
Technology Licensing and Electronic Contracting: Draft Article 2B of the Uniform Commercial Code Reviewed

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The National Conference of Commissioners on Uniform State Laws has been actively developing Article 2B of the US Uniform Commercial Code to provide statutory regulation of technology licences.

The most recent draft was released on 4 September 1996 and considerably varies previous drafts. It is anticipated that the final reading of the draft will occur in the US spring of 1997 and be sent to the States in the US summer of 1997.

The latest draft has expanded the coverage of Article 2B from software to a wide range of "digital information". The definition of "information" now covers licences of data, text, images, sounds, computer programs, software, databases and mask works. The Article covers not only information in existence at the time of the contract, but also information to be developed.¹

Transactions not covered by Article 2B include employment contracts, entertainment services agreements, transactions unrelated to software (such as trade names), and embedded programs.²

The scope of the Article as currently drafted includes online services contracts relating information and all software transactions (other than as excepted above). Because this scope creates a distinction between transactions involving a licence and transactions involving the sale of a copy, significant segments of the information industry are unaffected such as the sale of a copy of a book.

Article 2B presents 2 options for formal requirements in the formation of contracts. The first is that a contract is enforceable whether or not there is

a signed record. In other words the contract is electronic and not reduced to writing. This alternative has the effect of repealing the Statute of Frauds requirement that a contract be in writing.

The other alternative provides that a contract will not be enforceable unless a record of it has been signed or authenticated by the party against whom enforcement is sought. A written record will not be required where fees are less than \$20,000, or the licensor has already transferred copies of the information to the licensee.

While it is unclear which alternative the Commissioners will opt for, US copyright and patents law both require written agreements for an enforceable transfer.³ It is also arguable that the need for Statute of Frauds protection is greater in information contracts than in many others because of the intangible nature of the subject matter.

Section 2B-204 provides that acceptance to an offer can be indicated by an electronic agent⁴ even if the response is not reviewed or authorised by any individual.

The current draft of Article 2B introduces a new provision to regulate the formation of electronic transactions. To create a contract all that is required is for an electronic message initiated by one party to evoke an electronic message in response.⁵ The contract will be created although no individual was aware of or reviewed the initial message, response, reply, information, or action signifying acceptance⁶.

In other words, 2 computers can form a contract without any human review of, or reaction to, the electronic message or information product delivered. A frequent response to this

concept is that a contract principle that requires human assent would inject what might often be an inefficient and error-prone element into a modern format.

Shrink-wrap licences are validated by Section 2B-308 dealing with mass market licences. A person using a shrink-wrap product must have an actual opportunity to review both the contract and the product and must manifest assent. Consent can be indicated in a variety of ways, such as clicking on a designated icon or by an electronic agent sending an agreed signal.

The user of a shrink-wrap product will not be bound by any unusual terms unless they are made conspicuous and drawn to the licensee's attention. If a licensor wants to use surprising or objectionable terms in its mass market licences, and does not wish to risk their enforceability, the licensor must structure the transaction to obtain express assent by the licensee to the particular term⁷.

Another aspect of the draft Article is its prescription of certain implied and express terms. Significant terms include:

- that a licence is non-exclusive⁸;
- that a licensee is not entitled to rights in improvements or modifications made by the licensor, and a licensor is not entitled to rights in improvements or modifications made by the licensee⁹;
- that a licence of digital or similar information transfers the right for a single user at a single time to access, use, or copy the information on a single

machine¹⁰;

- that a party is not obligated to retain in confidence information given to it by another party, unless specified in the licence¹¹; and
- that a licensee has no right to the underlying data or source code¹².

Another key area of Article 2B is the codification of applicable warranties. All licences are specified to carry the following warranties:

- that the licensor has the authority to make the transfer and not interfere with the licensee's rights under the contract¹³;
- that at the time of transfer, the licensor has no reason to know that the transfer infringes existing intellectual property rights of a third party¹⁴. This warranty does not apply to pure licence of a patent;
- that if a demonstration model or sample forms part of the bargain, the final version will reasonably conform to the model or sample¹⁵.

In addition, Article 2B specifies an implied warranty of merchantability of computer programs marketed under a mass market licence. To be merchantable a computer program and any tangible media containing the program must:

- meet the contract description;
- be fit for the ordinary purposes for which it is distributed; and
- substantially conform to any promises or statements or facts on the container, documentation, or label¹⁶.

Warranties can be excluded or modified either by express words which, in the case of mass market licences, must be conspicuous¹⁷, or where a computer program is modified by a licensee¹⁸.

Part 5 of the draft Article deals with transfers of licences. The fundamental rule is that transfer of title to, or possession of, a copy of information does not transfer ownership of the intellectual property rights in the information. In other words, a licensee's right to possession or control of a copy is governed by the contract and does not depend on title to the copy¹⁹.

The provision for transfer of a copy by electronic means is more controversial. It provides that transfer of a copy will transfer title of the copy if the transfer constitutes a first sale under US copyright law. This provision reflects current thinking in the US as indicated in the White Paper²⁰. The White Paper resolved that electronic delivery of a copy of a copyrighted work is not a first sale because it does not involve transfer of a copy from the licensor to the licensee²¹.

If a party is in breach of a contract, the draft Article provides that the party should be given an opportunity to cure the breach at its own expense. The obligation is to make an effort to cure "in good faith" or to provide a refund. The opportunity to preserve the contractual arrangement is a pragmatic response to a breach which is not fundamental²².

The remainder of the draft Article deals with termination, damages, and

the consequences of termination.

As complex legal issues arise with the increase in electronic commerce, Australian courts will no doubt look from time to time to the provisions of Article 2B. It is a valuable attempt at codifying current US contract law in an electronic environment.

¹ Section 2B-102(a)(18)

² Section 2B-103(d)

³ 17 USC 204; 35 USC 261

⁴ Defined as "a computer program designed to initiate or respond to electronic messages or performances without review by an individual"

⁵ Section 2B-205

⁶ Section 2B-205(b)

⁷ Commentary by the Reporter to the National Conference of Commissioners on Uniform State Laws

⁸ Section 2B-310

⁹ Section 2B-311

¹⁰ Section 2B-313

¹¹ Section 2B-316

¹² Section 2B-317

¹³ Section 2B-401(a)

¹⁴ Section 2B401(b)

¹⁵ Section 2B-402

¹⁶ Section 2B-403

¹⁷ Section 2B-406

¹⁸ Section 2B-407

¹⁹ Section 2B-501

²⁰ Intellectual Property and National Information Infrastructure", Report of the Working Group on Intellectual Property Rights, September 1995

²¹ Ibid, p.213

²² Section 2B-620