

# OVERVIEW OF THE UNIFORM COMPUTER INFORMATION TRANSACTIONS ACT (UCITA)

Report of the Joint Task Force of the Delaware State Bar Association Sections of Commercial Law, Computer Law, Intellectual Property, and Real and Personal Property

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## I. EXECUTIVE SUMMARY

- **Current Laws Were Not Written For The Computer Age.** Courts today are divided over what laws should apply to computer information transactions, leading to inconsistent results across jurisdictions. Current UCC Article 2, based on the sale of goods, is a poor fit. As UCITA makes clear, computer information contracts are in fact licenses, and as such involve a host of different legal considerations.
- **Common Rules Are Necessary For The Internet And E-Commerce.** As our economy moves from one centered around transactions in goods to an information economy, the need has grown dramatically for coherent and predictable legal rules to support these transactions that underlie the economy. UCITA establishes rules where none exist now or improves present law, and represents the first comprehensive uniform computer information licensing law. UCITA is about jobs, wealth creation and global leadership.
- **Major Innovations Of UCITA:** UCITA sets up a uniform contracting regime for licenses of information, and provides a “road map” for practitioners who may not be experienced in licensing. It contains a progressive electronic commerce package in parallel with the Uniform Electronic Transactions Act (UETA). It provides clear rules which must be followed in order for shrinkwrap contracts to be enforceable. It puts reasonable fences around the exercise of electronic self help.
- **UCITA Will Benefit Delaware:** UCITA and other steps by the Delaware Legislature will facilitate e-business by providing predictable and reasonable rules for transactions that are critically important to our economy. Companies will locate in Delaware to take advantage of the legal climate. Delaware courts will earn an enhanced reputation in the field of e-commerce. UCITA will help to place Delaware in the forefront of the fastest-growing segment of the economy.

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- **Other States Are Seeking Early Adoption of UCITA.** Pennsylvania’s governor has dubbed Pennsylvania “the state of technology,” and is pressing for comprehensive legal reform to attract e-business. In Winter, 2000, UCITA will start to be introduced in the state legislatures. Early passage is expected in Virginia, Maryland, Pennsylvania, State of Washington, and possibly the District of Columbia. Delaware will be an economic disadvantage if it delays.
- **UCITA Will Benefit Licensees and Consumers:** Clear and predictable rules that match commercial expectations result in lower cost transactions and less barriers to trade. UCITA gives licensees and consumers substantial safeguards that do not exist today under the UCC or common law. In addition, UCITA makes clear that consumer protection statutes and regulations continue to apply to transactions within the scope of UCITA.
  - Recognizes courts may refuse to enforce ridiculous or unfair terms.
  - Clarifies that advertising and product documentation can create express warranties.
  - Creates new implied warranties for noninfringement, system integration and computer programs.
  - Requires limitation of damages to be explicitly stated in the license.
  - States a choice of law or forum will not be enforced if it is unreasonable and unjust.
  - Provides important new protections for licensees in the area of electronic self help.
  - Imposes an obligation of good faith performance in all information contracts.
  - Makes many software licenses perpetual although current law would make them terminable at will.
  - Gives consumers a statutory right to avoid the consequences of errors in online transactions.
  - Creates a state law presumption that licenses are transferable.
  - Creates a cost-free right of refund if mass market terms are not acceptable.
  - Prevents mass market contract terms from contradicting express agreement.
  - Creates a warranty of quiet enjoyment of rights under a license which does not exist under current sales law
  - Provides that non-waivable warranties can be made by advertising.
  - Allows licensees to use nonexclusive licenses as a basis to obtain financing
  - Prevents licensor from canceling license except for material breach
  - Creates implied license of rights needed to fulfill contractual purpose.
- **UCITA Was Produced After Long And Careful Deliberation:** UCITA has been under consideration for a decade. It was drafted by the National Conference of Commissioners on Uniform State Laws (NCCUSL), the same organization that drafted the Uniform Commercial Code and many other uniform laws. NCCUSL received input from industry groups, state bar groups, the ABA and others.

## II. HISTORY AND BACKGROUND

UCITA was produced in an open, thoughtful, even-handed process. On July 29, 1999, after a decade of considerations, years of input from information industries, state bar groups, the ABA, and others, the National Conference of Commissioners on Uniform State Laws (NCCUSL) adopted the Uniform Computer Information Transactions Act ("UCITA") by a 47 to 6 vote of the states, District of Columbia, Puerto Rico and the Virgin Islands. The Commissioners are distinguished judges, law professors and practicing lawyers who are appointed by and answerable to their states' Governors of legislatures. They are the organization that drafted the Uniform Commercial Code and many other uniform laws. Their conclusions deserve a strong presumption of fairness and correctness.

In November of 1999, the Delaware State Bar Association's Commercial Law Section, Computer Law Section, Real and Personal Property Section, and Intellectual Property Section made up a Joint Task Force to review and comment upon UCITA. After eight meetings at which the provisions of UCITA and UETA were discussed in detail, the Task Force voted on January 5, 2000, to recommend a Delaware version of UETA to the Executive Committee of the DSBA and to the respective sections for endorsement. This is the Task Force's report concerning the Delaware UCITA.

#### **A. Need for Uniformity**

America is in the Information Age. Information technology already accounts for more than one-third of the U.S. economy and is, by far, its most rapidly growing sector. However, this new information-based economy will fail to reach its full potential without predictable rules of commercial law. The Uniform Commercial Code, Article 2, governs commercial transactions in tangible goods, but there are no comparable uniform state rules today for computer information and Internet (e-commerce) contracting. This unfortunate state of affairs is an open invitation to confusion, controversy and litigation that will inevitably slow economic growth. UCITA addresses this need. It lays down clear, fair rules for electronic contracting that are a major improvement over the *status quo* for businesses, whether licensors/licensees or sellers/buyers, and for consumers.

UCITA is a product of compromise that, like every compromise, fully satisfies no one, but, on balance, is very fair. Some consumer representatives want more consumer protections; some vendors want fewer. Some corporate information technology managers criticize UCITA as unfairly restrictive while their own lawyers endorse it as far better than current law. NCCUSL thoughtfully balanced these and other competing interests and produced a Uniform Act that is fair to all. As UCITA moves to state legislatures, the same arguments *pro* and *con* that were made to NCCUSL will be made again. It is important to recognize that these arguments have already been heard with respect and addressed. The critical goal of uniformity would not be met if each of the 50 states attempted to develop a new consensus.

UCITA is a uniform law that we urgent need if we are to keep this country's economic engine running. Its enactment by the states, as approved by NCCUSL, should be given high priority.

#### **B. Urgency**

There is no existing law providing clear, consistent and uniform rules governing the intangibles of transactions involving computer information. The Conference Communiqué of the Steering Committee of Global Business Dialogue on Electronic Commerce, which includes Richard Brown (EDS), Steve Case (AOL), Michael Eisner (Disney), Louis Gerstner (IBM), Gerald Levin (Time Warner), Lew Platt (HP) and Bert Roberts (MCI WorldCom), stated on September 13, 1999, that:

We came together today for this inaugural conference of the GBDe in order to express our sense of urgency with respect to addressing electronic issues...It is the consensus position of the GBDe that inconsistent local, national, and international patchwork regulation and inflexible regulatory restraints will deprive consumers of the economic benefits of an innovative electronic marketplace and would lead to significant uncertainty to consumers.

The White House, in its paper entitled “A Framework for Global Electronic Commerce,” dated July 1, 1997, stated, “Many businesses and consumers are still wary of conducting extensive business over the Internet because of a lack of a predictable legal environment governing transactions.”

### III. UCITA THEMES

**Freedom of Contract:** UCITA, like the UCC, is premised on the parties having freedom of choice. The terms and effect of a contract are determined by agreement rather than by legislative fiat. The exercise of contract choice opens up full opportunities for innovation and growth. With certain limited exceptions the terms expressed by the parties in their agreement control. If their agreement is silent, then trade usage and the parties’ course of dealing and performance are looked to, and only if the contract is both silent and trade usage and course of performance is unhelpful, do the “gap-filler” provisions of UCITA apply.

**Information and First Amendment:** Rights in intellectual property are established by other law such as patent and copyright law. UCITA specifically provides that federal preemption applies (Section 105(a)). State intellectual property law supplements UCITA and is not displaced by UCITA (Section 114(a)). UCITA adopts a neutral position with respect to what, ultimately, are issues of federal and international information rights policy. However, UCITA provides a basis for case by case resolution of the myriad issues in Section 105(b).

**Fundamental Public Policy Issues:** A principal concern of consumers and other users and developers of computer information has been that the contracts which provide for its use not contain provisions which violate fundamental public policies. The Drafting Committee did not want to depart from the longstanding policy that a statute premised on freedom of contract should not be a regulatory statute, and thus was reluctant to include in the statute a laundry list of impermissible terms. Instead, members of the Drafting Committee worked with members of the academic community for several months to craft a solution which would recognize the legal principle that certain terms of certain contracts may be unenforceable because

they violate a fundamental public policy. That solution is now embodied in Section 105(b) and accompanying comments.

#### **IV. KEY PROVISIONS OF UCITA**

##### **A. SCOPE**

**Limited to “Computer Information Transactions” (Section 103 (a)).** UCITA covers “computer information transactions”, i.e. “an agreement...to create, modify, transfer, or license computer information or informational rights in computer information (102(11)). UCITA applies to contracts to license or buy software, contracts to create computer programs, contracts for on-line access to databases and contracts to distribute information over the Internet. UCITA does not apply to goods such as television sets, stereo equipment, airplanes or traditional books and publications. Goods generally remain subject to UCC Article 2 or Article 2A.

**Opting in and Opting Out (Section 104).** Under common law, the right of parties to choose generally permits them to adopt the law they may wish to apply to their transaction. However, UCITA places some specific restrictions on opting in or out in order to safeguard the parties (Section 104).

**Exclusions from UCITA.** UCITA does not affect transactions in the core businesses of other information industries (e.g. print, motion picture, broadcast, sound recordings) whose commercial practices in their traditional businesses differ from those in the computer software industry. UCITA expressly excludes:

- a. Financial services transactions;
- b. Broadcast and cable TV;
- c. Motion pictures, sound recordings, musical works, phonorecord or enhanced sound recording;
- d. Compulsory licenses (103(d)(3));
- e. Contracts of employment of an individual other than as an independent contractor (103(d)(4));
- f. A contract which does not require that the information be furnished as computer information or in which the form of the information as computer information is otherwise *de minimis* with respect to the primary subject matter of the transaction (103(d)(5));
- g. Newspapers, magazines, books, and other print forms by the definition of “computer information” except when that part is transferred in electronic form (e.g. over Internet by license), and (Section 102(11));
- h. E-mail communications merely about the agreement

##### **B. ASSENT**

UCITA provides safeguards against inadvertent assent and safe harbors to give certainty a contract has been made and attributed. (Section 112)

### **C. ELECTRONIC CONTRACT (SECTIONS 212-215)**

A record or authentication may not be denied legal effect, validity or enforceability solely on the ground that it is electronic (Section 107). A group of sections then set forth particular rules to be used when an electronic record or authentication is at issue.

### **D. WARRANTIES (PART 4)**

UCITA provides the following basic warranties which will be familiar to practitioners in the field of licensing law: Quiet Enjoyment and Non-infringement, Merchantability of a Computer Program, Information Content and Fitness for Licensee's Purpose and System Integration. It also clarifies what is an express warranty. It sets forth the manner in which implied warranties may be disclaimed. Implied warranties are not generally recognized and/or clear under common law. UCITA thus significantly extends warranties over those under current law.

**Implied Warranty, Informational Content (Section 404).** UCITA establishes a new implied warranty which focuses on the accuracy of data provided under a contract. The basic warranty states: "...a merchant that, in a special relationship of reliance with a licensee, collects, compiles, processes provides or transmits informational content warrants to its licensee that there is no inaccuracy in the informational content caused by the merchant's failure to perform with reasonable care." Note that this warranty does not guarantee that there will be no inaccuracies; rather it gives some protection by assuring that there will be no inaccuracies caused by a failure to use reasonable care.

**Implied Warranty, Licensee's Purpose; System Integration (Section 405).** If licensor has reason to know of any particular purpose for which the information is required and that the licensee is relying on the licensor for expertise, there is an implied warranty that the information will be fit for that purpose unless, from all the circumstances, it appears that licensor was to be paid for the amount of its time or effort regardless of the suitability of the information, in which case, the implied warranty is that there is no failure to achieve the licensee's particular purpose caused by the licensor's lack of reasonable care and workmanlike effort to achieve that purpose.

### **E. TRANSFER OF INTERESTS AND RIGHTS (PART 5)**

UCITA generally permits transfer of a contractual interest under a license. However, transfer may be prohibited under other law, or may not be allowed if such a transfer would materially change the duty of the other party, materially increase the burden or risk imposed on the other party, or materially impair the other party's property or its likelihood or expectation of obtaining return performance. However, if the parties agree to a term prohibiting transfer, that term is enforceable. In a mass-market license it must also be conspicuous.

### **F. FINANCING ARRANGEMENTS (SECTIONS 507-511)**

UCITA establishes bridge rules for license financing transactions that are not governed by UCC Article 9.

#### **G. REMEDIES: LIMITATIONS ON ELECTRONIC SELF-HELP (SECTION 816)**

Electronic self-help is prohibited (i) if its exercise will result in substantial harm to the public health and safety or grave harm to the public interest (ii) unless the license has a term that allows a limited exercise of electronic self-help. Upon cancellation of a license, use of electronic means to exercise a licensor's right to repossession in **NOT** permitted except as provided in Section 816. *(Note: This is a change from current common law under which electronic self-help is more broadly permitted.)*

These provisions, when taken together with the provisions of Section 815, are so restrictive that it is unlikely that any licensor will be able to effectively use electronic self-help except in the most egregious cases; e.g. where a licensee is improperly disclosing the licensor's confidential and proprietary information. Most licensors would not agree to negotiate such provisions into their standard form contracts; thus it is a major benefit for licensees that UCITA effectively excludes electronic self-help from standard form contracts.

#### **V. SAFEGUARDS AGAINST INADVERTANT ASSENT AND SAFE HARBORS FOR CONTRACT FORMATION**

There are a number of concepts in UCITA that need to be read together to fully appreciate the safeguards incorporated to protect the parties from inadvertent contracts, particularly in e-commerce. Some of these protections do not exist in common law. These concepts include:

1. "Authenticate" (Section 102(6)) includes "signature" but also are "with the intent to sign a record, otherwise to execute or adopt an electronic symbol, sound or process referring to, attached to, included in, or logically associated or linked with, a record or term." There is no authentication without an intent for the authentication to be a signing;
2. Agreement by conduct: "intentionally engages in conduct or makes statements with reason to know that the other party or its electronic agent may infer from the conduct or statement that the person assents to the record or term"; (see also Restatement, Contracts(Second))
  - there must be "intent" and also "reason to know to be proven from all the circumstances
  - the circumstances may include a "double click" as a safe harbor, i.e. an initial click on "I agree" followed by a second display asking whether the person really intends to agree and a second click in response thereto (Section 112(d)).

3. Opportunity to Review Before conduct can be assent above, there must be an opportunity to review the terms (Section 112(e)),
4. Later terms, after beginning performance or use, are adopted only “...if the parties had reason to know that their agreement would be represented...by a later record to be agreed on.” (Section 209)
5. In a Mass-market License, the licensee is entitled to reject the contract with later terms for any reason and obtain not only a refund but incidental costs of return or destruction and reasonable and foreseeable costs of restoring the licensee’s system (Section 210(b));
6. Pretransaction Disclosure (Section 211) provides a strong incentive for disclosure of all terms before the licensee must pay or gets delivery, and lastly
7. “Attribution” to the party to be bound is required. The efficacy of an attribution procedure is determined by the circumstances including any agreement of the parties (Section 213(c)). Commercial reasonableness of an attribution procedure may be a factor in making that determination (Section 212).

In short, a party to be bound must have an opportunity to review the terms, then assent with an intent to authenticate or intent by conduct and with reason to know that the other party will infer assent; (or if the opportunity to assent is after performance or use, the party to be bound must have reason to know there are later terms and in a mass-market transaction the party can return the item with a cost-free refund), and lastly, the claimant has the burden of establishing attribution (Section 213(a)).

## **VI. CONSUMER PROTECTIONS ARE PRESERVED**

While many of the transactions to be covered by UCITA are commercial between merchants, UCITA also extends consumer protections to UCITA transactions. Section 105(c) explicitly provides: “Except as provided in Subsection (d), if this [Act] or a term of a contract under this [Act] conflicts with a consumer protection statute [or administrative rule], the consumer protection statute [or rule] governs.”

Subsection (d) sets forth rules that enable e-commerce by allowing an electronic record, authentication, and conspicuousness . The Official Comments clearly state that “timing, manner and content” of disclosures are unmodified by those e-commerce enabling rules. However, to the extent a state provides for a “writing” and does not wish an electronic message to be authorized, a legislative note instructs the state to except such statutory provisions.

UCITA retains existing consumer protections laws, adopts consumer rules in Article 2, and adds limited additional protections appropriate for issues associated with computer information transactions.

Many contract law rules in UCITA benefit consumers. The doctrines of unconscionability, good faith, and fundamental public policy provide important consumer protections. But these rules also affect more than consumer transactions and respond to commercial concerns as well. So do the rules in UCITA (like those in Article 2) that disclaimer of implied warranties in a record must be conspicuous, or the rule in UCITA that a contractual choice of forum is unenforceable if it is unreasonable and unjust, or the rule in UCITA that assent is not effective unless there was an opportunity to review terms prior to giving assent. All of these and other rules benefit consumers but are not typically denominated as “consumer protection” rules. They contribute to the fact that UCITA creates a world in which consumers are better off than under current law.

UCITA also includes rules focused solely on consumer contracts and rules focused on mass-market contracts, which include all consumer contracts.

Section 105(c) provides that, except for stated rules regarding electronic commerce, if there is a conflict between UCITA and a consumer protection statute, the consumer protection law governs. Consistent with this theme, UCITA enacts rules preserving existing consumer law even if that result would not necessarily occur under other state law, such as:

- Section 104: an agreement to opt into or out of UCITA cannot change a mandatory consumer protection law that would otherwise apply
- Section 109(a): an agreed choice of law cannot alter an otherwise applicable consumer protection rule that cannot be varied by agreement

UCITA retains consumer protection rules contained in UCC Article 2 including:

- Section 303: a contract term requiring that modifications of contract be in writing is not enforceable in a consumer contract unless the consumer manifests assent to the term
- Section 704: licensee has a right to refuse tender of a copy that does not perfectly conform to the contract
- Section 803: consequential damages for personal injury cannot be disclaimed for a computer program contained in consumer goods

UCITA establishes various consumer protection rules focused on computer information transactions that do not exist under current law. These include:

- Section 209: a license cannot alter terms expressly agreed between the parties and, if presented after delivery, licensee has cost-free right of return if it refuses terms
- Section 214 a consumer has a right to avoid an online contract if it acts promptly to avoid the effect of an electronic mistake
- Section 302: safe harbor rule for changing terms in a continuing contract requires that the licensee that is a consumer be given a right to terminate when change is made
- Section 409(b): a warranty to a consumer extends to all individual consumers in the family or household if use should have been expected by the licensor
- Section 805: the statute of limitations for consumers cannot be reduced by agreement
- Section 104: a term changing the application of UCITA to the transaction must be conspicuous in a mass market transaction
- Section 503: a term that prohibits transfer of a contract right must be conspicuous for a mass market transaction

## VII. OVERVIEW OF UCITA'S PARTS

Part 1 of UCITA provides rules to establish norms and to provide guidance when the parties do not deal with a matter in their contracts for computer information transactions. These transactions cover computer software, Internet and online information, multimedia interactive products and computer data and databases. UCITA, however, generally treats software embedded in goods (like a computerized braking system) as goods, and excludes motion pictures, sound recordings and print media, leaving the current common law and statutes, which are deemed adequate, to govern their core businesses. Moreover, UCITA will allow the parties to choose UCITA, or other law, in transactions, where otherwise different bodies of law might apply to different aspects of the same transaction.

In addition to defining the coverage of the law, Part 1 of UCITA provides:

- Important limitations on the ability of the parties to bind each other by agreement and on the use of standard forms and shrink wrap licenses §§ 104, 105, 111, 112.
- Recognition of e-commerce. §§ 107, 108; and
- Much needed guidance for choice of law and forum, §§ 109, 110.

Part 2 of UCITA supplies modified contract formation rules adapted to permit and to facilitate electronic contracting, and rules to determine the terms of contracts formed, including protections against "imposed" terms, unauthorized communications, and electronic error, and incentives for pretransaction disclosure of all terms to be a part of the contract.

Part 3 of UCITA provides rules governing parol evidence, modification, changes in terms, and for interpretation in the absence of explicit treatment by the parties.

Part 4 of UCITA adjusts commonly recognized warranties as appropriate for computer information transactions; for example, to recognize the international context in connection with protection against infringement and misappropriation, and First Amendment considerations involved with informational content.

Part 5 of UCITA provides much needed clarification as to ownership rights and as to the ability to transfer rights (and duties) under a license, including by way of security so that financing for these transactions can be secured.

Part 6 of UCITA adapts traditional rules as to what is acceptable performance to the context of computer information transactions, including providing rules for the protection of the parties concerning the electronic regulation of performance ( 605), to clarify that the appropriate general rule is one of material breach with respect to cancellation (rather than so-called "perfect tender") (see 601; see also \_ 701, 704, and 802), and to carry over the familiar rules of Article 2 when appropriate in the context of the tangible medium on which the

information is fixed and for impracticability (Subparts B and D). Part 6 also supplies guidance in the case of certain specialized types of contracts (Subpart Q and for termination (Subpart E).

Part 7 of UCITA for the most part carries over the familiar rules of Article 2 concerning breach when appropriate in the context of the tangible medium on which the information is fixed, but also adapts common law rules and rules from Article 2 on waiver, cure, assurance and anticipatory breach to the context of computer information transactions.

Part 8 of UCITA provides a remedy structure somewhat modeled on that of Article 2 but adapted in significant respects to the different context of a computer information transaction. For example, 808 of UCITA recognizes the focus in a license context for a licensor's remedy should properly be on recovery for benefit conferred or for lost profit, rather than on damage measurement by a substitute transaction, where the license is non-exclusive so additional transactions are permitted and there is very little cost in reproduction of the information and its redistribution. Section 816 of UCITA also contains very important limitations on the generally recognized common law right of self-help as applicable in the electronic context.

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