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TREATMENT OF CONSUMERS UNDER PROPOSED U.C.C. ARTICLE 2B LICENSES

by MARY JO HOWARD DIVELY & DONALD A. COHN†

I. INTRODUCTION

Much has been written and said recently regarding the ability of the Uniform Commercial Code (the "U.C.C." or the "Code"), and the U.C.C. drafting process in general, to adequately reflect the concerns of consumers.¹ Other than commenting that proposed U.C.C. Article 2B Licenses ("Article 2B") contains more protection for consumers than any other existing commercial statute,² we will not join that debate here. Instead, this article will describe the actual provisions of Article 2B³ which are

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1. See Jean Braucher, *Foreword: Consumer Protection and the Uniform Commercial Code*, 75 WASH. U.L.Q. 1-9 (1997); James J. White, *Comments at the 1997 American Association of Law Schools Annual Meeting: Consumer Protection and the Uniform Commercial Code* 219 (Jan. 1997); Gail Hillebrand, *The Uniform Commercial Code Drafting Process: Will Articles 2, 2B and 9 Be Fair to Consumers?*, 75 WASH. U.L.Q. 69, 81-85 (1997).

2. See Raymond T. Nimmer, *Issues Paper: U.C.C. Article 2B-Licenses* (1997).

3. Proposed U.C.C. Article 2B still is in the drafting stage, and has not yet been finally approved by the Drafting Committee, NCCUSL, ALI, or any state. As such, the authors' observations are limited to the draft dated September 25, 1997 (the "Draft"). Those

intended to increase consumer protection beyond that which is traditionally afforded to consumers under existing commercial statutes. This article will further summarize various modifications to benefit consumers which have been requested by consumer advocates in the course of the drafting process, discuss how the drafting process has responded to these requests for modification. Finally, this article will offer a recommendation for a methodology for approaching other requested changes to enhance consumer protection.

A. THE TENSION

In his thoughtful article, Professor Fred H. Miller describes the tension between consumer and commercial interests in the Code.⁴ He notes that when the Code initially was drafted, the "concept of discrete legal rules applicable in consumer transactions was only beginning to emerge" but that "even at this early stage there was recognition that the same legal rule that works well for commercial parties might not work as well where a consumer is involved."⁵ As Professor Miller describes, commercial law generally is made up of a series of gap fillers or default rules which operate in areas in which two commercial parties have not reached their own agreements. When the default rules reflect commercial practice, they have the added benefit of encouraging commercial parties to defer to them rather than drafting lengthy and complicated private agreements. Finally, these rules assist courts in analyzing and adjudicating the contract lawsuits that arise under the Code.

As commercial information licensing lawyers who practice daily in this specialty on behalf of both licensees and licensors, we can attest to the particular need for these latter two benefits. As consumers in our private lives, however, we understand that the effect of these default rules on consumers often is not so favorable, and can be, in Professor Miller's words, "a license for the unscrupulous to take unfair advantage of the consumer."⁶ Most consumers are not in a position to negotiate these provisions, nor can most consumers be expected to appreciate their often complicated legal effects. Thus, great importance has been given to the process of drafting Article 2B to examine how the provisions applicable to licensees would affect not just commercial licensees, but also consumer licensees, and to determine whether there are circumstances in which special protection to consumer licensees is warranted.⁷ One must

readers wishing to review the latest version of proposed Article 2B may find it on the World Wide Web at <<http://www.law.upenn.edu/library/ulc/ulc.htm>>.

4. See Fred H. Miller, *Consumers and the Code: The Search for the Proper Formula*, 75 WASH. U.L.Q. 187-217 (1997).

5. See *id.* at 187.

6. See *id.* at 187.

7. Consumers most likely to be affected by Article 2B will be licensees not licensors.

also remember that this process is not intended to rewrite the law for *commercial* parties, the fundamental tenets of which have been in place since the creation of the U.C.C.⁸

Overlaying Professor Miller's concerns are two additional and competing concepts that must be reconciled if we are to produce a viable U.C.C. Article.

A basic tenet of the U.C.C. since its creation has been freedom of contract. With very few exceptions, parties to a commercial contract are permitted to negotiate terms and conditions that reflect their agreement even if these agreements are not consistent with the "gap fillers" of the U.C.C. and even when the agreements that parties privately reach seem harsh or incomprehensible when viewed against an objective standard. The proponents of additional protection of consumers in the U.C.C. have called for additional mandatory U.C.C. provisions that will supersede the parties' agreement. The decision to abandon or dilute a fundamental underpinning of the U.C.C. requires more consideration than we can give it in this space. The continuing challenge to the Drafting Committee has been to try to fairly and equitably balance these conflicting public policy issues.

Secondly, the inclusion of mandatory, non-waivable provisions will have the effect of allocating risk between the contracting parties in ways that are contrary to current industry practice in many cases. To the extent that suppliers and vendors will be required to accept additional risks in the transaction, transactional costs for information licensing will most likely increase. These additional transactional costs will have an impact on all purchasers or licensees of information. Again, the Drafting Committee has attempted to balance the need for appropriate risk sharing with the need to keep transactional costs as low as possible make information technology available to all licensees, especially consumers, at affordable prices. A key consideration in this analysis is to determine when there is a real commercial risk rather than a non-existent theoretical risk.

8. Article 2B uses as its paradigmatic transaction the license between a licensor and licensee. A commercial licensee under Article 2B essentially is in the same position as a commercial buyer under Article 2. The authors have observed that many of the comments made by consumer representatives appear to use the words "licensee" and "consumer" interchangeably, when in fact they are two very different things. The danger in analyzing Article 2B in this fashion is that it takes the focus off of extending additional protections to a narrow group of users for which there is historical precedent. Miller, *supra* note 4, at 187. Instead, this analysis suggests that all licensees, both commercial and consumer, should be granted these additional protections. This would be a significant departure from the other articles of the U.C.C.

II. THE DRAFTING PROCESS

The Drafting Committee is made up of NCCUSL Commissioners and ALI representatives. Professor Raymond T. Nimmer⁹ is the Article 2B Drafting Committee Reporter. Creation of Article 2B began as part of the revision of Article 2. In 1994, NCCUSL decided that a separate drafting committee should be formed to focus on information licensing issues. Since its formation, the Drafting Committee has met ten times,¹⁰ and the Reporter has produced new drafts of Article 2B after each Drafting Committee meeting to reflect the decisions made or guidance provided by the Drafting Committee.

At the Drafting Committee meetings,¹¹ issues are debated and discussed, and input is given by interested observers, including industry trade groups, consumer groups, the ABA and other groups, companies, and individuals who attend the Drafting Committee meetings, including representatives of the motion picture industry, the publishing industry, banks and other financing groups, all of which will be affected by 2B.¹² It is not unusual for one point to be debated for hours, or at multiple meetings, with those observers vying for time to emphasize views that they have already supplied to the Drafting Committee in writing. The information industry representatives can be counted on to make their points for their industry, the consumer representatives are rarely silent on the issues that may affect consumers, and the representatives of large business licensees also are out in full force. Although the meetings can be tedious, with what often seem to be the same points being made over and over again, Carlyle C. Ring, the Chairman of the Drafting Commit-

9. Professor Nimmer is the Leonard Childs Professor of Law at the University of Houston Law School.

10. Memorandum from Carlyle C. Ring, Jr., Chairman of the Drafting Committee to Commissioners, NCCUSL, for the 1997 Annual Meeting of NCCUSL (on file with the authors) [hereinafter Ring Memorandum].

11. See *id.* (noting that attendance at the Drafting Committee meetings has been between 54 and 80, and that included in these meetings was a session marked by the largest attendance of any drafting meeting in recent history). The Ring Memorandum also summarizes the backgrounds of the observer/participants as follows:

- Licensor/Licensee
- Software Industry
- Major Non-Information Companies
- Entertainment studios
- Publishing Industry
- Financing Groups
- Consumers
- Banking Industry
- Libraries
- Additional Trade Associations

Id.

12. The authors regularly attend and participate in the Drafting Committee meetings in their capacity as Advisors on Article 2B from the ABA Section of Business Law.

tee, and all of the members of the Drafting Committee have been gracious and generous in allowing all points a complete and fair airing. Anyone who has attended any of the Drafting Committee meetings can clearly recognize that all points of view expressed at the meetings, or submitted to the Drafting Committee in writing, are seriously considered by the Drafting Committee. It is important to distinguish being provided a fair hearing for a point of view from the rejection of that point of view as being inappropriate, impractical, unnecessary, uneconomical or burdensome after completing a rigorous series of legislative, cost benefit, and risk benefit analyses.

In addition, due in large part to the efforts of the Reporter, Article 2B has been presented and discussed in many forums throughout the country for the past few years, and input received in those discussions has been brought back to the Drafting Committee. Article 2B is not a law driven solely by the licensor industry (if one can even determine what the "licensor" industry is in a field where the same entities often act as both licensors and licensees depending upon the circumstances of the particular transaction); rather Article 2B is emerging as a law which, in the spirit of the Uniform Commercial Code as originally conceived, recognizes and reflects true commercial practice.¹³

As much as any other group, consumers have been represented in the Article 2B drafting process. A representative of the Consumer Project on Technology has attended almost all of the Drafting Committee meetings and has been one of the most frequent observer speakers at the meetings. The Consumers Union also has sent a representative to many of the Drafting Committee meetings and has presented at least six written submissions since June 1996, more than any other single group that the authors have seen. These submissions have contained requests for dozens of changes to Article 2B, some major, some minor. All have, in the authors' observation, been taken seriously by the Drafting Committee. It is not surprising that not all of their proposals have been adopted; however, many valuable upgrades to Article 2B have resulted from their input. It is also important to remember that many members of the Drafting Committee and other interested observers have proposed

13. See U.C.C. Article 2B, Preface (Proposed Draft, Sept. 25, 1997). The Preface to the Draft states that:

From the outset, the Article 2B process has reached out for the widest range of input and commentary possible. To a greater extent than in any other recent U.C.C. project, this has led to an active engagement of the views of many different groups and individuals. During the period from March, 1994 through today, the Reporter and various members of the Committee have met with representatives or members of a wide range of groups to review provisions of various interim drafts.

Id. The Reporter goes on to list thirty organizations which have had representatives at Drafting Committee meetings, including the Consumers Union and the Consumer Project on Technology. *Id.*

changes to Article 2B that favor consumer interests. Many of these proposed changes have also been adopted.

Article 2B has been read to the full Conference on two occasions and to ALI on one. Both ALI and the Conference provided valuable consumer insights that subsequently were addressed in revised versions of Article 2B. Two scheduled meetings of the Drafting Committee remain to review the Draft before it is presented to NCCUSL and ALI in 1998 for its final reading. The Draft is, at this point, in nearly final form, subject to refinements which will occur at those meetings.

III. WHAT THE PROCESS HAS WROUGHT FOR CONSUMERS SO FAR

Article 2B currently contains several innovative consumer protection provisions that will be grouped for purposes of this discussion into two distinct categories.

The first category contains provisions which exclusively protect consumers. The second category contains provisions which protect all "mass market licensees" (which include consumers in almost all instances). First, we will provide background on the definitions of "consumer" and "mass market licensee," and then will discuss the special provisions applicable to each.

A "consumer" is defined by Article 2B as:

[A]n individual who is a licensee of information that at the time of contracting is intended by the individual to be used primarily for personal, family, or household use. The term does not include an individual that is a licensee of information primarily for profit-making, professional or commercial purposes, including agricultural, business management and investment management, other than management of the individual's personal or family investments.¹⁴

The Reporter's comments to Section 2B-102(a)(8) note that existing Article 2 does not define "consumer" and that the Article 9 definition focuses on persons acquiring property primarily for personal or household uses. The Reporter writes that while Article 9 serves as the template for the Article 2B definition, there are serious questions of interpretation which arise when the Article 9 definition is used for other than security interest transactions, and that the 2B definition attempts to clarify these issues:

Distinguishing these personal business uses and truly consumer uses holds great importance in Article 2B because software and other information can be used "personally" in traditional business contexts. The exclusions in the definition apply to profit-making, professional or business use. In the modern economy, where individuals can and often do

14. U.C.C. § 2B-102(a)(8) (Proposed Draft, Sept. 25, 1997).

engage in seriously significant commercial enterprises without the overlay of a large corporation, the personal use idea needs to respect and reflect the modern practice, especially in this area. The proposed definition distinguishes between persons using information in profit making and business uses and personal or family uses such as ordinary asset management for an ordinary family.¹⁵

A “mass market transaction” is defined by Article 2B as:

[A] transaction in a retail market 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 under terms and in a quantity consistent with an ordinary transaction in the general retail distribution. The term does not include:

- (A) a transaction between parties neither of which is a consumer in which either the total consideration for the particular item of information or the reasonably expected fees for the first year of an access contract exceeds [_____];
- (B) a transaction in which the information is customized or otherwise specially prepared for the licensee;
- (C) a license of the right publicly to perform or display a copyrighted work; or
- (D) a site license, or an access contract not involving a consumer.¹⁶

A mass market license is defined by Article 2B as “a standard form that is prepared for and used in a mass-market transaction.”¹⁷

The concept of the mass market has been extensively discussed by the Drafting Committee over several meetings. It is important to understand that the focus is on the market in which the information will be used and on the form of the transaction rather than on the nature of the buyer or licensee. The Reporter’s comments to Section 2B-102(a)(29) are illustrative:

The definition contemplates a retail marketplace where information is made available in pre-packaged form under generally similar terms. It applies to information that is aimed at the general public as a whole, including consumers. This captures most of a true retail setting, such as transaction in a department store, or the like. Article 2B will be the first U.C.C. article to extend consumer-like protections to business transactions in any form, and the first to tailor at least some default rules based on that concept . . . the goal is to do this in a limited manner, reflecting the innovative nature of the concept, while confining the risk created by focusing on small transactions for information oriented toward the broad general public.¹⁸

15. See Reporter’s Notes to U.C.C. § 2B-102(a)(8) (Proposed Draft, Sept. 25, 1997).

16. U.C.C. § 2B-102(a)(29) (Proposed Draft, Sept. 25, 1997).

17. U.C.C. § 2B-102(a)(28) (Proposed Draft, Sept. 25, 1997).

18. U.C.C. § 2B-102(a)(29) (Proposed Draft, Sept. 25, 1997).

The decision to limit the included transactions by use of a dollar cap was made for a number of reasons: first, so that there would be a "bright line" test of inclusion/exclusion to help both licensors and licensees understand more certainly whether they are in a mass market transaction; second so that licensors could limit the extra business risk that they are taking on under the Draft by virtue of 2B extending many consumer-like protections for the first time ever to a category of business transactions, and thirdly to make clear that larger, purely business transactions would not be extended these protections. The dollar limit has not yet been selected by the Drafting Committee, but it is important to note that consumers are not subject to the dollar limit.

As noted by the Reporter in the Preface to the Draft:

Although the idea of "mass market" goes past traditional concepts of consumer protection, the combined effect of using that term and covering some transactions involving consumers specifically produces a draft that, in general, retains all existing U.C.C. consumer protections and in fact creates some protections that are not present under current law.¹⁹

A. PROVISIONS EXCLUSIVE TO CONSUMERS

The provisions of Article 2B that provide special treatment exclusively for consumers are those affecting choice of law,²⁰ choice of forum,²¹ electronic error,²² the effect of a no-oral modification clause,²³ and a limitation on what are commonly called "hell and highwater clauses."²⁴ These are discussed in more detail below.

B. RELATION TO STATE CONSUMER LAWS

Before discussing these sections, however, it is important to note that the protections afforded to consumers under Article 2B are in addition to other State law protections, including consumer protection statutes, not a substitute for them.

Section 2B-104, "Transactions Subject to Other Law" provides that in the case of a conflict between Article 2B and another law of the state, the conflicting law of the state will control if it exists on the effective date of Article 2B and establishes a consumer protection.²⁵ The only exceptions to the consumer law controlling the conflict are with respect to those special characteristics of Article 2B which are directly applicable to

19. U.C.C. Article 2B, Preface (Proposed Draft, Sept. 25, 1997).

20. U.C.C. § 2B-108 (Proposed Draft, Sept. 25, 1997).

21. U.C.C. § 2B-109 (Proposed Draft, Sept. 25, 1997).

22. U.C.C. § 2B-117 (Proposed Draft, Sept. 25, 1997).

23. U.C.C. § 2B-303 (Proposed Draft, Sept. 25, 1997).

24. U.C.C. § 2B-618 (Proposed Draft, Sept. 25, 1997).

25. U.C.C. § 2B-104 (Proposed Draft, Sept. 25, 1997). This section also treats other special types of conflicting laws, but they are not relevant for the consumer discussion. *Id.*

electronic transactions and would not be likely to be addressed by the consumer statute.²⁶ Those exceptions are limited to the following:

- (1) a requirement that a contractual obligation, waiver, notice, or disclaimer be in writing is satisfied by a record;²⁷
- (2) a requirement that a record or contractual term be signed is satisfied by an authentication;²⁸
- (3) a requirement that a contractual term be conspicuous or the like is satisfied by a term that is conspicuous in accordance with Article 2B;²⁹
- (4) a requirement of consent or agreement to a contractual term is satisfied by an action that manifests assent to a term in accordance with Article 2B;³⁰

26. U.C.C. § 2B-104, Reporters Notes (Proposed Draft, Sept. 25, 1997). The Notes to this section state that the section implements a balance between the modernization themes in Article 2B relating to electronic commerce and existing law regulating consumer contracts, and note that Article 2B adopts a limited, circumspect reconciliation in sharp contrast to the many non-uniform digital signature laws that either have been enacted or are in the process of being enacted in many states. *Id.* The Reporter further explains that electronic concepts that were not at issue when existing consumer law developed require adjustments appropriate to promote uniformity and certainty in commerce that is truly national in nature, while preserving the intent of the regulations. *Id.* Finally, the Reporter notes that there is no effort to alter content terms, such as whether a disclaimer can be made, what language must be used and like issues. *Id.*

27. U.C.C. § 2B-102(a)(35) (Proposed Draft, Sept. 25, 1997). The term "record" is defined as "information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form." *Id.* It is the Article 2B equivalent of a writing. *Id.*

28. U.C.C. § 2B-102(a)(3) (Proposed Draft, Sept. 25, 1997). The term "authenticate" means to sign, or to execute or adopt a symbol or sound or encrypt a record in whole or in part, with intent to identify the party; adopt or accept a record or term or establish the authenticity of a record or term that contains the authentication or to which a record containing the authentication refers." *Id.* It is the Article 2B equivalent of the common law signature. *Id.*

29. U.C.C. § 2B-102(a)(7) (Proposed Draft, Sept. 25, 1997). "Conspicuous" is defined in Article 2B to deal with electronic contexts and expanded by an enhanced concept of manifestation of assent, as is discussed below. *Id.*

30. "Manifest Assent" is a new concept under Article 2B which describes what a party must do in order to indicate consent or agreement with a record or term. It seems to us to have been somewhat misunderstood by many, both in concept and in application. We will attempt to clarify both here. Here's what is required to manifest assent under Article 2B: A party must, *after* having had an opportunity to review the record (which, we should note, is a *meaningful* opportunity to review), or with knowledge of the terms of the record, either authenticate the record or engage in other affirmative conduct or operations that the record conspicuously provides or the circumstances clearly indicate constitute acceptance of the record. The use of the words "conspicuously" and "clearly" are key in this section. If a party cannot tell by the terms of the record or the circumstances of the transaction whether a particular conduct will constitute acceptance of the record, it is highly unlikely (we cannot think of a reasonable scenario) that the conduct will constitute manifest assent. It has been suggested by consumer representatives that allowing licensors to define in the record what type of conduct will manifest assent somehow undermines the licensee's rights. This

(5) a statute authorizing electronic or digital signatures, or authorizing electronic or digital substitutes for requirements of a writing controls over the provisions of this article to the extent of a conflict with Article 2B.³¹

These limitations are necessary because the electronic concepts which they address are not likely to have been addressed by a state's consumer laws, unless the consumer law has been amended to reflect changes made necessary by electronic contracting. It is the authors' understanding that the Drafting Committee intends to focus on all of the electronic contracting provisions, including these, at the next two Drafting Committee meetings, in order to ensure that they are consistent and appropriate. Except in the foregoing limited situations, the consumer law of a State will preempt Article 2B.

C. CHOICE OF LAW

Most consumers will be protected by having the law of the jurisdiction where they purchased the software or other information govern the transaction, which is the reasonable expectation of most consumers.

Section 2B-108 provides that choice of law terms in an agreement are enforceable. In the event a choice of law is not made by agreement, the default rules are that: (1) in access contracts or contracts providing for delivery by electronic communication, the contract will be governed by the law where the licensor is located; (2) consumer contracts which are not governed by the rule stated in subsection (1) and which require delivery of a copy on a physical medium to the consumer is governed as to the contractual rights and obligations of the parties by the law in which the copy was located when the licensee receives possession of the copy or where the receipt was to have occurred; and (3) in all other cases, the contract is governed by the law of the State with the most significant

seems to us to be contrary to a basic tenet of contract law which most of us learned in the early days of our first contracts class: that the offeror has the right to designate the manner in which acceptance of the offer shall be effective. In an electronic transaction, the typical conduct which will be found to manifest assent will be "clicking" on an "I Accept" icon or similarly designated icon. It may be difficult for those who do not routinely engage in electronic transactions to equate clicking on an "I Accept" icon with the gravity of signing one's name to the bottom of a document, but those who do routinely engage in electronic transactions understand that clicking on such an icon is the accepted equivalent of signature in cyberspace. As long as the record makes it clear that this conduct will manifest assent (and we note that if it does not, the assent is not effective) we do not see why the licensee should object. Further, although it has been suggested many times by the consumer representatives that the mere failure to return shrinkwrap software constitutes manifest assent, we note that Section 2B-112(b) expressly states that "Merely retaining information or a record without objection is not a manifestation of assent." U.C.C. § 2B-112(b) (Proposed Draft, Sept. 25, 1997).

31. U.C.C. § 2B-104(b) (Proposed Draft, Sept. 25, 1997).

relationship to the contract.³² The rule contained in subsection (2) will apply to all situations in which consumers purchase software at a local software or department store, where the bulk of consumer transactions take place.³³

D. CHOICE OF FORUM

Article 2B provides that parties may choose an exclusive forum, but, recognizing that these types of choices often are not negotiable by consumers, limits that right by providing that in a consumer contract the choice is not enforceable if the chosen jurisdiction would not otherwise have jurisdiction over the consumer and the choice is unreasonable and unjust as to the consumer.³⁴

E. DETECTION OF CHANGES AND ERRORS: CONSUMER DEFENSES

The most recent draft of Article 2B contained a new section 117 designed to provide a simple remedy for consumers who are damaged by errors in electronic commerce, with the goal of encouraging consumers to use electronic commerce and avoid unjust results. The Reporter's Notes describe Section 2B-117 as setting forth a rebuttable presumption regarding the effect of the use of an attribution procedure at least part of which has the effect of precluding changes made in a record without detection and a rebuttable presumption for error detection procedures. Since this is an important new protection for consumers, it is worth quoting the text in whole:

(c) In a transaction involving a consumer, the consumer is not responsible for content that the consumer did not intend but that was caused by an electronic error if, on learning of the other party's reliance on the erroneous content, the consumer:

(1) in good faith promptly notifies the licensor of the error and that it did not intend the content received by the other party;

32. U.C.C. § 2B-108(b)(1)-(3) (Proposed Draft, Sept. 25, 1997).

33. U.C.C. § 2B-108(b)(2) (Proposed Draft, Sept. 25, 1997). The Reporter's Notes to Section 2B-108 state that choice of law clauses are routine in commercial licenses, that except in Article 2A and cases of consumer regulatory statutes, no current uniform law in the United States precludes enforcement of contract choice of law on issues that a contract could control, and that neither the Restatement, current Article 1 or Article 2, nor revised Article 2 place special restrictions on choice of law. *Id.* To the extent that a consumer regulatory statute of a state precludes the choice of law provisions in Section 2B-108, the consumer regulatory statute will prevail according to Section 2B-104.

34. U.C.C. § 2B-109 (Proposed Draft, Sept. 25, 1997). The Reporter's Notes indicate that this section provides separate protection for consumers where the risk of over-reaching is more severe, while noting that protection of this sort may already exist in applicable state consumer protection law. *Id.* The Drafting Committee has considered, but not voted upon, a limitation to the consumer exception covering access contracts for informational content or services.

(2) takes reasonable steps, including steps that conform to the licensor's reasonable instructions, to return to the licensor all copies of any information received or, on instructions from the licensor, to destroy all copies; and

(3) has not used or received value from the information or made the information available to a third party.

(d) In subsection (c), the burden of proving intent and lack of an error is on the party dealing with the consumer, while the consumer has the burden of proving compliance with subsection (c)(1)(2)(3).³⁵

The Reporter's Notes state that the basic approach of Subsection (c) is to provide a relatively simple method for a consumer to contest the results of errors in his or her transmissions to a third party. The Reporter cautions that it does not propose a rescission right which would allow the consumer to reconsider his deal, but merely provides an error resolution system.³⁶

F. THE "HELL OR HIGHWATER CLAUSE"

The financing provisions of Article 2B extend common financing and security concepts to the subject matter of Article 2B, tailored as necessary to accommodate the special characteristics of information assets. The "hell or highwater clause" which is common in equipment leasing and similar transactions has been adopted in subsection (d) of Section 2B-617. It states that if the agreement so provides, as between the financier and the licensee and any transferee of either party, the licensee's promises under the agreement become irrevocable and independent of

35. U.C.C. § 2B-117(c)(d) (Proposed Draft, Sept. 25, 1997).

36. U.C.C. § 2B-117, Reporter's Notes (Proposed Draft, Sept. 25, 1997). The illustrations of the operation on consumers of Section 117 contained in the Reporter's Notes are edifying:

Illustration 1: Consumer intends to send an order for ten copies of the latest video game released by Jones Corp. In fact, the information processing system, through no fault of the consumer, records 110. The electronic agent maintaining Jones' site, after validating that the order came from Consumer and that the number entered was 110, electronically disburses 110 copies to Consumer's location, with an appropriate bill. The next morning, Consumer notices the mistaken shipment. He sends an E-mail to Jones describing the problem, offering to immediately return or destroy copies and does not use the games. Under subsection (c) there is no presumption that the content was as intended and, if it pursues the matter, Jones must prove that there was no error. Alternatively, Jones may instruct Consumer to destroy the excess 100 game copies and pay a revised bill for 10.

Illustration 2: Same facts as above, except that Jones' system before shipping the materials sends a confirmation notice, asking Consumer to confirm that it ordered 110 games. Consumer sees the message. If it confirms 110 copies, even though it later claim rebuts any presumption, confirmation of the same volume twice would be strong evidence of intent to contract at the indicated amount. If it refuses to confirm, of course, the contract must be made later on the basis of the 10 copies confirmed.

Id.

the license on the licensee's acceptance of the license as long as the information was not selected, created, or supplied by the financier or the financier was not otherwise actively involved as indicated in Section 2B-617. Importantly for consumers and consistent with existing law on traditional "hell or highwater" clauses, Section 2B-617 expressly does not apply to licensees who are consumers.

G. MASS MARKET CLAUSES WHICH ALSO PROTECT CONSUMERS

As discussed above, in addition to the aforementioned protections afforded exclusively to consumers, there are a series of additional protections for mass market licensees which also will protect consumers in most cases. Following is a brief discussion of each.

1. *Opting in to Article 2B*

Under Section 2B-106, even parties whose transaction ordinarily would not be covered under Article 2B may elect to have 2B apply to their transaction. This election is analogous to a choice of law, however, and, as such a party to a mass market agreement who is not likely to understand differences in law, should not have this election imposed upon him. Accordingly, Section 2B-106 bars this right of election in mass market transactions. As indicated in the Reporter's Notes, this provision implements a form of extended consumer protection and applies it to both consumers and businesses operating in the mass market.

2. *Restrictions on Terms in Mass Market Contracts*

The Drafting Committee has overwhelmingly voted to permit licensees in mass market transactions to have a right of refund if a mass market contract has been formed with terms and conditions that the licensee did not see prior to the creation of the contract. An important but controversial innovation of Article 2B has been this validation of so-called "shrink-wrap" software licenses. The recent Committee action balances the validation of shrink wrap licenses with a very liberal right on the part of mass market licensees, including consumers, to return software for a complete refund.

The most recent draft of Section 2B-208 sets forth the basic terms which will govern mass market licenses. This section has been much discussed and altered over the last three years, and is likely to undergo further revision before being finalized. Because it has been the subject of so much controversy, it is worth setting it out in full text below, so that the reader can judge exactly what all the fuss is about. In its current form, Section 2B-208 provides:

- (a) Except as otherwise provided in Section 2B-209, a party adopts the terms of a mass market license if the party agrees, including by mani-

fest assent to the license before or in connection with the initial performance or use of or access to the information. However, except as otherwise provided in this section, a term [for which there was no opportunity to review before payment of the contract fee is not adopted and] does not become part of the contract if the party does not know of or manifest assent to the particular term and the term creates an obligation or imposes a limitation that:

- (1) the party proposing the form should know would cause an ordinary reasonable person acquiring this type of information in the general mass market to refuse the license if that party knew that the license contained the particular term; or
 - (2) conflicts with the negotiated terms of the agreement between the parties to the license.
- (b) Subsection (a)(1) does not exclude a term that:
- (1) states a limit on the licensee's use of the information which limit would exist under intellectual property law in the absence of the contractual term;
 - (2) was disclosed in compliance with any federal or state law;
 - (3) was reasonably disclosed on the product packaging or otherwise before payment of the license fee, or was part of the product description; or
 - (4) becomes part of the contract under other provisions of this article.³⁷

The ABA Subcommittee, in its briefing paper on Article 2B which was submitted to the Conference for the 1997 Annual Meeting concluded that giving the typical mass market licensee the right to return the product for a full refund and limited incidental damages was superior to some standard that seeks to determine whether the terms of the license were surprising, whether a reasonable licensee under the circumstances would have accepted the terms or whether the licensee actually agreed to the terms. The ABA Subcommittee also concluded that the refund model achieved certainty and fairness and that a Restatement Section 211 approach to mass market licenses was not productive. Giving the costs of return associated with obtaining a refund would place the parties on a level playing field, the Subcommittee felt, while also protecting licensees who see terms for the first time post-payment. Finally, the Subcommittee noted that other provisions already existing in Article 2B regarding the requirements of conspicuousness, etc., would apply equally to mass market licenses as they do to others, and that as such, the Subcommittee believed that its recommended approach would eliminate any uncertainty in the terms of the license while allowing the equivalent of prior

37. U.C.C. § 2B-208(a),(b) (Proposed Draft, Sept. 25, 1997).

review.³⁸

At a recent meeting, the NCCUSL Article 2B Drafting Committee, by a vote of 10 to 2, adopted the ABA proposal for this section. The Reporter will modify Article 2B to provide: (1) for a right of refund if the buyer or licensee has not seen the terms of the license prior to completion of the sale or formation of the license; (2) that the licensor is responsible for incidental damages of the licensee in collecting the refund; and (3) that if the licensee suffers damage in booting up the software to read the terms of the license, then the licensor is responsible for damages arising out of the use of the software to that point. The definition of mass market transaction will be revisited after the Committee has an opportunity to review the rewritten Section 2B-208.

3. *Modification of Continuing Contracts*

Section 2B-304 contains the general rules for modification of continuing contracts. For non-mass market contracts, a modification in good faith made pursuant to a term in a contract providing that the contract may be modified as to future performances by compliance with a described contractual procedure is effective if compliance with the procedure reasonably notifies the other party of the change.

In mass market licenses, however, Article 2B provides the added mass market licensee and consumer protection of requiring that the procedure permit the licensee to terminate the contract if the modification deals with a material term and the licensee in good faith determines that the modification is unacceptable.

4. *Implied Warranty of Merchantability*

The "gap filling" implied warranty of quality for computer programs in non-mass market transactions under Article 2B is that any physical medium on which the program is transferred is merchantable and that the computer program will perform in substantial conformance with any promises or affirmations of fact contained in the documentation provided by the licensor at or before the delivery of the program.³⁹

38. See "Briefing Paper on Article 2B-Licenses" dated July 24, 1997 submitted by the ABA Subcommittee to the 1997 NCCUSL Annual Conference (on file with the Conference and the authors).

39. U.C.C. § 2B-314, Reporter's Notes (Proposed Draft, Sept. 25, 1997). The Reporter's Notes to Section 2B-314 state with respect to this warranty:

Article 2B warranties blend three legal traditions. One tradition stems from the U.C.C. and focuses on the quality of the product. This tradition centers on the result delivered: a product that conforms to ordinary standards of performance. The second tradition stems from common law, including cases on licenses, services contracts and information contracts. This tradition 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 tradi-

In mass market contracts, however, the default standard is that *both* the physical medium on which the computer program is delivered and the computer program itself must be merchantable.

5. *Disclaimer of Warranty*

Section 2B-406 requires that disclaimers and modifications of warranties be in a record, and sets forth safe harbor language for purposes of disclaiming the various warranties. Two important additional requirements are needed to disclaim or modify an implied warranty in a mass market contract. First, the disclaiming or modifying language must be conspicuous.⁴⁰ Second, if the intent is to disclaim all warranties in a single sentence, a safe harbor is set forth which is designed to give more disclosure to the consumer of what is disclaimed.⁴¹

6. *Transferability of License*

The sections of Article 2B dealing with transfers of licenses and security interests demonstrate the interplay between federal intellectual property law and state contract law. Section 2B-504 provides that a transfer of a licensee's rights under a non-exclusive license is ineffective,⁴² unless: (1) the licensor consents to the transfer; or (2) the transfer is subject to the terms of the license; and (3) if the contract is a mass-market license, the licensee received delivery of a copy of the information and transfers or destroys the original copy and all other copies made by it.⁴³ The basis for allowing less restricted transferability of non-exclusive mass market licenses is that in the mass market the licensor has chosen not to be concerned about the parties which acquire its product as licensee, but instead has marketed its product to the general public.

tion comes from the area of contracts dealing with informational content and essentially disallows implied obligations of accuracy or otherwise in reference to information transferred outside of a special relationship of reliance. Current law selects the applicable tradition in part based on characterizations about whether a transaction involves goods or not. The distinction is not reliable in information contracting, especially in light of the ability to transfer intangibles electronically without the use of any tangible property to carry the intangibles.

Id.

40. See U.C.C. § 2B-406(d) (Proposed Draft, Sept. 25, 1997).

41. *Id.*

42. This follows current federal law which holds that a licensee cannot assign its rights in a nonexclusive license. See *Everex Systems, Inc., v. Cadtrak Corp.*, 89 F.3d 673 (9th Cir. 1996). The Reporter's Notes indicate that the non-transferability premise flows from the fact that a nonexclusive license is a personal, non-assignable contractual privilege, representing less than a property interest. U.C.C. § 2B-504, Reporter's Notes (Proposed Draft, Sept. 25, 1997).

43. U.C.C. § 2B-504 (Proposed Draft, Sept. 25, 1997).

7. *Perfect Tender*

Article 2B generally adopts a substantial performance standard for acceptance of software.⁴⁴ The Drafting Committee, from a public policy viewpoint, has elected to treat mass market transactions differently by the adoption of a modified perfect tender rule.⁴⁵

The decision to substitute a substantial performance standard for the perfect tender standard contained in Article 2 has been controversial. The ABA Subcommittee was an early proponent of the need to adopt the substantial performance standard for software, which often contains "bugs" or small imperfections which, though they might technically cause the software to fail the perfect tender rule, reasonably should not be able to be used to obtain the traditional remedies available in such cases. However, there has been much comment in the Drafting Committee meetings, and in writings submitted to the Drafting Committee, that the substantial performance rule is not appropriate for the mass market. The Drafting Committee has embraced this position, and has returned to Article 2B a modified perfect tender standard applicable to mass market contracts.⁴⁶

IV. THE RESPONSE OF THE PROCESS TO REQUESTS FOR CHANGES

As mentioned earlier, consumer representatives have been active participants throughout the drafting process, and have requested, both at the meetings and in writing, dozens of changes to Article 2B. While space constraints do not permit us to examine each of the requested changes here, it is illustrative for purposes of example only to review the response of the drafting process to a set of fundamental changes which were requested by the Consumers Union in June, 1996. In a letter to the Drafting Committee, Gail Hillebrand of the Consumers Union stated:

The most important areas where we seek improvement in Article 2B are: 1) the addition of a simple statutory mechanism for a full refund for nonconforming software; 2) a higher dividing line between mass market and other licenses; 3) improved treatment of unexpected terms which are standard in the industry; 4) elimination of the partial preemption of

44. See U.C.C. § 2B-607, Reporter's Notes (Proposed Draft, Sept. 25, 1997).

45. *Id.*

46. *Id.* The Reporter's Notes state that this tender rule does not mean that the tendered information is in fact perfect, but that it meets the general contract description in light of ordinary expectations and trade use. *Id.* As in Article 2, this rule applies only to tender of a copy and the resulting duty to accept or right to refuse the tender that is the single performance in the transaction. As under current law, however, substantial performance rules apply in reference to on-going performance for both parties, services such as continuous access, and deliveries of a series of copies in an installment contract.

state consumer statutes; and 5) treatment of the merchantability, virus, and non-infringement issues.

Article 2B has responded to these requests as follows:

(1) The Addition of a Simple Statutory Mechanism for a Full Refund for Nonconforming Software

(3) Improved Treatment of Unexpected Terms which are Standard in the Industry

Article 2B now provides a right of full refund for any mass market/shrinkwrap licensee who did not have an opportunity to review the license before paying.⁴⁷ The licensee can seek the refund from one of two sources, the retailer or the manufacturer. This refund right does *not* even require that the software be *nonconforming*. The only prerequisite is that the licensee decline the terms of the license (for any reason or no reason) and return the product. This refund right does not exist in current law, and although it is fairly dramatic to provide a refund right that is not predicated on some defect in the product itself, the Subcommittee finds it to be an appropriate response to the shrinkwrap controversy because it puts the shrinkwrap licensee in exactly the same position as it would have been in had it had the opportunity to review the license before paying.

In addition, as discussed above, the perfect tender rule has been restored for mass market transactions (which encompass all retail consumer transactions).⁴⁸

A. A HIGHER DIVIDING LINE BETWEEN MASS MARKET AND OTHER LICENSES

While it is not clear exactly what was meant by this request, we assume that the request was to provide a meaningful mass market definition and meaningful differences in the treatment between mass market licenses and other licenses. That has been done. Mass market transactions are treated differently from other licenses as described above in this article, from the restoration of perfect tender to heightened disclaimer requirements.⁴⁹

Based upon recent Drafting Committee actions, the definition of mass market transaction will be addressed at the next Drafting Committee meeting. It is expected that there will be a clear bright line dollar cap test. It is very likely that the final version of these sections will result in an expanded concept of mass market transactions.

47. This will cover the bulk of transactions in which consumers are involved.

48. See generally U.C.C. § 2B-607 (Proposed Draft, Sept. 25, 1997).

49. *Id.*

B. ELIMINATION OF THE PARTIAL PREEMPTION OF STATE
CONSUMER STATUTES

As discussed in Section III of this article, although a partial preemption still exists, it has been severely limited in Section 2B-104, which provides that in the case of a conflict between consumer protection laws of any State and Article 2B, the consumer protection law will control except as follows: (1) a requirement that a contractual obligation, waiver, notice, or disclaimer be in writing is satisfied by a record; (2) a requirement that a record or a contractual term be signed is satisfied by an authentication; (3) a requirement that a contractual term be conspicuous or the like is satisfied by a term that is conspicuous in accordance with Article 2B; and (4) a requirement of consent or agreement to a contractual term is satisfied by an action that manifests assent to a term in accordance with Article 2B.⁵⁰

In our opinion, to delete this limited preemption from Article 2B would severely cripple the application of Article 2B in electronic transactions, while gaining no substantive advantage for consumers.

C. TREATMENT OF THE MERCHANTABILITY, VIRUS, AND NON-
INFRINGEMENT ISSUES.

It is unclear to the authors what changes are being proposed. The Drafting Committee has reviewed each of the areas and has taken the following actions:

As discussed earlier, with respect to merchantability, § 2B-403(b) restores the requirement that a computer program and any physical medium containing the program must, at a minimum, pass without objection in the trade under the contract description.

The Drafting Committee recently voted to delete proposed § 2B-311 dealing with virus protection because of the inability of the Drafting Committee members to reach a consensus on the proper risk allocation between the licensor and licensee. Virus protection is a complex issue. While dealing with the introduction of viruses into physical media, such as diskettes, is somewhat straightforward, it is much more complicated to determine what the rights and liabilities should be in cyberspace, where many people (known and unknown) may have access to information and, accordingly, viruses can be introduced at many different points, sometimes by third parties not even involved in the transaction.

Finally, with respect to the warranty of non-infringement, the Drafting Committee when faced with a choice between a "reason to know" standard or a more absolute assurance, by a unanimous vote, elected to adopt the more absolute assurance approach to this warranty in parallel with comparable language in the proposed redraft of Article 2.

50. See U.C.C. § 2B-104 (Proposed Draft, Sept. 25, 1997).

V. CONCLUSIONS AND RECOMMENDATIONS

The current draft of Article 2B affords more protections for consumers than any existing commercial statute.⁵¹ The ABA Subcommittee, attempted to answer the following policy question posed by the Reporter in his Issues Paper: Should Article 2B adopt new consumer protections or retain a posture of leaving current consumer law largely intact while providing some additional protections?

We concluded that Article 2B should retain a posture of leaving consumer law essentially intact, while adding some enhanced protection where the subject matter or specific industry practices indicate that additional protection is needed, and where doing so would not violate the fundamental themes of the Draft as a commercial code—(1) to support contractual choice and “freedom of contract” and (2) to provide a useful and usable commercial framework for the rapidly expanding information industry.⁵²

As members of the ABA Subcommittee, we concur with this conclusion, and note that the enhanced consumer and mass market protections which have been provided for in Article 2B have been added at no small price in terms of complicating the statute, and limiting in many of these cases, contractual choice, but we support these enhanced protections in these cases because we find those limitations to be reasonable based upon the foregoing analysis and will continue to review future changes in similar fashion.

We all should have an interest in preserving the keystone of the U.C.C., freedom of contract. We also should champion a fair and rational balancing of benefits, costs, and risks to avoid creating expensive but illusory protections.

Finally, we close by noting that, despite the dire predictions of some, and at risk of subjecting ourselves to the amused raised eyebrows of our colleagues, the drafting process appears to us to be working much as it should be. As noted in the Ring Memorandum:

Every interest must go away somewhat unhappy about particular provisions, but all must be happy in part with the improvements made overall and on balance. The Conference should undertake to improve the law to the extent a consensus can be maintained but leave to agreement and developing common law or other law the areas where policies

51. See Appendix A hereto which contains a chart prepared by the Reporter and appended to the Draft comparing consumer treatment under Article 2B with consumer treatment under existing law.

52. In its Briefing Paper, the Subcommittee stated that it had examined each of the protections which had been added and found them to be appropriate in light of this method of analysis, and that with respect to the changes which have not been included in Article 2B, that there were sound policy reasons, also based upon the above analysis, for not including them.

differences made impossible the formulation of a choice that will be embraced by all interest groups.⁵³

The art of legislative politics is the ability to compromise and to build broad consensus. There is a danger in becoming too rigid in the good faith defense of policies and proposals that are impractical, legislatively impossible, or solutions in search of problems. A strategy of disregard for this need to compromise will foster an atmosphere that will discount otherwise important positions and result in a disservice to the very groups such interested parties are trying to represent.

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This corresponds with lessons taught to us as young lawyers that the perfect result is one that no one is either completely satisfied with or dissatisfied enough with to abort. We suggest that that is exactly what is happening with Article 2B.

Very few of the groups and individuals participating in the drafting process are completely satisfied with the treatment their positions have received. This is true for the information industry, consumer and business users. Notwithstanding the foregoing, it is clear that most of the participants and the policy or interest groups they represent, have been willing to engage in reasonable compromises to fashion an article that they can support. None of the positions adopted by the Drafting Committee to date tilts the risk/benefit or cost/benefit analysis to require any interested groups to oppose the proposed article. It is our belief that, when the final draft of Article 2B is accepted by NCCUSL and the ALI, it will be actively supported by most of the drafting process participants and will be embraced by the State legislatures. After years of attempting to negotiate and litigate information transactions in a legal vacuum, we are hungry for a law that, even if imperfect, will assist us in answering our clients questions. The only real unacceptable result would be for the statute to fail due to the disappointment of a few groups with a few provisions.

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53. Ring Memorandum, *supra* note 10.

discount otherwise important positions and result in a disservice to the very groups such interested parties are trying to represent. The authors call upon all interested parties to reaffirm the spirit of compromise and fair dealing that has marked the Article 2B drafting process. It is time for all parties to work together to fashion a statute that balances the needs of all interested parties in a fair and equitable way.