September 11, 2000

Secretary
Federal Trade Commission
Room H-159
600 Pennsylvania Ave., NW.
Washington, D.C. 20580

VIA FEDERAL EXPRESS &
E-MAIL: software-comments@ftc.gov

Re: High-Tech Warranty Project—Comment, P994413

Ladies and Gentlemen:

I write in response to Ms. Major's letter to me dated August 21, 2000, requesting comment on the issues described in the Federal Trade Commission's (the "Commission") Invitation for Public Comment published in the May 11, 2000 Federal Register (at page 30411).

I. Warranty Protections for Software (Questions 1-6 and 13)

A host of issues have been targeted for comment, a number of which relate to the existence, scope and efficacy of warranty protection for software and other high-tech goods and services marketed to consumers. *See* Questions 1-6 and 13. While many questions can (and are) raised about the scope and source of warranty protections for software and similar information products under current law, the Uniform Computer Information Transactions Act ("UCITA"), just recently being introduced in various states, clearly provides for warranties as to various information products and services. UCITA carries forward—indeed expands—the scope of implied warranty protections for computer software transactions from the regime of warranty protection under Article 2 as to goods. That UCITA largely builds upon the existing warranty model in Article 2 cannot be seriously debated. Article 2, of course, provides implied warranties of title and non-infringement, merchantability and fitness for a particular purpose with respect to sales of goods transactions.[1] These implied warranties can be disclaimed.[2] UCITA also affords licensees with comparable implied warranties of title and non-infringement, merchantability,

[1] *See* UCC §§ 2-312, 2-314 and 2-315.

[2] *See id.* §§ 2-312(b) and 2-316.

etc.[3] UCITA creates two new implied warranties for the benefit of licenses: informational content and system integration.[4] However, UCITA does (as it must) tailor its implied warranties to characteristics peculiar to information products and services. UCITA also carries forward Article 2's practice of allowing disclaimers.

Thus, with respect to warranties, licensees will fare no worse under UCITA than they would if Article 2 applied – indeed, I believe they would fare better. Also, UCITA is not meant to preempt, and in fact expressly excepts from its coverage, state consumer protection laws.[5]

II. Mass Market Contracts (Questions 8, 12 and 14)

The issue implicitly raised by Questions 8, 12 and 14 has far reaching significance for mass market contracting generally. In essence, they ask, "should clickwrap and shrinkwrap contracting models work"? Though the questions ostensibly are limited to commerce in software, they cannot be so confined, for the methods of contracting prevalent in that commerce replicate those prevalent in mass market commerce generally. We all know that millions of dollars of consumer goods trade over the Internet on the strength of a click. Software may also be downloaded by a similar click. If the terms of sale in the click purchase are effective, then why would not the terms in the software click license? Conversely, to the extent that the click license transaction creates no enforceable agreement, then the enforceability of the click purchase is cast into doubt.

Shrinkwrap models build on other currently-accepted methods of contracting. Take, for example, the order by telephone, followed by shipment of a good. No one expects that the operator will read all of the terms of sale, including the limited warranties, over the phone. Everyone knows that terms arrive in the box. Shrinkwrap contracting relies on similar expectations. Many millions of dollars change hands by way of direct sales of goods over the telephone, by mail, by the Internet. If the contracting model used for "clickwrap" and "shrinkwrap" does not work for software, why would the exact same model of contracting work for goods? Fundamentally, therefore, the issue raised by your questions really is, "Does mass market contracting work?"

With rare exception (Magnuson-Moss being one) these questions concerning the enforecability of contracts or certain contract terms have been one left to the contract law of the various states. Under state law, standard form, mass market contracts have been enforced, subject to policing by unconscionability doctrines and consumer protection statutes. Indeed, most courts facing the issue have concluded that standard form contracting in the form of "clickwrap"

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[3] *See* UCITA §§ 401, 403 and 404.

[4] *See id.* § 405.

[5] *See id.* § 105(c).

and "shrinkwrap" licenses are valid, often without discussion.[6] I note, in this regard, since UCITA is a *contract* statute it continues this approach--an approach in which it has been preceded by the Uniform Commercial Code (the "UCC"), the *Restatement (Second) of Contracts* and the common law of contracts. I submit that the efficacy of mass market contracts relating to computer information transactions should also remain a matter of state law.

Standard forms are ubiquitous in all contracting situations. Indeed, when a consumer protection law mandates disclosure, those disclosures also come in standard form along with the standard contract forms. Now all of this may be done electronically. Why are any of these forms effective? That is the question that UCITA answers in manner consistent with the traditions of contract law. Indeed, UCITA represents a fundamental advance in providing a test for whether assent in a mass market transaction has been fairly gained. Most often, those courts that have examined the effectiveness of mass market contracts in computer transactions have--to put matters bluntly--looked more to the choreography of the steps in contracting rather than to what the parties' behavior and expectations have been. In order to understand just how tremendous an advance UCITA marks in this area, we need to examine these cases and the arguments of the critics of UCITA. In essence, as we will see, there are three schools of thought about standard forms.

(a) The First Approach: Choreography in Contract. Central to the analysis of cases relating to mass-market licenses is the modern contract doctrine that makes contracts easy to come by: minimal behavior, such as an exchange of forms, or start of performance by one side, suffices to create a contract. Once the precise time of contract creation is fixed, terms present at that point are given effect. All terms arriving thereafter are proposed additional terms. This line of thought, supposedly rooted in Article 2, is thus more concerned with the choreography of the contract, not with whether the parties have in fact contracted on common terms, and if so, what those terms were. In this regard, consider two of the most celebrated cases treating standard form software licenses.

[6] *See, e.g., Micro Star v. FormGen Inc.*, 154 F.3d 1107 (9th Cir. 1998). In *Micro Star*, the court had no problem whatsoever in enforcing the standard license granted by a computer game manufacturer to its players. *See id.* Other courts have been similarly untroubled in enforcing standard form licenses or terms of use, electronic and paper. *See also, e.g., M.A. Mortenson Co., Inc. v. Timberline Software Corp.*, 970 P.2d 803 (Wash. 2000) (installation and use of software constituted assent to software licenses printed in the user manual and on envelopes contained inside of the box that held the diskettes); *Caspi v. Microsoft Network, L.L.C.*, 732 A.2d 528 (N.J. Super. Ct. App. Div. 1999) (forum selection clause included in "clickwrap" license upheld as valid as the user was "free to scroll through the various computer screens that presented the terms of their contracts before clicking their agreement" just as a user is free to read the entirety of the fine print of an agreement); *Hotmail Corp. v. Van$ Money Pie, Inc.*, 47 U.S.P.Q.2d. 1020, 1025 (N.D. Cal. 1998) (ISP's terms of service prohibiting "subscribers from using Hotmail's services to send unsolicited e-mail or 'spam' or to send obscene or pornographic messages" given effect as a contractual matter); *Green Book International Corp. v. Inunity Corp.*, 2 F. Supp. 2d 112, 115-117 (D. Mass. 1998) (terms of shrinkwrap license allowing use and distribution enforced against *licensor*).

The facts of *ProCD, Inc. v. Zeidenberg* were straightforward.[7] ProCD offered a database compilation of telephone directories, both to the general public and "to the trade." However, the price "to the trade" was higher because the database was far more valuable for those in business. To prevent a commercial licensee from obtaining the lower retail price, each box containing the ProCD's software distributed at retail announced that use of the software was subject to the terms of a license residing in the box. The license allowed only "use of the application program and listings for non-commercial uses."[8] This license also appeared on the screen each time the program ran.[9] Zeidenberg bought a consumer package of the software at a retail outlet, and then promptly ignored the license, making the database available on the Internet for a price substantially lower than ProCD's commercial price.

The court enforced the license restrictions. It began by finding that the purchase transaction was sufficient to create a contract and that the license was present at that point, relying, interestingly enough, on Section 2-204 of the Uniform Commercial Code. With this as preface, Judge Easterbrook noted that, "ProCD proposed a contract that a buyer would accept by *using* the software after having an opportunity to read the license at leisure. This Zeidenberg did. He had no choice, because the software splashed the license on the screen and would not let him proceed without indicating acceptance."[10]

Zeidenberg maintained that, while the terms on the box arguably could be part of the contract, the license lurking in the box could not. The court responded that it would be too cumbersome to alert consumers to the terms of their contracts because of length and space considerations.[11] In any event, however, Zeidenberg had the chance to undo the transaction if he were revolted by the license terms: the license provided for a refund upon return of the software encumbered by the obnoxious terms. Now, the logic of the court's position would not require this refund after opportunity to review, for the court enforced the license because <u>ProCD</u> *said* certain behavior by its prospective licensee would constitute acceptance. But the fact of the matter was that the court fixed Zeidenberg's <u>acceptance</u> – the point of contract formation – at the point when the license was "splashed . . . on the screen" and he clicked his acceptance.

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[7] 39 U.S.P.Q.2d 1161 (7th Cir. 1996).

[8] *Id*. at 1163.

[9] The license was "encoded on the CD-ROM disks as well as printed in the manual, and ... appear[ed] on a user's screen every time" the software ran. *Id*. at 1162-63.

[10] *Id.* at 1165. *Cf.* UCITA § 112(d) ("Conduct or operations manifesting assent may be proved in any manner, including a showing that a person or an electronic agent obtained or used the information or informational rights and that a procedure existed by which a person or an electronic agent must have engaged in the conduct or operations in order to do so. Proof of compliance with subsection (a)(2) is sufficient if there is conduct that assents and subsequent conduct that reaffirms assent by electronic means.")

[11] *ProCD*, 39 U.S.P.Q.2d at 1163.

Step-Saver Data Systems, Inc. v. Wyse Technology[12] shares with *ProCD* a focus on where the terms of the standard form were when the contract was formed.[13] Again the facts were simple. Software Link, Inc. ("SLI") shipped its software from time to time to Step-Saver based on telephone orders, and Step-Saver would send a purchase order with price, quantity, shipping and payment terms. No disclaimer of warranties was made on the phone, by purchase order or invoice, though packages containing the software contained a printed license that disclaimed warranties. When difficulties developed with the system, Step-Saver sued SLI based on warranty claims. SLI pointed to the terms of its printed license, which disclaimed express and implied warranties.[14]

Invoking Article 2, the court held that SLI's shipment of the order and Step-Saver's payment and acceptance was sufficient to evidence "the existence of the contract." The issue was what the terms of that contract were. To assist it in divining the terms of the contract, the court resorted to Section 2-207, which it read as establishing that

> proceeding with a contract after receiving a writing that purports to define the terms of the parties' contract is not sufficient to establish the party's consent to the terms of the writing to the extent that the terms of the writing either add to, or differ from, the terms detailed in the parties' earlier writings or discussions. In the absence of a party's express assent to the additional or different terms of the writing, Section 2-207 provides a default rule that the parties intended, as the terms of their agreement, the terms to which both parties have agreed, along with any terms implied by the provisions of the UCC.[15]

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[12] 939 F.2d 91 (3rd Cir. 1991).

[13] *See also Klocek v. Gateway, Inc*., 104 F. Supp. 2d 1332, 2000 U.S. Dist. LEXIS 9896 (D. Kan. 2000). In *Klocek*, the court denied Gateway's motion to dismiss because Gateway had failed to produce "evidence sufficient to support a finding . . . that plaintiff agreed to the arbitration provision contained in Gateway's Standard Terms . . . ." *Id.* at *27. Exactly how the transaction took place is not clear from the record. Gateway alleged that it shipped the computer to the plaintiff, while the plaintiff alleged he bought it in person in Kansas. Citing *Step-Saver*, the court then stated: "Regardless whether plaintiff purchased the computer in person or placed an order and received shipment of the computer, the parties agree that plaintiff paid for and received a computer from Gateway. This conduct clearly demonstrates a contract for the sale of a computer." *Id.* at *13. The court then stated that since Gateway did not inform the plaintiff that the transaction was based on the conditional acceptance of the Standard Terms that were contained in the box, the Standard Terms constituted an expression of acceptance or a written confirmation rather than a counter-offer. *See id.* at *23-24. Therefore the Standard Terms did not become part of the agreement between the parties because the plaintiff never expressly agreed to them. The court rejected Gateway's argument that the mere act of keeping the computer past five days (the Standard Terms purported to become binding upon its customer if the customer kept the computer for over five days) was sufficient indicia of the plaintiff's agreement to the Standard Terms. *See id.* at *26. Again, the precise timing of terms, rather than the expectations and behavior of the parties, dictated the outcome.

[14] *See Step-Saver*, 939 F.2d at 93-97.

[15] *Id*. at 99. *See also* UCC §§ 2-204, 2-207(2), 2-207, cmt. 2.

Though the court denied that the time of the contract's formation was important, time was, in fact, central to the court's analysis. For its logic dictated that terms could be included up to the time of formation without being additional or differing terms.[16] Tacitly, the court found that the contract was formed based on the telephone conversation.[17] So, the contract included terms relating to price, shipment and payment because as to those terms the invoice and purchase order agreed.[18] But since the warranty disclaimers were in a form delivered "*after* the contract was formed" they were additional terms that could be ignored because, as a matter of law, they "would materially alter the parties' agreement."[19]

Note how outcomes under *Step-Saver*, no less than in *ProCD*, turn on choreography. Certainly such a mechanistic approach is unsatisfactory. Should practitioners really counsel their clients not to use the telephone in accepting orders for their products? Should unlimited consequential damages be visited upon a licensor merely because it sent a shrink-wrapped license with the product in response to a phone order, but denied to a licensee who purchases a copy of the same software off the shelf at Computer City?

(b) The Second Approach: Extracting Unfair Terms Based on Substantive Notions of Justice. The adherents of the second approach would dispense with the whole project of looking at the process of formation. They would argue that standard form of contracts cannot, under almost any circumstances, reflect the terms of a fair bargain because they are not negotiated and because they invariably reflect the dictates of just one party to the bargain.[20] This view presumes that a court or a legislator can determine what a substantively fair contract would be, or at least what a substantively unfair contract is.

This approach permeated many of the proposed revisions to Article 2 until last year. For example, the February 1999 Draft of the Proposed Revisions to Article 2 would have equipped a court with the power to "refuse to enforce a standard term in a consumer contract[21] the inclusion

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[16] *See also Arizona Retail Systems, Inc. v. Software Link, Inc*., 831 F. Supp. 759 (D. Ariz. 1993) (enforced standard form license in one context and not as to subsequent orders, following *Step Saver* in a scholastic analysis of the contract sequence).

[17] Logic suggests this: even though the court found shipment *and* payment to evidence the contract, payment followed invoice and the license came with the invoice. If the contract had been formed at payment, the license would have been not an additional term, or a proposed modification.

[18] *See Step-Saver*, 939 F.2d at 95-96, 98.

[19] *Id*. at 105.

[20] *See, e.g.*, PROPOSED REVISION TO UNIFORM COMMERCIAL CODE--ARTICLE 2-SALES § 2-206, cmt. 1 (February 1999 Draft). For Section 2-206 to apply, the term in question had to be a 'standard term' included in a record.

[21] The Reporters at that time noted that for the proposed (and since withdrawn) Section 2-206 to apply, the

of which was materially inconsistent with reasonable commercial standards of fair dealing in contracts of that type."[22] This power would have supplemented the authority of courts to void or alter unconscionable terms.[23] Specifically, "similarly, an included term that was beyond what a reasonable seller in a competitive market would include in contracts of that type might be denied enforcement."[24] Clearly this now abandoned approach contemplated that somewhere there floats a body of reasonable, commercial standards relating to fair dealing that can be brought to bear on any consumer contract. Even if a term, or the process of its making, was not unconscionable, it is of suspicious birth if in a standard form consumer contract, ripe for removal if an Ideal Commercial Contract would not, in a court's view, have included the term.

In this, as the then Reporters for Proposed Revised Article 2 acknowledged, the proposed section echoed Section 211 of *Restatement (Second) Contracts*[25] though Section 211 is followed in very few states. Section 211 provides, "Where [a] party has reason to believe that the party manifesting…assent to [writing] would not do so if he knew that the writing contained a particular term, the term is not a part of the agreement."[26]

Some of the most vocal critics of UCITA fault UCITA for failing to embrace Section 211. Thus, during the consideration of UCITA predecessor, Article 2B, at the May 1998 Annual Meeting of the American Law Institute, Jean Braucher and Peter Linzer attacked Article 2B's approach to assent to standard form records because Article 2B did not adhere to the approach taken in Section 211 the *Restatement (Second) of Contracts*.[27] But look at Section 211 of *Restatement (Second) of Contracts*. Clearly its language sweeps far more broadly than allowing a court to pluck the bizarre or oppressive term from a contract. It asks a court, *post hoc*, to speculate about whether one party had a reason to know what the other party might have expected.

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term must be in a consumer contract. 2-102(a)(9). An individual who buys goods that at the time of contracting are not intended to be used "primarily for personal, family, or household use" is not a consumer. 2-102(a)(9). On the other hand, if the goods are consumer goods when purchased and later are used in a business operation, there is a consumer contract.

Id.

[22] *Id.* § 2-206.

[23] *Id.* cmt. 1.

[24] *Id.*

[25] *Id.*

[26] RESTATEMENT (SECOND) CONTRACTS § 211 (1981).

[27] *See, e.g.*, Memorandum from Jean Braucher & Peter Linzer to Members of the American Law Institute 3 (May 5, 1998) <http://ali.org/ali/braucher.htm> at pp.1, 5-7.

That said, closely read, the comments and illustrations to Section 211(3) of the *Restatement* do raise serious problems that deserve addressing, though they support a less expansive rule than the black-letter rule of Section 211(3). Thus, the *Restatement's* comment (f) mentions as an instance inviting exclusion of a term where the term "eviscerates the non-standard terms explicitly agreed to"; similarly, the *Restatement* mentions cases where terms are microscopic or are "bizarre or oppressive," for example in situations involving posted signs and similar circumstances where contractual terms had no reasonable prospect of coming to the attention of a party.[28] As discussed below UCITA specifically addresses these evils.

(c) The Third Approach: Procedural Fairness. The third approach treats standard forms as a neutral fact of commerce, the only issue being whether the *process* of contracting was sufficient to the task of providing the parties with an opportunity to review and assent to or reject standard form terms. This school of "Procedural Fairness" informs proposed UCITA. Section 208, the general section dealing with forms <u>outside</u> of the mass-market, provides that "A party adopts the terms of a record, including a standard form, as the terms of the contract if the party agrees to the record, *such as by manifesting assent.*"[29] So, the standard form binds a party if he agrees to it. Here "agreement" is the "agreement" known for years under the Uniform Commercial Code: an "agreement" is the "bargain of the parties in fact as found in their language or by implication from circumstances including course of dealing or usage of trade or course of performance…."[30] This agreement can come by "manifesting assent" to the form. Under Section 112 a party "manifests assent *to a record or term* if the person, acting with *knowledge* of, *or after having an opportunity to review* the record or term or a copy of it *authenticates* the record or term...or intentionally engages in conduct or makes statements *with reason to know that the other party . . . may infer from the conduct or statement that the person assents to the record or term*."[31] Note the elements of assent: (1) knowledge <u>or</u> opportunity to review <u>plus</u> (2) <u>either</u> (i) authentication or (ii) conduct that the party fairly should know will create the inference of assent.

But note: authentication or conduct calculated to evidence assent suffices only as long as the party had an opportunity to review.[32] Embedded in the idea of an "opportunity to review" is the concept of a *fair* chance to review. Section 112(e) provides that a person "has an opportunity to review a record or term *only if* it is made available in a manner that *ought* to call it to the attention of a *reasonable person* and permit review."[33] This concept addresses one of the chief

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[28] RESTATEMENT (SECOND) OF CONTRACTS § 211, cmt. (f) (1981).

[29] UCITA § 208(1) (emphasis added).

[30] UCC 1-201(3).

[31] UCITA § 112(a) (emphasis added).

[32] *See id.* § 112(e).

[33] *Id.* § 112(e)(1) (emphasis added).

problems with standard forms identified by the comments to Section 211 of the *Restatement (Second) of Contracts* — namely, hidden records.

UCITA extends procedural protections even further as to "mass-market licenses," which--it should be noted--include standard form licenses not only in consumer transactions, but also generally in other retail transactions.[34] A mass-market license must satisfy the Section 208 procedural standards for assent discussed above; even then, it will be binding "only if the party agrees to the license, such as by manifesting assent, before or during the party's initial performance or use of or access to the information."[35] Moreover, a "term is not part of the license if: (1) [it] is unconscionable or unenforceable under Section 105(a) or (b); or (2) subject to [the parol evidence rule], the term conflicts with a term to which the parties to the license expressly agreed."[36]

The reference to unconscionability is telling. The official comments to the unconscionability section state that the unconscionability doctrine is especially suited to the task of combating "oppression and unfair surprise."[37] Moreover, Section 209 invalidates a form term contradicting expressly agreed upon terms. Thus, again, UCITA addresses oft-expressed concerns about standard forms—*i.e.* that they would allow the author of the form to trump express agreements. Truly outrageous abuses by those who employ standard form contracts would undoubtedly be punished by UCITA no less than by the *Restatement (Second) of Contracts*.

In fact, UCITA goes even further than existing Article 2 to protect licensees from abuse. Thus, in Section 105(b) UCITA provides that if "a term of a contract violates a fundamental public policy, the court may refuse to enforce the contract, enforce the remainder of the contract without the impermissible term, or limit the application of any impermissible term as to avoid a result contrary to public policy, in each case to the extent that the interest in enforcement is clearly outweighed by a public policy against enforcement of that term."[38] As the official comments make clear, this principle is intended to supplement the unconscionability concept. Comment 2 to Section 105 states that "subsection (b) sets forth the general legal principle that terms may be unenforceable if they violate a fundamental public policy that clearly overrides the policy favoring enforcement of private transactions as between the parties."[39]

[34] *See id*. § 102(43) and (44).

[35] *Id*. § 209(a).

[36] *Id*.

[37] *Id.* § 111 cmt. 2.

[38] *Id.* § 105(b).

[39] *Id.* § 105 cmt. 3.

Even so, UCITA clearly establishes that standard forms will be enforceable--as is recognized by Article 2 and the common law. But it does so by doing more than having the courts look to the choreography of the contracting steps. UCITA binds parties to standard forms, but does so based on their objective behavior only if they know of the form or have the opportunity to review it. By the same token, it also rejects a retrospective speculation about what the parties may have expected as permitted by Section 211 of the *Restatement (Second) of Contracts*. As long as unconscionability does not mar the contract, or as long as the contract does not transgress fundamental public policy, the form will be given effect if the evidence shows agreement or manifest assent to it.

One other protection against potential problems in mass-market licensing points the way to another innovation in UCITA. UCITA provides that if a licensee does not have an opportunity to review a mass-market license or a copy of it before becoming obligated to pay and does not agree, by manifesting assent or otherwise, to the license after having that opportunity, the licensee is entitled to a return and to:

> (1) reimbursement of any reasonable expenses incurred in complying with the licensor's instructions for returning or destroying the computer information or, in the absence of instructions, expenses incurred for return postage or similar reasonable expense in returning the complete information; and
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> (2) compensation for any reasonable and foreseeable costs of restoring the licensee's information processing system to reverse changes in the system caused by the installation, if:
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> > (A) the installation occurs because information must be installed to enable review of the license; and
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> > (B) the installation alters the system or information in it but does not restore the system or information after removal of the installed information because the licensee's rejection of the license.[40]

Note the detailed refund rights. But note also how opportunity to review may follow initial performance, thus relaxing the focus on the sequence of contracting steps so important to *Step-Saver*. UCITA thus allows the timing of the sequence of contracting steps to be loosened.

I hasten to add, however, that mass-market license terms will be not be invariably enforced no matter when they appear. For any record with terms appearing "after beginning performance or use" under the agreement to be enforced, "the parties [must have] reason to know that their agreement would be represented in whole or part by a later record to be agreed on and

[40] *Id*. § 209(b).

there [must be no] opportunity to review the record or a copy of it before performance or use begins."[41] As any business lawyer knows, performance may commence before terms are finalized. Under UCITA if the recipient of a standard form appearing after performance commences finds the form repugnant, he may usually extricate himself from the contract. Even more to the point, that form would not be given effect at all if its arrival were not *expected* at the time of performance.

This clearly articulates the implicit premise in contracting models that are built upon the recognition that terms cannot be always made to march according to a one-time-sequence-fits-all approach to contracting. UCITA would give effect to standard form terms appearing after the initial stages of performance to the extent the form was <u>expected</u> and later <u>gained manifest assent</u> (after an opportunity to review, of course). Thus it rejects the wholly artificial narrowing of period when forms must appear in order to make them part of the contract, while limiting those forms to those that are fairly anticipated.

(d) Brower: A Preview of Sections 208 and 209 in Action. The *Brower v. Gateway 2000, Inc*. case provides us with a simple example of how these various interwoven sections in UCITA might work in practice.[42] In *Brower*, consumers supposedly representing a class of Gateway 2000's consumers of computer hardware and software challenged the efficacy of the arbitration clause in Gateway 2000's standard form. Specifically, when Gateway 2000 shipped its products to one of its consumers, a Standard Terms and Conditions Agreement resided in the box with the merchandise. Emblazoned across the top of this agreement was a box, containing within it a printed warning, in type "slightly larger…than the remainder of the document," that

> This document contains Gateway 2000's Standard Terms and Conditions. By keeping your Gateway 2000 computer system beyond thirty (30) days after the date of delivery, you accept these terms and conditions.[43]

Included among the sixteen paragraphs of substantive terms was a paragraph--ten, to be precise--relating to dispute resolution, requiring all controversies relating to the agreement to be arbitrated "in accordance with the Rules of Conciliation and Arbitration of the International Chamber of Commerce" and in Chicago, Illinois. When the plaintiffs filed suit alleging that Gateway's alleged promise "service when you need it" was an empty one, Gateway invoked the arbitration clause.[44]

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[41] *Id*. § 208(2).

[42] 246 A.D.2d 246, 676 N.Y.S.2d 569 (N.Y. Sup. Ct. App. Div. 1998). I note that UCITA might not have applied to all issues in the case; the facts were unclear about whether software or goods gave rise to the complaints.

[43] *Id.* at 248.

[44] *See id.* at 248-49.

In response, the plaintiffs argued that the arbitration clause never really became part of the contract at all. Echoing *Step-Saver*, the plaintiffs maintained that "when they placed their order they did not bargain for, much less accept, arbitration of any dispute, and therefore the arbitration clause in the agreement that accompanied the merchandise shipment was a 'material alteration' of a pre-existing oral agreement."[45] The Appellate Division, as had the trial court, rejected this argument, though on both broad and narrow grounds.

The real issue, and the issue as to which the *Brower* court gave a compelling answer, is, "Why should we assume that the contract had been concluded over the phone?" To this much subtler question, the *Brower* court stated that "in *such* transactions, there is no agreement or contract upon the placement of the order or even upon the receipt of the goods."[46] What are "such transactions"? Clearly, the court was referring to its previous statements that

> [t]ransactions involving 'cash now, terms later' have become commonplace, enabling, the consumer to make purchases of sophisticated merchandise such as computers over the phone or by mail--and even by computer. Indeed, the concept of 'payment preceding the revelation of full terms' is particularly common in certain industries, such as air transportation and insurance.[47]

Note that the court, in taking into account, the "realities of conducting business in today's world" was pointing to specific types of transactions where expectation or practice suggested that terms were to follow. Retail or mail orders for goods, especially of sophisticated merchandise, airline ticket orders, insurance policy subscriptions, all had become the type of transactions where one expects (or should expect) that the contract remains open, even though performance by one party (e.g. through payment) has commenced or been completed. *That* was why the terms of the Agreement fairly and properly could be treated as part of the contract. In the words of Section 208, "the terms of a record may be adopted [as the terms of the contract] after beginning performance or use *if the parties had reason to know* that their agreement would be represented in whole or part by a later record to be agreed on and there would not be an opportunity to review the record or a copy of it before performance or use begins."[48]

This did not end the tale, however. Though the arbitration term found its way into the contract, the court found the term unconscionable because the excessive fees entailed in an ICC arbitration effectively left consumers "with no forum at all in which to resolve a dispute."[49] But

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[45] *Id.* at 250.

[46] *Id.*

[47] *Id.*

[48] UCITA § 208(2).

[49] *Brower*, 246 A.D.2d at 254.

instead of invalidating the arbitration clause completely, the court remanded the case for the trial court to appoint an arbitrator that did not inflict "egregiously oppressive" costs. Regardless of whether one accepts the conclusion that an ICC arbitration provision in a retail contract is substantively unconscionable, the *Brower* court's approach is consistent with Section 209, which specifically points to unconscionability as being grounds for avoiding a mass market term and Section 110, which allows a court to "limit the application of the unconscionable term so as to avoid an unconscionable result."[50]

III. Why License in Mass Market Transactions? (Questions 8 and 12)

On one level licensing helps to smooth the jagged contours of intellectual property protection for software programs[51] by providing a contractual basis for the software licensor to set articulate the permitted uses of its information product.[52] More fundamentally, however, by marking the boundaries of permitted use, a license creates the "product" that the licensor is willing to provide to the licensee. What the licensee "acquires" is that scope. This is not true with a good: the good defines itself. But as with a lease or other arrangement where the "product" being transferred is a defined use for a specified period subject to certain terms, the scope of use so carved out is the product.

At the heart of a license is control over the licensee's use: in the words of UCITA, a license is "a contract that authorizes access to, or use, distribution, performance, modification or reproduction, of information or of informational rights, but expressly limits the access or uses authorized or expressly grants fewer than all rights in the information . . . ."[53] In other words, the nature of licensing makes the rights of the licensee conditional or limited, subject to control by

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[50] *See* UCITA §§ 209(a), 110(b).

[51] *See, e.g., Lotus Development Corp. v. Borland International, Inc.*, 116 S. Ct. 804 (1996) (Court split 4-4 on whether menu-commands included in a Lotus spreadsheet were protected by copyright; split resulted in affirmance of 1st Circuit ruling that menu-commands were not an expression of an idea). For an extended critique of existing intellectual property law's over-and under-inclusive scope of protection of computer programs, *see* Samuelson, Davis, Kapor & Reichman, *A Manifesto Concerning the Legal Protection of Computer Programs*, 94 COLUM. L. REV. 2308 (1994).

[52] Let us take an example. Many software companies hold the trick of their software in the deepest confidence, treating it as a trade secret, though they would also claim copyright protection for the expression inhering in the software. *See* RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 39 cmt. c, reporter's notes to cmt. c (1995) (stating that trade secrets may be claimed with respect to "a work that is the subject of a copyright registration" as long as the work otherwise qualifies for protection under trade secrecy principles). Trade secret claims, of course, broadly protect ideas, but arguably, they may be lost by reverse engineering. *See id.* § 39 cmt. b. Licensing helps to bolster trade secret claims by forbidding reverse engineering. *See* Dominic Bencivenga, *Beyond Copyright Law: How to Protect Software*, NAT'L L.J., April 22, 1996, at B1 (stating that copyright law, alone, may not provide adequate protection against reverse engineering).

[53] *Id.* § 102(40).

the licensor. With licenses, therefore, the standard terms in issue are not merely liability limiting devices. They govern *use* by the licensee. The ambit of permitted use is really what the consumer "buys." This control over use inherent in a license transaction makes the general legal issues concerning standard form agreements—issues that scholars and courts normally wring their hands over—of far greater moment in mass-market software and information transactions.

Licensing is extremely crucial to many information providers because of the characteristics inherent in software and many other information products. For example, while I cannot allow thirty people to use a truck simultaneously, I might be able to allow thirty people or more to use a software product on a network. The truck manufacturer is not deprived of sales because of the inherent physical barriers to use, but the software company would be deprived of "sales" because the absence of inherent physical barriers to use. Similarly, while I could copy a music CD or a book and thereby violate the intellectual property rights of the author or publisher of the CD or book, multiple simultaneous uses are generally not feasible. Even more to the point, with a music CD or a book the value of the product is put on display for all to see--indeed what is on display is what the consumer wants. In contrast, software companies invest enormous sums on the delicate operations of a program that they would not willing put on display to their competitors. Therefore, contractual use restrictions serve as substitutes for practical, physical barriers to use.

Again the product and its "price" are defined by reference to these restrictions. By turning over the software or other information product, the licensor does not imply that unlimited use or multiple sales are permissible or that its price reflects the myriad ways that its product may be re-distributed. Moreover, the licensors of software and many other information products divide their distribution channels into, say, consumer and business categories; here use restrictions serve as a method for calibrating pricing to markets and distribution channels.

Billions of dollars in software have traded hands based on the prospect that all of these use restrictions will be given effect, and many of these licenses repose in standard forms. The very economic basis for distribution of information products, the very pricing model that has been built into software transactions, rests on the efficacy of license use restrictions, regardless of whether they came in a standard form.

IV. Conclusion

UCITA tailors Article 2 warranties for information transactions and incorporates them in a commercial statute generally applicable to computer information transactions. Moreover, UCITA's revolutionary procedural fairness approach eschews the empty formalism of the "choreography" approach employed by some courts and the cynicism inherent in punting to the courts the unreasonable task of determining which terms are proper and which are not. UCITA provides a framework for testing fairness in mass-market contracting, while embracing common commercial practices prevalent in information transactions. UCITA thus stands as testament to the sufficiency of the uniform law process in formulating answers to many of the important questions listed in your Invitation for Comment.

Very truly yours,

Jeff C. Dodd

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