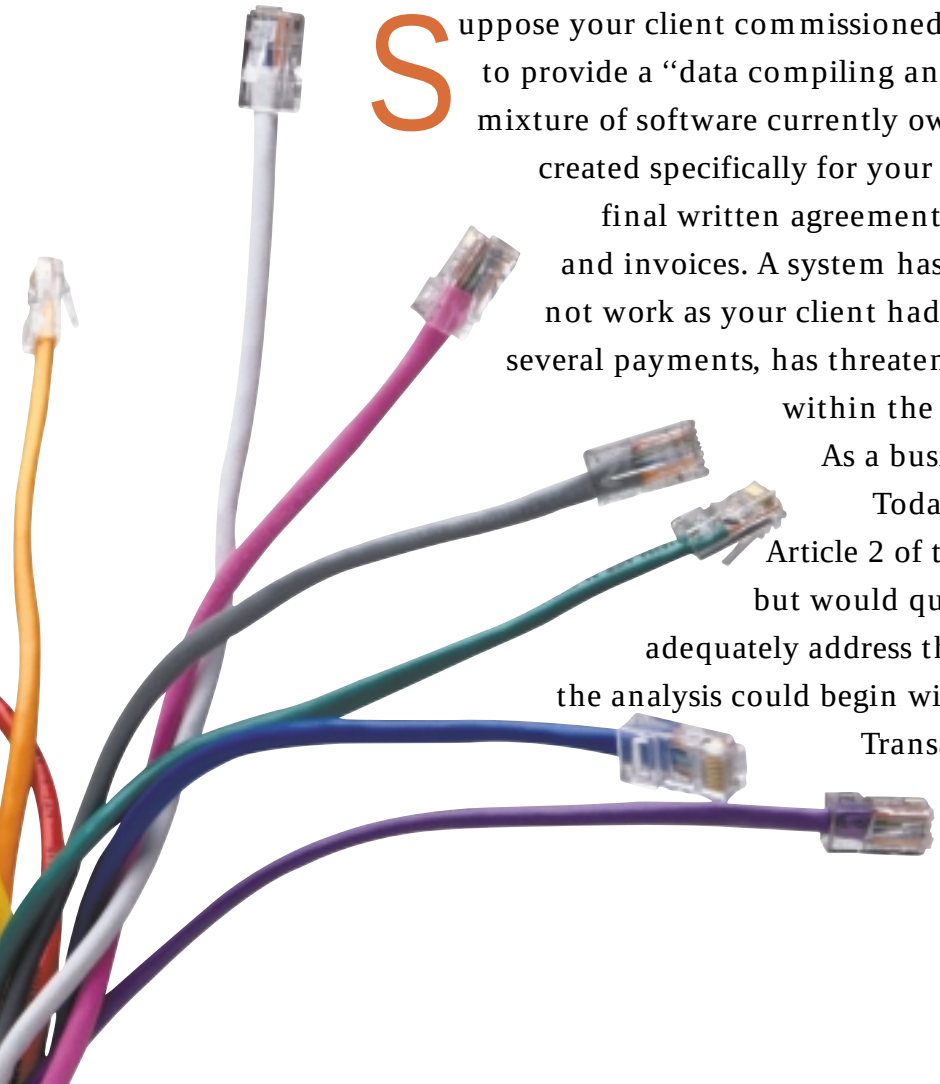
acting in the 21st Century

The Uniform Computer Information Transactions Act is a statute whose time has come

BY FREDERICK E. SCHUCHMAN, III



Suppose your client commissioned an out-of-state computer programmer to provide a "data compiling and transmitting" system, composed of a mixture of software currently owned by that programmer and software created specifically for your client by that programmer. There is no final written agreement, only the exchange of purchase orders and invoices. A system has been delivered and installed, but does not work as your client had hoped. The programmer, who is owed several payments, has threatened to trigger a disabling device hidden within the system if payment is not forthcoming. As a business attorney, what would you advise?

Today business attorneys would first look to Article 2 of the Uniform Commercial Code (UCC),[1] but would quickly determine that the UCC does not adequately address these issues. In the not-so-distant future, the analysis could begin with the Uniform Computer Information Transactions Act (UCITA),[2] the self-described "commercial contract code for computer information transactions."

UCITA is the result of a decade of discussions and debates involving leaders from the information industries, state bar groups, the ABA, and other concerned parties. It arose out of the existence of a fundamentally new method of transacting business in our economy, focusing on information products and services. Just as Article 2 addresses the sale of manufactured goods, UCITA addresses the sale and transfer of computer information and computer information services.[3]

On July 29, 1999, the National Conference of Commissioners on Uniform State Laws (NCCUSL), by a vote of 43 to 6, promulgated UCITA for enactment by the states. NCCUSL, a national organization of practicing lawyers, judges, and academics, crafted UCITA to provide clear, consistent, and uniform rules to govern the intangibles of transactions involving computer information. To date, it has been enacted in Virginia (with several amendments) and Maryland, and has been introduced in Illinois, Maine, Arizona, New Jersey, Oregon, New Hampshire, the District of Columbia, and Texas.[4] While UCITA is debated in various circles in Michigan, it has not found a champion and has yet to be introduced in our legislature.

Practitioners welcome the certainty that UCITA would bring to computer information transactions. UCITA operates, much like Article 2, as a "gap filler," providing the necessary legal framework to preserve agreements created electronically. Pro-licensee practitioners are uncomfortable with some aspects of UCITA, such as the vendor's ability, under certain circumstances, to place disabling devices in software. They are also concerned that the unequal bargaining position granted licensors contracting electronically will be untenable to smaller businesses and individual licensors. However, such provisions are the result of compromise within the NCCUSL and may be acceptable to achieve uniformity and consistency in computer information transactions.

Computer Information Transactions

UCITA is a contract law statute, coming into effect only when enacted in each jurisdiction. It does not create new property rights or amend tort law and is not a new federal law governing information transactions.[5]

Section 103 of UCITA defines "Computer Information" as "information that is in electronic form and is obtained from, accessible with, or usable by, a computer." A "Computer Information Transaction" is an agreement involving computer information, including transfers of computer programs or multimedia products, software, and multimedia development contracts, access contracts, and contracts to obtain information for use in a program.

UCITA's applicability to a specific transaction depends upon the subject matter of that transaction. An agreement to transfer software falls under UCITA; an agreement to use e-mail to communicate about the sale of a car does not.

UCITA covers contracts to license or buy software or create computer programs; it addresses online access to databases and contracts to distribute information on the Internet. If the contract is for goods with embedded software, UCITA does not apply unless the main purpose was to obtain the software. Cars, toasters, and microwaves generally include embedded software, but UCC, and not UCITA, would cover those transactions.

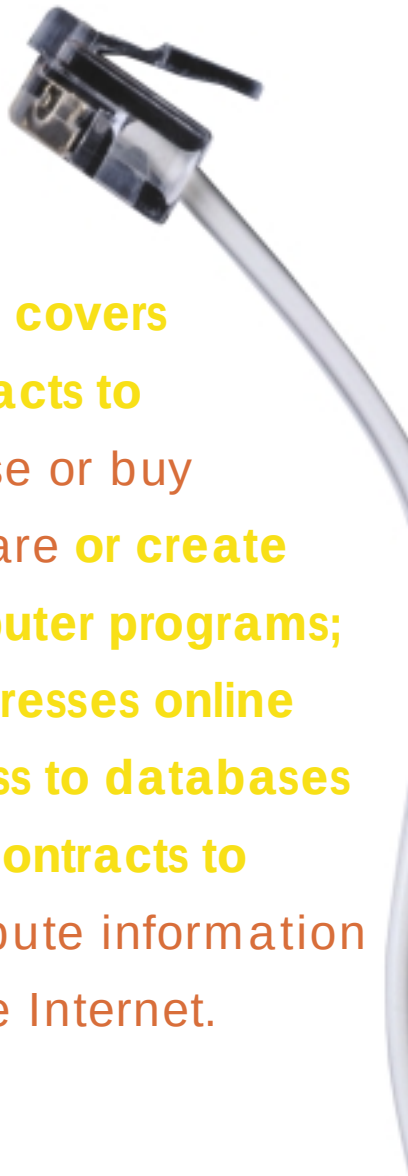
Freedom of Contracting

Article 2 of the UCC served as both a model and a point of departure for UCITA. UCITA, like Article 2, would remain in the background of many transactions. It fills the gaps when the parties do not explicitly set forth all of the terms of their transaction. The parties negotiate the deal and UCITA provides "default rules" to apply only if a specific issue is not addressed.

UCITA strives to preserve the freedom of the parties to make their own agreements. As pointed out by Carlyle C. Ring, Jr., chair of the UCITA Drafting Committee, freedom of contracting, plus the ability to opt out of UCITA, was essential to the drafters:

> *Contract law only creates background rules. We have a free-market, contract-choice economy. UCITA preserves that. This means that parties can sell, buy or license (or not) and decide what terms are acceptable for their transaction. Opting to let UCITA apply or not is one way of doing this. Second, because UCITA and our information economy break new ground, UCITA was drafted with a relatively narrow scope. There may be transactions where several different contract laws apply. This same thing happens under current contract law today. In each case, if they so choose, the parties need to be able to resolve the issues by agreement. They can do this by choosing UCITA as applicable law.*[6]

Opting in or out of UCITA does not allow a licensor or seller to avoid obligations. UCITA does not contract away tort law. Antitrust, copyright, patent, FTC advertising restrictions, product liability, tax law, regulatory law, consumer protection, and similar laws will still apply. Further, UCITA preserves existing state consumer protection statutes and strives to follow traditional contract law, which does



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not create a long list of detailed restrictions to the freedom of contract. It does not alter federal consumer law and applies new rules only where change is needed to facilitate electronic commerce. If a law prevents changing some rules of contract by agreement, opting in or opting out cannot alter that fact.

Relation to Federal Law

Federal law specifically preempts UCITA (Sec. 105). Parties enjoy the freedom to make their own contract, but if a term of a contract violates a "fundamental public policy," a court may refuse to enforce the contract. UCITA does not alter intellectual property or other fundamental information law but attempts to balance the freedom of contract with fundamental public interests.[7] For example, parties can agree to restrict the use of confidential information, but public policy concerns arise if there is an attempt to restrict, by contract, the use of public information. A term in a shrink-wrap license prohibiting the criticism of the quality of the software may raise public policy concerns, whereas a similar provision in a software development agreement between a developer and a corporation would not.

Warranties/Perfect Tender

UCITA retains, with some necessary modifications, the warranties in Article 2 and even creates new warranties where appropriate to address the unique concerns of this subject matter. It expands user protection by providing that an express warranty can be created by advertising (Sec. 401), as well as additional warranties such as the implied warranty of data accuracy (Sec. 404) and system integration (Sec. 405). While such warranties can be "disclaimed" by the licensor, UCITA requires any disclaimer to be more informative and obvious than similar disclaimers under Article 2.

UCITA recognizes that a licensor cannot always tender a perfect product and sets a "substantial performance" standard for determining fulfillment of the contract. This acknowledges the inherent imperfection of software and software products and allows the licensee to terminate the agreement if there is a "material breach" such that the licensee is substantially deprived of the significant benefit it reasonably expected under the contract. Courts have applied this standard for years as a method of protecting injured parties but avoiding unwarranted forfeitures. Licensees will still retain the right to damages and to offset the amount owed against the amount lost.

Electronic Commerce Guidelines

UCITA can be seen as a substantive contract law statute, setting forth formal requirements for electronic agreements (Sec. 201). These include

- what makes a term conspicuous (Sec. 102)
- when and how an on-screen action establishes a contract (Sec. 201–207)
- choice of law (Sec. 109)
- choice of forum clauses (Sec. 110)
- warranties for published information (Sec. 404)
- forming contracts by electronic agents (Sec. 206)
- remedies for online agreements (Sec. 801–806)

Setting forth the formal requirements for electronic contracting is an invaluable part of UCITA. Licensors know that they can distribute goods electronically under valid, enforceable agreements. These guidelines are a positive step for the furtherance of electronic commerce.

Mass-Market Licenses

UCITA introduces a "Mass-Market License" (MML), a standard form contract used for transactions with the general public in a retail setting where the information is generic and the customer is either a consumer or a small business. Standard form contracts are not a new concept, but the use of standard agreements such as MML to deal with intellectual property is new and innovative. The license conveys important rights to the licensee and provides a coherent background for marketing products in the information industry today.

An MML is effective only if the licensee manifests assent to it (clicks a button accepting the terms) after having an opportunity to review the terms. MMLs are limited by some general contracting limitations, such as unconscionable terms. Terms that violate a fundamental public policy or conflict with the actual agreement (for example, 90-day refund right vs. 30 days in terms of license) are unenforceable.

Shrink-wrap Licenses

UCITA also brings acceptance to the familiar "shrink-wrap" license—nonnegotiable documents that users frequently encounter in purchasing software or similar products. In so doing, the UCITA committee adopted, as uniform law, the position of the majority of the cases and added some procedural and substantive protections for the licensee that might be inferred from the decisions.

Essentially, shrink-wrap licenses require users to agree to terms after the product has been opened or received. The user generally commits some act such as breaking the shrink-wrap or clicking "I accept" on a screen. UCITA would make such licenses enforceable, even though the user may not have been able to review the terms before that act. However, the user does have the right to return the product, cost-free, if they didn't like the terms, as well as the right to reasonable costs of restoring their system if it was altered when trying to obtain the license terms.

Elements such as this truly underscore UCITA's goal of enhancing commerce—it empowers parties to conduct billions of dollars worth of transactions under uniform terms.

This provision, however, may prove to be fertile ground for future litigation as courts struggle to determine what the parties agree to in the course of their dealings. This author envisions situations where licensors offer products only through such transactions, which will require licensees to affirmatively agree to the licensor's terms to obtain their product. In these situations, there will be no real negotiation of individual agreements, since the terms are offered on a "take it or leave it" basis. UCITA may require some tweaking in order to prevent small business licensees and consumers from being forced to accept narrow warranties and scant product service to obtain products electronically.

Self-Help Repossession

When a license is canceled for a material breach, the licensor has the right to obtain possession of all copies of the licensed software or information and to prevent any further use of it by the licensee. UCITA specifically grants licensors the limited right to exercise self-help, through various electronic

measures (Sec. 816). Licensors are able to electronically disable software possessed by licensees for material breaches under certain specific circumstances:

- express consent by the licensee to the self-help clause
- the clause must be conspicuous
- licensee must receive 15 days notice, directed to a person and place designated earlier in their agreement, before the device is triggered
- notice must specify the nature of the breach
- licensee may recover direct and incidental damages for improper use of this remedy
- no self-help if licensor has reason to know of substantial risk to public health or third parties
- courts are required to promptly consider injunction requests against self-help

User groups and practitioners often cite this provision in voicing their concerns about UCITA claiming that it grants too much control to licensors. It was reviewed and modified by the Executive Counsel of NCCUSL as recently as January, 2001 and may prove to be a fertile ground for future litigation.

The Law for Tomorrow

Michigan will someday be called upon to vote for or against UCITA. At that time, factions with strong opinions will continue to debate this complex piece of legislation. No one will agree with everything in UCITA, but everyone acknowledges that UCITA, or some version thereof, is a statute whose time has come. ✦

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Footnotes

1. Article 2 of the UCC is found at MCL 440.1101 et seq.; in this article, the author uses UCC and Article 2 interchangeably.
2. UCITA can be found at www.law.upenn.edu/bll/ulc/ucita/ucita1200.htm.
3. See "Series of Papers on UCITA Issues" by Carlyle C. Ring, Jr., chair, and Ray Nimmer, reporter, UCITA Drafting Committee. This can be found at www.ucitaonline.com/docs/ring.pdf.
4. Up-to-date information on the status of UCITA in the various states' legislatures can be found at www.ucitaonline.com/whatsnu.html.
5. The author's review of UCITA in this and subsequent sections is indebted to the aforementioned "Series of Papers on UCITA Issues," UCITA, and the "Overview of Uniform Computer Information Transactions Act" by Mary Jo Dively, ABA Advisor to Drafting Committee. The author is solely responsible for any comments or opinions expressed herein.
6. See "Series of Papers on UCITA Issues," above, page 3.
7. See "Official Comment" to Section 105 of UCITA.