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ARTICLE 2B: AN INTRODUCTION

by RAYMOND T. NIMMER†

INTRODUCTION

Information industries and information commerce dominate our economy. With the advent of digital technology, all of the previously distinct information industries are converging into a single whole that faces common issues of law. Historic lines distinguishing motion pictures, broadcast, publishing, software, and records are increasingly insignificant.¹ The converging industries exceed in importance and potential all of the older manufacturing sectors in our economy. They are the future of commerce, especially in this country.

The transactions that characterize these industries provide the framework for Article 2B. They involve subject matter and contract structures entirely unlike transactions in goods. Yet, it is in this subject matter that the modern economy reverberates. The United States was once the major producer of goods in the world, and today it is the major consumer of goods. However, we are now the major developer and distributor of information (e.g., software, content, news, entertainment and the like). Our economy emphasizes information and services. Article 2B reflects this; it deals with transactions and subject matter that by and large have never been covered by a Uniform Commercial Code (“U.C.C.”).²

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1. Motion pictures, books, and records are now often digital in content and provided through various digitally enabled systems, such as Internet access. Thus, for example, a recently successful motion picture (TOY STORY) was in effect a lengthy computer program, entirely digital in development and presentation. Various publishers, such as the New York Times, the Wall Street Journal, and West Publishing, provide their basic information resources on-line as well as in paper form. They do business in the same environment in which Oracle Software provides its commercial software products to end users.

2. Of the transactions treated in Article 2B, only software contracts have previously been within the U.C.C. Even for computer software, coverage under the U.C.C. is limited. But *Article 2B is not just a software contract statute*. Contracts involving the other subject matter of licensing (e.g., digital texts, motion pictures, databases, on-line services, photographs) are today governed not by the U.C.C. at all. They fall, instead, under a complex mixture of common law, federal property law, and some regulation. As was the case in the

This Symposium deals with Article 2B. The issues are many, reflecting modern commerce. The economic shifts that characterize the information age dislocate many vested economic interests centered around a relatively stable goods-centered economy. This is a major transition; it is not controlled by law. Decisions in various areas of law and policy affect and shape this dislocation, but the economic, technological, and social forces involved have their own dynamic.

Article 2B provides a framework document for this new commerce. This article does not debate the substantive issues in drafting this new framework document for the information age. I reserve that for later when all of the policy choices have been formulated. I concentrate here on several general, but critical issues in Article 2B and the law reform enterprise.

Part One starts at the beginning, by dealing with the idea of difference. To understand what is occurring in our legal system, including in reference to Article 2B, we must understand why an economy and commerce based on information differs fundamentally from one whose features were etched in the economics of the 1950s and 1960s when the production and distribution of goods was at the core of the economy. This is not the place to engage in a broad analysis of sociology or political economics. Rather, Part One focuses on a narrow sub-theme: the relationship between the economic shift and the nature and importance of contract and contract law. One comparative point is paramount. Goods occupy a bounded space; that corpus is the subject mater *to which* the contract refers. Information does not occupy a bounded space; the contract defines the product since it defines what rights are transferred. Some argue that the contract is the product. This reflects an important reality. Contract has greater relevance in information deals and a commercial desire for greater emphasis on contract autonomy and contract clarity.

Part Two examines the nature of commercial contract and the process that creates the statutes that shape contract principles. Here, quite simply, a conflict exists between two views of contract law. The conflict involves a debate between a philosophy of regulation and a philosophy of contract autonomy. As we shall see, a commercial code must emphasize contract choice or autonomy. The range of practical, marketplace and relational choices that characterize commercial commerce are far too broad and far too nuanced to admit of singular or monolithic regulatory solutions. Thus, Article 2B rejects a regulatory approach. It follows the fundamental philosophy of the U.C.C. and emphasizes the right of parties to set their own contractual course. That approach results in a con-

original development of Article 2, a major aspect of the project involves making accommodations between U.C.C. premises and commercial practice in these other fields.

tract statute that largely consists of certain “default” rules; by statutory provision, applicable only if the parties have not otherwise agreed. Of course, however, that approach to contract law generally receives sharp criticism from those who favor broad regulation or judicial review through encouraged litigation.

In Part Three we overview some of the basic default rules and approaches employed in Article 2B to deal with the complex world of information licensing. I focus on several of the major types of Article 2B transactions, covering the following: electronic commerce issues; general licensing models; informational content; and the new idea of mass market licensing. In each case, rather than an in-depth consideration, the purpose of the discussion is to present the broad parameters of the Article 2B approach.

PART I

A. THE FACT OF DIFFERENCE

Current commercial contract law reflects decisions and doctrines premised on transactions in “goods.” Article 2, the primary source of commercial contract law in this country, reflects a 1950s economy. In the 1950s, clear distinctions existed between goods, information, and services in commercial relationships. Clearly, sales of goods dominated at that time. Today, much of the “value provided by the successful enterprise . . . entails services [and information].”³ This economic shift, reflected in Article 2B, forces us to ask to what extent concepts grounded in that subject matter remain viable when the subject matter of the transaction is information, rather than goods.⁴

1. *Information and Contract*

Information transactions are not equivalent to transactions in goods. Quite simply, a contract to acquire investment data differs fundamentally from a contract to purchase a toaster.⁵ Similarly, an information

3. ROBERT REICH, *THE WORK OF NATIONS* 85-86 (1991).

4. Contracts involving information, however, have not historically been viewed as an important part of commerce. They were not important in the 1950s. For the academic community, they are still not considered mainstream concerns. There is an understandable tendency to defend the *traditional* status quo. That view, while reasonable in the 1950s, no longer states a sustainable view of law, academic theory, or modern commerce.

5. Many court decisions place pre-designed software licensing in Article 2 even though software is licensed and not sold and even though the focus of the transaction centers not on the acquisition of tangible property, but on transfer of rights intangibles. See *Advent Systems Ltd v. Unisys Corp.*, 925 F.2d 670 (3d Cir. 1991); *RRX Industries, Inc. v. Lab-Con, Inc.*, 772 F.2d 543 (9th Cir. 1985); *Triangle Underwriters, Inc. v. Honeywell, Inc.*, 604 F.2d 737 (2d Cir. 1979); *In re Amica*, 135 B.R. 534 (Bankr. N.D. Ill. 1992). Cases excluding software and data processing from Article 2 include: *Data Processing Services, Inc.*

economy is not equivalent to an economy based on the manufacture and sale of goods. No commercial entity that adhered to the old economy exists today. Just like the blacksmith in the industrial era, so will many occupations of the industrial era disappear in the information era. Contract law cannot alter that fact. An information economy rewards entirely different activities, creates different risks, and involves an entirely different set of critical actors than a goods economy. It requires different contract law concepts.

To begin, the transactional goals of an information transaction differ from the goals of a transaction involving goods. In reference to goods, the buyer typically desires and the seller transfers ownership or possession of *specific* goods. A sale entails relatively straightforward and consistent rights granted to the buyer with regard to the goods. In an information transfer, in contrast, the goals of a transferee are to acquire the information and appropriate contractual rights to use it. The goals of the information provider are to provide the information and rights in a manner that satisfies the transferee's interests, while retaining value for future transactions that involve the *same information*. There is an immense variance (potential and real) in what rights are given and what rights are withheld.

Of course, the balance or mix of the transferee's (and transferor's) goals vary. The important point, however, is that the transferee's goals concentrate on rights, rather than on physical possession or control. Similarly, for the transferor, a transfer of goods focuses on the return (profit) from an item (or a group of items), while in a transfer of rights in information the transferor does not typically give up information that it does not also retain. Information is typically both transferred and retained. For example, the fact that I disclose (transfer) a secret to you does not mean that I no longer know that same information. For goods, the transaction is bounded by a reference point focused on the tangible items. For information, the extent and character of the transfer hinges not on what physical item is delivered, but on what rights are granted or withheld *by the contract*.

This outlines the importance of contract in the information age. There are other transactional differences that flow from the focus on rights, rather than items. One involves required performance of the contract. Article 2 transactions presume that performance requires *delivery* of the goods; that framework builds a structure of obligations and rights around the delivery of the goods. In contrast, in information transactions, "delivery" is not always part of the deal. Information can be trans-

v. LH Smith Oil Corp., 492 N.E.2d 1329, (Ind. Ct. App. 1986) (software development); Micro-Managers, Inc. v. Gregory, 434 N.W.2d 97 (Wis. Ct. App. 1988) (development contract).

ferred in many ways, such as a telephone call; an electronic message; or a diskette. In many transactions, it may not be "transferred" at all. The only transactional issue involves a grant to the licensee of rights to use what it already has.

A legal system that supports the information economy must recognize the differences. The terms of the contract, especially those terms related to the scope of the granted rights, have greater importance in the information economy than in the goods economy. While the physical attributes of the subject matter typically define its focus in reference to goods, those attributes do not similarly define the focus for information. A person who acquires a disk containing a database with the *unrestricted* right to use the data acquired a different asset than a person who acquired the same database with the right only to use the database for non-commercial purposes.⁶ The contract (license) defines and, some say, is the product.

As a result, digital information products require a contractual base that entails a greater degree of certainty and explication, at least as to significant terms, than transactions in goods. Uncertainty in the definition or enforceability of contract terms regarding rights transferred, or withheld, would be equivalent in the world of goods to uncertainty about whether one has sold a car or a typewriter. The contract has a special place in the nature of the commerce.

2. License Contracts

Article 2B is not an intellectual property licensing statute. Neither contracts nor commerce in information hinge on the existence of "property" defined by intellectual property law.

Article 2B deals with *contract* law. A contract does not require a transfer of "property" rights.⁷ Indeed, in the information era, many contracts will involve what we once loosely described as services, rather than property. Other important forms of transaction, especially on the Internet, entail contractual grants of access to electronic databases; the relevant contractual framework being built around the resource owner's right to control access to and use of its own computer system.⁸ Enforceable contracts require "consideration." Consideration lies in promises,

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

7. See *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447 (7th Cir. 1996); *Architectronics, Inc. v. Control Systems, Inc.*, 935 F. Supp. 425 (S.D.N.Y. 1996) (Copyright Act does not preempt breach of contract claims. It is not necessary that the contractual promise relate to actions not otherwise covered by copyright law. A promise itself could supply the "extra element" necessary to defeat preemption).

8. See *Ticketron Ltd. Partnership v. Flip Side, Inc.*, No. 92-C-0911, 1993 WL 214164 (N.D. Ill. June 17, 1993); *Soderholm v. Chicago Nat'l League Ball Club*, 587 N.E.2d 517 (Ill. App. Ct. 1992).

permissions, actions and other forms of value. Most of these do not relate to ownership of intellectual property.

In Article 2B, the paradigm contract is a license. A license "grants permission to access or use information" and expressly conditions, withholds, or limits the scope of the rights granted.⁹ Licenses thus apportion rights or permission to use, reproduce, modify and otherwise benefit from *information*. Focusing on intellectual property licenses, a license was described by the Supreme Court as "a mere waiver of the right to sue," effectively providing the licensee with the ability to use information or resources in ways that might otherwise infringe property rights of the licensor in the information.¹⁰

A license is not a lease and it is not a sale. Both of those terms apply to transfers of *goods*, not rights in information.¹¹ In leases and sales, the transferee's primary purpose is to acquire goods. In a license, the transferee desires the information and its use.

Licensing is a dominant means of commerce in digital information and in commercial information transactions. A body of license contract law exists outside the U.C.C. Indeed, while many courts apply Article 2 to contract disputes involving software, Article 2 has never been applied to determine the effectiveness of information use restrictions.¹²

Article 2B does not *create* licensing contract law—these contracts have long been used in information transactions. Article 2B seeks to provide a coherent framework for contract issues. They have been dominant for many years in commercial arrangements relating to information assets. However, with the continued maturation of the information econ-

9. U.C.C. § 2B-102 (Proposed Draft, Sept. 25, 1997).

10. *General Talking Pictures Corp. v. Western Electric Co.*, 304 U.S. 175, 181 (1938). See *Spindelfabrik Suessen-Schurr v. Schubert & Salzer*, 829 F.2d 1075, 1081 (Fed. Cir. 1987) (description is appropriate even if the licensee is "given the right to make, use, or sell" the technology); *Cohen v. Paramount Pictures Corp.*, 845 F.2d 851 (9th Cir. 1988) (one of the least forms of transfers possible).

11. In fact, because they deal with different issues, it is possible to have both a license and either a sale or a lease of the tangible copy. The license would contractually define the licensee's rights to use the information, while the sale or lease terminology deals with ownership and control of the tangible copy. See, e.g., RAYMOND T. NIMMER, *THE LAW OF COMPUTER TECHNOLOGY* ¶ 7.03 (2d ed. 1992), see also *DSC Communications Corp. v. Pulse Communications, Inc.*, 976 F. Supp. 359 (E.D. Va. 1997).

12. Courts generally enforce contract terms unless a specific term in a particular context conflicts with federal antitrust or related doctrines of patent or copyright misuse. Thus, courts have enforced license restrictions precluding non-commercial use of a mass market digital database, limiting a right to access by barring the making of a copy of software, limiting use to a specific computer, limiting use to internal operations of the licensee, restricting redistribution to a particular grouping of software and hardware, precluding modification of a computer game, and various other contract limitations. In these and other cases, the license accompanied distribution or delivery of a copy that enabled the licensee to use the licensed information.

omy, there has been a movement outward to encompass the mass market of information, including transactions involving computer software, cable access contracts, rented video cassettes, and Internet access arrangements. Throughout, while the detailed content and terms vary, the basic structure is the same: a person in control of particular information grants another person conditional rights of access to, or use, of that information.

3. *Commercial Practice*

In industries covered by Article 2B, copyright is a dominant source of property rights. One basic commercial choice for a copyright owner is whether to *license* information or to *sell* copies of information. The practices vary. Today, books and most musical records in the mass market are sold, while in its acquisition of the information the publisher licenses or receives an assignment of intellectual property rights. In the motion picture industry, studios license theaters to engage in public performances, while copies of motion pictures are sold or rented for consumer *non-public* performance. On-line data services license access. Software is licensed for both end users and upstream distribution. Video game cartridges, on the other hand, are often distributed through sales of copies.

In many cases, the licensee deals directly with the copyright owner. Direct licenses sometimes entail a transfer of a tangible copy of the information to the licensee subject to license restrictions. Increasingly, however, copies are transmitted to the licensee's site electronically. In part because of the different capital and manufacturing parameters involved, it is important to recognize that the common assumption applied in reference to goods is often not true in direct licensing. The vendor (licensor) is not routinely the larger or more asset rich entity. Indeed, most software companies are small and routinely involved in licensing into much larger client companies.

Commercial licensing also occurs through distribution channels involving third parties. These methods of distribution in information industries, however, are not analogous to distribution chains used for goods because of the subject matter and the intellectual property rights involved. Under copyright law, one of those *property* rights is the exclusive right to distribute copies of the copyrighted work.

While it over-simplifies the matter, it is useful to discuss two distinct frameworks. First, a master copy is provided to the distributor. This is common in the motion picture industry and in software. The "distributor" receives a single copy and a license to make and distribute additional copies or to make and publicly perform the work. For example, Correl Software may license a distributor to allow its software to be

loaded into the distributor's computers or video games. The contract limits the number of copies to be distributed and may restrict how they are distributed.¹³ Since both the making and the distribution of copies are within control of the owner's exclusive rights under copyright law, acts that go outside the contract limits and are therefore not authorized, not only breach the contract, but also constitute copyright infringement.¹⁴

A second distribution format transfers multiple copies for redistribution. This still occurs in software, books, record, and home video distributions, even though in each field, digital technology is rapidly eliminating the need for physical transfers or, even, for distributors. For example, in a physical transfer format, Quicken grants a distributor a *license to distribute* its accounting software. The distribution license places restrictions on how the distributor can retransfer the copies. The distributor may be allowed to distribute copies to retailers only if certain conditions are met, such as terms of payment, retention of the original packaging, and making the eventual end user distribution occur subject to an end user license.

In the vast majority of cases, this distribution method is supported by copyright law. Distribution is an exclusive right owned by the copyright owner under copyright law. Distributions outside the license infringes the copyright unless permitted by the commercial license. In either distribution format, in the mass market, the information eventually reaches an end user. There are three distinct scenarios here, with distinctly different consequences for the end user.

First, if the end user obtains the copy in an authorized distribution complying with the distribution license, the end user is in rightful possession of the copy. Its rights hinge on how it acquired the copy and whether it has a license from the copyright owner. If the distribution was a sale of a copy and was an authorized sale, the owner of the copy would obtain limited rights under copyright law (e.g., the right to distribute the copy, the right to make a back-up and changes essential to its use if the work is a computer program). These rights are equivalent to "default rules" under contract law. They state that, if a copy of a work is sold, the copy owner obtains certain rights unless the contract provides otherwise. Unless there is a contractual relationship between the copyright owner (publisher) and the "end user," those are the *maximum*

13. See *Microsoft Corp. v. DAK Industries, Inc.*, 66 F.3d 1091 (9th Cir. 1995) (court holds that distribution agreement involving lump sum payment and delivery of a master disk sold the right to make the stated number of copies, and was not an executory license for bankruptcy law).

14. See *Religious Technology Center v. NETCOM On-Line Communication Services Inc.*, 923 F. Supp. 1231 (N.D. Cal. 1995) (court holds that making available a copy to the general public in itself constitutes an infringing distribution unless authorized by a license).

rights obtained. The end user cannot make a *public* display of the information, even for “clip art.” It cannot make derivative works except for personal use, and it cannot make copies of the work except for archival purposes. These are not rights conveyed at a first sale.¹⁵ They can only be granted by the copyright owner.

Second, if the distribution system did not authorize a sale of the copy, but an unauthorized sale occurred, the end user is not a buyer at a first sale and does not obtain the “first sale” rights.¹⁶ Under copyright law, the end user cannot claim protection as a good faith purchaser, because that concept does not exist.¹⁷ Most probably, the end user is an infringer—unauthorized to take any action with respect to the work except perhaps to read it without copying it which is an impossibility for most digital works. The vendor has probably breached its warranty of good title or non-infringement, but that merely gives the end user a right of action against the distributor (retailer). In effect, the end user has failed to receive adequate rights from the actual copyright owner, unless of course it makes a separate agreement with the owner.

Third, if the distribution was authorized, but the end user does not become an owner of the copy, its right to use the copy depends *entirely* on the contractual permissions it receives from the *copyright owner*. By definition, it has not become an owner of a copy. Similarly, if the end user desires to do more than what copy ownership allows (e.g., make a copy on a desktop and a laptop computer), that too depends on contractual permissions. This is one arena of the so-called shrink wrap license. When an end user acquires a copy from a distributor (e.g., a retail store), it has no contract with the copyright owner (publisher). Its contract is with the retailer, although one could argue that there is an implied license of some type from the publisher, that theory has never been tested. Absent a contract, copyright restrictions apply with full force.

In many forms of mass market transaction and in some other forms of licensing, publishers limit the right of intermediaries to transfer copies and seek a direct contract relationship with the end user. As we have seen, in some of the most common distribution situations, the end user’s right to “use” (e.g., copy) the software depends on the license from the producer to the end user. The direct contractual relationship here jumps

15. See *Red Baron-Franklin Park v. Taito Corp.*, 883 F.2d 275 (4th Cir. 1989).

16. See *Microsoft Corp. v. Harmony Computers & Electronics, Inc.*, 846 F. Supp. 208 (E.D.N.Y. 1994) “Entering a license agreement is not a “sale” for purposes of the first sale doctrine. Moreover, the only chain of distribution that Microsoft authorizes is one in which all possessors of Microsoft Products have only a license to use, rather than actual ownership of the Products.” *Id.*

17. See *Microsoft Corp. v. Harmony Computers & Electronics, Inc.*, 846 F. Supp. 208 (E.D.N.Y. 1994); *Microsoft Corp. v. Grey Computer*, 910 F. Supp. 1077 (D. Md. 1995); *Marshall v. New Kids on the Block*, 780 F. Supp. 1005 (S.D.N.Y. 1991).

the chain of distribution and creates a direct link to the copyright owner (producer) and the end user. How these contracts are formed and whether they are enforceable has been controversial. Outside of "battle of the forms" cases, the limited case law enforces these contracts.¹⁸ Enforceability issues are a two-edged sword; the licenses contain terms that benefit the licensee, but also terms beneficial and often essential to the licensor. Article 2B as proposed places significant limitations on the enforceability of such licenses, while allowing them, as it must.

PART II

A. NATURE OF A COMMERCIAL STATUTE

Commercial law codification plays a unique role in contract law. The goal of contract law codification has never focused on regulating commerce or enabling litigation. Regulation typically occurs solely in consumer laws where protection of an identifiable and limited class is deemed important, as in federal antitrust and related competition law, and industry specific regulations (such as payment systems, banking law, and securities transactions). The goals of commercial contract law are to facilitate, not disrupt, and to support, not redirect, commercial practice. The goals do not pursue an academic agenda, but a commercial one.

1. *Contract Freedom and Personal Autonomy*

Article 2B supports the idea of contract freedom and adopts it as a basic principle. While this position has been attacked by consumer lobbyists and others who favor regulation, regulation of terms is unacceptable contract law in the information age.¹⁹ It would place the state and the courts in the position of determining fundamental aspects of the most vibrant part of modern commerce.

The concept of contractual freedom simply assumes that parties can better define and adopt or reject contract terms for their context than a statute, a legislature or a court. As a theme, it permeates the U.C.C. If one were to list the rules in *current Article 2* which preclude contractual choice, the list would be very short. Comments to *Article 2A*, the last general transaction statute added to the U.C.C. state: "This article was greatly influenced by the fundamental tenet of the common law . . . freedom of the parties to contract . . . [This includes] the ability of the parties to vary the effect of the provisions of Article 2A, subject to

18. See *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447 (7th Cir. 1996), *Arizona Retail Systems, Inc. v. Software Link Inc.*, 831 F. Supp. 759 (Ariz. Ct. App. 1993).

19. See Memorandum from Gail Hildebrandt to the National Conference of Commissioners on Uniform State Laws, *Consumer Objections to Article 2B* (July, 1997).

certain limitations [that] relate to the obligations of good faith, diligence, reasonableness and care."²⁰ Article 2B adopts that same principle and identical limitations.

Codification should facilitate commercial practice. The rules should mesh with expected or conventional practice. As observed by Grant Gilmore: "the principal objects of draftsmen of general commercial legislation . . . are to . . . assure that if a given transaction . . . is initiated, it shall have a specified result [and] to state as a matter of law the conclusion which the business community apart from statute . . . gives to the transaction in any case."²¹

The idea of contract freedom is embedded in contract law theory.²² It leads to a preference for laws that provide background rules, playing a default or gap-filling function in a contract relationship, rather than statutory mandates. A default rule governs only if the parties do not agree to the contrary. This is in contrast with rules that dictate terms. For example, a default rule states that information extraneous to a written contract can be used to alter contract terms *unless* the parties intended the writing to be the exclusive statement of the bargain. A regulatory rule would state that information extraneous to the written contract can *always* be used to add or delete terms, *even if* the parties intended their writing to be the exclusive terms of the deal when the writing was adopted. One rule presumes the autonomy of the parties. The other assumes the autonomy of a court or jury to disregard written terms if necessary to achieve what the particular judge or jury might regard as a "fair result."

There is today, quite simply, a conflict about which approach one should take to the formulation of contract law. Article 2B assumes that *parties*, not *statutes* or *courts* form contracts and control their terms. A contrary philosophy takes one into the realm of regulation. It presumes an omnipotence for legislatures and judges that simply ignores the capacity of either of these institutions to manage the myriad of choices that occur in commerce. A regulatory approach has been continuously rejected in the U.C.C.

A regulatory approach is particularly inappropriate in cyberspace and the commercial environment that it creates. In a recent paper dealing with electronic commerce, the White House listed contract freedom as a primary principle for electronic commerce. The report states the following:

20. U.C.C. § 2A-101 (1990).

21. Grant Gilmore, *On the Difficulties of Codifying Commercial Law*, 57 YALE L. J. 1341 (1957).

22. See Randy E. Barnett, *The Sound of Silence: Default Rules and Contractual Consent*, 78 VA. L. REV. 821 (1992); Ian Ayres & Robert Gertner, *Strategic Contractual Inefficiency and the Optimal Choice of Legal Rules*, 101 YALE L.J. 729, 734 (1992).

Parties should be able to enter into legitimate agreements to buy and sell products and services across the Internet with minimal government involvement or intervention. Unnecessary regulation . . . will distort development of the electronic marketplace . . . Business models must evolve rapidly to keep pace with the break-neck speed of change in the technology; governmental attempts to regulate are likely to be outmoded by the time they are finally enacted. Accordingly, governments should refrain from imposing new and unnecessary regulations . . . on commercial activities that take place via the Internet.²³

Although the project began long before the White House Report was issued, Article 2B embraces that same premise. Contract choice, rather than regulation, must govern in this new sphere of commercial activity.

2. *Contract Freedom and Standard Forms*

Contract freedom serves as a fundamental cornerstone of contract law. The idea of contract freedom, however, does not assume that each party separately negotiates each term of each transaction that does not routinely happen in any area of commercial or consumer contract practice, including in contracts between fully competent and successful businesses. The insight of one court on this issue is instructive:

Ours is not a bazaar economy in which the terms of every transaction, or even of most transactions, are individually dickered; even when they are, standard clauses are commonly incorporated in the final contract, without separate negotiation of each of them. Form contracts, and standard clauses . . . enable enormous savings in transaction costs, and the abuses to which they occasionally give rise can be controlled without altering traditional doctrines, provided those doctrines are interpreted flexibly, realistically.²⁴

This recognizes the reality of modern commerce, both in consumer and non-consumer transactions. Given that reality, the fact that a writing that records a contract consists of a standard form presented to another party without opportunity to barter about the terms cannot be said to be per se suspect in any context that recognizes that the function of contract law is to support reasonable commerce, not to regulate commerce to fit the objectives of particular interest groups.

This is not a setting to fully discuss the question of contract choice and autonomy in a contract world where standard forms and standardized bargains predominate. I confine myself to two factual observations. The first deals with the view stated by some that a form contract in some settings is unenforceable because it constitutes an "adhesion" contract. This viewpoint simply misreads generations of contract law. The idea of

23. U.S. WHITE HOUSE REPORT, "A FRAMEWORK FOR GLOBAL ELECTRONIC COMMERCE" (July 1, 1997).

24. *Northwestern National Insurance Co. v. Donovan*, 916 F.2d 372 (7th Cir. 1990).

an adhesion contract as a special subject matter that arises in commerce has been with us for decades. Courts across the country routinely enforce adhesion contracts. Indeed, there are very few and mostly superficial judicial rulings that imply or hold to the contrary.²⁵ By and large, adhesion contracts presented by shipping companies, car rental companies, insurance companies, automobile sales companies, airline ticket issuers, cruise ship companies, and myriad other companies are enforced when issues arise in court.

When used in a reported opinion, the idea of an “adhesion” contract does not equate to all uses of standard forms presented without an opportunity to negotiate terms. It refers to situations involving a complete lack of choice and a lack of sophistication or economic power on one side. For those contracts, courts will often more closely scrutinize the meaning of these standard forms, but seldom question whether the contract itself is enforceable. Even the *Restatement (Second) of Contracts*, an academic exposition of contract law rather than an actual restatement of existing law, acknowledges this.²⁶ That pattern of enforcement recognizes, in a very explicit way, that standard forms and standard presentations of products into a market are acceptable, even vital ways of doing business, even when they entail no actual choice in a marketplace, except the choice simply to not purchase or license the applicable product.

This leads to a second factual observation that pertains to why enforcement of adhesion and other standard form contracts is the dominant approach. Simply stated, a decision or rule that invalidates a standard form or even a term in a standard form works in two directions. While it may protect the ability of the recipient to choose terms, after the fact, it invalidates the ability of the provider to define its product or service commitment; to choose the terms on which it markets product or services. The one effect arguably protects one individual; the second effect denies marketing choices and invalidates autonomy for the other party.

Assume that a court decides that it will enforce a written form contract only if it believes that the terms were, in its view, “fair.” Assume further that a provider of information distributed the information via a standard form stating that there were no assurances that the data were

25. *Vault Corp. v. Quaid Software Ltd.*, 847 F. 2d 255 (5th Cir. 1988). Interestingly, one of the few decisions to hold otherwise occurred at the District Court level in a computer software case. In *Vault*, a Louisiana District Court concluded, with essentially no discussion and no citation of authority, that a software mass market license would be an *invalid* contract of adhesion, had it not been in that case for a special authorizing statute. The court, and later the Fifth Circuit, went on to conclude that the statute was preempted by federal law for creating rights where none would have otherwise existed. The Fifth Circuit did not reconsider or discuss the lower court's summary conclusion on the enforceability question.

26. RESTATEMENT (SECOND) OF CONTRACTS § 211 (1982).

correct. What is the effect of a court determining that this condition was "unfair?" The result, of course, benefits the recipient by presumably giving it a cause of action, but it denies the provider the right to define its own product or risk. In essence, the ability of a court to apply this result means that no vendor can provide information unless it guarantees accuracy; few books or newspapers meet that standard. That rule, if ever adopted, would have a great and chilling impact.

One result of the recognition that regulation improperly denies autonomy in marketing and contracting is that most decisions placing restrictions on adhesive and other standard form contracts in this country, do so on a case by case basis where some definable form of over-reaching occurred. By and large, in general contract law, this arises under doctrines of unconscionability, duress, and fraud. Decisions under these doctrines are mirrored as to particular types of clauses by court-made doctrines in situations involving, for example, ideas of copyright or patent misuse²⁷ and in judge-made decisions involving restrictions on "choice of forum" clauses in contracts if the clause is "unjust and unreasonable."

This is the realm of common law scrutiny to avoid abuse. It is not to sustain a call for detailed regulation or for doctrines that make contract choices inherently uncertain of ultimate enforcement in court. Article 2B expressly preserves the general concepts that courts sometimes employ for this over-view function, but goes no further to intrude on contract choices.

3. *Property Law Overlay*

Article 2B is not an intellectual property licensing law. It is an information licensing statute. The distinction is important. Some, but not all, of the information transactions in which the subject matter comes under Article 2B involve subject matter that falls under traditional intellectual property law. Many of the licenses governed by Article 2B are based on rights and on contractually adequate consideration, premised on control of resources, willingness to transfer assets, and other insights or advantages that the one party holds which the other party does not.

Nonetheless, there is an interaction of state contract law and federal property law. That interaction differs from the property-contract interaction for other commercial contracts.

Even with respect to information and assets governed by intellectual property law, Article 2B does not create a contract law applicable to these resources. It clarifies and codifies aspects of that law. Article 2B

27. *See, e.g., DSC Communications Corp. v. DGI Technologies, Inc.*, 81 F.3d 597 (5th Cir. 1996) (court denied a preliminary injunction suggesting that party might prevail on a misuse defense).

does not create contract as an option for transactions in information. For generations, owners and possessors of information have contracted for selective distribution of these assets. They have done so with agreements that limit use by the licensee because that type of limitation is essential to maintaining the asset as a viable commercial resource.

Licensing law today consists of contract practice that entails a myriad of contract relationships, but also a myriad of conflicting or at least inconsistent contract law doctrines. Article 2B clarifies and integrates these various sources of law, many of which are not fully understood even by the persons who actively practice in this field.

The relationship between contract and property law here involves some controversy, which Article 2B does not resolve. Federal copyright (property) law preempts any state law that creates rights equivalent to the property rights created under copyright.²⁸ But as both a practical and a conceptual matter, copyright does not preempt contract law.²⁹ A contract defines rights between *parties* to the agreement, while a property right creates rights against *all the world*. They are not equivalent, but have coexisted for as long as intellectual property rights have been recognized. Contracts and contract law are not generally preempted by copyright law.

Rather than preemption, in fact, the better view of the relationship between the two bodies of law is that intellectual property rules set out background or default provisions which shape the relationship of parties unless a contract otherwise provides. This being said, in specific provisions, intellectual property law does restrict contract choices through explicit federal enactment. Thus, for example, a fundamental premise in property law is that possession of a copy does not in itself give the possessor full rights to use that copy in any way it pleases. The purchaser of a book cannot reprint the work or resell rights in the work to commercial parties who will use the transfer as a means of commercial exploitation of the work itself. Copyright remains in the owner of the intangible rights and these preclude the following: the making of additional copies; public performances of the work; rental (in the case of software); and many forms of modification. In contrast to your unhindered rights in the toaster you own, an end user's rights in a copy are limited and circumscribed.³⁰

In addition, intellectual property law places limited, specific limits

28. 17 U.S.C. § 301 (1990).

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

30. Of course, most of us do not contemplate making additional copies of the toaster or modifying its performance. The same cannot be said for digital products. Loading the product into one or more computers makes additional copies. See *MAI Sys. Corp. v. Peak Computer, Inc.*, 991 F.2d 511 (9th Cir. 1993). Modification of the software is not that unusual. Of course, 17 U.S.C. § 117, reflects the nature of the environment and grants the "owner" of

on contract freedom. These include restrictions on transferability,³¹ recording requirements,³² a statute of frauds,³³ and a rule allowing enforceability of property rights against good faith purchasers.³⁴ A state law *cannot* ignore these specific rules. This interaction of state law and specific federal yields default rules that, in some cases, do not correspond to the treatment of analogous issues in other parts of the U.C.C.

PART III

A. BASIC DEFAULT RULES

Dealing with a less complex world of commerce, the image is that the drafters of Article 2 formulated purely general rules of broad applicability not tied to industry practices, despite a wide industry divergence, such as heavy equipment manufacturers, producers of oil and gas, consumer products, and many other aspects of commerce.

That image of truly general rules is disingenuous. However, it has survived for over forty years. Part of why it survives lies in the U.C.C. definition of an "agreement." Article 1-201 defines "agreement" as the bargain of the parties "in fact."³⁵ This produces a commercially important premise through which all of Article 2 flows. That premise is that, if one can discern from the words, conduct or context, a bargain in fact as to a particular issue, that bargain controls: point stated and issue closed. The statutory default rules become irrelevant. That being the case, trade practices in each industry dominate simply because a court can conclude that those trade practices frame the agreement, rather than the abstract default rules of the statute. In effect, the idea of "agreement" and its dominating effect constitutes the single most important default rule in Article 2.

Indeed, there are many rules in Article 2 that are specific to particular industries and industry practices: the drafters of Article 2 did not ignore divergence in commerce and did not fail to address at least some industry-specific issues. The rules include the following: (1) the rule on

a copy some limited rights to do the foregoing in the absence of a contrary contractual arrangement.

31. See *Everex Systems, Inc. v. Cadtrak Corp.*, 89 F.3d 673 (9th Cir. 1996).

32. Compare *Broadcast Music Inc. v. Hirsch*, 41 U.S.P.Q. 2d 1373 (9th Cir. 1997); *Yount v. Acuff Rose-Opryland*, 103 F.3d 830 (9th Cir. 1996) (copyright law does not govern royalty arrangements after assignment of copyrights has been effected).

33. 17 U.S.C. § 204 (1990). Copyright law requires a written agreement for an enforceable transfer of a copyright. 35 U.S.C. § 261 (1990). A similar rule applies for patents. 35 U.S.C. § 261. A transfer of property rights occurs when there is an "assignment" or an "exclusive license."

34. See *Microsoft Corp. v. Harmony Computers & Electronics, Inc.*, 846 F. Supp. 208 (E.D.N.Y. 1994).

35. U.C.C. § 1-201(1) (1990).

firm offers (an issue seldom present outside construction-related contracts; (2) the rule on requirements and output contracts (an issue not found in most areas of goods commerce); (3) the rules on "shipment terms" (an issue that assumes the remote transport of tangible items); (4) the rule on sale or return agreements; (5) the rules on consignments; and 6) the rules on auctions.

The Article 2 tradition *in fact* rests on four elements. The first requires that a decision maker focuses on what, in context, the "agreement" meant and to allow that agreement to control. Article 2B follows that premise.

The second defines most default rules in a way that makes them acceptable (even though not optimal) to myriad areas of diverse practice. Article 2B follows that premise.

The third enacts some provisions that reflect specific industry practices. Article 2B *does not* broadly adopt that approach. These are converging industries whose legal framework insofar as contract law pertains is and will be uniform.

The fourth rejects standards that broadly allow courts to invalidate actual agreements other than under common law traditional doctrine augmented by the doctrine of unconscionability. Article 2B follows that premise.

Article 2B follows the traditions of Article 2. It adapts those traditions to the different subject matter, transactional themes, and commercial demands of an information economy. To see some of these themes, we can look at four different contexts: (1) electronic commerce issues; (2) "general license" issues; (3) informational content as a subject matter; and (4) the "mass market paradigm."

B. ELECTRONIC AND ONLINE COMMERCE

Article 2B deals with on-line and electronic contracts. Indeed, Article 2B provides a template for the rest of the U.C.C. and will either be replicated in other articles or moved to a general part of the Code.³⁶ The field of electronic contracting involves three primary themes: (1) the mechanics of contract creation, (2) the substantive terms and how the parties can modify those terms via electronic contacts, and (3) what law and jurisdiction applies.

36. A United States governmental report endorsed this aspect of the project. See INTELLECTUAL PROPERTY AND THE NATIONAL INFORMATION INFRASTRUCTURE, THE REPORT OF THE WORKING GROUP ON INTELLECTUAL PROPERTY RIGHTS 58 (1996) ("[The] challenge for commercial law . . . is to adapt to the reality of the NII by providing clear guidance as to the rights and responsibilities of those using the NII. Without certainty in electronic contracting, the NII will not fulfill its commercial potential.").

1. *Mechanics of Electronic Contracting*

Modern computer contract formation issues entail both relatively tame mechanical issues and deeply philosophical questions. The fundamental policy choice in Article 2B holds that, in modern society, contracts created and documented in digital systems must be enforceable; this means of communication and record keeping are the dominant forms of communication.

At the mechanical level, the relevant issues focus on the extent to which digital records or machine operations satisfy traditional concepts about writings, signature, notice and conspicuousness. The question is not whether there should be a rough legal equivalence between digital operations and older concepts from a paper world. The basic thrust of Article 2B has been to focus on when and in what form the equivalence arises.

a. *Records*

For example, consistent with other U.C.C. revisions, Article 2B replaces the concept of a writing with the concept of a record, a term defined in a manner analogous to the Copyright Act definition of "copy" and formulated in sufficiently broad terms as to encompass all types of electronic records.³⁷ Having made the basic shift, however, Article 2B does not deal with the evidentiary problems created by a transition from paper to electronic records. These include potentially difficult questions of proof in court since a digital record entails a potentially seamless risk of modification. The evidence problems must be worked out in a forum where evidence law is fully developed.

b. *Signatures*

A more difficult transition deals with signatures. At one level, no barrier exists to transporting the U.C.C. definition of signature to the electronic world. Under current law, a signature occurs whenever one adopts a symbol with the intent to authenticate a writing or record.³⁸ Typing a name or adopting an image electronically comes within this concept.³⁹ The difficulties arise, however, when attempts to cope with

37. U.C.C. § 2B-102 (Proposed Draft, Sept. 25, 1997). *See also* 17 U.S.C. § 101 (1997). Article 2B also contains a separate definition of a "copy" since, at least in current technology, transfers of copies are an important method of distributing information.

38. U.C.C. § 1-201 (1990).

39. State law definitions of signature in other contexts are not uniformly as permissive as this broad concept. *See, e.g.,* *Parma Tile Mosaic & Marble Co. v. Short*, 663 N.E.2d 633 (N.Y. 1996) (concluding that "the automatic imprinting, by a fax machine, of the sender's name at the top of each page transmitted" did not constitute a signature under the New York State Statute of Frauds).

practical issues about reliability and proof use encryption and other techniques to create greater assurance about who signed a record and what that record contained. Encryption is a process and does not necessarily entail adopting any symbol; other forms of assurance in digital media similarly do not rely on anything equivalent to a symbol.

Two distinct issues arise. The first focuses on adequacy in law, while the second deals with reliability in law and fact. A number of states have adopted electronic signature laws that deal with adequacy.⁴⁰ Article 2B also expressly establishes the adequacy of electronic authentication, whether in the form of a signature or encryption. To reflect substantive differences, the current draft changes terminology, replacing the word "signature" with the word "authentication."⁴¹ The concept does not hinge on any particular technology. As urged by a recent White House Report on electronic commerce, the approach widely embraces all forms of technological authentication.⁴²

While establishing legal adequacy is important, markets are likely to demand enhanced reliability in law and fact. While even if typing my name on an e-mail constitutes a signature, the person receiving the e-mail is not likely to rely on that for a significant transaction; in the anonymous world of electronic commerce, no way exists to document that the typing was by me or by an unauthorized party. In other settings, other indicia of reliability adequately support reliance, but those indicia are often lacking in the open world of anonymous electronic commerce.

Reliability in fact ultimately hinges on practical considerations, but laws contribute to the reliability quotient. Several states have enacted "digital signature" laws aimed at enhanced legal (and practical) reliability for certain types of electronic signatures.⁴³ The statutes create a presumption that a message is attributable to the purported sender if a particular public-private key encryption method is used pursuant to certified encryption key issuers. Article 2B deals with reliability, but rejects the single technology and regulatory approach in these digital signature laws. It relies instead on agreement and open technology. If the parties *agree to or adopt* a commercially reasonable method for attributing a record to a party, compliance with that method creates a signature and contributes to making the party attributable with the message.⁴⁴ Article 2B refers to this as an "attribution procedure." Compliance with an attribution procedure constitutes an effective "authentication" and creates a re-

40. See RAYMOND T. NIMMER, INFORMATION LAW 514-4 (1996 & Supp. 1997) (compendium of current legislation).

41. U.C.C. 2B-102(2) (Proposed Draft, Sept. 25, 1997).

42. U.S. WHITE HOUSE REPORT, "A FRAMEWORK FOR GLOBAL ELECTRONIC COMMERCE" (July 1, 1997).

43. See, e.g., Utah Admin. Code Rev. § 54-2-101; Wash. Rev. Code § 101-605 (1996).

44. U.C.C. § 2B-110 (Proposed Draft, June 25, 1997).

buttable presumption that the authentication was made by the person made attributable by the procedure.⁴⁵

c. Loss Allocation

Ultimately, questions of reliability in law deal with loss allocation when signatures or records are tampered with and the wrongdoer is not available to repay loss. Essentially, the legal issue is when is a party responsible for electronic messages purporting to be from it. In current law, there are several different approaches to analogous problems: (1) in the telephone system, a party is responsible for any charges incurred for long distance calls from its equipment, neither fault nor actual authorization are relevant; (2) credit card and electronic funds regulations limit liability for a consumer for unauthorized use of its card or number; (3) in commercial funds transfers, the presence or absence of a "security procedure" conditions loss allocation; (4) in check collections, loss falls on the recipient of a fraudulent instrument unless the party whose signature was forged contributed to the fraud by its negligence.

The issues deal separately with questions about the source of a message and its content. As to source, Article 2B allocates responsibility based first on actual involvement, second on compliance with an agreed attribution procedure, and finally, on a lack of reasonable care contributing to the ability of the wrongdoer being able to effectively falsify the source of the message or performance. Article 2B rejects any rule of liability without proof of fault. It also rejects the regulatory rule that restricts consumer risk for credit cards and funds transfers. That rule, which of course continues to govern loss allocation for tampering with payment systems, is appropriate where the protected party is routinely the less economically resourceful party and the other is typically a deeper pocket that can spread loss among many transactions. It is not viable for an open system, heterogeneous environment. In electronic commerce, the vendor will be a small business or an individual as often as is the licensee.

d. Electronic Agents

A more philosophically interesting question involves legal treatment of cases where one or both parties are represented not by a human agent, but by a computer program designed or programmed to act on behalf of a person or company. Is the interaction of two such agents adequate to create a contract?

The answer must be "yes." In Article 2B, if the agent(s) was selected for that purpose, its operations bind the represented party. This is em-

45. U.C.C. § 2B-111 (Proposed Draft, June 25, 1997).

bodied in the idea of an “electronic agent:” a computer program or similar automated device established to act on behalf of a party. While not an “agent” in traditional senses, the use of programmed surrogates to make contracts, find information, and otherwise interact with computers of other parties is increasingly important in electronic commerce, especially for information assets where no need ever exists for a human being to handle the transaction or its result in a digital world.⁴⁶ Article 2B adopts the view that electronic contracts can be formed without human choices being made to offer and accept a particular transaction and that notice can occur without a human review of the subject matter. If a party creates a situation in which an electronic agent is to act on its behalf, then that party is bound by the actions of the “agent.”⁴⁷

2. *Substantive Terms in Electronic Commerce.*

The substantive terms of a contract in electronic commerce are determined by the agreement of the parties and the default rules applicable to the subject matter of the transaction. A transaction in goods yields different default rules than a transaction in information or services.⁴⁸ In closed relationships, such as electronic trading partner agreements, the issues are identical to traditional contracting; substantive terms are outlined by a written agreement that precedes the electronic transaction.⁴⁹ In open environments such as the Internet, the parties will rely on default rules or create contract terms electronically.

a. *Substantive Default Rules*

Article 2B default rules reflect both the subject matter (information) and the context (electronic contact and performance).⁵⁰ These can be shown in two illustrations.

46. U.C.C. § 2B-102 (Proposed Draft, Sept 25, 1997).

47. U.C.C. § 2B-111 (Proposed Draft, July 25, 1997). In Article 2B, this is a question of “attribution.”

48. Determining when a digital transaction entails goods, as compared to other property is often uncertain. In the United States, many cases hold that, at least in some situations, transactions in digital products involve transactions in goods. See *Coast Ridge Constr. Group, Inc. v. Newcort, Inc.*, 78 F.3d 146 (5th Cir. 1996); *Advent Sys. Ltd. v. Unisys Corp.*, 925 F.2d 670 (3d Cir. 1991); *USM Corp. v. Arthur Little Sys., Inc.*, 546 N.E.2d 888 (Mass. App. Ct. 1989); *Hospital Computer Sys., Inc. v. Staten Island Hosp.*, 788 F. Supp. 1351 (D.N.J. 1992); *In re Amica*, 135 B.R. 534 (Bankr. N.D. Ill. 1992).

49. See Michael S. Baum et al., *The Commercial Use of Electronic Data Interchange: A Report and Model Trading Partner Agreement*, 45 Bus. Law. 1645 (1990).

50. For a variety of reasons, Article 2B failed to create a consensus on allocation of loss in contract law with respect to computer viruses injected by third parties. In September 1997, the Committee determined that, lacking consensus, the issue of viruses should be left to other law.

Access Contracts. One modern commercial format is an "access contract." These contracts establish a right of access by the licensee to an information system of the licensor. The model covers websites, WESTLAW, and America On-line.⁵¹ Article 2B deals with access contracts whose subject matter entails information.⁵² Access contracts are licenses; they grant permission to use a resource controlled by the licensor. This is not an intellectual property license, but a modern application of traditional licenses for use of physical resources.⁵³ Under current law, many of these contracts are viewed as services or information contracts.⁵⁴

Article 2B default rules reflect the reality that access contracts entail two distinct frameworks. In one, access and performance occur at one point in time. There is no on-going relationship. In the other, the license gives the licensee a right to intermittent access at times of its own choosing within the time period of agreed availability. This latter relationship is used by many on-line services. The transaction requires that the subject matter be accessible on a predictable basis. Article 2B states:

[Access] must be available at times and in a manner consistent with: (1) express terms of the agreement; and (2) to the extent not dealt with by the terms of the agreement, in a manner and with a quality that is reasonably consistent with ordinary standards of the business, trade or industry for the particular type of agreement.⁵⁵

Intermittent and occasional failures to have access available do not constitute a breach of contract if they are consistent with the agreement, ordinary standards of the business, or scheduled downtime or reasonable needs for maintenance. This not only reflects common understanding, but tracks the limited case law on point which rejects goods-based ideas of perfect tender and applies service contract concepts of

51. It also covers out-sourcing contracts. *See* Hospital Computer Systems, Inc. v. Staten Island Hospital, 788 F. Supp. 1351 (D.N.J. 1992).

52. Many of these contracts involve more than a two party arrangement, of course, in that the system provider contracts to make available to the licensee services and information developed by third parties. U.C.C. § 2B-102 (Proposed Draft, Sept. 25, 1997) provides that, in an access contract, "as between a provider of services and a customer, the provider of services is the licensor, and as between the provider of services and a provider of content for the service, the content provider is the licensor."

53. *See, e.g.,* Ticketron Ltd. Partnership v. Flip Side, Inc., No. 92-C-0911, 1993 WL 214164 (N.D. Ill. June 17, 1993); Soderholm v. Chicago Nat'l League Ball Club, 587 N.E. 2d 517 (Ill. App. Ct. 1992) (license revocable at will).

54. *See* Reuters Ltd. v. UPI, Inc., 903 F.2d 904 (2d Cir. 1990); Ticketron Ltd. Partnership v. Flip Side, Inc., No. 92-C-0911, 1993 WL 214164 (N.D. Ill. June 17, 1993); Kaplan v. Cablevision of Pennsylvania, Inc., 671 A.2d 716 (Pa. Super. Ct. 1996).

55. U.C.C. § 2B-614(c) (Proposed Draft, July 25, 1997).

reasonableness.⁵⁶

In many access contracts, the client receives the benefit of frequently updated information (in addition to communications and other system capabilities).⁵⁷ Article 2B acknowledges this by providing that the access granted is a right to access "information as modified from time to time," rather than solely as it exists at the outset. Changes made in the content do not breach the contract unless they conflict with an express term of the agreement. Similarly, in most such services, changes in the terms of service occur intermittently. Article 2B generally allows changes in contract terms without consideration and provides a methodology to make the changes which requires notification of the changes to the affected party.⁵⁸

Unless it provides for a fixed term, an access contract is subject to termination at will without notice by either party. In the event of a material breach, the license may be immediately canceled by the aggrieved party.⁵⁹ These rules reflect the conditional nature of the relationship. They give a party important capability. It can end relationships where the licensee may be obtaining or providing infringing or tortious material for which the licensor may be ultimately liable.⁶⁰

There is a distinction between licensed access and use of the information obtained by virtue of access. Article 2B holds that information downloaded by the licensee is not subject to use restrictions unless they are expressly imposed by the contract, by intellectual property, or by other law.⁶¹ On the other hand, an access contract provides a right to access, not necessarily a right to make copies of the information obtained. As a default rule, the client has a right to make temporary copies necessary for viewing or licensed use. The client can make permanent copies only if the agreement so provides. Of course, where a permanent

56. *See* *Reuters Ltd. v. UPI, Inc.*, 903 F.2d 904 (2d Cir. 1990); *Kaplan v. Cablevision of Pennsylvania, Inc.*, 671 A.2d 716 (Pa. Super. Ct. 1996).

57. Where the system involves interactive exchanges between or among various licensees, such as in an e-mail list serve or a chat room, questions frequently arise about the rights of the licensee in information it places into the system. In most systems, the operators seek to obtain releases of intellectual property rights pertaining to this type of material. Article 2B follows current law in most states and makes such releases enforceable without consideration if the party assents to a record providing for the release. U.C.C. § 2B-207 (Proposed Draft, July 25, 1997). Assent requires an opportunity to review the terms, that the terms be called to the party's attention, and that there be an affirmative act indicating assent.

58. U.C.C. § 2B-304 (Proposed Draft, July 25, 1997).

59. U.C.C. § 2B-714 (Proposed Draft, July 25, 1997).

60. *See* *Ticketron Ltd. Partnership v. Flip Side, Inc.*, No. 92-C-0911, 1993 WL 214164 (N.D. Ill. June 17, 1993); *Hospital Computer Systems, Inc. v. Staten Island Hospital*, 788 F. Supp. 1351 (D.N.J. 1992).

61. U.C.C. § 2B-614(b) (Proposed Draft, July 25, 1997).

copy is the only way to make use of the information as intended by the parties, that defines the agreement.

b. Choice of Law

Choice of law rules are in disarray. One leading text on choice of law comments: “[C]hoice-of-law theory today is in considerable disarray—and has been for some time. [It] is marked by eclecticism and even eccentricity. No consensus exists . . . [f]our or five theories are in vogue among the various states, with many decisions using—openly or covertly—more than one theory.”⁶² That is not a framework within which electronic commerce can thrive.

Litigation rules do not support commerce. Article 2B provides a stable choice of law for electronic commerce that allows even a small vendor and small purchaser to discern what law covers their electronic commerce. Article 2B proposes choice of law rules that correspond to the Second Restatement and also provides clear guidance for persons doing business on Internet. In Internet transactions, Article 2B holds that choice of law is the location of the licensor. This concept has been extensively discussed. Where an on-line licensor provides information to the world, any other default rule formulation would require the licensor to comply with the law of all states and over 170 countries. Opting for a more stable, identifiable source of underlying law is an important step toward facilitating electronic commerce. This rule is subject to conflicting consumer and other regulations. Furthermore, Article 2B adopts the approach of the Restatement (Second) test.⁶³

3. Contracting for Terms

Article 2B affirms freedom of contract. Parties should be free to define under what terms they market their information or services and parties acquiring those services should be free to elect to take or not take the product, or if possible, to negotiate terms. Commerce functions best without regulation. In electronic commerce, the contract issue entails how contract terms can be created.

62. WILLIAM RICHMAN & WILLIAM REYNOLDS, UNDERSTANDING CONFLICT OF LAWS 241 (2d ed. 1992).

63. RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 6, 188. *The factors include:* (a) the place of contracting; (b) the place of negotiation of the contract; (c) the place of performance; (d) the location of the subject matter of the contract; (e) the domicile, residence, nationality, place of incorporation and place of business of the parties; (f) the needs of the interstate and international systems; (g) the relevant policies of the forum; (h) the relevant policies of other interested states and the relative interests of those states in the determination of the particular issue; (i) the protection of justified expectations; (j) the basic policies underlying the particular field of law; (k) certainty, predictability and uniformity of result; and (l) ease in the determination and application of the law to be applied.

a. *General Issues*

Article 2B follows current law to the effect that a party adopts the terms of a record if the party agrees to the record or manifests assent to that record.

“Manifesting assent” is a key to electronic commerce. The idea of adopting terms by manifesting assent comes from the *Restatement (Second) of Contracts* § 211 and is substantially elaborated on in Article 2B.⁶⁴ Manifesting assent requires two events. The first is an affirmative act (including a signature) that the circumstances clearly indicate constitutes adoption of a record. The second is that the affirmative act must occur after the party had an opportunity to review the record (or contract) to which it assents. This sets out a procedure for establishing terms of a contract. For there to have been an opportunity to review a record, the record must have been called to the party’s attention (not hidden in the process) and have been readily available for review (not difficult to access).

b. *Choice of Law and Forum*

The idea of contract freedom carries over to contract terms regarding choice of law and choice of forum. A White House Report and recent case law underscore that a crucial issue in electronic commerce involves determining what law and what forum governs.⁶⁵ The White House Report comments:

The expansion of global electronic commerce also depends upon the participants’ ability to achieve a reasonable degree of certainty regarding their exposure to liability Inconsistent local . . . laws, coupled with uncertainties regarding jurisdiction, could substantially increase litigation and create unnecessary costs that ultimately will be born by consumers. The United States should work . . . to clarify applicable jurisdictional rules and to generally favor and enforce contract provisions that allow parties to select substantive rules governing liability.⁶⁶

64. U.C.C. § 2B-112 (Proposed Draft, July 25, 1997).

65. RAYMOND T. NIMMER, INFORMATION LAW ¶ 1.06 (1996). See also *Compuserve, Inc. v. Patterson*, 89 F.3d 1257 (6th Cir. 1996); *Panavision Int’l, L.P. v. Toepfen*, 938 F. Supp. 616 (C.D. Cal. 1996) (Internet use did not create California general jurisdiction over Illinois resident; contacts were not “substantial, systematic, or continuous”); *McDonough v. Fallon McElligot, Inc.*, 40 U.S.P.Q.2d (BNA) 1826 (S.D. Cal. 1996) (“allowing computer interaction via the web to supply sufficient contacts to establish jurisdiction would eviscerate the personal jurisdiction requirement as it currently exists”); *Banco Nacional Ultramarino, S.A. v. Chan*, 641 N.Y.S.2d 1006 (N.Y. Sup. Ct. 1996); *Bensusan Restaurant Corp. v. King*, 937 F. Supp. 295 (S.D.N.Y. 1996); *Inset Systems, Inc. v. Instruction Set, Inc.*, 937 F. Supp. 161 (D. Conn. 1996).

66. U.S. WHITE HOUSE REPORT, “A FRAMEWORK FOR GLOBAL ELECTRONIC COMMERCE” (July, 1997).

The Internet is a new commercial environment. It presents the first situation where even persons with limited resources immediately access a national and international market. Participants in Internet commerce, even the smallest entrepreneurs, are faced with the risk that, without leaving their homes and without advertising or aiming their product at a particular state, they are subject to the laws and the jurisdiction, of all fifty states in the United States and all countries in the world. Compliance with all laws is impossible even for large companies. "[The] business operator [must] be able to structure [its] primary conduct with some minimum assurance as to where the conduct will and will not render [it] liable to suit."⁶⁷ The problems extend to both jurisdiction and choice of law. Article 2B addresses this problem as it applies to contract law. A person setting out an Internet site should ask: with which laws must I comply in my contractual arrangements? If the answer is difficult or refers that person to the law of all states and all countries, law imposes a great burden on commerce or becomes irrelevant because it cannot be complied with.

Article 2B allows the contract to control. This reflects the theme of Article 2B. In choice of forum, this reflects an increasingly dominant position in case law. Prior to the early 1970's, choice of forum clauses were looked on with disfavor. Since then, however, case law has shifted, treating contract as a form of consent to jurisdiction and enforcing contract clauses that arise from agreements, even if the agreements are unbargained and reflect standard form contract terms.⁶⁸ Of course, this pattern does not over-ride state consumer protections and does not repeal the Due Process clause. Article 2B is subject to these limitations. In addition, it enacts a protection rule: the choice of forum is not enforceable if the consumer is not otherwise subject to the selected jurisdiction and the choice creates an unreasonable and unjust result.⁶⁹

In supporting a choice of exclusive forum clause in reference to maritime cruise tickets, the Supreme Court noted:

[A] cruise passenger [cannot] negotiate the terms of a forum clause in a routine commercial cruise ticket form. Nevertheless . . . a reasonable forum clause [is] permissible for several reasons. Because . . . a mishap in a cruise could subject a cruise line to litigation in several different fora, the line has a special interest in limiting such fora. Moreover, a

67. *Compuserve, Inc. v. Patterson*, 89 F.3d 1257 (6th Cir. 1996).

68. See *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585 (1991); *The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972) (Court enforces clause in a maritime contract that all disputes were to be adjudicated in the United Kingdom); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506 (1974) (enforcing choice of forum in Paris); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 631 (1985) ("strong presumption" in favor of contractual choice-of-forum provisions).

69. See *Carnival*, 499 U.S. at 587 (choice of forum enforced even though cruise line trip purchaser could not defend in that environment).

clause establishing [the forum] has the salutary effect of dispelling confusion as to where suits may be brought . . . [P]assengers purchasing tickets containing a forum clause . . . benefit in the form of reduced fares reflecting the savings that the cruise line enjoys.⁷⁰

The Court's comments have relevance to Internet contracting where exposure to multiple jurisdictions and potentially multinational liability exposure is even more pronounced and applicable to far smaller commercial entities.

In choice of law, case law favoring contract choice is even more apparent. Common law generally enforces contractual choice of law.⁷¹ The major exception occurs where the choice contradicts the basic policy of the state that would otherwise have its law apply, but the *Restatement (Second) of Conflicts* allows choice of law terms to govern in any case (including consumer contracts) where the issue could be resolved by contract. Even if contract rules might not otherwise govern, under the Restatement, the contract choice is presumed to be valid, subject to limited exceptions.⁷² Current U.C.C. § 1-105 allows a choice of law clause only if the chosen state has a "reasonable relationship" to the transaction. This rule reflects law that existed when the U.C.C. was adopted five decades ago, but that has little merit in modern transactions. Article 2B rejects it.

C. GENERAL OR ORDINARY LICENSES

Article 2B applies concepts of contractual freedom to ordinary licenses to the same extent as it does to Internet contracts. In this, Article 2B follows the traditions of *existing* Article 2 and rejects efforts to regulate contract.

The basic obligation of both parties is to conform to the contract, that is, the enforceable agreement.⁷³ The general default rule states: "If the performance required of a party is not fixed or determinable from the terms of the agreement or this article, the agreement requires performance that is reasonable in light of the commercial circumstances." This formulation makes default concepts subordinate to agreed terms. Addi-

70. *Carnival*, 499 U.S. at 587.

71. See, e.g., *Finch v. Hughes Aircraft Co.*, 469 A.2d 867, 887 (Md. Ct. Spec. App. 1984) (patent license); *Medtronic Inc. v. Janss*, 729 F.2d 1395 (11th Cir. 1984); *Universal Gym Equipment, Inc. v. Atlantic Health & Fitness Products*, 229 U.S.P.Q. (BNA) 335 (D. Md. 1985); *Northeast Data Sys., Inc. v. McDonnell Douglas Computer Sys. Co.*, 986 F.2d 607 (1st Cir. 1993).

72. RESTATEMENT (SECOND) OF CONFLICTS § 187 (invalid only if not resolvable by contract *and* either there was no "reasonable basis" for the choice of that state's law, or "application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of the particular issue . . .").

73. U.C.C. § 2B-601(a) (Proposed Draft, Sept. 25, 1997).

tionally, it refers to *commercial* circumstances, grounding a court's analysis in the commercial relationship, rather than in abstract theories of how commerce *should* unfold.

As to general licensing, a variety of transactional frameworks exist. Rather than provide a detailed precise of the various frameworks that exist today, Article 2B follows the lead of Article 2 in building default rules around a relatively simple transaction as a model, emphasizing the general agreement of the parties controls.⁷⁴ More to the point, in ordinary licensing, Article 2B relies extensively on Article 2 and Article 2A law, making substantive changes in default assumptions only when subject matter and transactional differences compel change.

The basic model is a single simultaneous user or use (e.g., performance or display) license.⁷⁵ This is the most common license although, of course, many commercial licenses entail far different grants. There is no way to gauge which framework is more common, but the basic judgment is to use the least complex structure possible. Where more is intended, the "agreement" controls.⁷⁶

The basic model further assumes that the license deals with information as it exists when the "activation of rights," that is the start up, of the license, occurred. Unless the agreement or intellectual property law provide otherwise, neither party is entitled to rights in improvements or modifications made by the other party, or to receive source code, schematics, or other design material. Again, while many licenses do convey source materials, the model assumes the least complex transaction. In this area also, the assumption corresponds to general intellectual property law concepts that do not presume broad grants giving away intellectual property rights unless the contract calls for such a grant.

Article 2B also follows intellectual property law distinguishing transactional issues pertaining to the copy of the information and to the rights in the work represented in the copy. Transfer of a *copy* of information does not in itself transfer ownership of intellectual property rights

74. Thus, for example, many, but not all current Article 2 default rules relate to a fundamental model that assumes a single delivery transaction that, in most instances, occurs between parties dealing directly with each other or through a carrier. This is true even though Article 2 applies to a very wide range of transactions, including very sophisticated and complex development and on-going relationships.

75. U.C.C. § 2B-307 (Proposed Draft, Sept. 25, 1997).

76. It is important to recognize here that throughout the U.C.C., the idea of "agreement" is not confined to the commercial concept of the "written agreement." "Agreement" refers to the entire bargain of the parties in fact. "Contract" likewise goes beyond the "written contract" at least in many cases and refers to that portion of the "agreement" that is enforceable in law. Both terms are defined in U.C.C. § 1-201(3)(11). Because of their more expansive connotations, for example, agreement encompasses trade use, course of dealing, course of performance, and various other informal elements of the deal.

in the information.⁷⁷ Title to intellectual property, of course, sometimes passes in a contract. When this is intended, title passes when the “information has been so far identified to the contract as to be distinguishable in fact from similar property even if it has not been fully completed and any required delivery has not yet occurred.” This moves the point of ownership forward to protect the transferee. It solves the problem in *In re Amica*,⁷⁸ where the court applied Article 2 theories to hold that title to a computer program being developed for a client could not pass until the program was completed *and* delivered. The transfer of title hinges on completion to a sufficient level that separates the transferred property from other property of the transferor.⁷⁹

License agreements vary about the placement of title to any copy of the information and often are silent on the issue. Under Article 2B, title to a copy is determined by the agreement, but regardless of placement of title, the right to use or control the copy is governed by the contract.⁸⁰ If there is an intent to transfer title of a copy, title transfers on physical delivery of a tangible copy, but transfers on electronic delivery of a copy only when a first sale occurs under federal copyright law.

Within this simple model, Article 2B makes a further distinction among commercial licenses and “mass market” licenses. Putting that issue aside, for further understanding the general default rules applicable to general licenses, we can focus on four issues: (1) grant and contract interpretation rules; (2) electronics default rules; (3) performance default rules; and (4) transferability.

1. *Interpretation Rules*

Ultimately, in cases of dispute, courts must interpret and enforce the contract of the parties. How they generally do so entails application of various contract interpretation principles. Beyond litigation, however, for a transactional lawyer, the primary issue focuses on “what language will achieve the result that the parties intend?” Article 2B provides important guidance on both questions.

77. U.C.C. § 2B-501 (Proposed Draft, Sept. 25, 1997)

78. *In re Amica*, 135 B.R. 534 (Bankr. N.D. Ill. 1992).

79. See *In re Bedford Computer*, 62 B.R. 555 (Bankr. D.N.H. 1986) (disallows transfer of title in software where “new” code could not be separately identified from old or pre-existing code).

80. U.C.C. § 2B-501 (Proposed Draft, Sept. 25, 1997). Article 2 and 2A differ on title issues, reflecting the differences in the transaction that is involved. In Article 2, passage of title to the buyer is presumed to occur on delivery of the copy. Reservation of title merely reserves a security interest. Thus, all Article 2 transactions, including fully commercial software licenses, are arguably “first sales” under Article 2. Article 2A, on the other hand, assumes that title always stays with the lessor, regardless of delivery. Neither assumption fits with licensing practice and neither is adopted in Article 2B.

As a basic principle, Article 2B holds that a license grants "all rights expressly described and all rights within the licensor's control during the duration of the license which are necessary to use the rights expressly granted in the ordinary course in the manner anticipated by the parties at the time of the agreement." The affirmative coverage of rights necessary to granted uses expands so-called implied license law. Under current law, some courts infer a limited implied right consistent with the grant, but others do not.⁸¹ This provision gives a stronger expectation right to licensees present in all cases.

Article 2B in several situations spells out "safe harbor" or "exemplary" language that, by statutory definition, links to certain defined results. These include:

- interpretation of demands for acknowledgment of electronic messages
- language granting current and future media and applications
- interpretation of the term "quit claim" license
- interpretation of a reference to the "sole discretion" of a party
- language adequate to disclaim warranties
- interpretation of "as is"
- interpretation of language of "rescission" or the like.

2. *Electronic Default Rules*

Because modern licenses frequently involve digital technology, a statute dealing with any transaction in the modern economy must consider performance issues involved using digital systems to enforce contractual obligations. Article 2B focuses on two questions.⁸²

The first deals with electronic regulation of performance.⁸³ Here, Article 2B recognizes a party's right to include devices in digital information that constrain uses by the other party to the terms of the contract. Thus, for example, the provider of software through Java applettes can include code that erases the applette on the expiration of its licensed use, while the provider of shareware can disable the shareware thirty days

81. See *MacLean Assoc., Inc. v. William M. Mercer-Meidinger-Hansen, Inc.*, 952 F.2d 769 (3d Cir. 1991) (clients, even if misled by a consultant holding himself out as an employee, receive no ownership rights, but may receive an implied license to use the software). A parallel rule is adopted for development contracts where the terms of the contract do not adequately convey ownership to a client even though the parties' agreement intended the ownership to transfer. See U.C.C. § 2B-616(a) (Proposed Draft, Sept. 25, 1997).

82. Prior drafts of Article 2B attempted to delineate rights related to third party viruses injected into a contract relationship. The provisions dealing with this question were deleted in September 1997, based on the conclusion that no consensus could be achieved in light of conflicting positions of participants in the process. Also, while viruses have been a major issue in other contexts, no reported cases deal with the question in a contract environment.

83. U.C.C. § 2B-310 (Proposed Draft, Sept. 25, 1997).

after delivery if that reflects the terms of its agreement. A licensor of a single user license can include code that precludes a second simultaneous user. Where the code merely prevents a breach or acts to implement a short term termination, no notice is required. In effect, the licensor is merely using technology to enforce its contract terms, much like the technology of a laundromat clothes dryer shuts the machine off when the allocated time of usage is completed. Otherwise, there must be prior notice to the licensee.

The second issue is controversial and the Committee is seeking a consensus position with respect to its terms. This deals with electronic self-help in which digital code allows a licensor to preclude use of information by the licensee through self-help in the event of a breach.⁸⁴ The basic approach of Article 2B, however, has been to allow such right, but to constrain it with substantive limitations, liability risks and notice requirements that are far in excess of the equivalent rights created in Article 9 and Article 2A. Current case law precludes self-help remedies where no notice was given, but otherwise allows them to be used.⁸⁵

3. *Performance Rules*

The basic standard is simple: a party must conform to its contractual promises. For general licenses, Article 2B follows current Article 2 in large part on the assumption that conveyance of a copy of the subject matter of the transaction is an important part of the transaction. In licensing and information transactions, however, actual conveyance of a tangible copy is only one means of making the transaction occur—rights can be created and exercised with no transfer of any copy or with an electronic message. Given that distinction, Article 2B adopts a number of basic principles that include:

- licensor must complete the steps to make possible use of rights
- rules generally equivalent to tender of delivery are spelled out
- performance is due at one time if that is commercially reasonable
- payment is not generally due until completion of performance
- acceptance of performance obligates party to pay
- acceptance of performance puts burden of proof of defect on accepting party
- licensor tenders first, but need not complete until licensee tenders its performance
- licensee has right to inspect before accepting
- a party can refuse performance if it is a material breach

84. U.C.C. § 2B-716 (Proposed Draft, Sept. 25, 1997).

85. See *American Computer Trust Leasing v. Jack Farrell Implement Co.*, 763 F. Supp. 1473 (D. Minn. 1991) (remote deactivation was permitted for a breach of payment obligations in a software license).

- in mass market licensee can refuse copy if it fails to conform to contract
- risk of loss as to copy transfers when licensor completes its obligations of delivery.

Article 2B differs from the Article 2 model in two important respects. The first is that, in light of the potential involvement of confidential information or other proprietary rights in a tendered information product, Article 2B does not routinely allow the rejecting licensee to resell or otherwise unilaterally dispose of the copy. Also, and more important, Article 2B expands the licensee's rights in reference to a licensor's right to cure. Cure can only come if it precedes cancellation or refusal. Cancellation based on material breach shifts the balance toward the licensee and allows it to cut off the other party's ability to cure the tendered defect.

4. *Warranties*

Article 2B subject matter and warranties blend three different legal traditions. One stems from the U.C.C. and focuses on the quality of the product. This centers on the *result* delivered: a product that conforms to ordinary standards of performance. The second stems from common law, including cases on licenses, services contracts and information contracts. This focuses on how a contract is performed, the *process* rather than the result. The obligations of the transferor are to perform in a reasonably careful and workmanlike manner. The third comes from the area of contracts dealing with informational content and disallows implied obligations of accuracy that create liability fault or otherwise for information transferred outside of a special relationship of reliance.

Under current law, many of the contracts covered in Article 2B are services (or information) contracts. In many states, these contracts carry no implied warranty. In others, and under *Restatement* law, an implied obligation exists, but does not guaranty an accurate result. It entails an assurance of workmanlike or reasonably careful effort. In transactions in information, tort and contract law implied obligations, when they exist, typically hinge on assurances that no false information is provided as a result of a failure by the provider to exercise reasonable care in a context where the provider supplies information for the business guidance of a particular client.⁸⁶ Case law typically limits this to relationships such as consulting contracts, accountant audits, professional client services, and the like; in the vast majority of reported cases, the obligations do not apply to information products distributed outside such relationship and in a form not tailored to a particular client (e.g., newspaper distribution, books). To reflect the different traditions and the subject matter addressed in Article 2B, several tailored warranty rules are developed.

86. RESTATEMENT (SECOND) OF TORTS § 552 (1989).

Article 2B sets out an implied warranty of merchantability with respect to computer programs distributed in the mass market, applying a standard of substantial conformance to documentation for programs not distributed in the mass market. The merchantability standard follows existing Article 2. It compares the particular program to programs of similar kind and asks whether the program meets ordinary standards for its description. As in Article 2, the warranty can be disclaimed.

For computer programs not in the mass market, there is an implied warranty that the program substantially conforms to its documentation. This corresponds to the most common warranty in commercial licensing. It differs from merchantability in its focus. The warranty focuses on the program's documentation itself for the implied obligation, rather than seeking to discern "ordinary" characteristics in "similar" programs outside the mass market as would be required by a merchantability concept. Besides creating a parallel with modern commercial practice, this warranty reflects the fact that *outside of the mass market* a wide diversity exists in program capabilities and characteristics, even within the same generic type of software. Non-mass-market programs of similar type differ widely in attributes, speed, capacity, and other traits that make comparisons across categories of software uninformative. An "ordinary" data compression program may not exist in this market.

The two standards both give assurances of quality, but focus on different reference points. Merchantability asks what are normal characteristics of ordinary products of this type, while the documentation warranty focuses on the manuals and contours of the particular product. Beside conforming to ordinary commercial practice (e.g., disclaim merchantability and give substantial conformance warranty), the substantive question here deals with whether merchantability is a relevant standard and at all protective in cases where software is often relatively unique. For example, assume a commercial computer program that provides data compression functions on an *ABC* computer with an *XYZ* operating system. Merchantability would ask whether that product passes without objection among all data compression products of all types (e.g., mass market, Windows-based, Apple systems, etc.) even though the particular environment, approach, and capabilities of this product may be unique. How that standard protects the licensee is not clear and in fact it may set out standards well below what the documentation provides.

5. *Material Breach*

A further question arises, however, about to what extent a simple breach of contract in itself enables the other party to refuse the performance and to cancel the contract, leaving the other party without any compensation for value it provided. Article 2B follows the dominant

approach in this country and internationally, which holds that a minor breach entitles the injured party to damages, but only a "material" breach entitles that party to entirely avoid the contract and refuse the party's performance. The *Restatement (Second) of Contracts* § 237 expresses the rule as follows: "[It] is a condition of each party's remaining duties to render performances . . . that there be no uncured material failure by the other party to render any such performance due at an earlier time." The Convention on the International Sale of Goods encapsulates the same principle in a concept of "fundamental breach." Article 25 states: "A breach . . . is fundamental if it results in such detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract, unless the party in breach did not foresee and a reasonable person . . . would not have foreseen such a result."⁸⁷ *UNIDROIT Principles of International Commercial Law* state: "A party may terminate the contract where the failure of the other party to perform an obligation under the contract amounts to a fundamental non-performance."⁸⁸

Article 2B adopts this rule. What constitutes a material breach depends on the context and the terms of the contract. Contract terms can define what is material.⁸⁹

6. *Transferability*

Article 2B presumes that neither party may transfer its interest under the contract if the transfer would make a material, adverse change in the other party's position.⁹⁰ A mass market license is presumed to be transferable as are licenses where the licensee becomes the owner of a copy. As a general rule, a party may delegate its performance unless the contract precludes this or the delegation would create a material adverse impact on the other party's position.⁹¹ Contract restrictions of transfer of a license are enforceable, but cannot prevent the creation

87. *Convention on the International Sale of Goods art. 25.*

88. UNIDROIT art. 7.3.1(1).

89. See U.C.C. § 2B-108(b) (Proposed Draft, July 25, 1997) This can happen in three ways. The first two involve either expressly providing a remedy for a particular breach (e.g., failure to meet "X" test permits cancellation of the contract) or expressly defining a particular breach per se material. The third context involves what, under common law is described as "express conditions." These are express contract terms conformance to which is implicitly or expressly a precondition to the performance of the other party. The nature of the express agreement itself conditions the remedy. The idea does not allow a party to promise performance at one level and deliver less, expecting a court to rewrite the agreement. Thus, despite what some who have not read common law contract cases suggest, express specifications contained in a contract must be performed in full and failure to do so will routinely be treated as a material breach.

90. U.C.C. § 2B-502 (Proposed Draft, July 25, 1997).

91. U.C.C. § 2B-506 (Proposed Draft, July 25, 1997).

(as compared to enforcement) of a security interest.⁹²

Non-exclusive licenses outside the mass market, however, cannot be transferred without the licensor's consent. This rule flows from federal policy and ownership concerns.⁹³ A consistent line of federal court decisions holds that, as a matter of federal policy, a licensee's rights under a non-exclusive license of a copyright or patent cannot be transferred without the consent of the licensor. This was recently confirmed by the Ninth Circuit. The explanation for this rule can be stated in terms of the limited nature of a license. It is also an outgrowth of federal policy allowing a licensor to control to which licensee's its intellectual property rights are conveyed:

Allowing free assignability . . . would undermine the reward that encourages invention because a party seeking to use the patented invention could either seek a license from the patent holder or seek an assignment of an existing patent license from a licensee. In essence, every licensee would become a potential competitor with the licensor-patent holder in the market for licenses under the patents. And while the patent holder could presumably control the absolute number of licenses in existence under a free-assignability regime, it would lose the very important ability to control the identity of its licensees.⁹⁴

Licensed information that is transferred is not second hand property, but identical to the original. This is true not only in pure licenses, but also in licensing digital information. Article 2A, not faced with the over-riding gloss of federal intellectual property policy, recognized a similar right of an owner to control its property, noting that the "lessor is entitled to protect its residual interest in the goods by prohibiting anyone other than the lessee from possessing or using them."⁹⁵

A basic principle is that state law rules should not create a misleading impression by contradicting partially preemptive federal law. The Draft contains provisions that push close to limits in order to accommodate financing by allowing creation and enforcement *against the licensee*, but not sale or control as *against the licensor* without consent of the licensor.⁹⁶

92. U.C.C. § 2B-503 (Proposed Draft, July 25, 1997).

93. See *Everex Systems, Inc. v. Cadtrak Corp.*, 89 F.3d 673 (9th Cir. 1996); *Unarco Indus., Inc. v. Kelley Co., Inc.*, 465 F.2d 1303 (7th Cir. 1972); *Harris v. Emus Records Corp.*, 734 F.2d 1329 (9th Cir. 1984); *In re Alltech Plastics, Inc.*, 71 B.R. 686 (Bankr. W.D. Tenn. 1987).

94. *Everex Systems, Inc. v. Cadtrak Corp.*, 89 F.3d 673 (9th Cir. 1996).

95. U.C.C. § 2A-303, cmt. 3 (1995).

96. See U.C.C. § 2B-504 (Proposed Draft, July 25, 1997).

D. INFORMATIONAL CONTENT

Transactions focused on informational *content* present a special case and are treated as such in Article 2B. "Informational content" refers to information intended to be perceived or understood by the reader, viewer or other human recipient.⁹⁷ Transactions involving content are as far from the subject matter of Article 2 as possible. They are also different from the other forms of licensed information governed by Article 2B. However, they provide a central facet of the information age. Two of the differences are relevant in this overview.

First, in at least some informational content transactions, merely seeing, hearing, experiencing, or understanding the informational content conveys the entire value contemplated by the transaction and that value (whatever it is) cannot be returned. For example, in a contract to obtain a credit report on an individual, the licensee receives all of the value from the transaction by merely learning that there are no adverse credit factors in the report. Once having read that fact, the knowledge cannot be returned or ignored. This calls into question the applicability of Article 2 concepts of inspection and rejection since inspection conveys the entire value an rejection assumes that the value (item) is returned or refused. Equally important, commercial practice and expectations here do not typically incorporate the Article 2 model and no reason exists to superimpose that model on contrary commercial practice.

Second, the subject matter has a special place in the policy and constitutional regimes of this country. Especially for published informational content, our culture associates free availability and unencumbered transfer with the achievement of important social values. We accept that, once set out into the world, information roams freely, whether accurate or not, and that in general, this is a protected event.⁹⁸

1. *Transactional Aspects*

Article 2B contains two sections dealing with transactional elements of informational content contracts. One deals with the application of Article 2 concepts of tender, rejection, and revocation to information industries. Unlike general rules in common law and the Restatement, Article 2 contains an explicit focus and set of events that reflect a particular type of transaction (sale of goods). That framework does not comfortably or appropriately apply to many transactions involving informational content, especially at the upstream levels of the entertainment and publishing sectors. Forcing that model onto that practice would introduce new and undesirable standards. Article 2B solves that problem through a

97. U.C.C. § 2B-102 (Proposed Draft, Sept. 25, 1997).

98. *See, e.g.,* Winter v. G.P. Putnam's Sons, 938 F.2d 1033 (9th Cir. 1991).

concept of "information submissions."⁹⁹ This concept applies to cases involving contracts where the submission is reviewed in terms of aesthetics and market suitability.

For these cases it is a mistake to assume that the initial submission is equivalent to tender of delivery of a product. Rather than requiring immediate acceptance or rejection, submissions of content more often initiate a process of review and revision with a later decision to accept or reject the submission. Article 2B reflects that; it places these transactional situations entirely outside of the tender-acceptance rules, relying heavily on common law themes (as implemented in Article 2B) and trade practice to define the rights of the parties. One consequence is that, in information submission contexts, acceptance does not occur unless and until there is an express indication of acceptance (or rejection) by the licensee. This corresponds to commercial practice in this context.

A second setting in which Article 2 concepts of tender inspection create an uneasy fit with practice in information industries arises with respect to transactions in which, by merely viewing information, the licensee receives all the value of the transaction and because of the nature of the performance, that value *cannot* be returned in the sense that a defective toaster can be returned. This might involve, for example, a Dun and Bradstreet report on a company, a license of a formula for Coca Cola, a credit report, or a screening at home of a pay per view motion picture. In these cases, the idea of a right to reject is not relevant. What is relevant is ensuring that the recipient can recover if the received performance was not consistent with the contract. Forcing an Article 2 framework on these transactions creates a dysfunctional change from common law principles, especially in the Article 2 right to inspect before payment. Inspection in such cases in effect transfers the value and the licensee *cannot* return (a basic requirement of rejection) the value even if it desires to do so.

Article 2B treats such transactions outside the sale of goods framework.¹⁰⁰ It places the transaction under the general rules of 2B-601 which parallel common law; the law currently applicable to such transactions. The common law principle does not describe a right of rejection, but allows one to avoid paying anything for performance that constitutes a material breach or to recover back the full payment previously made and allows recovery of damages for lesser breaches.

2. *Liability and Warranty Issues*

While one can speak about defective products, in dealing with informational content, the critical issues of performance typically relate to

99. U.C.C. § 2B-602 (Proposed Draft, Sept. 25, 1997).

100. U.C.C. § 2B-608 (Proposed Draft, Sept. 25, 1997).

whether the information provided is or is not accurate. However, accuracy per se, has never been subject to an implied warranty in content-based transactions in the sense that one speaks of implied warranties of merchantability which yield potential liability regardless of any fault in causing the defect in the product.¹⁰¹ Rather, reflecting the character of the subject matter, liability for inaccuracy in current law deals with liability based on fault and also reflects a distinction between generally published information and information given from person directly to another.

Informational content is, quite simply, not treated as a product as are toasters, television sets, and automobiles. The *Restatement (Third) of Products Liability* § 19 recognizes this fact and expressly limits the concept of what constitutes a “product” for purposes of that law to “tangible personal property.” This excludes services. As to informational content, the comments to that section note:

Although a tangible media such as a book, itself clearly a product, delivers the information, the plaintiff’s grievance in such cases is with the information, not with the tangible medium. Most courts, expressing concern that imposing strict liability for the dissemination of false and defective information would significantly impinge on free speech have, appropriately, refused to impose strict products liability in these cases.¹⁰²

Strict liability without proof of fault (e.g., negligence, intentional misrepresentation) is not appropriate for this subject matter in tort or contract law. Further more, even with reference to fault-based, courts and the *Restatement* limit the scope of liability in deference to the protected position of published speech.

This Draft proposes a new term: “published information content” to identify content distributed on a general, non-tailored basis outside any special relationship. No implied warranty exists in Article 2B about the aesthetic merit or marketability of information content. These are matters of taste and judgment, not of warranty, unless the parties seek and receive express commitments.

Section 2B-404 creates a warranty that there is no inaccuracy in data caused by the failure of the informational content provider to exercise reasonable care. This establishes a warranty applicable to consulting, data processing, information content, and similar contracts involving an information provider or processor dealing directly with a client and, with respect to content, where the provider tailors or customizes its information for the client’s purposes or being in a special rela-

101. See, e.g., *Lockwood v. Standard & Poor’s Corp.*, 682 N.E.2d 131 (Ill. App. Ct. 1997); *Great Central Insurance Co. v. Insurance Services Office, Inc.*, 74 F.3d 778 (7th Cir. 1997); *Rosenstein v. Standard and Poor’s Corp.*, 636 N.E.2d 665 (Ill. App. Ct. 1993).

102. RESTATEMENT (THIRD) OF PRODUCTS LIABILITY § 19, cmt. d (1997).

tionship of reliance with that client. The warranty reflects case law on information contracts. In *Milau Associates v. North Avenue Development Corp.*,¹⁰³ for example, the New York Court of Appeals rejected a U.C.C. warranty of fitness for a purpose in a contract for the design and installation of a sprinkler system. “[Those] who hire experts for the predominant purpose of rendering services, relying on their special skills, cannot expect infallibility. Reasonable expectations, not perfect results in the face of any and all contingencies, will be ensured under a traditional negligence standard of conduct . . . unless the parties have contractually bound themselves to a higher standard of performance.”

Restatement (Second) of Torts Section 552 regarding negligent misrepresentation provides a framework for this warranty. It states that: “One who, in the course of his business, profession or employment, or in any other transaction in which he has a pecuniary interest, supplies false information for the guidance of others in their business transactions, is subject to liability for pecuniary loss caused to them by their justifiable reliance on the information, if he fails to exercise reasonable care or competence in obtaining or communicating the information.”

In most states, this liability does not exist in the absence of a “special relationship” between the parties justifying a duty of reasonable care.¹⁰⁴ The obligation consists of a commitment that the content provided will not be wrong due to a failure by the provider to exercise reasonable care.¹⁰⁵ Under Restatement case law, the obligation is limited to cases involving a special or fiduciary relationship. Under Section 2B-404(a) the obligation does not center on delivering a correct result, but on care and effort in performing. A contracting party that provides inaccurate information does not breach unless the inaccuracy is attributable to fault on its part.¹⁰⁶ Liability under the Restatement for inaccurate information exists only if the information was intended or designed to guide the business decisions of the other party. This section is not limited to cases involving business guidance.

The cases largely exclude liability for information distributed to the public. This concept is captured by the term “published informational

103. 368 N.E.2d 1247 (N.Y. 1977).

104. See *Daniel v. Dow Jones & Co., Inc.*, 520 N.Y.S.2d 334 (N.Y. Civ. Ct. 1987) (electronic news service not liable to customer; distribution was more like a newspaper than consulting relationship); *A.T. Kearney v. International Business Machines*, 73 F.3d 238 (9th Cir. 1997).

105. *Rosenstein v. Standard and Poor's Corp.*, 1993 WL 176532 (Ill. App. Ct. May 26, 1993) (license of index; liability for inaccurate number tested under Restatement concepts in light of contractual disclaimer; information, although handled in commercial deals is not a product taking it outside this Restatement approach).

106. See *Milau Associates v. North Avenue Development Corp.*, 368 N.E.2d 1247 (N.Y. 1977); *Micro-Managers, Inc. v. Gregory*, 434 N.W.2d 97 (Wis. Ct. App. 1988).

content." "Published informational content" refers to information made available without being customized for a particular business situation of a particular licensee and where no "special relationship" of reliance exists between the parties. It is material made available in a standardized form to a public defined by the nature of the material involved. The information is not tailored to the client's needs. This definition and the liability exclusion reflects the vast majority of case law under the Restatement and modern values of not inhibiting the flow of content. The policy values supporting this stem in part from First Amendment considerations, but also from ingrained social norms about the value of information and of encouraging its distribution.

Section 2B-404 states as a contract law principle case law that holds the publisher harmless from claims based on inaccuracies in third party materials that are merely distributed by it. In part, this case law stems from concerns about free speech and leaving commerce in information free from the encumbrance of liability where third parties develop the information. In cases of egregious conduct, ordinary principles of negligence apply. As a contractual matter, however, merely providing a conduit for third party data should not create an obligation to ensure the care exercised in reference to that data by the third party.¹⁰⁷

The issue is important for information systems analogous to newspapers and are treated as such here for purposes of contract law.¹⁰⁸ The District Court in *Cubby, Inc. v. CompuServ, Inc.*,¹⁰⁹ commented: "Technology is rapidly transforming the information industry. A computerized database is the functional equivalent of a more traditional news vendor, and the inconsistent application of a lower standard [enabling] liability [for] an electronic news distributor . . . than that which is applied to a public library, book store, or newsstand would impose an undue burden on the free flow of information."

3. *Mass Market Licenses*

Modern contract statutes distinguish between commercial contracts (two or more businesses) and consumer contracts (one party is an individual acquiring the subject matter of the contract for personal or household use). The commercial-consumer dichotomy draws a line between

107. See *Winter v. G.P. Putnam's Sons*, 938 F.2d 1033 (9th Cir. 1991); *Walter v. Bauer*, 439 N.Y.S.2d 821 (N.Y. Sup. Ct. 1981). Compare *Brockelsby v. United States*, 767 F.2d 1288 (9th Cir. 1985) (liability for technical air charts where publisher designed product) (query whether this is a publicly distributed product).

108. See *Daniel v. Dow Jones & Co., Inc.*, 520 N.Y.S.2d 334 (N.Y. Civ. Ct. 1987) (electronic news service not liable to customer; distribution was more like a newspaper than consulting relationship).

109. 776 F. Supp. 135 (S.D.N.Y. 1991).

total freedom of contract (commercial deals) and limited regulation (consumer deals) to protect the individual consumer.

Article 2B creates a new expansive concept of a "mass market" contract that shifts away from the focus on "consumers." The term refers to a retail marketplace; it includes transactions involving two businesses. The idea of a mass market transaction goes far beyond the idea of a consumer transaction. Indeed, a significant percentage if not a majority of mass market licensees will be businesses, rather than consumers. Some will be small businesses, but under current licensing practice, many of the licensees will be large business entities, larger than the licensor from whom they may be "protected."

Definition of mass market has been elusive.¹¹⁰ Part of the difficulty lies in the fact that, while many have an intuitive understanding of what constitutes a mass market transaction, the concept has not been used in any other statutory provision. Most contract statutes focus on the consumer-commercial dichotomy. Some broaden the idea of "consumer" to include some business purchasers, but typically do so under dollar amount limitations. Federal law in the Magnuson Moss Act uses a concept of "consumer product" which focuses on the general or most common purchaser of a product and then applies the federal regulations to the product, regardless of whether the specific purchaser was or was not a consumer. The current definition is: "a transaction in a retail market for information involving information directed to the general public as a whole under substantially the same terms for the same information, and involving an end-user licensee that acquired the information in a transaction under terms and in a quantity consistent with an ordinary transaction in the general retail distribution."¹¹¹

The focus is on non-negotiated retail transactions involving end users. The concept includes *all consumer* transactions. Based on a goal of minimizing regulatory intrusions into Internet transactions, it excludes *access contracts* between two businesses. The goal is to focus on relatively small transactions involving businesses, but to incorporate most of what would intuitively be seen as general purpose mass market information transactions. As these concepts indicate, one way to conceptualize the "mass market" involves identifying a marketplace in which most participants are consumers in the traditional sense. Thus, for example, transactions made in general retail store environments are typically mass market transactions and also very often characterized by

110. Perhaps more importantly, neither of the other revision projects currently in place (Article 2 and Article 2A) adopt this approach. Each retains the more traditional and simplistic distinction between consumer transactions and commercial transactions. This is true even though, demonstrably, a mass market exists with respect to transactions in goods.

111. U.C.C. § 2B-102 (Proposed Draft, Sept. 25, 1997).

predominantly consumer transactions. On the other hand, purchases from wholesale distributors are not purchases in the mass retail market.

While the idea of mass market transaction in some cases blends into questions about when it is appropriate to regulate contracts, the primary purpose is to identify a form of transaction or a transactional context in which default rules different from those applicable in other types of licensing are appropriate because of the apparent marketplace expectations of the typical contracting parties. Thus, the theme is parallel to the idea of an access contract and an informational content contract. The overlap between protective regulation and these marketplace assumptions causes some conceptual difficulty, especially in light of the uncertainty involved in the definition itself. The bases on which "consumer" protections are justified in modern contract law are not always present in the broader mass market. This, the regulation typically comes from a belief that consumers are unsophisticated and lacking in economic power to negotiated terms or seek alternative sources of supply. While mass market terms are often not subject to individualized negotiation, lack of sophistication and absence of alternative supply sources are often not characteristic of purchases made by businesses in the mass market. A lawyer who, representing her law firm, acquires software from a retail store did not become unsophisticated about contracts simply because she chose the retail market place, rather than another source of software. A software developer, in business for himself, did not lose his sophistication about the technology simply by entering the door of a retail software vendor.

The idea of a mass market transaction is better viewed as identifying a marketplace in which particular assumptions might be made about the nature of the transaction and the expectations of the parties. Thus, a mass market is typically an anonymous market and one in which the purchaser-licensee anticipates being able to retransfer its purchase and to use it in ordinary ways in its own machines. It is a market in which multiple copies of identical information or products are transferred to multiple purchasers without customization, making it possible to ask questions about what are the characteristics, for example, of an ordinary database system or word processing system.

Consistent with these assumptions, the basic default rule structure for mass market transactions, overlaid on the general rules applicable to all other licenses, include the following (note that, as indicated, some of the default rules only apply to consumer transactions, an included subset of mass market transactions):

- presumed transferable without consent of the licensor

- security interest may be created without the consent of the licensor
- licensee may refuse some performance under perfect tender rule
- computer program carries an implied warranty of merchantability
- disclaimer of warranty must be conspicuous
- written contract term cannot contradict negotiated deal
- right of refund and repair if post payment contract refused
- choice of law in some *consumer transactions* where delivery occurred or was to occur
- choice of forum not enforceable in some *consumer transactions*
- licensee cannot opt into Article 2B
- term that precludes oral modifications *in consumer transaction* not enforceable unless consumer manifests assent *to the term*
- for change of continuing contract terms, notification to licensee and right to withdraw
- “hell and high water” clause less effective in a *consumer transaction*.

CONCLUSION

As this discussion indicates, Article 2B presents much that is new to the U.C.C., but also brings forward much that has been good and stable in the U.C.C. since its foundation in the midst of the goods-based economy. This is a contract statute that resists the temptation to regulate and control, presuming that the parties themselves are the best suited to shape their own contractual relationships. In that decision lies the basis of a commercial contract code and the foundations for information commercial in the next century.

The completion and enactment of Article 2B will bring the U.C.C. into the new economy with a tailored treatment of the new forms of commerce that shape that economy. Article 2B does not create contract law in this realm, but brings together pieces of common law, business practice, and economic development to build a stable and coherent framework.

