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TEAR-ME-OPEN SOFTWARE LICENSE AGREEMENTS: A UNIFORM COMMERCIAL CODE PERSPECTIVE ON AN INNOVATIVE CONTRACT OF ADHESION*

I. INTRODUCTION

A. THE DEVELOPMENT OF THE TEAR-ME-OPEN AGREEMENT

The introduction of powerful low-cost microcomputers has resulted in the development and mass marketing of inexpensive, ready to use software by the software industry for use in personal computers.¹ The market for such software is large, lucrative, and rapidly expanding.²

In order to protect intellectual property rights in the software they produce,³ and to limit their liability for defective software, software developers are attempting to establish contracts which will govern the software transactions between themselves and their customers in the

* National Third Place, Third Annual Computer Law Writing Competition.

1. A whole new software industry has developed around the personal computer. Instead of programs being customized for individual users, the marketed programs tend to be standardized and designed to meet common purchaser needs. The computer programs that are currently marketed are varied and include programs for video games, programs for automatic flight systems, and programs for business planning. The basic idea is to allow a computer owner who has neither the time, the skill nor the inclination to write or pay for his or her own customized programs to obtain sophisticated, easy to operate programming at a relatively low price.

Note, *Software Piracy and the Personal Computer: Is the 1980 Copyright Act Effective?*, 4 COMPUTER L.J. 171, 173 (1983).

2. See THE COMPUTERWORLD SOFTWARE BUYERS' GUIDE, Vol. 7 (Dec. 1983) (This publication contains about 10,000 products from 3200 vendors and by no means includes every software product or vendor in the United States.); McComas, *The Hard Sell Comes to Software*, 110 FORTUNE 59 (Sept. 17, 1984). (The market for microcomputer software in the business environment, mainly spreadsheet analysis, word processing, and data base management will reach \$1.8 billion in sales in 1984 and is expected to double by 1988.); Toong & Gupta, *A New Direction in Personal Computer Software*, 72 PROC. IEEE 377, 378 (Mar. 1984) (Whereas customized software for small systems is typically priced between \$500 and \$5000, home oriented software is usually priced under \$50. Between these two extremes are the general business packages such as VisiCalc, VisiPlot, and Lotus 1-2-3.).

3. See generally Brooks, *Shrink-Wrapped License Agreements: Do They Prevent the Existence of a "First Sale"?*, 1 COMPUTER LAW. 17 (1984).

mass market. Logistical problems exist in obtaining signed agreements from purchasers in the mass market.⁴ Therefore, software developers are using so-called "tear-me-open" agreements to accomplish their goals.

A tear-me-open agreement consists of a printed agreement placed on the outside of a computer diskette or cassette package which is then shrink-wrapped under transparent cellophane.⁵ The written terms of the agreement are legible through the cellophane, enabling the potential customer to read the contract without opening the wrapper. The writing contains a notice indicating that if the shrink-wrap is removed, the purchaser is bound by the terms of the putative agreement.⁶

The typical tear-me-open agreement contains the following provisions:⁷

- 1) A "license agreement" which permits the purchaser/licensee/tearer⁸ to use the software on one computer only. The customer is permitted to copy the software for archival or backup purposes and may merge it or parts of it into other programs. A copyright notice must appear on all such copies. The customer may transfer the software to another user provided the other user agrees to the terms of the original agreement.⁹ If the first customer transfers the program, he or she must destroy all copies of the program remaining in his or her possession. The license is terminated by non-compliance with any of the terms of the agreement. The duration of the license is indefinite, but on termination the licensee must destroy all copies of the software in his or her possession.
- 2) A limited warranty, in which the developer warrants that the

4. Software for microcomputers is usually distributed via a network of publishers, distributors, dealers, and retailers, and often by mail-order. J.T. SOMA, *COMPUTER TECH. AND THE LAW* 89-90 (1983).

5. Brooks, *supra* note 3, at 19.

6. IBM's tear-me-open agreement contains the following notice: "YOU SHOULD CAREFULLY READ THE FOLLOWING TERMS AND CONDITIONS BEFORE OPENING THIS DISKETTE PACKAGE. OPENING THIS DISKETTE PACKAGE INDICATES YOUR ACCEPTANCE OF THESE TERMS AND CONDITIONS. IF YOU DO NOT AGREE WITH THEM, YOU SHOULD PROMPTLY RETURN THE PACKAGE UNOPENED; AND YOUR MONEY WILL BE REFUNDED."

7. This is based on IBM's tear-me-open software license agreement found accompanying such packages as DisplayWrite 2 and Disk Operating System.

8. As this Note will demonstrate, it is not clear whether the tear-me-open agreement results in an outright sale, lease, or license of the software. This Note will refer to the tearer of the shrink-wrap as the "customer" or "purchaser" in order to prevent any confusion in this regard.

9. Some agreements prohibit any transfer of the software to third parties. See Cooper, *Forming and Enforcing "Tear Me Open" Licenses*, *PRACTISING L. INST. COMPUTER LAW* 4 (Nov. 1983).

cassette or diskette is free from defects in materials or workmanship. The duration of this warranty is limited.¹⁰ The software contained on the disk is expressly provided "as is" with no warranties. Implied warranties of merchantability and fitness for a particular purpose are expressly disclaimed.

- 3) Remedies available to the customer are limited to replacement of disks not meeting the warranty standards or a refund of the purchase price of the software.
- 4) A choice of law clause stating that the agreement will be governed by the laws of a particular state.¹¹
- 5) A merger clause stating that the writing is the complete and exclusive agreement between supplier and customer.
- 6) A warranty registration card which must be returned to the supplier. Some software suppliers attempt to obtain acknowledgement of the terms of the agreement by means of this warranty registration card which must be returned to the supplier for any warranty terms to be effective.¹²

After demonstrating that the software purchase transaction is best analyzed from a Uniform Commercial Code (UCC) perspective,¹³ this Note will examine the enforceability of the warranty disclaimer terms, limitation of remedies, choice of law terms, and merger clause from a UCC perspective. While state and federal consumer protection laws are obviously relevant to tear-me-open agreements, a survey and analysis of the impact of such laws is beyond the scope of this Note.¹⁴ Copyright aspects will not be covered except where they are helpful to the analysis of the above topics.¹⁵

B. THE COST OF RETURNED GOODS: SOFTWARE VERSUS OTHER GOODS

The concept of warranty disclaimers offered in connection with consumer goods on a take-it-or-leave-it basis is not a new one. Manufacturers frequently attempt to limit their liability through the use of legal limitations. These limitations include limited warranties; warranty disclaimers and limitations of remedies printed on packages, labels, and containers;¹⁶ warranty cards to be mailed in by the consumer;¹⁷ and

10. The period of IBM's warranty is 90 days.

11. IBM's agreement specifies that Florida law governs.

12. Brooks, *supra* note 3, at 19.

13. See *infra* notes 36-81 and accompanying text.

14. Magnuson-Moss Warranty Act - Federal Trade Commission Improvement Act, 15 U.S.C. §§ 2301-2312 (1982). This Act sets minimum standards for the content and for consumer remedies.

15. For a discussion of the copyright aspects of tear-me-open agreements, see generally Brooks, *supra* note 3.

16. See, e.g., Hill v. BASF Wyandotte Corp., 696 F.2d 287 (4th Cir. 1982); Monsanto

warranty disclaimers printed in owners manuals and instruction booklets.¹⁸ In these cases the purchaser can reject the offered terms by returning the goods for a refund of the purchase price. Despite the apparent similarities between these agreements and tear-me-open agreements, the nature of computer software is such that tear-me-open agreements pose some unique analytical problems.

The manufacturer of non-software goods suffers a minimal loss if a purchaser returns the product after inspecting it and its limited warranty. The manufacturer recovers the product and the consumer recovers the purchase price, provided the consumer has not damaged the goods. This is not true in the case of computer software in the mass market.

Unless prevented from doing so, the consumer can easily copy the contents of the disk before returning it to the manufacturer for a refund. By doing so, the consumer receives the products of the software producer's labors and intellectual efforts without paying for them. The warranties offered by the software producer are extremely limited and offer the consumer little protection. Therefore, the consumer who purchases the software and obtains its limited warranties and remedies is in a similar position to a person who steals the software and receives no warranties or remedies.¹⁹ Because consumers seem to be indifferent about purchasing the software and receiving limited warranties or copying the software and receiving no warranties, software producers have attempted to use the protective cellophane wrapper and the tear-me-open agreement to protect themselves. The cellophane wrapper protects the producer because once the cellophane is removed, the purchaser is deemed to have accepted the agreement which prohibits copying.

Tear-me-open software agreements thus pose an unusual problem for courts faced with the question of whether or not to enforce them. Conventional analysis of standard form agreements may not provide satisfactory answers. This Note will use the UCC and classical contract analysis to predict and suggest ways in which courts might handle the issue of enforcement of the warranty and remedy terms of tear-me-open agreements.

Agric. Prod. Co. v. Edenfield, 426 So. 2d 574 (Fla. Dist. Ct. App. 1982); Pennington Grain & Seed v. Tuten, 422 So. 2d 948 (Fla. Dist. Ct. App. 1982); Pfizer Genetics v. Williams Management, 204 Neb. 151, 281 N.W.2d 536 (1979); Willoughby v. Ciba Geigy Corp., 601 S.W.2d 385 (Tex. Civ. App. 1979).

17. See, e.g., Van Den Broeke v. Bellanca Aircraft Corp., 576 F.2d 582 (5th Cir. 1978).

18. See, e.g., Taterka v. Ford Motor Co., 86 Wis. 2d 140, 271 N.W.2d 653 (1978); Schroeder v. Fageol Motors, 86 Wash. 2d 256, 544 P.2d 20 (1975); Dougall v. Brown Bay Boat Works & Sales, 287 Minn. 290, 178 N.W.2d 217 (1970).

19. See *supra* notes 10-12 and accompanying text.

II. APPLICABILITY OF THE UCC TO TEAR-ME-OPEN SOFTWARE AGREEMENTS

A. SOFTWARE AS GOODS

In analyzing the effect of particular terms in the tear-me-open agreements, the first step is to determine whether or not the UCC governs the transaction.²⁰

Off-the-shelf computer software transactions in the mass market differ from many other computer software transactions. They are not incident to any sale or lease of hardware,²¹ nor are they a part of data processing services,²² and they do not involve custom designed software.²³ Software transactions involving tear-me-open agreements simply involve computer programs fixed in a material medium such as a diskette or cassette.²⁴

Article 2 of the UCC applies broadly to "transactions in goods."²⁵ Thus, in order to fall under the UCC, software must be categorized as "goods."²⁶ Initially, computer software, however, appears to defy legal

20. U.C.C. § 2-314(a) implies a warranty of merchantability, while U.C.C. § 2-315 implies a warranty of fitness for a particular purpose. U.C.C. §§ 2-302 and 2-316 impose limitations on warranty disclaimers. If the tear-me-open transaction is not governed by the U.C.C., customers acquiring defective software through such agreements would most probably have to rely on negligence theories in order to recover damages caused by the defects.

21. See, e.g., *Jaskey Fin. & Leasing v. Display Data Corp.*, 564 F. Supp. 160 (E.D. Pa. 1983) (contract for the sale of computer equipment, programming, and installation services within the scope of the U.C.C.); *Chatlos Sys. Inc. v. Nat'l Cash Register Corp.*, 479 F. Supp. 738 (D.N.J. 1979), *aff'd*, 635 F.2d 1081 (3d Cir. 1980) (purchase of hardware and software was found to be subject to the implied warranties found in the U.C.C. Article 2); *Triangle Underwriters, Inc. v. Honeywell Inc.*, 457 F. Supp. 765 (E.D.N.Y. 1978), *rev'd on other grounds*, 604 F.2d 737 (2d Cir. 1979) (the fact that software is intangible does not mean it is not "goods" as defined by U.C.C. § 2-106); *Suntogs of Miami, Inc. v. Burroughs Corp.*, 433 So. 2d 581 (Fla. Dist. Ct. App. 1983) (purchase of a computer system consisting of hardware and software was covered by the U.C.C.); *Kalil Bottling v. Burroughs Corp.*, 127 Ariz. 278, 619 P.2d 1055 (Ariz. Ct. App. 1980) (contract for the sale of computer hardware and software fell under the U.C.C.).

22. See *Computer Servicenters, Inc. v. Beacon Mfg. Co.*, 328 F. Supp. 653 (D.S.C. 1970), *aff'd*, 443 F.2d 906 (4th Cir. 1970), (contract for the performance of data processing services was not governed by the U.C.C.).

23. See *supra* note 21 (most of the cases in note 21 involve custom designed software).

24. Off-the-shelf software is sold in package form with no service backup. The user merely loads it into a computer and runs it. See Goldberg, *Software Protection and Marketing*, 2 PRACTISING LAW INST. COMPUTER LAW at 62-63 (1983).

25. U.C.C. § 2-102.

26. *Id.* This is not always the case. Article 2 of the U.C.C. may be applied to service contracts where "application is suitable by analogy." See *Vitromar Piece Dye Works v. Lawrence of London, Ltd.*, 119 Ill. App. 2d 301, 256 N.E.2d 135 (1969).

categorization.²⁷ A computer program is, in essence, information directing a computer to execute certain operations.²⁸ The value of a computer program thus lies in the intangible information it conveys.²⁹ A computer program, however, must be encoded on some material medium in order for it to exist outside of the mind of the programmer.³⁰ Computer software encoded in a magnetic disk, tape, punch cards, or read only memory possesses the features necessary to make it a "good" under UCC Article 2, sections 2-102 and 2-105. Section 2-105 defines "goods" as: "all things (including specially manufactured goods) which are moveable at the time of identification to the contract for sale" The tangible embodiment of a computer program on a disk, tape, printout, or other storage medium is certainly a "thing" and is clearly moveable, whether in the form of storage medium or electronic data transmission.³¹ For this reason, ready made computer software should be regarded as "goods" for the purposes of a UCC analysis.³²

Using the above analysis, it is hard to see how mass-marketed software could be regarded as a service rather than a good.³³ Any confusion over whether such software is a good or a service may arise because computer software production is labor intensive.³⁴ Furthermore, in the past, most computer-software-related-litigation involved custom-written software,³⁵ computer service bureaus, or data processing companies.³⁶ The intangibility of intellectual property may also present conceptual problems in this area.³⁷

27. Note, *Computer Programs as Goods Under the U.C.C.*, 77 MICH. L. REV. 1149 (1979).

28. *Honeywell, Inc. v. Lithonia Lighting, Inc.*, 317 F. Supp. 406, 408 (N.D. Ga. 1970). ("[S]oftware denotes the information loaded into the machine and the directions given to the machine . . . as to what it is to do and upon what command.").

29. The trial court in *Triangle Underwriters, Inc. v. Honeywell, Inc.*, 457 F. Supp. 765, 769 (E.D.N.Y. 1978), *rev'd on other grounds*, 604 F.2d 737 (2d Cir. 1979), acknowledged that the purchaser of computer software is buying the product of ideas or concepts. Thus, the value of software, for which consumers will pay, must lie in those ideas or concepts.

30. Program disks indisputably involve ideas and their expression, but they are, and must be, in tangible form. Brooks, *supra* note 3, at 20.

31. Note, *supra* note 27, at 1152.

32. *See id.* at 1150; Brooks, *supra* note 3, at 20.

33. "Service" usually involves labor supplied for a price. "[A] 'service' is not property—tangible or otherwise. Rather it is an act. . . ." *Indiana Dept. of State Revenue v. Cable Brazil, Inc.*, 177 Ind. App. 450, 460, 380 N.E.2d 555, 561 (1978) (deciding whether supply of electricity is goods or services; software may be in the form of electrical impulses travelling along a wire for the purposes of data transmission).

34. Goldberg, *supra* note 24, at 27-28.

35. *See, e.g., Burroughs Corp. v. Hill Affiliates, Inc.*, 423 So. 2d 1348 (Ala. 1982).

36. *See, e.g., Computer Servicers, Inc. v. Beacon Mfg. Co.*, 328 F. Supp. 653 (D.S.C. 1970), *aff'd*, 443 F.2d 906 (4th Cir. 1971).

37. This confusion is well resolved by the trial court's statement in *Triangle Underwriters, Inc. v. Honeywell, Inc.*, 457 F. Supp. 765, 769 (E.D.N.Y. 1978), *rev'd on other*

B. SALE OR LICENSE AGREEMENT?

Even though ready-made computer software is easily categorized as goods under the UCC, this alone does not mean that the tear-me-open transaction is governed by Article 2 of the UCC³⁸ Article 2 of the UCC is entitled "Sales." The Code defines a "sale" as "the passing of title from the seller to the buyer for a price."³⁹ It can be surmised from the provisions of the typical tear-me-open software agreement that the drafters do not intend to convey title of the software to the purchaser.⁴⁰ Therefore, the agreement is styled as a "license agreement," rather than as a "sale." In fact the word "sale" is never mentioned in IBM's license agreement.⁴¹ The fact that full title may not have passed to a customer acquiring software which contains a tear-me-open agreement should not, however, preclude application of the UCC to the transaction.

The tear-me-open agreement purports to grant the purchaser a license to use the accompanying software. It is not, however, clear exactly what "license agreement" means in the context of tear-me-open agreements.⁴² License agreements are commonly used in the computer trade when large systems and custom-written software are involved.⁴³ Courts have generally treated these as lease agreements,⁴⁴ which are fully paid up at the beginning of the term.⁴⁵ But in the case of mass marketed software, the term is indefinite.

Although Article 2 of the UCC is entitled "Sales," courts have applied it to non-sale transactions such as leases and bailments.⁴⁶ The rationale for this is based on the use of the word "transactions" in Article

grounds, 604 F.2d 737 (2d Cir. 1979). "Although the ideas or concepts involved in the custom designed software remained Honeywell's intellectual property, Triangle was purchasing the product of those concepts. That product required effort to produce, but it was a product nevertheless and, though intangible, is more readily characterized as 'goods' than 'services.'" *But see* 4 THE SCOTT REPORT 1, 4 (July 1984) (identification of intellectual property with "services").

38. Article 2 of the U.C.C. may be limited to sales only. The transaction under consideration is styled as a "license agreement" as opposed to a "sale."

39. U.C.C. § 2-106(1).

40. Cooper, *supra* note 9, at 5.

41. *Id.*

42. *Id.*

43. Goldberg, *supra* note 24, at 60.

44. Holmes, *Application of Article Two of The Uniform Commercial Code to Computer System Acquisitions*, 8 RUTGERS COMPUTER TECH. L.J. 1, 25 (1982).

45. *See, e.g., Vitromar Piece Dye Works v. Lawrence of London Ltd.*, 119 Ill. App. 2d 301, 256 N.E.2d 135 (1969).

46. W. HAWKLAND, UNIFORM COMMERCIAL CODE SERIES § 2-102:1; *see also* Annotation, *Application of Warranty Provisions of Uniform Commercial Code to Bailments*, 48 A.L.R. 3d 668 (1973).

2, section 2-102.⁴⁷ This term is not defined within Article 2 and arguments have been made that the word "transactions" encompasses contracts other than sales.⁴⁸ Some courts have applied Article 2 to transactions in goods not involving a sale by analogizing the transaction to a sale.⁴⁹ Courts will also treat the transaction as a sale if the policies underlying the UCC section to be applied are reasonably applicable to the non-sale situation.⁵⁰ An important factor in this policy argument is the degree of similarity between the non-sale transaction and an actual sale.⁵¹

The license agreement under consideration in this Note is similar to a sale. Although the licensor does not intend the licensee to get full title to the software,⁵² the licensor gives the licensee a right to use and dispose of the software subject to certain conditions.⁵³ The licensee views the transaction as a conditional sale. The conditions involved are similar to those which publishers of books and musical recordings impose in order to preserve their copyright.⁵⁴ The conditions used by publishers are substantially the same as the provisions of the Copyright Act pertaining to the sale of media containing copyrighted material.⁵⁵ In fact some tear-me-open agreements explicitly state that the "purchaser" owns the disk, not the program on the disk.⁵⁶

C. TEAR-ME-OPEN AGREEMENTS AS SALES

As indicated above, courts have given conflicting opinions as to the

47. Annotation, *What Constitutes a Transaction, a Contract for Sale or a Sale Within the Scope of U.C.C. Article 2*, 4 A.L.R. 85, 91 (1981).

48. Nycum, *Liability for Malfunction of a Computer Program*, 7 RUTGERS COMPUTER TECH. L.J. 1, 3 (1979).

49. W. HAWKLAND, *supra* note 46, § 2-102:1. See generally Annotation, *supra* note 46, at 668.

50. *Id.* See generally Annotation, *supra* note 46.

51. See, e.g., *W.R. Weaver Co. v. Burroughs Corp.*, 580 S.W.2d 76 (Tex. Civ. App. 1979) (the court relied on the economic equivalency between a sale and the transaction in question to place the transaction within the UCC).

52. The licensor views the transaction as a license, and title does not pass in a license agreement.

53. See *supra* text accompanying notes 8-9.

54. Most paperbacks contain a notice similar to the following: "All rights reserved. No part of this book may be reproduced or utilized in any form, by any means, electronic or mechanical, including photocopying, recording, or by any information storage and retrieval system without permission in writing from the publisher." Musical recordings contain a notice similar to the following: "All Rights Reserved. Unauthorized duplication is a violation of applicable laws."

55. 17 U.S.C. § 202 (1978). See also *Stephens v. Cady*, 55 U.S. (14 How.) 528 (1853) (buyer of a map does not acquire the right to print the map).

56. Brooks, *supra* note 3, at 17.

applicability of Article 2 to non-sale transactions.⁵⁷ In the case of tear-me-open agreements, the issue may be resolved by a finding that the agreement is completely unenforceable due to the manner in which the contract was supposedly formed.⁵⁸ If the agreement is found to be unenforceable, courts would have to supply the contract terms based on the conduct and intent of the parties.⁵⁹ The consumer's intent would most likely be the outright purchase of the software. The software producer's intent would probably not be an outright sale, at least to the extent that it would deprive the software producer of the right to prevent copying of the software.⁶⁰ The producer's fear of losing the copyright is unfounded because the fact that there has been a sale for UCC purposes (i.e., for the use of UCC warranty theories) does not necessarily mean that the purchasers are owners of the copyright.⁶¹

D. TEAR-ME-OPEN AGREEMENTS AS ANALOGIES TO SALES

Analogizing transactions involving tear-me-open license agreements to sales is an additional method to have Article 2 of the UCC govern. If the license is found to be a lease or bailment, policy may require that it be governed by the UCC⁶²

Courts, however, should interpret these license agreements as sales and not leases or bailments due to several factors. These factors include the rule that ambiguous contracts should be construed against the drafter, the fact that the transaction is economically equivalent to a sale, and the fact that courts traditionally disfavor terms limiting the use and disposition of property by "purchasers." A corollary to this would be to regard the license agreement as a conditional sale. The conditions would be acceptance of terms disallowing copying the software.⁶³

As a result of the numerous ways in which a transaction in ready made software can be placed within the scope of the UCC, this Note

57. Annotation, *supra* note 47, at 91.

58. See *infra* notes 64-92 and accompanying text.

59. See *supra* note 3 and accompanying text.

60. *Id.*

61. Brooks, *supra* note 3, at 21; ("license is an intellectual property notion, not a tangible property notion").

62. Hertz Commercial Leasing Corp. v. Transp. Credit Clearinghouse, 59 Misc. 2d 226, 298 N.Y.S.2d 392, 395 (1969), *rev'd on other grounds*, 64 Misc. 2d 910, 316 N.Y.S.2d 585 (App. Div. 1970) (In finding that a lease fell under the U.C.C., the court stated: "[I]t would be anomalous if this large body of law were subject to different rules of law than other transactions which tend to achieve identical economic results."). See also Baker v. City of Seattle, 70 Wash. 2d 198, 484 P.2d 405 (1971). *But see* Bona v. Graefe, 264 Md. 69, 285 A.2d 607 (1970) (warranty provisions of the UCC were not applied to a lease).

63. R. ANDERSON, UNIFORM COMMERCIAL CODE § 2-204, 47 (3d ed. 1982). See also U.C.C. § 2-615.

concludes that the transaction is best analyzed under the provisions of the UCC.

III. FORMATION OF THE AGREEMENT

As a result of the unusual nature of the acceptance specified in the tear-me-open agreement, courts might find that no binding contract results from the agreement. Such a finding would obviously render the warranty disclaimers and limitations of remedy inoperative.⁶⁴

There are two probable methods in which customers would obtain software accompanied by tear-me-open agreements. The most common occurs when the customer obtains the software from a computer store.⁶⁵ The other method is by mail order.⁶⁶ In both situations, an issue arises as to the validity of the specified mode of acceptance of the license agreement.

It is easy to imagine the circumstances surrounding the acquisition of the typical tear-me-open agreement. In the over-the-counter situation the following is likely to occur. The customer chooses the software he or she wants without reading the license agreement. He or she pays for and takes the software home or to his or her office to run on his or her computer. In his or her eagerness to use the newly acquired package he or she tears open the shrink wrap, not expecting to be bound by any contract in doing so. At some stage the license agreement tumbles out and the unfortunate licensee discovers its terms. If the customer actually notices the agreement before tearing open the wrapper, he or she probably ignores it or at best makes a mental note to read it later. A similar process most likely occurs in the case of acquisition by mail order.

It is of course possible that the actual agreement took place in the store where the customer first took possession of the software in return for money.⁶⁷ Assuming that this is not the case, the issue becomes whether or not the tear-me-open offer is actually accepted.⁶⁸

To form an agreement, a "manifestation of mutual assent on the part of two . . . persons" is required.⁶⁹ Assent need not be in words, but may be manifested by conduct.⁷⁰ The party engaging in such conduct,

64. The following analysis of the validity of the process of offer and acceptance will also be helpful in determining whether the disclaimers of warranty and limitation of remedies are part of the bargain between the software customer and the software producer.

65. Cooper, *supra* note 9, at 1.

66. *Id.*

67. See *infra* notes 89 and 92 and accompanying text.

68. In this Note, offer and acceptance will be discussed without special reference to the UCC as the UCC does not deal in any great detail with the formation of contracts.

69. RESTATEMENT (SECOND) OF CONTRACTS § 3 (1979).

70. *Id.* § 19(1).

however, must know or have reason to know that the other party may infer assent from his or her conduct.⁷¹ Whether a party has reason to know this is a question of fact, to be determined by the circumstances of the case and by the person involved.⁷² The critical issue in contract formation is not assent, but what the other party is justified in regarding as assent.⁷³ It has been suggested that a reasonable person standard be used in determining whether or not there is acceptance.⁷⁴

Whether it is reasonable to believe that tearing open a wrapper is manifestation of the acceptance of an offer is debatable. Perhaps a reasonable software purchaser should be held to know that the act of tearing open a cellophane wrapper constitutes acceptance of an offer. Courts, however, could determine that the software customer, acting in his or her own interests, should examine and read the outside of a software packet. The customer would therefore be charged with knowledge of the offer and that tearing open the wrapper is its specified mode of acceptance.⁷⁵ The conspicuousness or legibility of the writing is clearly an important factor in the objective determination of the offeree's knowledge.⁷⁶

Corbin prophetically raised a closely analogous issue in the analysis of the situation in which an offeror attempts to infer acceptance from some ordinary act of the offeree that the offeree does not wish to be an acceptance.⁷⁷ If tearing open a shrink-wrapped package containing a newly acquired software program is an ordinary act which the customer does not intend to be an acceptance, then the offer is not accepted by that act. The unusual specified mode of acceptance and the lack of conspicuousness of the notice are strong arguments against the formation of a contract. This argument does not, however, dispose of the issue. Acceptance of the offer may be found by other means.

It is possible that the offeror's specification of tearing open the wrapper as a manifestation of acceptance is not crucial to the accept-

71. *Id.* § 19(2).

72. *Id.* § 19(2) comment b.

73. S. WILLISTON, *CONTRACTS* § 35 (1957).

74. *Id.* at § 94.

75. The following principle would then apply: "It will not do for a man to enter into a contract, and, when called on to respond to its obligations, to say that he did not read it when he signed it, or did not know what it contained." *Upton v. Tribilock*, 91 U.S. 45, 50 (1875).

76. S. WILLISTON, *supra* note 73, § 90C.

77. 1 A.L. CORBIN, *CONTRACTS* § 73 (1951)

(If A offers his land to B for a price, saying that B may signify his acceptance by eating his breakfast or hanging out his flag on Washington's birthday or by attending church on Sunday, he does not thereby make such an action by B operative as an acceptance against B's will. . . .)

ance of the offer. It may not be crucial as a result of two points. First, the offeree may be deemed to have accepted the offer by his or her silence⁷⁸ or exercise of dominion over the goods.⁷⁹ Second, the acceptance may be deemed to have occurred at the computer store with the tear-me-open agreement being a post-sale modification of the contract which may or may not be binding.⁸⁰

Based on the above analysis, the tear-me-open mode of acceptance may be found to be invalid.⁸¹ This may mean that the customer is free to open the software package without incurring any obligation. On the other hand, acceptance of the license agreement may be found in the offeree's silence or failure to return the goods.⁸²

Silence is an unusual form of acceptance⁸³ and might pose problems in this situation. Ordinarily, silence as a mode of acceptance should be stated in the offer, or the offeree should have reason to understand that silence or inaction is a manifestation of assent.⁸⁴ Once again, this hinges on whether the terms of the printed agreement and their conspicuousness would give the offeree reason to believe he or she had accepted the offer.⁸⁵ Allowing the offeree to open the shrink-wrap clearly defeats the drafters' objective of prohibiting copying. Furthermore, if the offeree is free to return the software for a full refund after opening it, there is little to stop the offeree from copying it.

Alternatively, the exercise of dominion over the software may be a more effective mode of acceptance. Any act inconsistent with the offeror's ownership of offered property binds the offeree to the offered terms unless they are manifestly unreasonable.⁸⁶ Thus if the software customer keeps the software and uses it,⁸⁷ the customer will be bound by the terms accompanying it,⁸⁸ as long as the terms are not unreasonable.

If the software customer is objectively ignorant of the existence of

78. See *infra* notes 82-85 and accompanying text.

79. See *infra* notes 89-92 and accompanying text.

80. See *infra* notes 86-88 and accompanying text.

81. See *supra* notes 68-77 and accompanying text.

82. RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 69, § 89 (1979).

83. *Id.* § 89 comment a.

84. *Id.* § 69(b).

85. See *infra* note 105 and accompanying text. See also RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 69, § 69 comment c (If there is some element of reliance by the offeror on the offeree's silence, or the offeree objectively manifests some intent to accept, albeit uncommunicated, acceptance is more likely to be found.).

86. RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 69, § 69(2). Compare U.C.C. § 2-606(1)(c).

87. W. HAWKLAND, *supra* note 46, at 2-606:6.

88. See *supra* text accompanying notes 7-11.

the license agreement lurking under the shrink-wrap⁸⁹ and the act of opening the wrapper is not a valid form of acceptance,⁹⁰ the software transaction must have occurred in the computer store when the goods were purchased. Thus, the contract containing the license agreement would only reach the customer after the transaction has taken place and would not form part of the original agreement.⁹¹ Circumstances, however, may lead to the conclusion that the post-sale writing is a modification of the original agreement and may be binding if accepted.⁹²

IV. WARRANTY DISCLAIMERS

The tear-me-open license agreement purports to disclaim all warranties on the software, express or implied.⁹³ The existence of warranties on software is of great importance, because a majority of the public is under the incorrect impression that computers never make mistakes. This impression is not justified by the realities of the computer world. While hardware may be extremely dependable, software is often unreliable.⁹⁴ Software is often put into the marketplace hurriedly and without adequate testing.⁹⁵ Software, moreover, is inherently unreliable⁹⁶ and the consequences of this unreliability may be serious. Personal injuries and property damages may even result from software errors.⁹⁷ A considerable amount of litigation has arisen as a result of defects in computer software.⁹⁸

Under the UCC, the implied warranties of merchantability⁹⁹ and fitness for a particular purpose¹⁰⁰ may be disclaimed by proper and conspicuous contract terms.¹⁰¹ Most tear-me-open license agreements satisfy the first requirement by using almost the exact language specified in the UCC.¹⁰² But it is by no means clear that they satisfy the UCC's

89. RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 69, § 19 comment b.

90. *See supra* notes 68-77 and accompanying text.

91. *See* R. ANDERSON, *supra* note 63, § 2-204:29. *See also* Willoughby v. Ciba Geigy Corp., 601 S.W.2d 385 (Tex. Civ. App. 1979).

92. *See* Karczenewski v. Ford Motor Co., 382 F. Supp. 1346, *aff'd mem.*, 515 F.2d 511 (7th Cir. 1975).

93. *See supra* text accompanying notes 7-11.

94. Immel, *Evaluating Software*, 3 POPULAR COMPUTING 43 (Sept. 1984) (There is too much software on the market that does not work properly due to defects.).

95. *Id.*

96. *Id.* at 45.

97. Nycum, *supra* note 48, at 1.

98. *See supra* text accompanying notes 21 and 22.

99. U.C.C. § 2-314.

100. *Id.* § 2-315.

101. *Id.* § 2-316(2).

102. IBM's warranty disclaimer reads as follows:

LIMITED WARRANTY

THE PROGRAM IS PROVIDED "AS IS" WITHOUT WARRANTY OF ANY

conspicuousness requirement.

Actual knowledge of a disclaimer is not required for it to be effective against the buyer, provided the disclaimer is conspicuous.¹⁰³ There is, however, a line of authority which holds that a purchaser must agree to the disclaimer for it to be binding.¹⁰⁴

Under the UCC, a term is conspicuous, "when it is so written that a reasonable person against whom it is to operate ought to have noticed it."¹⁰⁵ Whether a term is conspicuous is a question of law.¹⁰⁶ A strong case can be made that the disclaimer clause in the IBM tear-me-open agreement mentioned above is not conspicuous enough to be effective. Although the typeface of the disclaimer is larger than that of the surrounding text, the surrounding text is very small and may itself be inconspicuous.¹⁰⁷ The entire agreement is not easily noticeable. It is shrink-wrapped onto the back of the box in such a manner that a reasonable person might not notice it.¹⁰⁸

The disclaimers contained in the tear-me-open agreement could be regarded as a post-sale writing which will not affect any warranties made at the time of sale.¹⁰⁹ This argument follows from the fact that the customer only notices the agreement after purchasing the software. Therefore, the agreement was not part of the basis of the bargain and cannot be binding on the purchaser.¹¹⁰

KIND, EITHER EXPRESSED OR IMPLIED, INCLUDING, BUT NOT LIMITED TO, THE IMPLIED WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE. THE ENTIRE RISK AS TO THE QUALITY AND PERFORMANCE IS WITH YOU. SHOULD THE PROGRAM PROVE DEFECTIVE, YOU (AND NOT IBM OR AN AUTHORIZED PERSONAL COMPUTER DEALER) ASSUME THE ENTIRE COST OF ALL NECESSARY SERVICING, REPAIR OR CORRECTION.

103. R. ANDERSON, *supra* note 63, § 2-316:33. See *Architectural Aluminum Corp. v. Macar*, 70 Misc. 2d 495, 333 N.Y.S.2d 818, 822 (N.Y. Sup. Ct. 1972).

104. *Higel v. General Motors Corp.*, 190 Colo. 57, 544 P.2d 983, 989-90 (1975). See also R. ANDERSON, *supra* note 63, § 2-316:25.

105. U.C.C. § 1-201(10). See also *Hunt v. Perkins Mach. Co.*, 352 Mass. 535, 226 N.E.2d 228, 231 (1967) (disclaimer printed in capital letters on the back of the contract was not conspicuous). But see *Architectural Aluminum*, 70 Misc. 2d at 495, 333 N.Y.S.2d at 818 (disclaimer in bold-faced type surrounded by one inch black margin was conspicuous).

106. U.C.C. § 1-201(10).

107. *A & M Produce v. FMC Corp.*, 135 Cal. App. 3d 473, 186 Cal. Rptr. 114 (Cal. Ct. App. 1982).

108. See, e.g., *Willoughby v. Ciba Geigy Corp.*, 601 S.W.2d 385, 388 (Tex. Civ. App. 1979) (disclaimer of warranty printed on the side of a container, not brought to the attention of the purchaser was ineffective); *Pfizer Genetics, Inc. v. Williams Mgmt. Co.*, 204 Neb. 151, 281 N.W.2d 536, 539 (1979).

109. See R. ANDERSON, *supra* note 63, § 2-316:32. See also J. WHITE & R. SUMMERS, *UNIFORM COMMERCIAL CODE* § 9-4 (2d ed. 1980).

110. See *Eichenberger v. Wilhelm*, 244 N.W.2d 691, 697 (S. Dak. 1976) (Where the buyer is given no opportunity to see and read the label, the court will not elevate the disclaimer to the status of a bargain.).

Under the UCC, if the seller makes an express warranty, it may not be disclaimed.¹¹¹ In tear-me-open agreements, it is not easy to find an express warranty on the face of the writing.¹¹² The agreement includes an integration clause which excludes any express warranty which may be made by the supplier.¹¹³

The software itself is fixed on an anonymous mass-produced disk which is concealed in a sealed container. It therefore follows that some description of the goods is needed so that the agreement will not be void for lack of definiteness as to subject matter. Such a description may be found in the software package labels or in the advertising of the software's capabilities.¹¹⁴ It appears, however, that most software producers are careful to make very limited claims as to the capabilities of their products. Thus, even if an express warranty is found from advertising materials, it will probably not offer a great deal of protection as to the quality of the software.¹¹⁵ The descriptive language will merely give rise to a warranty that the programs are of a certain type,¹¹⁶ such as word processing, spreadsheet, or operating system. If the implied warranties of fitness for a particular use¹¹⁷ and merchantability¹¹⁸ are disclaimed, defective programs, unless almost entirely useless, would satisfy the producer's obligations under the express warranty.¹¹⁹ This would follow because the seller merely warrants that the software is something fitting the generic description on the box. There are cases which have upheld integration clauses as excluding all warranties and statements in advertising material which would constitute express warranties.¹²⁰ These cases, however, usually involve agreements reached

111. U.C.C. § 2-316 comment 1.

112. In the case of IBM, the same standard contract is used for a variety of software products such as DisplayWrite 2 and Disk Operating System. The contract contains no mention of the type of software it purports to license.

113. IBM's integration clause reads as follows: "YOU . . . AGREE THAT IT IS THE COMPLETE AND EXCLUSIVE STATEMENT OF THE AGREEMENT BETWEEN US WHICH SUPERCEDES ANY PROPOSAL OR PRIOR AGREEMENT, ORAL OR WRITTEN, AND ANY OTHER COMMUNICATIONS BETWEEN US RELATING TO THE SUBJECT MATTER OF THE AGREEMENT."

114. W. HAWKLAND, *supra* note 46, § 2-313:03 (The tendency under the Code seems to be to hold that most advertising rises to the level of express warranty.). See also *Interco, Inc. v. Randustrial Corp.*, 533 S.W.2d 257 (Mo. App. 1976). But see *Hill v. BASF Wyandotte*, 696 F.2d 287 (4th Cir. 1982) (oral representations by salesperson were not binding as warranties).

115. W. HAWKLAND, *supra* note 46, § 2-313:6.

116. *Id.* at § 2-313:6.

117. U.C.C. § 2-314.

118. *Id.* § 2-315.

119. W. HAWKLAND, *supra* note 46, § 2-313:06.

120. See *Jaskey Finance and Leasing Co. v. Display Data Corp.*, 564 F. Supp. 160 (E.D. Pa. 1983) (disclaimer of express and implied warranties on computer products held effective).

through some bargaining process. Therefore, where the disclaimer and integration clause are offered in circumstances involving no opportunity for bargaining, the opposite result may be reached.¹²¹

Courts could, however, view language such as "supplier warrants that the disk on which the program is embodied is free from defects in materials and workmanship,"¹²² as creating an express warranty. This express warranty would cover the actual software because the customer clearly does not intend to obtain a mere disk through the tear-me-open agreement. The goods which the customer intends to acquire consist of a disk containing a certain program. Although they look the same, a blank disk is different from one which contains a useful program. Thus the "disk" referred to in the limited warranty is the disk bargained for, meaning the one containing software. Defects in workmanship which occur during the production of the disk could also include defects in the programming which led to the altered magnetic properties distinguishing it from an unprogrammed disk.

Another basis for voiding the disclaimer of the implied warranties is the doctrine of unconscionability.¹²³ While the term "unconscionability" is not defined in the UCC and has many interpretations, certain guidelines for its application have emerged from the case law.¹²⁴ The principle behind the doctrine of unconscionability is the prevention of "oppression and unfair surprise."¹²⁵ Unconscionability is a question of law.¹²⁶ The basic test for unconscionability is "whether, in the light of the general commercial background and the commercial needs of the particular trade or case, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract."¹²⁷

tive where the agreement was integrated and the parol evidence rule barred inclusion of advertising material containing alleged express warranties). *See also* Pennsylvania Gas Co. v. Secord Brothers, Inc., 73 Misc. 2d 1031, 343 N.Y.S.2d 256, *aff'd*, 357 N.Y.S.2d 702 (N.Y. App. Div. 1973).

121. *See, e.g.*, Transamerica Oil Corp. v. Lynes, 723 F.2d 758 (10th Cir. 1982); Jaskey Finance and Leasing Co. v. Display Data Corp., 564 F. Supp. 160 (E.D. Pa. 1983).

122. IBM's tear-me-open agreement contains the following "limited warranty": "IBM warrants the diskettes or cassettes on which the program is furnished to be free from defects in materials and workmanship for a period of ninety (90) days from the date of delivery to you"

123. U.C.C. § 2-302 (a court may refuse to enforce any contractual clause which it finds to have been unconscionable at the time it was made).

124. *A & M Produce v. FMC Corp.*, 135 Cal. App. 3d 473, 186 Cal. Rptr. 114 (Cal. Ct. App. 1982) (This case gives a good outline of the elements of unconscionability as applied to the sale of technology in a business environment.). *See also* U.C.C. § 2-302 comment 1.

125. *A & M Produce*, 135 Cal. App. 3d at 484, 186 Cal. Rptr. at 120.

126. *Id.*

127. U.C.C. § 2-302 comment 1. *See also* Leff, *Unconscionability and The Code—The Emperor's New Clause*, 115 U. PA. L. REV. 485, 488 (1967).

Unconscionability involves procedural and substantive elements.¹²⁸ Procedural unconscionability is "bargaining naughtiness,"¹²⁹ while substantive unconscionability relates to "evils in the resulting contract."¹³⁰ Most courts require the presence of both procedural and substantive unconscionability in order to void a contractual clause.¹³¹

Under the UCC, procedural unconscionability is not usually found with respect to warranty disclaimers.¹³² Nevertheless, procedural unconscionability is possible in the case of tear-me-open agreements, because the contract is one of adhesion, offered on a take-it-or-leave-it basis.¹³³ The consumer has no opportunity to bargain for more favorable terms. If the tear-me-open mode of acceptance is valid, the consumer may unwittingly be bound to terms which the customer normally would not accept.¹³⁴ Agreements using the tear-me-open mode of acceptance may thus be regarded as leading to unfair surprise¹³⁵ and lacking meaningful choice¹³⁶ for the customer.

The relative sophistication of the parties is also a factor in determining the existence of procedural unconscionability.¹³⁷ Because computer technology is new to most consumers and businesspeople, they

128. Leff, *supra* note 127, at 487. See also Note, *Unconscionability Redefined: California Imposes New Duties on Commercial Parties Using Form Contracts*, 35 HASTINGS L.J. 161, 164 (1983).

129. Leff, *supra* note 127, at 487. See also Davenport, *Unconscionability and the Uniform Commercial Code*, 22 U. MIAMI L. REV. 121, 138 (1967) (equating procedural unconscionability with the "unfair surprise" language of comment 1 to U.C.C. § 2-302).

130. Leff, *supra* note 127, at 487.

131. *Johnson v. Mobil Oil Corp.*, 415 F. Supp. 264, 268 (E.D. Mich. 1976). See also, Leff, *supra* note 127, at 539.

132. See, e.g., *Avery v. Aladdin Products, Inc.*, 128 Ga. App. 266, 196 S.E.2d 357 (1973) (The court construed the contract strictly with respect to U.C.C. § 2-316, found that the exclusion of all warranties was not unconscionable, and prohibited the admission of parol evidence to prove the existence of any warranty.).

133. An adhesion contract is a standardized contract prepared entirely by one party to the transaction for the acceptance of the other; such a contract, due to the disparity in bargaining power between the drafting party and the second party, must be accepted or rejected by the second on a "take-it-or-leave-it" basis, without opportunity for bargaining and under such conditions that the "adherer" cannot obtain the desired product or service save by acquiescing in the form agreement. *Steven v. Fidelity & Casualty Co.*, 58 Cal. 2d 862, 882, 27 Cal. Rptr. 172, 185, 377 P.2d 284, 297 (1962).

134. See *supra* text accompanying notes 7-12 (terms of the typical tear-me-open agreement).

135. W. HAWKLAND, *supra* note 46, § 2-203:03 (Unfair surprise involves (1) assent obtained by reason of ignorance or carelessness of one party known to the other; (2) assent obtained by signature to forms difficult to read or deceptively arranged.).

136. *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445, 449 (D.C. Cir. 1965) ("Unconscionability has generally been recognized to include an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party.")

137. W. HAWKLAND, *supra* note 46, § 2-302:03.

may be unsophisticated. Vendors are sophisticated and therefore may be in an unfair bargaining position with the consumer.¹³⁸ This is particularly true in the case of tear-me-open agreements where the software producer offers no explanation or warranties to the unsophisticated consumer as to the strengths and weaknesses of the product. The consumer, relying on statements made by salespeople, may end up with useless software. If tear-me-open disclaimers of warranty are upheld, all software manufacturers might offer their products with such agreements. This would remove all opportunity for bargaining for better terms by consumers.

Substantive unconscionability in the case of warranty disclaimers is more difficult to find. The UCC expressly permits parties to disclaim implied warranties of merchantability and fitness for a particular purpose.¹³⁹ Therefore, additional circumstances must exist in order for the warranty disclaimer to be deemed unconscionable.¹⁴⁰ Courts have held that a disclaimer of warranty is reasonable in the case of novel and innovative goods.¹⁴¹ As a result of the inherently novel and innovative nature of software, it may be appropriate to exclude warranties on it. This, however, is subject to the principle that it is unconscionable to limit warranties in such a way as to limit remedies in all respects.¹⁴² The express warranty, which cannot be disclaimed,¹⁴³ may provide sufficient remedy to avoid such a result.

V. REMEDY LIMITATIONS

UCC Article 2, section 2-719 allows parties to a contract to limit the remedies available in the event of a breach¹⁴⁴ by a fair and reasonable agreement.¹⁴⁵ Section 2-719 imposes no requirement of conspicuousness.¹⁴⁶ Nevertheless, some courts have imposed such a requirement.¹⁴⁷

138. The relative "computer literacy" of the parties was important in leading to a finding of unconscionability in *Glovatorium v. National Cash Register Corp.*, No. C-79-3393 (N.D. May 1, 1983), *aff'd on other grounds*, 684 F.2d 658 (9th Cir. 1982).

139. U.C.C. § 2-316.

140. R. ANDERSON, *supra* note 63, at § 2-316:37.

141. *U.S. Fibres, Inc. v. Proctor & Schwartz, Inc.*, 358 F. Supp. 449, 460 (E.D. Mich. 1972), *aff'd*, 509 F.2d 1043 (5th Cir. 1975).

142. *Jacobs v. Metro Chrysler-Plymouth, Inc.*, 125 Ga. App. 462, 188 S.E.2d 250, 253 (1972).

143. U.C.C. § 2-316 comment 1.

144. *Id.* § 2-719.

145. *Id.* comment 1.

146. On its face, U.C.C. § 2-719 contains no conspicuous requirement.

147. *See, e.g., Seibel v. Layne & Bowler, Inc.*, 56 Or. App. 387, 641 P.2d 668 (Or. Ct. App. 1982) (The court lumped U.C.C. § 2-316, which does have a conspicuousness requirement, and U.C.C. § 2-719 together and made a requirement of conspicuousness for the disclaimer of warranty and limitation of remedies.).

Under UCC Article 2, section 2-719, the parties must be left with a minimum adequate remedy.¹⁴⁸ There are three ways in which a remedy limiting clause may be voided by the operation of section 2-719. A limitation of remedies clause may be void if it "fails of its essential purpose,"¹⁴⁹ is unconscionable,¹⁵⁰ or is not part of the bargain between the buyer and the seller.¹⁵¹

Neither the UCC nor the common law offer much explanation of the meaning of "failure of essential purpose."¹⁵² While limitation of remedies to replacement or return of the goods for refund is authorized by the UCC,¹⁵³ such a remedy may fail in its essential purpose if its purpose is to cure nonconformity of the goods supplied.¹⁵⁴

There is a distinct difference between a disclaimer of warranty and a limitation of remedies. The former reduces the obligations of a party in performing the contract, while the latter reduces the liability in the event of a breach.¹⁵⁵ A limitation of remedies must, therefore, be read with reference to the terms of the contract which give rise to the parties' obligations. Whether a limitation of remedies clause fails of its essential purpose will depend upon what was really bargained for in the contract.

The tear-me-open agreement is probably intended to supply computer software which will perform a particular function, determined by either its name or description on the package. For example, the words "Operating System" describe a system which will coordinate memory management, task scheduling, user interface, and peripheral control.¹⁵⁶ In such a case, if the software does not perform those functions, then a remedy which merely requires the supplier to replace the disk embodying the software has clearly failed of its essential purpose. Although the software producer may have successfully disclaimed all implied

148. U.C.C. § 2-719 comment 1.

149. *Id.* § 2-719(2).

150. *Id.* § 2-719(3).

151. See, e.g., *Van Den Broeke v. Bellanca Aircraft*, 576 F.2d 582 (5th Cir. 1978); *Mon-santo Agric. Prods. v. Edenfield*, 426 So. 2d 574 (Fla. Dist. Ct. App. 1982); *Dougall v. Brown Bay Boat Works*, 287 Minn. 290, 178 N.W.2d 217 (1970).

152. Eddy, *On the "Essential" Purposes of Limited Remedies: The Metaphysics of U.C.C. Section 2-719(2)*, 65 CALIF. L. REV. 28, 39 (1977).

153. U.C.C. § 2-719(1)(a).

154. *Kalil Bottling Co. v. Burroughs Corp.*, 127 Ariz. 278, 619 P.2d 1055, 1059 (Ariz. Ct. App. 1980) (In a contract for the purchase of computer hardware and software, an exclusive remedy of repair or replacement fails of its essential purpose when its purpose was to give the seller a chance to make the goods conform and the nonconformity could not be cured by replacement or repair.).

155. W. HAWKLAND, *supra* note 46, § 2-719:02.

156. Toong & Gupta, *supra* note 2, at 378.

warranties, the express warranty, which cannot be disclaimed,¹⁵⁷ would be applicable in the event the software does not perform any of the claimed functions. Programs which do not perform their minimal requirements breach their express warranties, and a remedy should provide a fair quantum of damages.¹⁵⁸ Furthermore, if, in a case involving a tear-me-open agreement, the court finds that the manufacturer gave a more extensive express warranty, as suggested above,¹⁵⁹ a remedy merely requiring replacement, repair, or refund will fail of its essential purpose.

Many limited warranties have a limited time span.¹⁶⁰ In many cases, it could be virtually impossible to discover a defect in the software in such a limited time span, except where the software was wholly and patently useless. The remedy would fail of its essential purpose because it would not provide any means of redress for a defect which could not have been discovered within the time period specified.¹⁶¹

The minimal express warranties which might be found in shrink-wrapped software packages will not benefit the consumer when the quality of the software is at issue.¹⁶² It seems reasonable and just, however, that courts should find some remedy when the software flagrantly fails to perform.

Most tear-me-open agreements attempt to disclaim all liability for lost profits and other incidental or consequential damages which may result from the use of the software.¹⁶³ Consequential damages are defined as losses "of which the seller at the time of contracting had reason to know and which could not reasonably be prevented. . . ."¹⁶⁴ Software in and of itself has limited intrinsic value. Its utility lies in its ability to perform tasks. Thus, the losses which computer users suffer as a result of a large scale computer failure are almost always consequential.¹⁶⁵

The UCC regards the limitation of consequential damages for per-

157. U.C.C. § 2-316 comment 1.

158. *Id.* § 2-719 comment 1.

159. *See supra* text accompanying note 122.

160. The time span for IBM's limited warranty is 90 days. *See supra* note 122.

161. *See supra* text accompanying note 154.

162. *See supra* text accompanying notes 115 and 116.

163. IBM attempts to limit liability for consequential damages as follows: "IN NO EVENT WILL IBM BE LIABLE TO YOU FOR ANY DAMAGES INCLUDING ANY LOST PROFITS, LOST SAVINGS OR OTHER INCIDENTAL OR CONSEQUENTIAL DAMAGES ARISING OUT OF THE USE OR INABILITY TO USE SUCH PROGRAM"

164. U.C.C. § 2-715(2). *See also* J. WHITE & R. SUMMERS, *supra* note 109, § 10-4 (The seller is liable when he or she had reason to know of the buyer's requirements regardless of whether he or she consciously assumed the risks in question.).

165. Note, U.C.C. § 2-719 *As Applied to Computer Contracts—Unconscionable Exclu-*

sonal injuries caused by "consumer goods" as prima facie unconscionable.¹⁶⁶ In situations where the buyer is a commercial entity or the consequential loss is economic, and the parties are of equal bargaining power, however, the courts will most often not find unconscionability.¹⁶⁷ A claim of unconscionability will only be allowed in an exceptional commercial setting.¹⁶⁸

In *Chatlos Sys., Inc. v. Nat'l Cash Register Corp.*,¹⁶⁹ the Court of Appeals for the Third Circuit concluded that excluding consequential damages by means of a computer hardware and software agreement was not unconscionable.¹⁷⁰ In the *Chatlos* case, both parties were businesses, and the plaintiff was a manufacturer of complex electronic equipment. Even though many software customers are businesses, courts should have no difficulty in finding that it is unconscionable to exclude consequential damages. The primary reasons that courts have not found these exclusions to be unconscionable are that the parties enjoyed similar levels of sophistication and bargained for the agreements.¹⁷¹ The court therefore found that procedural unconscionability was absent. Tear-me-open agreements do not involve a bargaining process and there is a varying degree of sophistication between software customers and vendors. Often, purchasers of computer software are not even businesses.

A substantively unconscionable contractual clause is commercially unreasonable¹⁷² and bears no reasonable relation to the risks involved.¹⁷³ The software user assumes a high risk when acquiring software by a tear-me-open agreement if its terms are strictly construed. The software supplier assumes no risk at all.

The *Chatlos* decision does not entirely defeat the claim that a remedy limitation in the case of a tear-me-open agreement is unconscionable. Courts, in the past, have upheld awards of consequential damages

sion of Remedies? Chatlos Sys., Inc. v. National Cash Register Corp., 14 CONN. L. REV. 70, 98 (1981).

166. U.C.C. § 2-719 states: "Limitation of consequential damages for injury to the person in the case of *consumer* goods is prima facie unconscionable . . ." (emphasis added).

167. *Lincoln Pulp & Paper Co., v. Dravo Corp.*, 436 F. Supp. 262 (D.C. Me. 1977).

168. *Id.*

169. *Chatlos Sys. Inc. v. Nat'l Cash Register Corp.*, 479 F. Supp. 738 (D.N.J. 1979), *aff'd*, 635 F.2d 1081 (3d Cir. 1980). For a more in-depth discussion of this case, see Note, *supra* note 165.

170. *Chatlos Sys. Inc.*, 635 F.2d at 1086.

171. See, e.g., *Earman Oil Co. v. Burroughs Corp.*, 625 F.2d 1291 (5th Cir. 1980); *U.S. Fibres, Inc. v. Proctor & Schwartz, Inc.*, 509 F.2d 1043 (6th Cir. 1975); *Phillips Mach. Co. v. LeBlond, Inc.*, 494 F. Supp. 318 (N.D. Okla. 1980).

172. *Phillips Mach. Co.*, 494 F. Supp. at 324.

173. *Id.*

even in cases involving clauses waiving such damages.¹⁷⁴ Where the latent defect causes the damage and the purchaser has no remedy, the disclaimer will be invalidated.¹⁷⁵ Defects in software are usually latent. This is indicated by the fact that software developers have great difficulties in isolating problems with the software.¹⁷⁶ The software user obviously has no way of seeing defects in advance by merely inspecting the shrink-wrapped package.

In *Majors v. Kalo Laboratories, Inc.*,¹⁷⁷ consequential damages were awarded, despite the exclusion of such damages in the sale contract.¹⁷⁸ The subject matter of the transaction was an unproven fertilizer, which had defects which were unknown to its manufacturers. The court found the clause limiting consequential damages unconscionable because of the disparity between the cost of the product and the extent of the damages.¹⁷⁹ In the case of software, the losses resulting from defects are also likely to be much greater than the cost of the software to the user.¹⁸⁰ This is not a particularly persuasive argument,¹⁸¹ but the facts that the defects are latent and the seller or developer of the software is probably in a far better position to discover and insure against defects than is the purchaser, make the argument more compelling.

The UCC requires an evaluation of the "commercial setting, purpose and effect" of the clause before a finding of unconscionability can be made.¹⁸² While the exclusion of consequential damages may be procedurally unconscionable, such an exclusion may be commercially reasonable. A heavy burden would be placed on software developers if they had to develop defect-free software or acquire insurance against all possible results of errors in their software. It may be economically undesirable to make the software industry bear this burden.¹⁸³ Software could become prohibitively expensive and small software producers might become reluctant to develop new programs.

174. See, e.g., *Majors v. Kalo Laboratories, Inc.*, 407 F. Supp. 20 (M.D. Ala. 1975).

175. *Neville Chem. Co. v. Union Carbide Corp.*, 294 F. Supp. 649, 655 (W.D. Pa. 1968), *aff'd in part, vacated in part on other grounds*, 422 F.2d 1205 (3d Cir. 1969), *cert. denied*, 400 U.S. 826 (1970).

176. *Immel*, *supra* note 94.

177. 407 F. Supp. 20 (M.D. Ala. 1975).

178. *Id.* at 23.

179. *Id.*

180. Packages typically retail for under \$50. *Toong & Gupta*, *supra* note 2 at 378.

181. The price of the software might be low because the producer need not procure insurance against the damages arising if it is defective. This cost is to be borne by the consumer. Note, *Frankly Incredible: Unconscionability in Computer Contracts*, 4 COMPUTER L.J. 695, 735 (1983).

182. U.C.C. § 2-302(2).

183. *But see* Note, *supra* note 181.

A limitation of remedy will not be enforced if it is not part of the bargain between the buyer and the seller.¹⁸⁴ Courts have refused to uphold a limitation of remedy on this basis when the plaintiff could not be charged with knowledge of the limitation at the time of the sale.¹⁸⁵ This situation usually arises in cases involving owners manuals that contain warranty and remedy limitations.¹⁸⁶ In these cases, the consumers could not discover the limitations until they purchased the goods. The tear-me-open remedy limitation will be unenforceable if the software transaction is deemed to have taken place in the computer store and the consumer is not charged with knowledge of the remedy limitation due to the lack of conspicuousness of the remedy limitation.¹⁸⁷

VI. CLOSELY ANALOGOUS CASES

As previously mentioned, certain cases are analogous to tear-me-open agreements. The most similar cases are those involving warranty and remedy limitations printed on the labels or containers of goods such as herbicides or seeds.¹⁸⁸ While the analysis offered by these cases is helpful, it must be noted that in deciding whether or not to enforce such disclaimers, the courts have not had to deal with an issue unique to computer software. This issue is the fact that computer software contains intellectual property which is easily copied without detection. This factor may supply a strong incentive for enforcing tear-me-open software agreements.¹⁸⁹

A case with facts strongly analogous to those which may be presented by litigation arising out of a tear-me-open agreement is *Monsanto Agric. Prod. Co. v. Edenfield*.¹⁹⁰ Monsanto marketed its herbicide "Lasso" through distributors who in turn sold it to dealers and farmers.¹⁹¹ Lasso was sold in five gallon cans with labels and instruction booklets affixed to their tops. The labels contained language limiting

184. See *Dougall v. Brown Bay Boat Works*, 287 Minn. 290, 178 N.W.2d 217 (Minn. 1970); *Pfizer Genetics v. Williams Management*, 204 Neb. 151, 281 N.W.2d 536 (Neb. 1979).

185. See, e.g., *Pennington Grain & Seed Co. v. Tuten*, 422 So. 2d 948 (Fla. Dist. Ct. App. 1982).

186. *Dougall*, 287 Minn. at 290, 178 N.W.2d at 217.

187. The same reasoning is applicable to the determination of whether the limitation of remedies is accepted as to the determination of whether the contract as a whole is accepted. See *supra* text accompanying notes 63-92.

188. *Monsanto Agric. Prod. Co. v. Edenfield*, 426 So. 2d 574 (Fla. Dist. Ct. App. 1982).

189. See *supra* text accompanying notes 16-19.

190. *Monsanto*, 426 So. 2d at 574.

191. Computer software is marketed in much the same way. Manufacturers sell to computer stores who in turn sell to customers. Courts generally no longer regard the lack of privity between manufacturer and customers as an obstacle to the customer recovering from the manufacturer.

warranties to those of chemical composition and fitness for the purposes described in the directions for use of the herbicide. Liability for breach of these warranties was limited to refund of the purchase price.¹⁹² The following notice appeared on the face of the instruction booklets: "Read 'LIMIT OF WARRANTY AND LIABILITY' before buying or using. If terms are not acceptable, return at once unopened."¹⁹³

The plaintiff, a soybean grower, bought the herbicide and used it to protect his crop from weeds. Unfortunately, the herbicide failed to control the weeds. Instead, the weeds choked the soybean plants.¹⁹⁴ The court stated that in order for a warranty limitation to be effective, certain requirements had to be met. First, it had to be part of the bargain between the parties and reasonably consistent with any express warranties made. It had to be in writing, conspicuous, and not unconscionable.¹⁹⁵ The court held that all these requirements were met by Monsanto's disclaimer.¹⁹⁶ The plaintiff conceded that he had read the directions for use of the herbicide. This led the court to hold that "even if appellee did not know of the limitation of warranty at the time of purchase of the product, it became a part of the bargain between appellee and Monsanto, by virtue of appellee's assent thereto."¹⁹⁷

A similar case from the same state, citing the same authority as *Monsanto*, reached a different result. In *Pennington Grain & Seed, Inc. v. Tuten*,¹⁹⁸ warranty disclaimers printed on labels attached to seed bags were held to be ineffective because they "amounted to a post-contract, unbargained-for unilateral attempt to limit [the seller's] obligations under the contract."¹⁹⁹ Interpreting Florida's version of UCC Article 2, section 2-316, the court stated:

The very purpose of the statutory requirement is that any limitation be brought to the attention of the buyer at the time the contract is made. An attempted limitation at the time of delivery long after a contract of purchase is signed does not accomplish this purpose, being a unilateral attempt of a party to limit its obligations.²⁰⁰

This language leads to a conclusion that unless the terms of the tear-me-open agreement are brought to the consumer's attention in the computer store or in the mail order catalog, they are unenforceable.

Both the *Monsanto* and *Pennington Grain* courts cited *Pfizer Ge-*

192. *Monsanto*, 426 So. 2d at 575.

193. *Id.*

194. *Id.*

195. *Id.* at 576.

196. *Id.* at 577-78.

197. *Id.* at 578.

198. 422 So. 2d 948 (Fla. Dist. Ct. App. 1982).

199. *Id.* at 951.

200. *Id.* (quoting *Christopher & Son, Inc. v. Kansas Print & Color Co.*, 215 Kan. 185, 523 P.2d 709 (1974)).

*netics, Inc. v. Williams Management Co.*²⁰¹ in support of their holdings. *Pfizer Genetics* involved disclaimers printed on seed bags which were delivered after the conclusion of a written agreement between the buyer and seller. The court stated the general rule that: "[D]isclaimers [of] warranty made on or after delivery of the goods by means of an invoice, receipt, or similar note are ineffectual unless the buyer assents or is charged with knowledge as to the transaction."²⁰² Similar reasoning was used to defeat a disclaimer of warranty printed on the side of a container in *Willoughby v. Ciba Geigy Corp.*²⁰³ The *Pfizer Genetics* case was remanded for consideration of the question whether the plaintiff assented or is charged with knowledge of nonwarranty as to the transaction.²⁰⁴

The court in *Hill v. BASF Wyandotte Corp.*,²⁰⁵ upheld a label warranty and limitation of remedies similar to that in *Monsanto*. Oral statements made by a salesperson concerning the capabilities of the herbicide were dismissed as mere "puffing."²⁰⁶ The disclaimer was upheld primarily because the plaintiff admitted having read it.

In many cases where label warranties have been upheld, the plaintiff had in fact read the challenged terms. IBM tries to ensure that the software user will read the agreement at some point by duplicating it in the instruction manual of the software. Thus, in the event litigation arises because a customer is dissatisfied with the performance of the software, IBM will argue that most software users read the instructions for new software at some stage. This might enable a court to charge the plaintiff with knowledge of the disclaimer. The plaintiff's response to this argument would be that he or she did indeed read the disclaimer, but only after unwrapping the software. Because of this, the plaintiff should argue that the software could not have returned for a refund. The consumer not only has a counterargument to IBM's, based on the uniqueness of tear-me-open agreements, but may also rely on cases refusing to uphold warranty and remedy limitations found in owners manuals and instruction books.²⁰⁷

VII. CHOICE OF LAW CLAUSE

The UCC and the case law generally allow parties to choose the state law which is to govern their transaction.²⁰⁸ Some states, however,

201. 204 Neb. 151, 281 N.W.2d 536 (Neb. 1979).

202. *Id.* at 155, 281 N.W.2d at 539.

203. 601 S.W.2d 385 (Tex. Civ. App. 1979).

204. *Pfizer Genetics*, 204 Neb. at 156, 281 N.W.2d at 539.

205. 696 F.2d 287 (4th Cir. 1982).

206. *Id.* at 291.

207. See *supra* text accompanying note 18.

208. See Goldberg, *supra* note 24, at 453. See also U.C.C. § 1-102(30) (parties can mod-

have adopted a public policy exception to this party autonomy rule.²⁰⁹ This view has been criticized because it defeats the UCC's objectives of uniformity and certainty.²¹⁰ The effect of the choice of law clause is of obvious importance where software is marketed in states which have enacted consumer protection statutes. This Note will not attempt an in-depth analysis of the relationship between state consumer laws and the UCC

VIII. CONCLUSION

There is little doubt that off-the-shelf computer software is here to stay. Because of the nature of software and the impossibility of producing defect-free programs,²¹¹ software manufacturers will probably continue to attempt to limit their liability for defective programs. At some stage, courts will undoubtedly be faced with the question of whether to uphold tear-me-open software agreements.

In some respects tear-me-open agreements should be treated no differently than any other standard form agreement. In deciding whether to uphold or void such agreements, courts should balance many competing factors. These factors include the relative bargaining positions of the parties,²¹² whether one party is a consumer or commercial entity,²¹³ and the harshness of the terms of the agreement.²¹⁴ The fact that computer software can easily be copied is a unique factor which cannot be ignored.

An important consideration underlying the decision of whether to enforce tear-me-open software contracts and their individual terms is the policy of encouraging new technological developments. The costs of developing and testing software are high. Insistence that software be perfect before it is put into the marketplace, or that the software makers be insurers, will most likely deter production of innovative software. The cost of software would thus become prohibitively high and would

ify all Code provisions with the exception of the obligations of good faith, diligence, reasonableness, and care). *See also* *Jaskey Finance & Leasing Co. v. Display Data Corp.*, 564 F. Supp. 160 (E.D. Pa. 1983) (the court upheld a choice of law clause). *But see* *Suntogs of Miami, Inc. v. Burroughs Corp.*, 433 So. 2d 581 (Fla. Dist. Ct. App. 1983) (A choice of law clause specified Michigan law as governing a contract, but made the Florida statute of limitations govern; the statute of limitations clause would be void under Florida, but not Michigan law. Although Florida did not enact the public policy exception to U.C.C. § 1-102(3), the court refused to enforce the statute of limitations clause.).

209. *See* Goldberg, *supra* note 24, at 453.

210. *Id.*

211. *See supra* text accompanying notes 94-96.

212. *See supra* text accompanying note 138.

213. *See supra* text accompanying note 67.

214. Note, *supra* note 181, at 734-35.

have a detrimental effect on the development of businesses and technology in general.

Courts faced with this issue should consider the nature of the process by which the agreement is brought to the attention of the customer. Currently, the standard tear-me-open agreement may not be sufficiently conspicuous to bind a software customer. The rights relinquished by the customer seem too important to be lost by the mere performance of an act which is not normally associated with the acceptance of a contractual offer. Unless courts expand their interpretation of the express warranties, customers will be bound by unconscionable contractual terms.

Nevertheless, tear-me-open agreements and their terms limiting liability are not fundamentally flawed in principle. The social and economic policies at stake may well require their enforcement.²¹⁵ If the software producers intend their tear-me-open agreements to do more than deter their dissatisfied customers from filing lawsuits, however, they should place a more conspicuous agreement notice on the software package. Software producers would be well advised to use a more distinctive means of implementing the theory behind tear-me-open agreements. A conspicuous seal which can only be broken by means of a knife or similar tool is a possible alternative to a cellophane wrapper. The seal would carry a notice warning the customer that breaking it will bind the customer to certain contractual terms which the customer should read in advance. In addition, the customer should be provided with more information as to the capabilities of the software. Currently, the customer is acquiring an unknown quantity and assuming all risks associated with it.

As is true in the label warranty cases, it will be difficult to formulate a single rule for all situations involving tear-me-open agreements. As computers and software become more sophisticated and powerful, their applications will become more diverse.²¹⁶ Computers are already used in the home, office, and factory for tasks varying from the management of household alarm systems to business accounting systems and industrial process control and will be used even more in the future. Much of the software which will be used will be ready made and acquired through mass marketing channels. Therefore, more people will become sophisticated in the use of computers and computer software. As such, certain agreements will be unconscionable for some and not for others. If the principle behind tear-me-open agreements finds acceptance in the courts, cases arising from such agreements should be

215. See *supra* text accompanying notes 182-183.

216. See Note, *supra* note 1.

evaluated with careful consideration of the facts of each situation in the context of societal needs.

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