Duquesne Law Review

Volume 38
Number 2 *Symposium on Approaching E-Commerce Through Uniform Legislation: Understanding the Uniform Computer Information Transactions Act and the Uniform Electronic Transactions Act*

Article 5

2000

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Recommended Citation
Raymond T. Nimmer, *Through the Looking Glass: What Courts and UCITA Say about the Scope of Contract Law in the Information Age*, 38 Duq. L. Rev. 255 (2000).
Available at: https://dsc.duq.edu/dlr/vol38/iss2/5

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Through the Looking Glass: What Courts and UCITA Say About the Scope of Contract Law in the Information Age

*Raymond T. Nimmer**

INTRODUCTION

What we often describe as "contract law" is comprised of heterogeneous clusters of case and statutory law pertaining to, and differently describing, various contractual relationships. Many who purport to study contract law and focus solely on the rules found in the Uniform Commercial Code ("UCC") regarding the sale of goods, or on the proposed rules of the *Restatement (Second) of Contracts*, ignore this heterogeneity. However, in modern U.S. law, contract law does not exist as a single, integrated whole in a manner relevant to those engaged in commerce.[1] While there are many common themes, the reality lies as much in differentiation as in commonality.

This is important because we are currently in an era of turmoil in contract law caused by fundamental change in the economy from which contract law emerges.[2] The turmoil is reflected in substantive changes in how contracts are made and in the primary subject matter of commercial contracts.[3] The turmoil comes

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1. " 'One system of precedent' we may have, but it works in forty different ways." Karl Llewellyn, *On Philosophy in American Law*, 82 U. PA. L. REV. 205, 205 n. * (1934).

2. In the United States, the Uniform Commercial Code ("UCC") is being redrafted. Two new articles were added (Article 2A (Leases) and Article 4A (Funds Transfers)). Article 2A was approved in 1987 and Article 4A was approved in 1989. Article 9 and virtually all other Articles of the Code have been redrafted. A revision of Article 2 (Sales) is being considered.

3. In terms of methods of contracting, various states and countries have adopted rules that clarify that electronic records and electronic signatures satisfy requirements from prior law. A comprehensive listing of enacted and proposed legislation dealing with this subject can be found at *Summary of Electronic Commerce and Digital Signature Legislation* <http://www.mbc.com/ecommerce.html> (last modified Jan. 13, 20000). This listing includes over 35 states with enacted legislation dealing with electronic or digital signatures. *See also* RAYMOND T. NIMMER, THE LAW OF COMPUTER TECHNOLOGY ch. 14 (3d ed. 1997) (for a discussion of several of the major statutes). Many of the state statutes have limited scope. However, a number of states, including Utah, Washington, Illinois and Minnesota, and various countries

primarily from the emergence of a new market economy.[4] Transactions in this new environment differ from transactions in the old, both in technique and in subject matter. Yet, older images of contract and commercial practice continue to affect decisions of legislators and courts.

We have changed from a goods-based economy to one that substantially relies on transactions in digital information and services. The fact that "information" is a primary subject matter of commercial exchange is now a central reality of the economy. Much of the contract law that developed in the 1940's and 1950's was based on an image of sales of goods. During the 1960's, an image of a "consumer" buyer was added and often wrongly generalized to extend to all buyers of goods. While adequate for their own purposes, these images do not fit contracts for licensed access to a digital database, for use of network or communications software, or for access to or use of other information assets.

The contract issues involved in creating, compiling, distributing, and enabling the use of information entail different questions than those involved in manufacturing and distributing hard goods. The subject matter of such contracts is intangible; the property is defined not by the law of goods but, rather, by control of computer systems or property rights as defined by intellectual property law.

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have enacted relatively comprehensive legislation that not only allows electronic signatures to satisfy traditional writing and signature requirements, but also deals with the liability of parties using and relying on digital signatures. Internationally, the European Union has issued a proposed directive dealing with electronic signature issues, intending to forestall the development of inconsistent national laws within the Union. *See* European Commission, *Proposed Directive on a Common Framework for Electronic Signatures* — COM (1998) 297. The mbc.com site lists 14 countries that have taken steps with respect to digital and electronic signature laws, including relatively elaborate legislation in Germany, Italy, and Singapore.

4. A related reshaping in law lies in changes in traditional intellectual property fields, and especially those associated with copyright law. Included are changes in expanded database protection in Europe and significant modifications in U.S. copyright law, including limited statutory recognition of "moral rights," digital performance rights, and most recently the enactment of expansive protections for digital monitoring and security devices that augment copyright protection. All of the following have been enacted within the past decade: 17 U.S.C. §§ 1201-121205 (Supp. IV 1998) (aspect of the Digital Millennium Copyright Act dealing with "copyright protection and management systems"); 17 U.S.C. § 1101 (1994) (protection from "unauthorized fixation and trafficking in sound recordings and music videos"); 17 U.S.C.A. § 106A (1990) (protection of the rights to "attribution and integrity" (so-called "moral rights") for certain works); 17 U.S.C. § 106(6) (1995) (right to exclusive control digital audio transmission of a sound recording). *See also* COUNCIL AND EUROPEAN PARLIAMENT DIRECTIVE, ON THE LEGAL PROTECTION OF DATABASES, 96/9/EC (1996) OJ L 77 (establishing new extraction rights with reference to otherwise unprotected content of a database).

The contractual relationships differ from those typical of the law of goods. Examples of the most common transactions include contracts for access to an online service or for a license of rights in information.

This article discusses the question of: "what contract law applies to computer information transactions?" The focus is not on the substance of contract law, but on the various sources of applicable contract law and the images they bring to the transaction. The answer to this question is embedded in conflict, misperception, and political debate. Contract law ideas today are dominated by concepts from yesterday.

Part I briefly describes the relationship between contract law and contract practice. Contract law fosters freedom of contract and facilitates commercial relationships. This is sometimes over-ridden by express regulation, but the basic principle is strikingly resilient because it sets the basis for our market economy: contract choices control unless there is a clear public interest need to curtail them. As a result, general contract law rules serve only a background function. They provide rules for commercial relationships, but only when the agreement does not otherwise provide. The agreement, not the law, controls. In that context, an appropriate body of contract law should be adapted to the type of commerce involved because it fills gaps when the parties are silent. The rules we achieve, however, are shaped by the images that law-makers bring to the task and often when the images are wrong, the rules are wrong.

Part II discusses what law applies to computer information transactions. There we trace, through case law, various sources of contract law. The overall contract law that emerges is complex, characterized by divergent authorities and unclear or erratically applied criteria. The policy issue is whether this complex and often obscure law is appropriate now that computer information transactions dominate large parts of the economy.

Within the complexity, one theme emerges. The images associated with sales of goods law and consumerism have greatly affected the development of modern contract law, including the law relating to computer information transactions. This much would have been obvious without great study. But the fact is that courts often use the sales image for transactions that have little to do with a title transfer of a tangible item to a buyer (the paradigm of a sale of goods). Again, when the images are wrong, the results are often wrong. When looked at from the vantage of the goods-centric

perspective in UCC Article 2, the world of contract law has often been construed as a world differentiated between the sales of goods and the sales of personal services. That image, never correct, is even more clearly incorrect today as information transactions emerge as a centerpiece of the economy.

The cases reveal not only a misperception by some courts, but also recognition by many others that transactions in information are different from goods. Overall, what is occurring is an often-wrenching shift away from a world of contract law dominated by images of the sale of goods to consumers. Sales of goods have been at the forefront of the economy for years; they remain important. Their law, represented by UCC Article 2, was drafted specifically to *carve out* sales contracts from general contract law. Contrary to that intent, this statute became a factor throughout all contract law. Now that other subject matter has become important, we must recognize that assumptions based on sales must be reevaluated and replaced with images attuned to transactions in digital information.

Part III discusses what the law relating to computer information transactions may be in the future, with the focus on the Uniform Computer Information Transactions Act ("UCITA"). This uniform act was promulgated in July of 1999 and sets out a contract law regime for the information age with respect to computer information transactions. Its contract law regime is based on a blend of common law, intellectual property, and UCC concepts. The goal is to provide coherent guidance relevant to the type of transactions involved. Rather than deal with the details of UCITA, the focus is on the general scope of the Act.

I. CONTRACT AND COMMERCE

A. *Contract Law: Images of the Past*

Contract law is comprised of generally applicable principles providing umbrella themes linked to differentiated rules applicable to different contract relationships. The general themes deal with certain issues of contract formation and limited restrictions on contract terms. These themes are not consistently applied among the states. But that is the nature of common law, where individual court decisions control.

Beneath the general themes, there are sub-themes and sub-fields. This too is an outcome of common law, which encourages courts

to make distinctions based on subject matter and context. The differentiation has been accentuated by statutory regulations that distinguish, for example, among "commercial contracts," "consumer goods," "credit contracts," and "transactions in securities." The contract law to which courts turn in deciding the enforceability of an employee contract is different from the law used in deciding the enforceability of a real estate deed, which is different from the law pertaining to the sale of a television set, and all three differ from the law that governs licenses of information. The differentiation is explicit in the UCC. The UCC contains transactional rules that give extensive treatment to transactions in goods and selected financial transactions, but which do not address other subject matter, even though the other subject matter may be more significant in commerce.[5]

The efficacy of contract law in this context hinges on drawing appropriate distinctions. This does not always occur; it is less likely to occur after the economy undergoes a paradigm shift. Courts and legislators often characterize issues based on their own experience and the images from that experience. Yet, the images of the past often mislead us. Llewellyn commented:

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5. The question of when it is appropriate or useful to treat a body of related case and statutory law as a field of contract or as suitable for inclusion in the commercial code or other body of uniform law is at best an inexact science. Llewellyn wrote:

> Our fields of law, our patterns of legal thinking, our legal concepts, have grown up each one around some 'type' of occurrence or transaction, *felt* as a typical something, *seen* in due course as a legally significant type, and, as a type-picture, made a standard and a norm for judging.

Karl Llewellyn, *The First Struggle to Unhorse Sales*, 52 HARV. L. REV. 873, 880 (1939). The first treatises on the law of sales did not appear until 1847. *See generally* W. STORY, A TREATISE ON THE LAW OF SALES OF PERSONAL PROPERTY (1847); COLIN BLACKBURN, A TREATISE ON THE EFFECT OF THE CONTRACT OF SALE ON THE LEGAL RIGHTS OF PROPERTY AND POSSESSION IN GOODS, WARES AND MERCHANDIZE (1847). Yet by 1940, the U.S. had already seen a uniform act and a proposed revision of that act (Article 2).

> This is very well, for it would be a very troublesome question, if anyone bothered to look into it, just what the relationship between the "field" of contract and the "field" of Sales might be, or indeed how a man can spot "a field" of law when he sees one, anyhow, and figure out its relation to its neighbors. Enough for us at the moment that Sales is supposed to center on the transfer of property in goods, and covers also contracts which look to that end, and that it must be a field because there are books about it . . . . But the presence of books, casebooks, and titles in encyclopedias would seem to settle the matter. It is a field.

Karl Llewellyn, *Across Sales on Horseback*, 52 HARV. L. REV. 725, 728-29 (1939). Elsewhere, I discuss some of the criteria that indicate the desirability of following the course that Llewellyn set. *See* Raymond T. Nimmer, *Intangibles Contracts: Thoughts of Hubs, Spokes, and Reinvigorating Article 2*, 35 WM. & MARY L. REV. 1337 (1994); Raymond T. Nimmer, *Services Contracts: The Forgotten Sector of Commercial Law*, 26 LOY. L.A. L. REV. 725 (1993).

> [If] the stock intellectual equipment [(image)] is [inapt], it takes extra art or intuition to get proper results with it. Whereas if the stock intellectual equipment is apt, it takes extra ineptitude to get sad results with it. And the work of the artist, accomplished with poor intellectual equipment, is not clearly intelligible to the inept reader. It does not talk to him, it does not provide him tools, it does not help him to focus issues.[6]

In litigation, wrong images may lead to wrong judicial decisions. In transactional contexts, this may be less important than other consequences. Rules based on wrong images do not provide guidance to those who plan transactions. A rule based on inapt images does not "talk to" the reader and, if it does, forces the reader to act to avoid the inappropriate effect of the rule.

B. Contract Law: Default Rules

At one level, the relationship between commercial contract law and commercial practice is simple: contract law provides background rules indicating how to create a contract and giving terms of contract that apply if the parties do not otherwise agree. General law also sets out limited rules about when the agreement should not govern.

At a different level, dealing with how this affects actual transactions, the relationship is complex. Contract law is a practical discipline that contemplates an impact on transactions, parties, and markets. We should evaluate it not on the basis of whether the rules support correct litigation results when very few contracts result in any litigation at all, but rather, based on whether their impact on *transactions* is positive. Yet, the actual relationship between contract law and contract practice is not well understood and there is little reliable empirical data.[7] We are not certain about what happens in the black box that encompasses contract negotiation and performance. However, there is one thing we do

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6. Karl Llewellyn, *The First Struggle to Unhorse Sales*, 52 HARV. L. REV. 873, 876 (1939).

7. *Cf.* Russell J. Weintraub, *A Survey of Contract Practice and Policy*, 1992 WIS. L. REV. 1 (discussing the results of a questionnaire about contract practices); Stewart Macauley, *Non-Contractual Relations in Business: A Preliminary Study*, 28 AM. SOC. REV. 55 (1963). The theoretical constructs used in some literature refer to behavior in an abstract world that does not correspond to actual, more complex transactional environments. *See, e.g.*, Ian Ayres & Robert Gertner, *Strategic Contractual Inefficiency and the Optimal Choice of Legal* Rules, 101 YALE L.J. 729 (1992); Daniel Farber, *Parody Lost/ Pragmatism Regained: The Ironic History of the Coase Theorem*, 83 VA. L. REV. 397 (1997).

know: given a rule of "contract choice" and the reality of a marketplace with multiple options, contract law affects actual transactions indirectly, rather than in a direct fashion. If they have any effect at all, the rules are background factors for the transaction, like the rules of property law. They *might* set a bargaining point or indicate what language yields what result,[8] but the relative strength of law as contrasted to market preference, market power, bargaining strategy, marketing choice, cost, timing and other considerations is not known. I suspect that contract law is not routinely the major consideration in contract practice.[9]

While some argue for background rules designed to alter

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8. *See generally* Ian Ayres & Robert Gertner, *Strategic Contractual Inefficiency and the Optimal Choice of Legal Rules*, 101 YALE L.J. 729 (1992) (discussing the extent to which theory can predict response in bargaining to default rules intended to shape contracting behavior).

9. The relative strength of law as contrasted to other more tangible effects such as market power, bargaining strategy, cost, and timing considerations remains largely unknown. One illustration involves the rule in Hadley v. Baxendale, 9 Ex. 341, 156 Eng. Rep. 145 (1854). Law and economics scholars typically treat *Hadley* as a rule that sharply limits the liability of a promisor for consequential damages in the event of breach. This is a "default" rule in that the parties can contract for a different result. A number of authors have justified this rule as a "penalty" or an "information forcing" rule that supposedly forces a promisee concerned about a risk of extensive consequential loss in the event of breach to signal that concern and seek to bargain around the default rule for contract terms that makes the promisor liable for more extensive damages. *See* Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87 (1989); John C. Coffee, *The Mandatory/ Enabling Balance in Corporate Law: An Essay on the Judicial Role*, 89 COLUM. L. REV. 1618, 1623 (1989); Robert E. Scott, *A Relational Theory of Default Rules for Commercial Contracts*, 19 J. LEGAL STUD. 597, 609-11 (1990). Arguably, this allows the promisor to take a proper level of precautions in return for a higher price. But, while this incentive may exist, it may be off-set by competing strategic considerations. Furthermore, strategic considerations that focus on obtaining a better "bargain" are more immediate and direct in the contracting party's contemplation than concerns about what rule would apply in the event of non-performance, large loss, and resulting litigation. As Jason Johnston notes,

> if we are talking about *bargaining* over the contract, then we are talking about a process of strategic information transmission, a process in which the promisee tries to persuade the promisor that she cannot pay a high price, and the promisor tries to persuade the promisee that she should. In this process, the promisee would generally want to convince the promisor that her value from performance is low.

Jason Scott Johnston, *Strategic Bargaining and the Economic Theory of Contract Default Rules*, 100 YALE L.J. 615, 616-17 (1990). The promisee would not desire to communicate that non-performance may inflict large loss. The world of commercial contracting in fact is complex. What actually occurs in reference to consequential loss or other default rules must be filtered through an understanding of that complexity and the uncertainty of prediction that it creates. Generally stated, conceptual models of contract bargaining are always inexact. "[R]elatively simple contractual settings can give rise to enormous complexity. While . . . different default rules . . . would be theoretically efficient, our model shows that there is small hope that lawmakers will be able to divine the efficient rule in practice." Ayres & Gertner, *supra* note 8, at 733.

contracting behavior, the complexity of the context argues against this ever being successful. The dominant view is that the law should allow contract choice and that, failing an agreed choice, contract default rules should mesh with conventional practice in a manner that projects a predictable result.[10] Predictability means predictable *by parties* engaged in the particular *type* of transaction. This is not the same as saying that a party (or advocates for a particular position) should receive what they would have wanted if they had the inclination and bargaining power to achieve it *in a transaction.* It cannot be asked or answered about individual parties, but only about transacting parties generally involved in such transactions from both perspectives.

Default rules of this type must be tailored to the commercial context.[11] Rules that are not so tailored increase costs because parties must negotiate to eliminate their effect. Yet, if our image of the context is wrong, the result will be wrong. Over fifty years ago, Llewellyn argued that commercial contract law should be developed by focusing on the particular commercial context in order to develop rules of relevance and positive effect *in that context.* The same holds true today. Then, the issues centered on a transition from agrarian commerce to mercantile commerce in manufactured goods. Now, contract law has a similar shift to account for, but the recent transition is away from sales of manufactured goods and toward subject matter that consists of

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10. This is in contrast with rules that dictate terms and attempt to regulate commercial behavior. As a matter of practice, default rules are most common in commercial contexts, while "consumer law" contains many immutable rules designed to protect the consumer against mercantile over-reaching.

11. *See, e.g.*, Ian Ayres & Robert Gertner, *Strategic Contractual Inefficiency and the Optimal Choice of Legal Rules*, 101 YALE L.J. 729 (1992); David Charny, *Hypothetical Bargains: The Normative Structure of Contract Interpretation*, 89 MICH. L. REV. 1815 (1991); Richard Craswell, *Contract Law, Default Rules, and the Philosophy of Promising*, 88 MICH. L. REV. 489 (1989); Jason S. Johnston, *Strategic Bargaining and the Economic Theory of Contract Default Rules*, 100 YALE L.J. 615 (1990). Charles J. Goetz & Robert E. Scott, *The Limits of Expanded Choice: An Analysis of the Interaction Between Express and Implied Contract Terms*, 73 CAL. L. REV. 261, 266 (1985); Randy E. Barnett, *The Sound of Silence: Default Rules and Contractual Consent*, 78 VA. L. REV. 821, 822 (1992)

> First, . . . default rules [that reflect the conventional or commonsense understanding existing in the relevant community] are likely to reflect the tacit . . . agreement of the parties and thereby facilitate the social functions of consent. Second, when parties have asymmetric access to the background rules of contract, enforcing conventionalist default rules will reduce subjective disagreements by providing parties who are . . . informed of the background rules with an incentive to educate those parties who are . . . ignorant of these rules.

Id. at 829.

services or transactions relating to computer information.

II. What Law Applies

What is the current contract law for computer information transactions? Initially, there is a bright line drawn between two areas of contract law.

On one side of this line are rules of contract law that apply to real estate transactions. This law, with its own terminology and transactional requirements, split off early from other contract law; over the years, it has proven remarkably resistant to influence by other commercial *contract* law. Real estate law is embodied in tailored statutory and tailored common law. There are some themes common with contract law for goods and other subject matter, but the dominant characteristic lies in the differences. Viewed from a perspective of one comfortable with the UCC, real estate contract law seems encrusted with old language, formalities, and concepts, which seem arcane in a commercial world. Of course, real estate law has been anything but stagnant and is characterized by continuous, creative efforts to extract value from assets in new ways. The same is true of all commercial law fields, but the language and images are often starkly different outside real estate transactions.

On the other side of the line, there is a multiplicity of subject matter and commercial practice or expectations. Contract settings here range from professional service agreements, to database contracts, to franchise agreements, patent licenses, sales of goods, airline tickets, stock brokerage, publishing, maintenance, leases, rentals of motion pictures, licenses of software, bank deposit agreements, access contracts for online services, loan agreements, agreements to conduct surveys, cable television contracts, parking lot agreements, cruise boat tickets, contracts for artistic performances, and insurance contracts.

This diverse side of the line contains the contracts relevant to the information economy. If we focus on computer information transactions, the potential sources of contract law include:

- Sales of goods law
- Leases of goods law
- Bailment law
- Services contract law
- Professional services law
- Information contract law

- Copyright law
- Patent law
- Trade secret law
- Trademark law
- Licensing law
- Consumer protection state law
- Consumer protection federal law
- Tort negligence law
- Negligent misrepresentation law
- Agency law
- Non-consumer state regulatory law
- Non-consumer federal regulatory law
- Miscellaneous other law

What does one make of this complexity? The answer is clear to any lawyer who practices transactional law. The transactional lawyer must contend with a mixture of laws applicable to any contractual transaction. Almost all commercial transactions in every field are "mixed transactions" in that multiple sources of contract law apply to them.

A. *Article 2 as an Influence*

A dominant influence in many areas of contract law as compared to regulation over the last fifty years comes from the law of sales of goods in UCC Article 2. The degree of its influence varies depending on the other subject matter involved and the coherence of contract law rules designed for that other subject matter, but the Article 2 influence has been pervasive.[12] It affects transactions where courts treat the transaction as if it were a transaction in *goods* when it is not, where courts apply the law of sales by *analogy* to a transaction admittedly not a transaction in goods, and by shaping views of what is appropriate *common law* for transactions other than transactions in goods.[13] Article 2 has

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12. For example, the law of sales has had relatively little impact on real estate contract law or on the law governing professional services agreements in law and medicine. *See, e.g.*, McCombs v Southern Reg'l Med. Ctr., Inc., 504 S.E.2d 747 (Ga. Ct. App. 1999) (holding that an operation to install a plate to stabilize the patient's spine was not a sale of goods); Pitler v. Michael Reese Hosp., 415 N.E.2d 1255 (Ill. Ct. App. 1980) (holding that the UCC did not apply to radiation treatments); In re Breast Implant Prod. Liab. Lit., 503 S.E.2d 445 (S.C. 1999) (holding that health care providers providing breast implants were not sellers of goods). On the other hand, Article 2 has a broad impact on other services contracts.

13. *See, e.g.*, Printers II, Inc. v. Professionals Pub., Inc., 615 F. Supp. 767 (S.D.N.Y. 1985), *aff'd on other grounds* 784 F.2d 141 (2d Cir. 1986); Telesaver, Inc. v. United States

become a major influence in modern contract law.

Why? One would like to say that it happened because Article 2 "got it right" for *all* commerce and all commercial contracts. But that is clearly not true, nor is it what Llewellyn sought to achieve.[14] The goal was to tailor contract law for a particular type of contract-sales of manufactured goods. Frankly, it is quite clear that the Article 2 sale of goods model did not, and could not, "get it right" for diverse contracts such as licensing agreements, employment contracts, repair agreements, consulting contracts and other commercial agreements that are important in commerce. Article 2 did set a base for contract law regarding sales of manufactured goods. That base was immediately reshaped for retail consumer sales of *goods* by law outside of Article 2.[15]

In part, the dominance arose because, for most of its fifty years, Article 2 was the only source of codified contract law. It contrasts with uncertain and often conflicting common law. One could teach, write, plan, and debate with respect to Article 2, knowing that it had broad effect. Courts and litigants looking for a reference point could use Article 2 with greater ease than the diverse and often

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Transmission Sys., Inc., 687 F. Supp. 997 (D. Md. 1988); Zapatha v. Dairy Mart, Inc., 408 N.E.2d 1370 (Mass. 1980).

14. A recent, very explicit illustration of this occurred in the ruling of the Court of Appeals for the Federal Circuit in DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999), where the court declined to apply the Article 2 concept that delivery of goods pursuant to a contract for sale transfers title to the goods in a case involving a license of computer software. Ownership was determined based on considerations unrelated to the Article 2 concept. *See also* Milau Assoc. v. North Avenue Dev. 368 N.E.2d 1247 (N.Y. 1977) (holding that the implied warranty of fitness for a particular purpose was not applicable to contract for services); Board of Trustees v. Kennerly, Slomonson & Smith, 400 A.2d 850 (N.J. Super. Ct. 1979) (holding that a professional engineer responsible for preparing specifications for plaintiff's lighting system and supervising its installation was not subject to action for breach of an implied warranty of fitness; the rendering of professional services not in a routine manner, but in plans and specifications tailored to individual requirements so that they reflect the exercise of professional judgment, is a personal service); R.J. Longo Const. Co., Inc. v. Transit America, Inc., 921 F. Supp 1295 (D. N.J. 1996) (holding that New Jersey law did not imply a warranty of fitness under the UCC in a professional services contract between an engineer and a purchaser of railroad cars). *But see* Minnesota in Robertson Lumber Co. v. Stephen Farmers Cooperative Elevator Co., 143 N.W.2d 622 (Minn. 1966) (stating that the warranty of fitness might apply in a construction contract); Air Heaters, Inc. v. Johnson Elec., Inc., 258 N.W.2d 649 (N.D. 1977) (stating that contracts involving the installation of an electrical system should not automatically be held to be outside Article 2 of the UCC); Department of Transp. v. Bethlehem Steel Corp., 368 A.2d 888 (Pa. Commw. Ct. 1977) (applying a warranty of fitness, but not under Article 2).

15. David W. Carroll, *Harpooning Whales, of Which Karl N. Llewellyn is the Hero of the Piece; or Searching for More Expansion Joints in Karl's Crumbling Cathedral*, 12 B.C. INDUS. & COM. L. REV. 139 (1970).

incomplete or obscure common law. Also, sales, of course, dominated the economy. Sales were the types of transaction with which most of us were most familiar.

This being said, the new subject matter and new transactions that emerged as major elements of the economy in the past two decades have loosened the grip of Article 2.

- Many of sales rules are not pertinent to leases of goods, which have become a major type of commercial contract. Thus, Article 2A on leases of goods evolved.[16] While it follows some Article 2 rules, in many contexts Article 2A is a tailored law to accommodate an image and practice of leases, rather than sales.[17]
- Many ideas of contracts in goods are not pertinent to transactions in information or services, which are now a predominant part of the economy. Thus, UCITA on computer information transactions evolved.[18]

More generally, modern cases that deal with the scope of Article 2 are increasingly alert to the fact that the law of sales is not appropriate for transactions for services, the design of products, or transfers of rights in information, and that the *other* subject matter has a coequal claim to tailored contractual law as does the law of sales.[19]

B. Nature of Influence: General or Specific Rules

While Article 2 has a dominant role, we must distinguish between general contract principles and specific contract law rules. A limited number of general Article 2 concepts are broadly dominant in contract law. A larger number of Article 2 rules that specify details of a sale are less commonly applied outside true sales or leases of goods; these include implied warranties, transfer of title, tender of delivery, damages, risk of loss, statute of limitations,

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16. *See* U.C.C. Article 2A, *Prefatory Note* (1998).

17. For example, while the warranty rules of Article 2A are parallel to Article 2 warranties (see, e.g., U.C.C. § 2-314 and § 2A-212), Article 2A does not presume that title to the goods passes to the lessee on delivery and Article 2A adopts much different rules for determining damages in the event of breach (see, e.g., U.C.C. § 2A-528 and § 2-708).

18. *See* U.C.I.T.A., *Prefatory Note* (1999 Official Text).

19. *See, e.g.*, Grappo v. Alitalia Linee Aeree Italiane, S.p.A., 56 F.3d 427 (2d Cir. 1995); Minnesota Forest Prods., Inc. v. Ligna Machinery, Inc., 17 F. Supp.2d 892 (D. Minn. 1998); Stewart v. Lucero, 918 P.2d 1 (N.M. 1996); Kirkpatrick v. Introspect Healthcare Corp., 845 P.2d 800 (N.M. 1992). *Cf.* Fournier Furniture, Inc. v. Waltz-Holst Blow Pipe Co., 980 F. Supp. 187 (W.D. Va. 1997) (involving a contract to design and deliver a furnace).

statute of frauds, and the like.

1. Sales Law and General Contract Principles

Several ideas in Article 2 have become core modern contract law with general relevance unrelated to details of a sale of goods. In the 1950's, as to many of these issues, Article 2 led a revision to the idea of the contract, more suited to a modern, flexible commerce, than to the rigid concepts characterizing earlier contract law.

When developed, Article 2 proposed a change in contract formation rules which moved away from the rigidity of the then-current common law requiring a mirror image of offer and acceptance to form a contract.[20] It affirmed, instead, a commercial reality that contracts are often formed with open or conflicting terms and that terms are developed over a period of time in a process, rather than coming together at a single point in time.[21] These rules are now "common law" in a number of states.[22] Of course, Article 2 did not "get it right" in all respects on contract formation, nor have all cases correctly followed its concepts.[23] But the idea of flexible, layered contracting in Article 2 influenced common law courts and the *Restatement*, even though many courts also get it wrong, reverting to a formalistic view of when contracts are formed,[24] and in many states, the "mirror image" rule and its associated formalities remain embedded common law and applied outside Article 2 and 2A.

What has been said about contract formation is also true about some other general rules in Article 2 and Article 1 of the UCC. For example, the UCC mandates interpretation of contracts based on their practical context, rather than on the terms of the statute.[25]

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20. *See* U.C.C. § 2-207 (1998) (stating that a contract can be formed by a clear acceptance, even if the acceptance contains terms that vary from the offer).

21. *See, e.g.*, Jeff C. Dodd, *Time and Assent in the Formation of Information Contracts: The Mischief of Applying Article 2 to Information Contracts*, 36 HOUS. L. REV. 195 (1999).

22. *See* 1 E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS § 3.21 (2d ed. 1998).

23. U.C.C. § 2-207 is perhaps the classic case of a provision that did not, and generally does not, work in litigation. Of course, properly construed, that provision is one of the linchpins of the entire flexible contract formation rules in Article 2.

24. *See, e.g.*, Step-Saver Data Sys. v. Wyse Tech., 939 F.2d 91 (3d Cir. 1991) (holding that a contract and all its terms were formed on the placing of a telephone order with the contract consisting largely of Article 2 default rules and that subsequently proposed terms could not be part of the agreement unless agreed to as a modification).

25. *See* U.C.C. § 1-205.

This requires that courts look at the context of the agreement, rather than the statute, to determine the relationship of the parties; default rules apply only when the context gives no answer. When properly used, this rule derogates from any idea that *law* controls: it clearly states that the "agreement" controls and that the meaning of an agreement is a contextual issue. This principle is as true for services, information and other contracts as it is for sales.

UCC Article 1 provides that all contracts carry an obligation to perform in "good faith."[26] Article 2 provides that a court can invalidate a contract term that is "unconscionable."[27] These substantive ideas are linked by a common perception that certain over-riding obligations exist in contracting and contract performance, which themes allow courts to invalidate instances of over-reaching. Both themes are incorporated in the *Restatement* and in common law in many, but not all, states.[28] The doctrines are narrow. "Good faith" does not provide a basis to contradict express contract terms or rights.[29] The express terms of the agreement control. Unconscionability claims are frequently rejected unless circumstances entail procedural and substantive over-reaching. Even within the UCC, these themes are not universally applied. For instance, the unconscionability rule does not apply to Article 9 transactions.

Yet, in these and a few other contexts, Article 2 set out a "hub" of basic rules with relevance beyond the sales of goods.

2. *Sales Law as a Separate and Distinct Field*

In contrast to the general rules we have discussed, Article 2 also contains many rules tailored to the structure and expectations of a sale. These rules, while sometimes applied in transactions that are

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26. *See* U.C.C. § 2-103.

27. *See* U.C.C. § 2-302.

28. RESTATEMENT (SECOND) OF CONTRACTS § 208 (1979). The comments on this section indicate a close correspondence to the treatment of this issue in the UCC. *Id.* at § 208, cmt. d. Not all states follow the rule on good faith or unconscionability. *See, e.g.*, McDonald's Corp. v. Watson, 69 F.3d 36 (5th Cir. 1995) (holding that the rule does not apply, under Illinois law, to a franchise agreement falling outside the UCC). *Cf.* Stanley A. Klopp, Inc. v. John Deere Co., 510 F. Supp. 807 (E.D. Pa. 1981) (holding that under Pennsylvania law, the good faith obligation from UCC applies even though Article 2 does not); Angus Medical Co. v. Digital Equip. Corp., 173 Ariz. 159, 840 P.2d 1024 (Ariz. 1992) (unconscionability).

29. *See* McDonald's Corp. v. Watson, 69 F.3d at 36 (5th Cir. 1995) (holding that the terms of the contract govern); Kham & Nates Shoes No.2, Inc. v. First Bank of Whiting, 908 F.2d 1351 (7th Cir. 1990) (holding that the good faith duty does not override the right to enforce the terms of the contract). *See generally* PERMANENT EDITORIAL BOARD OF THE U.C.C., COMMENTARY NO. 10 (regarding the scope and nature of the "good faith" obligation).

facially unlike a sale, are more often limited in impact to actual sales or, at least, transactions where sales of goods clearly predominate.

There are many rules in this category that have been, perhaps, extended to leases of *goods*, but not otherwise in contract law. For example:

- Article 2 provides for a complex dance associated with tender, inspection, and either acceptance or rejection of the goods tendered pursuant to the sales contract. This dance has been followed in Article 2A, but not in any other area of contract law.
- Article 2 creates a "perfect tender" rule for when or if a buyer can reject goods. This rule is followed in Article 2A, but not in any other contract law field.
- Article 2 contains numerous rules about delivery or shipment terms associated with carriers of goods. These rules are not present in other contract law and, in fact, conflict with modern international understanding even for shipment of goods.
- Article 2 creates an implied warranty of merchantability if the transaction involves a merchant seller. This rule is followed in Article 2A, but not in other areas of contract law.
- Article 2 establishes an implied warranty of fitness for a particular purpose in certain instances. This rule is followed in Article 2A, but not in other contract law.
- Article 2 presumes that title to goods passes on delivery to the buyer. Neither Article 2A nor other contract law presumes a transfer of title as an ordinary part of a transaction.
- Article 2 contains rules concerning risk of loss as to the goods, which have no counterpart in general law.
- Article 2 sets out damage formulas associated with resale or replacement of the particular item, but these rules are not followed in other contract law, including Article 2A.
- Article 2 allows consequential damages only for the buyer, while general contract law allows such recovery for either party to a transaction.

The point is not that these rules are *never* applied to transactions outside Article 2 or to subject matter included in a transaction that

also includes Article 2 subject matter.[30] The point is that Article 2 and Article 2A contain tailored contract laws suited to their own context. For that context, the rules provide a relatively well-suited base, while they may be entirely unsuited outside that particular context.

An aspect of judicial decision-making needs to be considered because it bears directly on the transactions to which Article 2 rules apply. This can be done by illustration.

Assume that Article 2 contains a rule for the sale of goods ("Rule X") that does not exist in common law. Common law for a particular type of contract contains a different rule ("Rule Y"). Now let's suppose that a transaction occurred and a dispute reached the court based on the issue associated with these two rules. If the transaction is indisputably an Article 2 transaction, we hope that the court will apply Rule X even if it believes that Rule Y is preferable. Alternatively, Rule Y will apply if the transaction is indisputably within the Rule Y subject matter. However, what result if the transaction is nether a sale nor a Rule Y deal? There may be an appropriate rule in existence for the particular type of transaction. If not, a court might ask "which type of transaction is this one *most like*," or it might ask "which rule do we believe *should apply*"?

These two approaches are very different. One proceeds by analogy (i.e., this is more like one than the other), while the other focuses on outcome (i.e., this is the right result for these parties). When the focus is on outcome, the choice can be implemented by describing the transaction as an Article 2 sale (or not), or by describing the transaction as one whose primary (predominant) purpose is a sale of goods (or not).

In litigation, an outcome-focused analysis serves well if the particular judge's preferred outcome corresponds to appropriate policy.[31] In planning transactions, a court's outcome-based

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30. *See, e.g.*, In re El Paso Refinery, L.P., 196 B.R. 58 (Bankr. W.D.Tex. 1996) (Article 2 analysis applied to determining damages in reference to a patent license); Angus Med. Co. v. Digital Equip. Corp., 840 P.2d 1024, 1031-32 (Ariz. 1992) (unconscionability); World Enter., Inc. v. Midcoast Aviation Serv., Inc., 713 S.W.2d 606 (Mo. Ct. App. 1986) (applies Article 2 rules on consequential damages, even though Article 2 does not generally apply to the transaction).

31. Of course, a judge's ability to reach an appropriate decision depends on the judge's reference point in approaching the particular issue. Views can often conflict, leaving choices to vagaries of the particular judge. For example, compare the lower court and the appellate court's view of appropriate application of the doctrine of unconscionability in the Integraph case. *See* Intergraph Corp. v. Intel Corp., 195 F.3d 1346 (Fed. Cir. 1999). The lower court

determination may be helpful or harmful for later transactions. It may create costs and uncertainty. The preferable basis for transactional law is a rule developed with a focus on the type of transaction in general and the ordinary expectations associated therewith.

C. *The Mystical Case of Electricity and Article 2*

Reported decisions on the "scope" of Article 2 often use analyses that are driven by the court's desired outcome. One illustration is in cases deciding whether an electricity services contract is an Article 2 sale of goods or a common law transaction. Viewed in the abstract, there is little reason to suspect that a contract to deliver electrical power is a sale of *goods*. True, electricity "moves" and, thus, could vaguely be said to be within the broad Article 2 definition of goods (all things movable when identified to the contract),[32] but the nature of the transaction and the associated expectations of the parties are so different from the sale of a car that it is inappropriate to force the transaction into an Article 2 framework. Many Article 2 rules are irrational if applied to this transaction. For example, how does one "inspect" electrical current before "accepting" it and how does one accept or reject it? When does title to electricity pass? Questions like these and the answers that they conjure up indicate the inappropriateness of the sale of goods model for electricity service.

Yet, when the issue was whether a transaction in electricity carries an implied warranty of merchantability, several decisions have held that, after it passes through the customer's meter, electricity becomes goods for the purposes of Article 2 and a product for the purposes of strict liability law.[33] This creates a mystical physical outcome. Electricity moving on wires that run from the power plant to the customer's location is not goods, but when delivered to the customer, it and the transaction are transformed and governed by different *contract* law.

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opinion, which makes for a study in diametric views of commerce, is reported at 3 F. Supp.2d 1255 (N.D. Ala. 1998).

32. U.C.C. § 2-105(1) defines "goods" as "all things that are moveable at the time of their identification to the contract."

33. *See, e g.*, Pierce v. Pacific Gas & Elec. Co., 212 Cal. Rptr. 283, 290-91 (Cal. App. 3d Dist. 1985) (in products liability context, electricity delivered to homes is a product); Hedges v. Public Serv. Co. of Indiana, Inc., 396 N.E.2d 933, 935-36 (Ind. Ct. App. 1979) (not goods before it passes the meter); Helvey v. Wabash County REMC, 278 N.E.2d 608, 610 (Ind. Ct. App. 1972) (goods for purposes of warranty claim and statute of limitations).

The core issue in such cases typically is whether the power company should have an implied obligation related to losses caused by unexpected surges in the power supplied to the customer. Asking that question by asking whether electrical power contracts are for a sale of goods misstates the point. The Massachusetts court "got it right" (at least analytically) in *New Balance Athletic Shoe, Inc. v. Boston Edison Co.*,[34] where the issue was whether a commercial customer could recover for breach of warranty when a power surge caused a fire in its facility. The court concluded that the true issue was whether the electricity company should have liability for malfunctions in its services. The court held that this was a legislative, not a judicial question, and dismissed the case. Other courts might approach the issue as a common law question: what, if any, implied obligations arise in tort or contract law in *electricity service* agreements.[35]

Judicial analyses that approach the issue as classifying the contract as either goods, services, intangibles or, simply, electricity, go in both directions on policy issues. Common law does not generally support a merchantability warranty. A ruling that an electricity service contract is not within Article 2 is in effect a holding that there is no implied warranty of this type in that transaction.[36]

On its face, excluding application of Article 2 seems correct. The Article 2 warranty of merchantability focuses on the result of the contract performance (i.e., the delivered product) and its quality. As to electricity, such a focus would ask whether the particular group of electrons delivered is consistent in character to electrons delivered in ordinary electricity contracts. In these cases, however, the issue typically is whether the provider is responsible for harm caused by a power surge, that is, a variation in its ongoing performance. This question is more analogous to questions about what, if any, are the implied assurances about the quality and

34. 1996 WL 406673 (Mass. Super. Ct. 1996).

35. *See* ZumBerge v. Northern States Power Co., 481 N.W.2d 103, 107-08 (Minn. Ct. App. 1992) (Article 2 issue not decided; issue resolved under negligence law); Wivagg v. Duquesne Light Co., 420 UCC Rep. Serv. 597 (Pa. Ct. Comm. Pl. 1975) (analysis suggesting that a common law implied obligation may exist).

36. *See, e.g.*, Lilley v. Cape Hatteras Elec. Membership Corp., 1990 WL 261819 (E.D.N.C. 1990) (not goods; warranty does not apply); Bowen v. Niagara Mohawk Power Corp., 590 N.Y.S.2d 628, 631 (App. Div. 1992) (not a product; breach of implied warranty claim dismissed); Farina v. Niagara Mohawk Power Corp., 438 N.Y.S.2d 645 (App. Div. 1981) (not goods; no warranty); Navarro County Elec. Coop., Inc. v. Prince, 640 S.W.2d 398, 400 (Tex. Ct. App. 1982) (not goods; merchantability warranty does not apply).

nature of performance of services over time. States answer *that* question differently for different types of services contracts, but at least the latter question addresses the appropriate issue.

A ruling that electricity service contracts are transactions in goods has ramifications outside the warranty issue and outside the field of electricity. For electrical services, do other Article 2 rules govern, including disclaimer rules, risk of loss, statute of frauds, measure of damages, inspection, rejection, revocation, and the like? For contracts not involving electrical service, what are the consequences of equating electricity with goods? If electrical current is goods, what of cable television service? Cable television images move. If a cable contract is a sale of goods, is the content of programming and availability of service judged by a standard of merchantability?[37] What about broadcast television or radio? Is a contract for telephone service a sale of goods?[38]

The idea that a body of law focused on the contractual relationship for the sale of a car or a toaster should govern these transactions and other transactions in services and information is a misuse of an important body of law. Yet, Article 2 has long had a role beyond its original mandate.

D. *Consumerism and Mass Market as an Image*

Before moving to the question of what sources of contract law shape the law related to computer information transactions, it is useful to note a second general source of law that has had an impact, albeit a more intermittent impact, on general law outside its own scope. This is the idea of consumerism (or consumer protection).

Article 2 has few consumer protection rules. Indeed, that was a major complaint when Article 2 was promulgated.[39] It was an

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37. For a case answering "no" to both questions, see Kaplan v. Cablevision of PA, Inc., 671 A.2d 716, 722-24 (Pa. Super. Ct. 1996). *See also* Singer Co. v. Baltimore Gas & Elec. Co., 558 A.2d 419, 423-24 (Md. Ct. Spec. App. 1989) (not a transaction in goods and thus no warranty basis for claim that defects in distribution system prevented electricity from reachng customer's meter).

38. *See* Whitmer v. Bell Tel. Co., 522 A.2d 584, 586-87 (Pa. Super. Ct. 1987) (holding that the use of a pay telephone was not a transaction in goods even though it involved some provision of communications because the predominant purpose involved transmission of customer-provided communications); Geotech Energy Corp. v. Gulf States Telecomm. & Info. Sys., Inc., 788 S.W.2d 386, 389 (Tex. Ct. App. 1990).

39. David W. Carroll, *Harpooning Whales, of Which Karl N. Llewellyn is the Hero of the Piece; of Searching for More Expansion Joints in Karl's Crumbling Cathedral*, 12 B.C. INDUS. & COMM. L. REV. 139, 139-41 (1970).

intentional omission; Article 2 focuses on general commercial contract law, rather than on being a consumer protection code.[40] Shortly after Article 2 was adopted by the states, states adopted positions on consumer protection. Some broadly regulated consumer contracts, while others created incentives and opportunities for litigation, and others did very little. The result varies among the states and has varied over time within each state. In the United States, consumer contract protection is addressed in a largely non-uniform manner; each state has its own policy.

If we step back from details, a general observation can be illuminating.[41] The idea of consumerism combined with the images of a mass market for tangible products has become a powerful image with impact beyond its true scope. The core premise of this image is that individual consumers lack sophistication, interest, and bargaining leverage to protect themselves. As a result, law should intervene to ensure balance or, at least, to require disclosures understandable for the consumer. Mass-market goods so dominate our personal experience that the images of consumerism influence contract law generally. In this expanded version, the image is that the buyer of goods is subservient and needs protection, while the seller dominates in leverage and legal sophistication. This image derives from a world of retail sales. In a commercial market, the image of routinely subservient buyers is inaccurate. The information marketplace accentuates the inaccuracy. Most providers of information to publishers are individuals dealing with large corporate *purchasers*. In the software industry, the average software provider has fewer than 12 employees.[42] These companies routinely deal with Fortune 1000 clients. In commercial transactions generally, it is as likely that the purchaser is more

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40. UCITA adopts the same approach for the same reason. Because it was promulgated against a background of widespread, existing state consumer protection law, UCITA expressly preserves all existing state consumer protection statutes and regulations, except with respect to four limited issues pertaining to electronic commerce. *See* U.C.I.T.A. § 105 (1999).

41. As might be expected, in the revision projects related to the generally applicable UCC articles, the conflict between consumer protection rules and the goal of designing an appropriate commercial code has been sharp and extensive. *See* Gail Hillebrand, *the Uniform Commercial Code Drafting Process: Will Articles 2, 2B and 9 Be Fair to Consumers?*, 75 WASH. U. L.Q. 69 (1997); Fred H. Miller, *Consumers and the Code: The Search for the Proper Formula*, 75 WASH. U. L.Q. 187 (1997); Mary Jo Dively & Donald Cohn, *Treatment of the Consumer under Proposed Article 2B*, 16 J. MARSH. J. COMPUTER & INFO. L. 315 (1997).

42. *See* AMERICAN ELECRONICS ASSOCIATION AND NASDAQ, CYBERNATION, THE IMPORTANCE OF THE HIGH-TECHONOLOGY INDUSTRY TO THE AMERICAN ECONOMY (1998); U.S. DEP'T OF COMMERCE, U.S. INDUSTRY AND TRADE OUTLOOK 24-28 (1998).

sophisticated as it is that the vendor dominates.

Rules informed by consumerism make little sense applied to large corporate buyers. Yet, that happens under a number of federal and states' laws. For example, the Texas Deceptive Trade Practices Act gives a right to treble damages for aggrieved "consumers."[43] Originally, it defined "consumer" to include any entity that acquired goods or services. After years of controversy, the definition was refined to define consumer as any entity with assets of less than $25 million. The California version of the Uniform Electronic Transactions Act (UETA) contains many consumer protections, but adopted these rules to apply to consumer and commercial agreements.[44] The Magnuson-Moss Warranty Act covers transactions in "consumer products," which are goods of a type normally used for consumer purposes regardless of who the actual purchaser is.[45] It thus imposes description and disclosure rules in a transaction between IBM and Ford. UCITA identifies some transactions as "mass-market transactions" and applies protective rules even if the transferee is not a consumer.[46]

The penetration of consumerism into merchant-merchant (commercial) law can be shown in many ways, one being the treatment of "standard forms." Viewed with a focus on a consumer market, standard form contracts epitomize the imbalance between consumers and sellers. The form is presented to the buyer and no bargaining is permitted. In fact, this occurs only in the relatively few consumer transactions that actually involve contract terms in a record. But standard forms are more common in deals between merchants. Here, the prevalence of forms is a by-product of efficiency concerns: it is too costly and unproductive to negotiate each and every contract term, even in many that involve large dollar amounts.[47]

There are competing views about the validity of standard forms

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43. *See* TEX. BUS. & COM. CODE ANN. §17.45(4) (West 1984) (defining "consumer" to include both individuals and businesses, but only businesses with assets of under $25 million). *See generally* Nancy Atlas, Scott Atlas & Raymond Nimmer, *DTPA in the Courts: Two Empirical Studies and a Proposal for Change*, 21 ST. MARY'S L.J. 609 (1990) (describing the outcome of a study of trial court decisions under the Texas Deceptive Trade Practices Act).

44. *See* Cal . Civ. Code § 1633.1-.17 (1999).

45. 15 U.S.C. § 2301(1) (1998).

46. U.C.I.T.A. §§ 102, 209 (1999).

47. *See, e.g.*, W. David Slawson, *Standard Form Contracts and Democratic Control of Lawmaking Power*, 84 HARV. L. REV. 529, 529-30 (1971) (stating that standard form contracts "account for more than ninety-nine percent of all the contracts now made" and that their "predominance . . . is the best evidence of their necessity").

in modern law. One, built in part on consumerism images, assumes that whenever a standard form is used, it results from economic imbalance and justifies rules restricting its enforcement or allowing courts to invalidate its terms.[48] This approach, as adopted in the *Restatement (Second) of Contracts* in 1971, is not restricted to consumer contracts and has been followed in only a handful of states.[49] The alternative approach, built on an image of contract choice, posits that standard forms should be treated no differently than any other written agreement. There is widespread but not universal support for this approach in commercial contracts.[50]

The image one brings to discussing contract law is important. Few would argue that there is a need to regulate, on other than antitrust bases, the terms of a standard form used between Citibank and General Motors, or IBM and Exxon. On the other hand, many argue for oversight of a standard form in a contract between a retailer and a consumer. The images of imbalance are strong in the latter case. These images become misleading when extended to the commercial context.

A rule based on a consumerism image that assumes the dominance of the seller makes little sense in many transactions

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48. *See* RESTATEMENT (SECOND) OF CONTRACTS § 211(3) (1979). This approach, however, does not stem solely from a mass market image. It also comes from a perspective on what should be the proper relationship between a court and the terms of the contract in cases of litigation. Stated simply, it flows from the view that judicial oversight of the terms of a contract (including most particularly a standard form) should be encouraged in order to avoid over-reaching and unfair surprise. The most commercially expansive illustration of this approach is found in the UNIDROIT *Principles of International Commercial Contract Law* Article 2.19 (1994).

49. *See* James J. White, *Form Contracts Under Revised Article 2*, 75 WASH. U. L.Q. 315 (1997).

50. *See, e.g.*, Klos v. Polske Linie Lotnicze, 133 F.3d 164 (2d Cir. 1998).

> The concept of adhesion contracts introduces the serpent of uncertainty into the Eden of contract enforcement. At the very least, it represents a serious challenge to orthodox contract law that a contract is to be interpreted in accordance with the objective manifestation of the parties' intent. . . . It may not be invoked to trump the clear language of the agreement unless there is a disturbing showing of unfairness, undue oppression, or unconscionability.

Id. at 168-69; Fireman's Fund Ins. v. M.V. DSR Atlantic, 131 F.3d 1336, 1338-39 (9th Cir. 1998); Chan v. Adventurer Cruises, Inc., 123 F.3d 1287, 1292 (9th Cir. 1997); Dillard v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 961 F.2d 1148 (5th Cir. 1992); Riggs Nat'l Bank v. District of Columbia, 581 A.2d 1229, 1251 (D.C. Ct. App. 1990); American Bankers Mortgage Corp. v Federal Home Loan Mortgage Corp., 75 F.3d 1401, 1412-13 (9th Cir. 1996) (contract of adhesion fully enforceable in the absence of showing of unconscionability); E.H. Ashley & Co. v. Wells Fargo Alarm Serv., 907 F.2d 1274, 1278-79 (1st Cir. 1990); Graham v. Scissor-Tail, Inc., 623 P.2d 165, 172 (Cal. 1981). *Cf.* Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96 HARV. L. REV. 1173 (1983) (raising questions about the desirability of enforcing standard forms).

involving information. Unlike for goods, where large capital and distribution systems are important, in information industries small companies often thrive and, indeed, small companies and individual entrepreneurs dominate many industry sectors. The average size of an Internet provider is unknown, but the media allows single entrepreneurs to become international businesses. Between two individuals, one a licensee and the other a licensor, it is not immediately clear why contract law should intervene in and regulate their transaction or, if it did, to whom the benefit should be extended.

E. *Current Law on Computer Information Transactions*

What then is the current law pertaining to computer information transactions?

The answer to this type of question is complex in any setting. In computer information transactions, the answer is not only complex, but uncertain, varying across the states and, often, within a state. It is made more uncertain by the fact that we are undergoing a paradigm shift in how business is conducted and what subject matter is central to commerce. Given that computer information is at the center of the modern economy, this uncertainty is inappropriate and fails to establish a coherent infrastructure for a significant part of our economy. Courts may get specific decisions right, but as a whole, law fails to provide guidance for transactions in this crucial subject matter.

We can look at this problem from three different angles. The first two concern how courts address the question—do courts start with the view that Article 2 might apply, or do courts start with the view that intellectual property and licensing laws apply? What difference does this make? The third angle concerns how decisions about particular types of information-related transactions deal with what law governs.

1. *Viewed From the Perspective of Article 2 Scope*

If you look at the issue from a perspective grounded in sales law, the analytical framework has several identifiable features. From this vantage, the question is seen as a matter of defining the scope of Article 2. There are four issues discussed in the decisions:

- First, is the entire subject matter comprised of "goods"? In some cases, such as with respect to electricity, a decision that a transaction involves "goods" has no clear relationship

to what in common understanding is within the idea of "goods." (*classification*)

- Second, if a transaction involves "goods" *and* another subject matter, most courts ask whether the "goods" or the "other" subject matter predominates. If the goods are the predominant purpose, Article 2 applies to the entire transaction, including subject matter that is "not goods." (*predominant purpose*)
- Third, if Article 2 does not apply, some courts ask whether Article 2 rules apply to things "not goods" by analogy, as defining common law. The issue is whether common law should fit Article 2. (*analogy*)
- Fourth, if all else fails, common law applies. (*not goods*)

This sequence reflects a goods-centric approach under which contract law is presumably governed by sales law, unless another body of law clearly must control. The goods-centric model is increasingly irrelevant in our economy where information and services dominate.

a. *The Predominant Purpose Test*

In litigation regarding the scope of Article 2, the most frequently occurring issue is: how should a court handle a *mixed* transaction covering both goods and other subject matter. The most commonly used test asks what is the predominant purpose of the transaction.[51] If goods are the predominant purpose of the transaction, Article 2 applies to the entire transaction, while if the other subject matter is the predominant purpose, Article 2 does not apply at all. This test creates a coherent framework *after* a decision is made on the *purpose* test, but this test also ensures that in *all cases* when it is used, the wrong law will be applied to *some* aspects of a transaction (e.g., goods law applied to services aspects of a mixed transaction). It is a test born in and suited for litigation, not transactions. To the extent that the outcome of applying the test cannot be predicted in advance, however, it leaves transacting parties with no guidance about what law applies, forcing either risk-taking or the cost of making contract terms to account for

51. *See, e.g.*, Princess Cruises, Inc. v General Elec. Co., 143 F.3d 828, 832-34 (4th Cir. 1998); Design Data Corp. v. Maryland Cas. Co., 503 N.W.2d 552, 556-57 (Neb. 1993); Kirkpatrick v. Introspect Healthcare Corp., 845 P.2d 800, 803-04 (N.M. 1992); Cincinnati Gas & Elec. Co. v. Goebel, 502 N.E.2d 713, 714-15 (Ohio Mun. 1986); Tacoma Athletic Club, Inc. v. Indoor Comfort Sys., Inc., 902 P.2d 175, 179 (Wash. Ct. App. 1995).

known contingencies.

The predominant purpose test is widely used, but when we look at the issue broadly, the predominant purpose test is not the only legal standard that courts use, nor even the one that is most often used. For example, there are no decisions that use a predominant purpose test to exclude application of laws such as the law of negotiable instruments, letters of credit, security interests, and other discrete contract law rules. The law on these subjects is routinely assumed to govern its own subject matter, even if goods are dominant in the overall transaction. The predominant purpose test actually focuses only on general contract law. Even there, a minority of courts reject it and use what some describe as a gravamen of the action test, where what law applies depends on the issue addressed: each body of law applies to its own subject matter.[52]

In information transactions, the predominant purpose test is often simply ignored in regard to certain issues. For example, courts that have asked whether "informational content" is governed by the Article 2 merchantability warranty because it is contained in a book or on a diskette, ignore the predominant purpose issue. "Informational content" is information intended in the ordinary course to be communicated to an individual.[53] This term includes the images of a motion picture, the sounds of recorded music, the text of a book, and the like. Here, there are strong policy interests for not imposing liability for defects in the absence of provable fault.[54] A court using a goods-centric analysis could conclude that the predominant purpose of buying a book or a digital work was goods. A predominant purpose analysis that concludes that a sale of a book or a digital encyclopedia is predominantly a transaction in goods would apply a warranty of merchantability to the content. As we see later, in other contexts, some courts fall into this type of trap. The court in *Cardozo v. True*,[55] however, avoided the problem by limiting the implied warranty to the paper and binding of a book and excluding the informational content.

> [W]e hold that absent allegations that a book seller knew that there was reason to warn the public as to the contents of a

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52. *See* Elkins Manor Assoc. v. Eleanor Concrete Works, Inc., 396 S.E.2d 463, 469-70 (W. Va. 1990) (declining to apply the predominant purpose test).

53. U.C.I.T.A. § 102 (1999).

54. *See, e.g.*, Winter v. G.P. Putnam's Sons, 938 F.2d 1033, 1035 (9th Cir. 1991). *See* U.C.I.T.A. § 404 (1999).

55. 342 So.2d 1053, 1057 (Fla. Dist. Ct. App. 1977).

> book, the implied warranty in respect to sale of books by a merchant who regularly sells them is limited to a warranty of the physical properties of such books and does not extend to the material communicated by the book's author or publisher.[56]

This does not absolve the provider of all responsibility in contract, but excludes any implied warranty based on an analogy to an Article 2 sale of goods for the simple contractual transfer.[57] Some courts seem to go even further to protect the seller.[58]

Under cases such as *Cardozo*, transactions involving informational content are found to entail a mixed transaction for the purpose of applying the warranty rules. UCITA brings both the informational content and the media (the copy) into the scope of a single act, but provides rules that reflect the policies underlying *Cardozo* and similar cases.[59]

b. Goods-Services as an Incomplete Framework

When the predominant purpose test is used, the most important question is how one determines what part of the transaction predominates. The case law on this issue is unpredictable. One pattern, however, emerged early and continues to have an influence. That pattern involves defining the question as a choice between *goods* and *services* as the dominant purpose. Indeed, some describe the predominant purpose test as a goods-services test.

This dichotomy ignores information and informational rights; that analytical mistake has significance in the modern information economy. Courts using the goods-services dichotomy sometimes reach wrong results and other times use inept language. The results can be surprising.[60] Treating this as the relevant dichotomy, for

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56. *Cardozo*, 342 So.2d at 1057.

57. *See also* Gilmer v Buena Vista Home Video, Inc., 939 F. Supp. 665 (W.D. Ark. 1996).

> Plaintiff does not complain in any respect about the physical properties of the film or the covers as opposed to the ideas, thoughts, or images contained thereon. There is no allegation that the videos contained physical defects. Rather, plaintiff's complaint is that the videos and/or the covers contain offensive or morally unfit images or messages. However, plaintiff does allege that BVHV, in promoting and marketing the videos, warranted that they were suitable for viewing by children despite its knowledge at the time of marketing that the videos contained subliminal messages.

Id. at 671.

58. *See, e.g., Winter*, 938 F.2d at 1033.

59. *See* U.C.I.T.A. § 102 (1999) (defining computer information).

60. Southwestern Bell Tel. Co. v. FDP Corp., 811 S.W.2d 572 (Tex. 1991) (dealing with whether Southwestern Bell breached a warranty by failing to include all contracted for "advertising" in its yellow pages; the case was argued, in part, as a sales of goods case, but

example, leads some courts to ask whether a license of software is a transaction in services, a question that leads to treating software as a transaction in goods because no services are involved.[61] Asking the question this way also ignores the fact that, in many cases, like with books and motion pictures, the purpose is to transfer information and rights in information. Obtaining a diskette, however valuable the plastic, is not the primary purpose of a software transaction.[62]

Not all courts coming to the issue from a goods-centric position ignore the fact that information and informational rights may predominate. When courts recognize that there is more than goods and services in the economy, however, the language used in their decisions often reveals the difficulty of the transition to modern commerce. Although it did not deal with the scope of Article 2, this difficulty was clear in *Snyder v. ISC Alloys, Ltd.*[63] In *Snyder*, the issue was whether a supplier of designs, technical advice and drawings along with a license to operate a process for converting solid zinc into zinc dust was liable for the death of an employee caused by operation of the plant constructed pursuant to the plans. Following a conventional goods-services dichotomy analysis, the court held that the transaction was not a transaction in goods, but a transaction in *services* that did not come under product liability law. However, in expressing its analysis, the court at least acknowledged the role of information in the transaction. For example, the trial judge commented:

> [ISC] cannot be held liable for breach of warranty because this theory of recovery is inapplicable to *ideas, information and services*. The concept of breach of warranty stems from

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the Texas Supreme Court rejected this argument, holding that the publication of advertising was a *services* contract); Gross Valentino Printing Co. v. Clarke, 458 N.E.2d 1027 (Ill. Ct. App. 1983) (holding that a contract for the printing of magazines was a contract for goods because the intent was delivery of finished copies).

61. *See, e.g.*, BMC Indus., Inc. v. Barth Indus., Inc., 160 F.3d 1322 (11th Cir. 1998) (holding that a contract to "design, fabricate, debug/test and supervise Field installation and start up of equipment to automate [production of eyeglass lenses]" was more a contract for goods than one for services); Neilson Business Equip. Ctr., Inc. v. Italo V. Monteleone, 524 A.2d 1172 (Del. 1987) (holding that a turnkey hardware and software system contract was a contract for the sale of goods).

62. As reflected in UCITA, however, this does not mean that warranty and other rules analogous to those in Article 2 or 2A may not be appropriate to some aspects of the computer information transaction. For example, for computer programs, UCITA adopts an implied warranty of merchantability analogous to that found in Article 2. *See* U.C.I.T.A. § 403 (1999).

63. 772 F. Supp. 244 (W.D. Pa. 1991).

> Article 2 of the Uniform Commercial Code [which] governs the sale of goods . . . . I have already decided that ISC sold services rather than products.[64]

Was the *Snyder* transaction a services contract or something different from either services or goods? The court came closer to the mark when it stated:

> Obviously, what ISC sold here — information — did not reach the decedents in substantially the same condition in which it was sold. That information did not cause them injury. [The] injury causing instrumentality, although derived from [the] plans, had an existence completely separate and independent . . . . Thus, when ISC relinquished control over the item it sold — namely the plans — the thing that ultimately caused decedents' deaths did not yet exist.[65]

The court thus blended a characterization of a license as a *services* contract and as a contract relating to *information*.[66] A court approaching this case from the perspective of intellectual property licensing would not have been concerned about whether this license was a services contract. It would simply observe that the transaction involved a license of information.[67] The *Restatement (Third) of Torts: Products Liability* expressly recognizes that information is treated differently than tangible products for purposes of product liability.[68]

Increasingly, courts approaching the issue as one of determining

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64. *Snyder*, 772 F. Supp. at 244 (emphasis added).

65. *Id.*

66. *See also In re* North American Liesure Corp., 468 F.2d 695 (2d Cir. 1972) (holding that a contract to produce cassettes from a master was not a contract for the sale of goods); R.J. Longo Constr. Co., Inc. v. Transit Am. Inc., 921 F. Supp. 1295 (D. N.J. 1996) (holding that a license of a design was not covered by UCC Article 2); Alesayi Beverage Corp. v. Canada Dry Corp., 947 F. Supp. 658 (S.D.N.Y. 1996) (finding that a license was a "services" contract).

67. *See* MCCARTHY ON TRADEMARKS § 18:74 (1996). *See also* Burkert v. Petrol Plus of Naugatuck, 579 A.2d 26 (Conn. 1990).

68. *See* RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 19, cmt. d (Proposed Final Draft, 1997) (limiting the definition of product to "tangible personal property"). The comment states:

> [Where plaintiffs] seek to recover against publishers in strict liability in tort based on product defect . . . [a]lthough a tangible medium such as a book, itself clearly a product, delivers the information, the plaintiff's grievance in such cases is with the information, not with the tangible medium. Most courts, expressing concern that imposing strict liability for the dissemination of false and defective information would significantly impinge on free speech have, appropriately, refused to impose strict products liability in these cases.

Id.

the scope of Article 2 recognize that there is more subject matter in commercial transactions than simply goods or services. This is clear in cases involving contracts for the sale of a business. Here, courts have long asked whether the predominant purpose focused on tangibles (goods) or intangibles (information and rights, such as copyrights, licenses, goodwill, patents).[69] Sometimes goods dominate, while sometimes the intangibles dominate.

For example, *Dravo Corp. v. White Consol. Indus., Inc.*,[70] held that Article 2 did not apply when, in the sale of a business, two assets that were not goods—a five-year non-competition agreement and various drawings and tracings—accounted for over half of the purchase price of the business. The fact that the drawings were in tangible form (on paper) did not indicate that their value consisted of goods, as compared to the information and the right to use it. As the court noted: "The significance of these items in this transaction is not their physical properties, but the ideas conveyed therein." Indeed, in the contract list of the value allocated to each of the major assets, the drawings were listed as the most valuable asset in the over eight million dollar transaction.

Similarly, *Stewart v. Lucero*[71] held that the sale of a catalogue business operated under the Sears trademark by a license from Sears was not a sale of goods. The court noted that:

> The sale of any business may involve the transfer of goods in the form of inventory, office equipment, and other movables . . . . In this case, however, any such transfer was merely incidental. The record discloses that Sears Catalog Sales Merchants retained no inventory other than a few display items and customer orders waiting to be picked up. Further, the sales agreement and the merchant agreement demonstrate that the basis of the [bargain] was the right to operate a catalog business using the Sears name and a noncompetition agreement from the [sellers]. These items are non-goods, and . . . Article 2 . . . is inapplicable.[72]

69. *See, e.g.*, Stewart v. Lucerno, 918 P.2d 1 (N.M. 1996) (predominant assets were intangible); Monarch Photo, Inc. v. Qualex, Inc., 935 F. Supp. 1028 (D. N.D. 1996) (sale of business involved predominantly intangible assets).

70. 602 F. Supp. 1136 (W.D. Pa. 1985). *See also* United States v. Antenna Sys., Inc., 251 F. Supp. 1013, 1016 (D. N.H. 1966) ("[B]lue prints, drawings etc., in reality the visual reproductions on paper of engineering concepts, ideas and principles, are general intangibles . . . not 'goods' [under] the Code.").

71. 918 P.2d 1 (N.M. 1996).

72. *Stewart*, 918 P.2d at 3.

The chief asset in *Stewart* was a license, which the court quite properly described as "not goods" and which certainly was "not services."

Decisions such as *Stewart* and *Dravo* show that courts are capable of getting the issue right when intangibles, such as information, informational rights, and licenses of information, are involved even if the case is approached as defining the scope of Article 2. Whether a predominant purpose test should ever apply with respect to information and informational assets and their relation to Article 2 law is a difficult question. As cases involving informational content suggest, there are instances where this is not appropriate if it leads to including the information within Article 2. UCITA proposes that, with respect to the relationship between goods and computer information as subject matter of a transaction, a gravamen of the action standard applies, rather than a predominant purpose test, because the contract issues merit different treatment in law.[73] Whether the predominant purpose test should be followed or not, it is clear that, if applied, the test must be used in a manner that gives recognition to information and other intangible subject matter, which can be and often is the predominant purpose of modern information transactions.

c. *Applying the Predominant Purpose Test*

How does one determine what purpose predominates in a transaction?

Predictably, the cases are difficult to reconcile and the criteria for decision often seem to lie in instinctive, rather than reasoned choices by a court. This, in itself, creates a problem. Yet, there are several patterns that can be usefully identified.

One concerns the importance attached to the fact that something tangible is delivered from the provider to the other party. If the contract does not require that the provider deliver something to the other party, the transaction is not likely to be treated as a contract in goods. There is no movable corpus to which the idea of "goods" can attach. Similarly, many cases indicate that, if what the provider is required to deliver are goods previously delivered to it by the other party, the transaction is not a sale of goods, but rather services or a lease.[74]

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73. U.C.I.T.A. § 103(b) (1999).

74. *See, e.g.*, BMC Indus., Inc. v. Barth Indus., Inc., 160 F.3d 1322, 1325 (11th Cir. 1998) (applying predominant factor test, a contract to "design, fabricate, debug/test and supervise

But does the fact that the provider is required to deliver something tangible to the other party indicate that the predominant purpose of the transaction focuses on the "goods" thus delivered? The answer should be no. There are many cases in which a services or an information contract involves delivery of something in tangible form, but that does not alter the nature of the deal. As the court in *Dravo* recognized, the fact that drawings are recorded on paper does not mean that the primary value lies in the paper, rather than in the ideas and information. To see that even more clearly, we need ask whether an attorney who drafts a will for a client and delivers it on paper or diskette engaged in a sale of goods (the will on the diskette). The answer is no, the purpose is to obtain the professional services. An architect or engineer who delivers written designs to a client with a right to use those designs is not selling goods, but providing services, information and a license of information.[75]

Yet, while mere delivery of something tangible should not resolve what is the predominant focus of the transaction, there are many courts that seem to assume that the reverse is true for computer information and other transactions, i.e. equating the existence of a "deliverable" with the conclusion that *goods* are the predominant purpose of the transaction. Sometimes the analysis is painfully explicit and inadequate. For example, *Advent Systems Limited v. Unisys Corp.*[76] held that a distribution license for software was governed by Article 2 under the predominant purpose test. The court described a computer program as instructions to operate a computer.[77] It described "software" as "the medium" that stores

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field installation and start up of equipment to automate [production of eyeglass lenses]" was more a contract for goods than one for services because: (1) it was captioned "Purchase Order;" (2) parties were described as "Buyer" and "Seller;" (3) it involved the sale of equipment; and (4) payment was pegged to delivery of the equipment, not to the completion of required services); Nim Plastics Corp. v. Standex Int'l Corp., 11 F. Supp.2d 1003 (N.D. Ill. 1998); Manes Org., Inc. v. Standard Dyeing & Finishing Co., 472 F. Supp. 687 (S.D.N.Y. 1979); Moore v. Allied Chem. Corp., 480 F. Supp. 364 (E.D. Va. 1979); Insul-Mark Midwest, Inc. v. Modern Materials, Inc., 612 N.E.2d 550 (Ind. 1993); Mail Concepts, Inc. v. Foote & Davies, Inc., 409 S.E.2d 567 (Ga. Ct. App. 1991). *But see* Vitromar Piece Dye Works v. Lawrence of London, Ltd., 256 N.E.2d 135 (Ill. Ct. App. 1969) (applying Article 2 to a processing contract without discussion of the scope issue).

75. *See, e.g.*, Inhabitants of Saco v. General Elec. Co., 779 F. Supp. 186 (D. Me. 1991); Minnesota Forest Prods., Inc. v. Ligna Machinery, Inc., 17 F. Supp.2d 892 (D. Minn. 1998); Board of Trustees v. Kennerly, Slomonson & Smith, 400 A.2d 850 (N.J. Super. Ct. Law Div. 1979).

76. 925 F.2d 670 (3d Cir. 1991).

77. *Advent Systems*, 925 F.2d at 674 ("In simplistic terms, programs are codes prepared by a progammer that instruct the computer to perform certain functions.").

data and computer programs, stating: "The medium includes hard disks, floppy disks, and magnetic tapes."[78] According to the court, when a program is "transposed onto a medium," it becomes "software;" that is, it becomes the medium itself.[79] This is like saying that, when printed, the text of a book becomes the paper. Given that theory, the court stated:

> Computer programs are the product of an intellectual process, but once implanted in a medium are widely distributed to computer owners. An analogy can be drawn to a compact disc recording of an orchestral rendition. The music is produced by the artistry of musicians and in itself is not a "good," but when transferred to a laser-readable disc becomes a readily merchantable commodity. Similarly, when a professor delivers a lecture, it is not a good, but, when transcribed as a book, it becomes a good.
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> That a computer program may be copyrightable . . . does not alter the fact that once in the form of a floppy disk or other medium, the program is tangible, movable and available in the marketplace [and therefore goods].[80]

But, of course, as we have seen, other courts dealing with information on media treat the physical material as goods, but do not treat the information as goods. The program is not the floppy disk any more than a work of authorship is the paper and binding of a book.

The substantive result in *Advent Systems* was that the distribution license was enforceable under Article 2 even though it failed to state a quantity term. This result may have been correct, but it could have been reached under common law and the court's analysis forcing this into an Article 2 framework is far off the mark.[81] Even under a predominant purpose test, the question should have been whether the predominant purpose was to obtain diskettes (if any were obtained) or a right (license) to distribute software (the program, not the diskette). For example, if the

78. *Id.*

79. *Id.*

80. *Id.* at 675.

81. Of course, the court could have reached that same result under the common law, at least in some states. *See* Kirkpatrick v. Introspect Healthcare Corp., 845 P.2d 800 (N.M. 1992) (holding that a design contract was not in Article 2 and, thus, the UCC statute of frauds argument was not applicable).

licensor supplied a single master disk from which the licensee was authorized to make thousands of copies onto its own diskettes, could we say that the transaction's predominant purpose was to deliver that single piece of plastic, or was the dominant purpose to allow the making of multiple copies of the digital information? It is difficult to conclude that anything other than the informational rights and license were dominant.

This being said, one factor in the cases determining the predominant purpose is whether a tangible deliverable is required. The other facts used in the analysis are widely varied.[82] In many cases, courts add up the allocated cost of services and goods, drawing a numerical comparison and giving the nod to the highest "bidder," that is, to the items attributed with the bulk of the contract cost. In other cases, courts look at the compensation scheme; that is, whether payment is for the deliverable or for work done in creating it. Others look to the language of the agreement and whether it refers to services or to products, owners and consultants or buyers and sellers, and other similar factors. Throughout, of course, lies the goods-services dichotomy and the role it plays in how courts approach the scope of Article 2. Properly understood, a test that incorporates an understanding of the separate role of information could follow a similar multifaceted approach, but the factors would weigh differently. For example, compensation based on delivery of completed designs or a completed program might indicate that the deal is not predominantly a services contract, but does not indicate whether goods or information predominate.

2. *Viewed From the Perspective of Intellectual Property and Licensing Law*

If we ask what law applies to computer information transactions from a perspective that begins with intellectual property law and licensing, an entirely different pattern arises. The cases here more commonly focus on common law or intellectual property law as a starting point and often ignore Article 2. At most, Article 2 has a minor role and many cases on licensing do not mention it. Nor, in

82. *See, e.g.*, Fournier Furniture, Inc. v. Waltz-Holst Blow Pipe Co., 980 F. Supp. 187 (W.D. Va. 1997) (use of sales language in agreement significant); Monarch Photo, Inc. v. Qualex, Inc., 935 F. Supp. 1028 (D. N.D. 1996) (comparative dollar value); USM Corp. v. Aurthur D. Little Sys., Inc., 546 N.E.2d 888 (Mass. Ct. App. 1989); Micro-Managers, Inc. v. Gregory, 434 N.W.2d 97 (Wisc. Ct. App. 1988).

most cases, should they do so. Instead of Article 2, cases dealing with issues from the vantage of licensing and intellectual property tend to rely on concepts from underlying property law (e.g., copyright, trademark, patent) and from a mixed federal-state common law tradition.

In part, this is true because the default rules of Article 2 do not address many of the questions that arise in this area. Thus, for example, Article 2 gives no guidance on whether a license of one technology extends to newly developed technologies that emerge after the initial contract; yet that issue has been extensively litigated in licensing law.[83] Similarly, Article 2 does not give guidance on what is covered by a license to *use*[84] or what default rules apply when there is no designation of the uses permitted or denied.[85] It does treat whether exceeding the scope of a license is a breach of contract, infringement, or both.[86] It does not suggest when or whether a licensee in breach can be enjoined from using the licensed information.[87] It does not address whether a licensor has a right to recover materials delivered under a license when the license term ends or there is a material breach by the licensee.[88] It does not address the relationship between a licensor and a third party who receives an unauthorized transfer of the licensed technology.[89] It does not discuss when a contract for continuous, ongoing performance can be canceled for breach.[90] It does not discuss whether the transferee has a right to modify subject matter of the contract after receiving it or who owns the modifications.[91]

The fact that Article 2 does not address these and other contract

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83. *See, e.g.*, Bourne v. Walt Disney Co., 68 F.3d 621 (2d Cir. 1995); Bloom v. Hearst Entertainment, Inc., 33 F.3d 518 (5th Cir. 1994).

84. *See, e.g.*, National Car Rental Sys., Inc. v. Computer Assocs. Int'l, Inc., 991 F.2d 426 (8th Cir. 1993); SOS, Inc. v. Payday, Inc., 886 F.2d 1084 (9th Cir. 1989).

85. *See, e.g.*, Tingley Sys., Inc. v. Norse Sys., Inc., 49 F.3d 93 (2d Cir. 1995) (holding that if the license does not restrict use in terms of purpose or persons, any use consistent with the number of copies permitted under the license is acceptable).

86. *See, e.g.*, Expediters Int'l of Washington, Inc. v. Direct Line Cargo Management Servs., Inc., 995 F. Supp. 468 (D. N.J. 1998).

87. *See, e.g.*, Reuben H. Donnelley Corp. v. Mark I Mktg. Corp., 925 F. Supp. 203 (S.D.N.Y. 1996).

88. *See* UCITA § 815 (1999).

89. *See*, e.g., Microsoft Corp. v. Harmony Computers & Elec., Inc., 846 F. Supp. 208 (E.D.N.Y. 1994).

90. *See, e.g.*, Schoenberg v. Shapolsky Publishers, Inc., 971 F.2d 926 (2d Cir. 1992). Article 2 does deal with cancellation of a so-called installment contract, defined as a contract calling for the delivery of goods in multiple installments, rather than at one time. *See* U.C.C. § 2-612.

91. *See, e.g.*, Midway Mfg. Inc. v. Arctic Int'l, Inc., 704 F.2d 1009 (7th Cir. 1983).

law issues important for licensing and other transactions in information is not surprising. The contract law paradigm in Article 2 is a sale of goods. In sales, the variety of issues addressed by Article 2 are not and were not intended to respond to issues arising in licensing or other transfers of information in digital or other form. Given the different focus, it would a surprise if Article 2 reasonably addressed important issues in licensing.

However, even when both areas deal with the same issue, viewed from the intellectual property perspective, traditional licensing law derived with little, if any, attention to Article 2. Thus, for example, treatises on patent and copyright licensing indicate that there are no implied warranties of quality or performance with respect to the licensed information.[92] This idea marks a striking contrast with the Article 2 assumption that all transactions involving merchant sellers have an implied warranty that the goods are merchantable.[93] Yet, in describing the rule for copyright and patent licensing, Article 2 is seldom addressed; Article 2 rules are viewed as remote *other* law not applicable to information transactions. Similarly, both Article 2 and common law discuss how damages are computed for breach, but Article 2 damages formulas, including the rule that excludes consequential damages for a seller, are seldom discussed in licensing and other information contract cases.[94] Licensing cases are grounded in common law and do not follow Article 2 formulations focused on replacing or reselling a particular item (the goods deal); information and informational rights are not linked to a tangible item. The bases for computing damages must be different.

92. For example, Milgrim, in a multi-volume treatise on licensing, does not discuss implied warranties and comments, simply, "In the area of industrial and intellectual property, however, the contract must make the law between the parties, subject only to overriding principles of public policy." ROGER MILGRIM, MILGRIM ON LICENSING 23-2 (1999). The Dratler treatise on the law of licensing discusses only one form of implied license—that relating to infringement and the like. *See* JAY DRATLER, LICENSING OF INTELLECTUAL PROPERTY § 10.02[2] (1999).

93. Although treated as a core premise in some traditional fields of licensing, the idea that there are no warranties (or warranty-like obligations) in patent and copyright licensing transactions is true only in part. It ignores the effect of RESTATEMENT (SECOND) OF TORTS § 552, which creates an implied obligation applicable to anyone who, as part of its business, transfers information to another in order to guide that other person's business decisions. Also, of course, it ignores those cases that hold that software licenses (arguably copyright licenses at their core) are within Article 2 and, thus, subject to such an implied warranty.

94. *See, e.g.*, Freund v. Washington Square Press, Inc., 314 N.E.2d 419 (N.Y. 1974). *Cf.* Krafsur v. UOP (In re El Paso Refinery, L.P.), 196 B.R. 58 (Bankr. W.D.Tex. 1996) (using an analogy to Article 2 lost profits remedy in discussing the value of a claim for breach of a patent license).

One of the most significant cases in licensing in the past year was the decision of the Court of Appeals for the Federal Circuit in *DSC Communications Corp. v. Pulse Communications, Inc.*[95] DSC involved whether a licensee of a copy of computer software qualified as an owner of a copy of a computer program, which would entitle it to the rights granted to such owners under Section 117 of the Copyright Act.[96] The case was argued in part on the basis that Article 2 applied to software and that, under Article 2, title to goods passes on delivery of goods. The court paid little attention to that issue, regarding Article 2 as beside the point. Instead, it held that a licensee is not an owner of a copy of a computer program if the license places restrictions on the licensee that are materially inconsistent with ownership.[97]

Here was a case with which Article 2 might have been viewed as expressly relevant. Yet, the court held that sales law did not determine the law relating to licensing. It viewed the rights in the information (computer program) as the relevant measure of ownership. The court fashioned a rule of licensing law that does not hinge on Article 2. The rule in *DSC* is consistent with UCITA—ownership of the copy depends on the terms of the license.[98]

In *Everex Systems, Inc. v. Cadtrak Corp.*,[99] the Ninth Circuit Court of Appeals addressed the question of whether a nonexclusive patent license was transferable without consent of the licensor. The court held that federal policy conflicted with state law. While state law allowed transfer of any contract right unless the contract forbade it or the transfer would materially harm the other party, federal law precludes transfer of non-exclusive licenses without consent. Federal law controls. Importantly, however, the state law to which the court referred was common law, not Article 2. Indeed, while Article 2 adopts a rule similar to common law on this issue, Article 2 was not discussed and its influence was nowhere in sight.

In several cases, federal courts have asked whether copyright law preempts state law as to when a license or a contract of

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95. 170 F.3d 1354 (Fed. Cir. 1999).

96. 17 U.S.C.A. § 117 (1999).

97. *See also* MAI Sys. Corp. v. Peak Computer, Inc., 991 F.2d 511 (9th Cir. 1993).

98. U.C.I.T.A. § 502 (1999).

99. 89 F.3d 673 (9th Cir. 1996). See also Harris v. Emus Records Corp., 734 F.2d 1329 (9th Cir. 1984) (copyright license not transferable); *In re* Patient Education Media, Inc., 210 B.R. 237 (Bankr. S.D.N.Y. 1997) (nonexclusive copyright license in photographs not transferable without consent).

indefinite duration can be terminated. The court in *Rano v. Sipa Press, Inc.*[100] held that there was a partial preemption of the state law rule, but two subsequent courts have held that there is no preemption.[101] In all of these cases, the state law rule gave the party a right to terminate at will. In none of the cases did the court rely on Article 2 as the source of state contract law. Common law for licenses provided the governing rule.

In these and many other cases, when the issue is examined from a perspective which presumes that licensing law applies unless displaced, the influence of Article 2 is far more remote and often entirely disregarded. From this viewpoint, the answer to the question of "what law governs" does not begin, and seldom ends, with Article 2.

3. Viewed From the Perspective of Specific Areas of Contract

A third way of looking at what law applies to computer information transactions is to deal with common cases that raise the issue. While most cases that we will discuss in this section use a goods-centric approach that asks whether a transaction is within Article 2, the cases indicate the complexity of the issue and how difficult it is for courts armed with the predominant purpose test and the services-goods dichotomy to reach reasonable results.

a. Development Agreements

Article 2 applies to contracts for specially manufactured goods as well as to contracts for goods in existence at the time of the contract.[102] Yet, one litigated aspect of Article 2 scope is where the agreement requires a provider to develop or design something and deliver to the client the results of that development, sometimes called a development contract. Even when approached from a goods-centric perspective, the cases split. Development contracts bring squarely into focus the goods-services distinction that drives most of the Article 2 case law regarding scope.

The choice between treating a development contract as "goods" or "not goods" spans many issues. The implied warranties are different, as are the rules relating to statutes of limitations and statutes of frauds. Also, there is an underlying difference in default

100. 987 F.2d 580 (9th Cir. 1993).

101. *See* Korman v. HBC Florida, Inc., 182 F.3d 1291 (11th Cir. 1999); Walthal v. Rusk, 172 F.3d 481 (7th Cir. 1999).

102. *See* U.C.C. § 2-105(2).

rules, such as whether title is transferred, when a contract can be canceled, and whether a transferee can inspect the item before deciding whether it has any obligation to pay.

The parameters are identifiable. If a purchaser contracts to acquire a product that fits pre-existing specifications and is ordinary goods, the contract is for goods even if the seller might have to build the particular item for the particular agreement. On the other hand, if the contract requires the provider to create a design, but not construct any other deliverable, the transaction is not within Article 2.[103] Consistent with what we have said before about the traditions of Article 2 case law, even if the design agreement entails a license, it is likely to be described as a contract for services.[104]

In *Incomm, Inc. v. Thermo-Spa, Inc.*,[105] for example, the court held that a contract to design an advertising brochure was not a contract for goods, even though the design, when completed, was delivered in tangible form, the contract was primarily for *services*. The "buyer" did not expect the advertising agency to create and produce copies of the printed brochure, but merely a layout of a brochure that it could take to a printer. Of course, to reproduce the design, the "buyer" required a license. The court did not discuss that, but concluded that a

> careful review of the evidence, including the purchase order [indicates] that this was predominately a contract for the purchase of services. The purchase order specifies such services as the concept, editing and contact layout. Moreover, as discussed previously, it was implicit in the parties' agreement that they would closely work together in producing the brochure.[106]

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103. *See* Board of Trustees v. Kennerly, Slomonson & Smith, 400 A.2d 850 (N.J. Super. Ct. 1979) (holding that a professional engineer who was contractually responsible for the preparation of specifications for plaintiff's lighting system and the supervision of its installation was not subject to an action for breach of an implied warranty of fitness; the rendering of professional services not in a routine manner, but through plans and specifications tailored to individual requirements, so that they reflect the exercise of professional judgment, is a personal service); Department of Transp. v. Bethlehem Steel Corp., 368 A.2d 888 (Pa. Commw. Ct. 1977).

104. *See, e.g.*, Minnesota Forest Prod., Inc. v. Ligna Machinery, Inc., 17 F. Supp.2d 892 (D. Minn. 1998); R.J. Longo Constr. Co., Inc. v. Transit Am., Inc., 921 F. Supp. 1295 (D.N.J. 1996); Snyder v. ISC Alloys, Ltd., 772 F. Supp. 244 (W.D. Pa. 1991).

105. 595 A.2d 954 (Conn. Super. Ct. 1991).

106. *Incomm*, 595 A.2d at 958. *Compare* Incomm, Inc. v. Thermo-Spa, Inc., 595 A.2d 954 (Conn. Super. Ct. 1991).*with In re* Fran Char Press, Inc., 55 B.R. 55 (Bankr. E.D.N.Y. 1985) (holding that a contract for printing advertising posters was a transaction in goods

Viewed from an intellectual property license perspective, this conclusion is rather bizarre since receiving the design is meaningless unless accompanied by an express or at least an implied license to reproduce copies of it.

There are many cases between these extremes where the results turn on details of the contract and the court's perception of an appropriate substantive result. Where a product is designed by the provider and the end result delivered as a traditional type of goods (e.g., furnace, equipment), the cases split. While many cases hold that a contract with design and development elements and a requirement to deliver the resulting product is a sale of goods,[107] as many or more hold that such contracts are for services consisting of the design and development, coupled with a permission, where applicable, to allow use of the designed system.[108]

When one focuses on cases involving development of computer information, the same split pattern holds true. The results in reported cases turn on details of the language of a contract or the predilections of the particular judge. In *USM Corp. v. David D. Little Systems, Inc.*,[109] for example, a Maryland court held that a

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governed by Article 2); Lake Wales Pub. Co., Inc. v. Florida Visitor, Inc., 335 So.2d 335 (Fla. Dist. Ct. App. 1976) (holding that a contract to compile and edit and publish was a contract for goods); Gross Valentino Printing Co. v. Clarke, 458 N.E.2d 1027 (Ill. App. Ct. 1st Dist. 1983) (holding that a contract for printing magazines was for goods, not services; the buyer worked with the printer in performing the layout and service functions of setting up the magazine, but the contract for simple printing had as its primary purpose the delivery of a finished product and its main thrust was the purchase of goods.).

107. *See* Republic Steel Corp. v. Pennsylvania Engineering Corp., 785 F.2d 174 (7th Cir. 1986) (furnace); Abex Corp./Jetway Div. v. Controlled Sys., Inc., 983 F.2d 1055 (4th Cir. 1993) (ground power units); Fournier Furniture, Inc. v. Waltz-Holst Blow Pipe Co., 980 F. Supp. 187 (W.D. Va. 1997) (furnace); Neibarger v. Universal Coop., Inc., 486 N.W.2d 612 (Mich. 1992) (automated milking equipment).

108. *See, e.g*, Inhabitants of Saco v. General Elec. Co., 779 F. Supp. 186 (D. Me. 1991) (waste to energy system); Lincoln Pulp & Paper Co., Inc. v. Dravo Corp., 436 F. Supp. 262 (D. Me. 1977) (chemical recovery unit); Nitrin, Inc. v. Bethlehem Steel Corp., 342 N.E.2d 65 (Ill. Ct. App. 1976); Care Display, Inc. v. Didde-Glaser, Inc., 589 P.2d 599 (Kan. 1979) (trade show display); Cork Plumbing Co., Inc. v. Martin Bloom Assoc., Inc., 1245, 573 S.W.2d 947 (Mo. Ct. App. 1978) (plumbing system); Herman v. Bonanza Bldg., Inc., 390 N.W.2d 536 (Neb. 1986); Kirkpatrick v. Introspect Healthcare Corp., 845 P.2d 800 (N.M. 1992) (interior design of health facility); Air Heaters, Inc. v. Johnson Elec., Inc., 258 N.W.2d 649 (N.D. 1977) (electrical distribution system designed); Allied Indus. Serv. Corp. v. Kasle Iron & Metals, Inc., 405 N.E.2d 307 (Ohio Ct. App. 1977) (pollution control equipment); Christiansen Bros., Inc. v. State of Washington, 586 P.2d 840 (Wash. 1978).

109. 546 N.E.2d 888 (Mass. App. 1989). *See also* Micro Data Base Sys., Inc. v. Dharma Systems, Inc., 148 F.3d 649 (7th Cir. 1998); NMP Corp. v. Parametric Tech. Corp., 958 F. Supp. 1536 (N.D. Okla. 1997); Colonial Life Ins. Co. v. Electronic Data Sys. Corp., 817 F. Supp. 235 (D. N.H. 1993); D.P. Tech. Corp. v. Sherwood Tool, Inc., 751 F. Supp. 1038 (D. Conn. 1990); Systems Design & Management Info., Inc. v. Kansas City Post Office Employees Credit

software development contract was a sale of goods, rather than a services contract. The agreement referred to a program that would substantially meet various systems specifications, but also bound the developer to use its "best efforts" to complete the system. The lower court had held that the contract was a services contract in light of the reference to "best efforts" and the fact that substantial time, skill and effort were involved in designing and creating the program. The appellate court focused on language referring to delivery of a turnkey system and warranties as indicating that this was a sale of goods. In contrast, in *Micro-Managers, Inc. v. Gregory*,[110] a Wisconsin court held that a software development contract was mainly for services. Here, the court emphasized that payment was based on hours of work and that the contract referred to an obligation to develop and design the program.

The decisions on software development contracts are divided in regard to whether the transaction involves goods or services.[111] But what are the "goods" in such transactions? They are the diskette (if any) on which the program was delivered or the electronic digits that constitute the program. Clearly, neither of the transactions in the foregoing cases emphasized acquiring the diskette. Yet, are digits, instructions, or words similar in any respect to goods? The answer should be no. What both courts failed to focus on was that the purpose of the transaction was to obtain the information – the program. This program is neither goods nor services. It is information in digital form and, under the contract, is coupled with transfer of a right to use that information.

b. *Distribution and Franchise Contracts*

In the world of goods, a distribution contract is a commitment by a manufacturer to sell products to a distributor with the expectation that the distributor will resell them to others in the stream of commerce. Even if the contract restricts the distributor on what terms or where it may resell, courts routinely hold that

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Union, 788 P.2d 878 (Kan. Ct. App. 1990); Pentagram Software Corp. v. Voicetek Corp., 1 Mass.L.Rptr. 320 (Mass. Super. Ct. 1993).

110. 434 N.W.2d 97 (Wisc. Ct. App. 1988). *See also* Data Processing v. L. H. Smith Oil Corp., 493 N.E.2d 1272 (Ind. Ct. App. 1986) ("DPS was to act with specific regard to Smith's need. Smith bargained for DPS's skill in developing a system to meet its specific needs."); Architectronics, Inc. v. Control Sys., Inc., 935 F. Supp. 425 (S.D.N.Y. 1996); Conopco, Inc. v. McCreadie, 826 F. Supp. 855 (D. N.J. 1993).

111. *See* cases collected in RAYMOND T. NIMMER, THE LAW OF COMPUTER TECHNOLOGY ¶ 6.02 (3d ed. West 1997).

such agreements are contracts for the sale of goods.[112]

Accepting this sterile transaction as a model epitomizing a sale of goods, there are many cases where distribution contracts do not fall within Article 2, even if the subject matter includes goods. One is where the "distributor" acts as the agent of the manufacturer, compensated based on a commission for goods sold.[113] Such agreements are services contracts.[114]

Another circumstance is a *franchise* agreement. In a typical franchise, there is much more going on than simply the delivery of completed goods for resale. Intellectual property issues are implicated by reliance on a license of a trademark. Many reported cases hold that a franchise contract is not predominantly a sale of goods and, because it is "not goods," that Article 2 does not apply.[115] The court in *Zapatha v. Dairy Mart, Inc.*[116] emphasized the complexity of the relationship in holding that the agreement was not a transaction in goods, but other courts have reached the same conclusion without dealing with as complex a relationship.

> We need not pause long over the question whether the franchise agreement and the relationship of the parties involved a transaction in goods. Certainly, the agreement required the plaintiffs to purchase goods from Dairy Mart. . . . However, the franchise agreement dealt with many subjects unrelated to the sale of goods by Dairy Mart. About 70% of the goods the plaintiffs sold were not purchased from Dairy Mart. Dairy Mart's profit was intended to come from the franchise fee and not from the sale of items to its franchisees. Thus, the

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112. *See, e.g.*, Heating & Air Specialists, Inc. v. Jones, 180 F.3d 923 (8th Cir. 1999); Monetti, S.P.A. v. Anchor Hocking Corp., 931 F.2d 1178 (7th Cir. 1991); Intercorp, Inc. v. Pennzoil Co., 877 F.2d 1524 (11th Cir. 1989); Paulson, Inc. v. Bromar, Inc., 775 F. Supp. 1329 (D. Haw. 1991); Thermal Sys. of Alabama, Inc. v. Sigafoose, 533 So. 2d 567 (Ala. 1988); Boyd v. Oscar Fisher Co., Inc., 210 Cal.App.3d 368 (Cal. Ct. App. 1989); *but see, e.g.*, Lorenz Supply Co. v. American Standard, Inc., 358 N.W.2d 845 (Mich. 1984).

113. *See, e.g.*, Zeno Buick-GMC, Inc. v. GMC Truck & Coach, 844 F. Supp. 1340 (E.D. Ark. 1992); Buttorff v. United Elec. Lab., Inc., 459 S.W.2d 581 (Ky. 1970); Simcoe v. Huszar, 27 UCC Rep. Serv. 627 (Pa. Ct. Comm. Pl. 1979).

114. *Cf.* Louis DeGidio Oil & Gas Burner Sales & Serv., Inc. v. Ace Engineering Co., Inc., 525 N.W.2d 217 (Minn. 1974) (contract was a transaction in goods).

115. *See, e.g.*, McDonald's Corp. v. Watson, 69 F.3d 36 (5th Cir. 1995) (UCC obligation of good faith does not apply to a franchise contract, which is not a transaction in goods); Wagstaff v. Protective Apparel Corp., 760 F.2d 1074, 1076-77 (10th Cir. 1985) (distributorship agreement not within the UCC); Wells v. 10-X Mfg. Co., 609 F.2d 248, 254 (6th Cir. 1979); Lorenz Supply Co. v. American Standard, Inc., 358 N.W.2d 845 (Mich. 1984) (franchise distributorship not a transaction in goods); Stewart v. Lucero, 918 P.2d 1 (N.M. 1996).

116. 408 N.E.2d 1370 (Mass. 1980).

> sale of goods by Dairy Mart to the Zapathas was, in a commercial sense, a minor aspect of the entire relationship. We would be disinclined to import automatically all the provisions of the sales article into a relationship involving a variety of subjects other than the sale of goods, merely because the contract dealt in part with the sale of goods.[117]

The court did hold that UCC concepts of unconscionability and good faith could be applied by analogy, thus concluding that these concepts are at least in part an aspect of the common law in that state.[118]

Franchise and similar arrangements are also licenses of rights. This takes these arrangements out of the simple model of sale of goods under Article 2. For example, in *Alesayi Beverage Corp. v. Canada Dry Corp.*,[119] the agreement, styled in part as a license, required the licensee to establish a soft drink bottling plant and to purchase soft drink extract from Canada Dry. The court held that, while there were sales of goods involved, they were incidental to the other activities under the agreement (characterized by the court as services) and, thus Article 2 did not apply. The "purpose behind the agreement was the establishment of a bottling business by Alesayi, not just the sale of extracts from Canada Dry to Alesayi." Similarly, in *Coca-Cola Bottling Co. of Elizabethtown, Inc. v. Coca-Cola Co.*,[120] an agreement for acquisition of soft drink mix, bottling and distributing the drink was not found to be within Article 2:

> Here the contracts involved are ancient, perpetual, and involve divisions of trademark rights, shared advertising, and the transfer of "the business of bottling." These factors establish a service orientation of the contracts that is much more than "merely incidental or collateral to the sale of goods." In reaching this conclusion, the court is mindful of the principle that the "scope of coverage of 'goods' is not to be given a narrow construction but instead should be viewed as being broad in scope so as to carry out the underlying purpose of the Code of achieving uniformity in commercial transactions."

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117. *Zapatha*, 408 N.E.2d at 1374-75 (internal footnotes omitted).

118. *Id.* at 1380. On applying these concepts by analogy to a franchise arrangement, *see also* Stanley A. Klopp, Inc. v. John Deere Co., 510 F. Supp. 807 (E.D. Pa. 1981) (employing UCC concepts as part of the common law).

119. 947 F. Supp. 658 (S.D.N.Y. 1996).

120. 696 F. Supp. 57 (D. Del. 1988).

> Indeed, it would be disingenuous to contend that the subject contracts do not involve the sale of "goods" within the meaning of U.C.C. § 2-102. Nevertheless, the importance of the non-sales aspects of the contracts mandates the conclusion that the contracts fall outside the coverage of the U.C.C.[121]

The results of the cases are mixed in the context of computer information (software) contracts involving a right to distribute the product. We earlier discussed *Advent Systems Limited v. Unisys Corp.*,[122] where the court wrongly equated software with a diskette and held that when a program is copied onto a disk, it becomes software (i.e., the disk itself). *Advent Systems* involved an agreement in which the distributor was authorized to market the software. The court held that this was a transaction in goods. The case did not involve a license to make additional copies of the software—only to distribute/market them.

In contrast, the court in *Architectronics, Inc. v. Control Systems, Inc.*[123] held that a software distribution license was not a transaction in goods, but a transaction predominantly focused on a license of rights. The contract involved an agreement to create modified software in which the copyright would be held by the licensor, and the transfer of an exclusive license to use, copy and distribute the software commercially. Copying and distribution, of course, are exclusive rights under copyright law. The court noted:

> The [agreement] provided for two licenses. Under the first license, Architectronics granted CSI the right to use its DynaMenu software prototypes for joint venture-related purposes only. That license gave CSI a tool necessary for the development of the "Derivative Work," a new display driver. Under the second license, CSI granted Architectronics and CADSource the right to use, copy, and distribute the "Derivative Work." That license was the centerpiece of the transaction, because it provided Architectronics and CADSource with the valuable right to manufacture the new display driver and sell it to the public. Architectronics and CADSource bargained primarily for the right to mass market the product, not for the right to install single copies of the display driver onto their own PCs. CSI's upside in the deal

121. *Coca-Cola Bottling Co. of Elizabethtown, Inc.*, 696 F. Supp. at 60.

122. 925 F.2d 670 (3d Cir. 1991).

123. 935 F. Supp. 425 (S.D.N.Y. 1996).

also was linked to the rights to reproduce and distribute: the parties anticipated thousands of sales of the new product, and Architectronics and CADSource promised to pay CSI a $20-per-copy royalty on those sales. CSI stood to gain in royalties a sum that would dwarf the $2,000 development fee. Because the predominant feature of the SDLA was a transfer of intellectual property rights, the agreement is not subject to Article Two of the UCC.[124]

c. Contracts for Licenses of Information

Most cases dealing with contract licenses of information (including computer information) do not refer to Article 2 or reject it, but rely on common law and rules deriving from intellectual property law.[125]

This is also true even when the issue is a question of the appropriate scope of Article 2.[126] For example, in *Mallin v. University of Miami*,[127] the court held that Article 2 did not apply to an agreement for the publication of a book manuscript. It noted:

> There is no need for extensive discussion. This transaction did not involve a sale of goods by the publisher to the author. The publisher agreed to perform services. The only sales to be made were those which it was contemplated would be made by the sale of books when published, by the publisher to persons who would buy the books from it. Therefore the fact that the number of books to be published was not specified in the publication contract was not material, and furnished no basis to hold that the contract was unenforceable [under the statute of frauds in Article 2].[128]

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124. *Architectronics*, 935 F. Supp. at 430.

125. *See, e.g.*, DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999).

126. *See, e.g.*, William B. Tanner Co., Inc. v. WIOO, Inc., 528 F.2d 262 (3d Cir. 1975) (deciding without discussion that a license for vocal and instrumental recordings to be used on the air cannot be characterized as a "transaction in goods" within Article 2); Snyder v. ISC Alloys, Ltd., 772 F. Supp. 244 (W.D. Pa. 1991); Incomm, Inc. v. Thermo-Spa, Inc., 595 A.2d 954 (Conn. Super. Ct. 1991). *Cf.* Miller v. Newsweek, 660 F. Supp. 852 (D. Del. 1987) (leaving unanswered the question of whether a contract between a photographer and a magazine regarding submission of negatives for possible publication was governed by Article 2 or by common law).

127. 354 So.2d 1227 (Fla. Dist. Ct. App. 1978). *See also* Stewart v. Lucero, 918 P.2d 1 (N.M. 1996) (holding that a license giving a right to conduct a catalogue business using the name of a major retail company was not goods, but an intangible).

128. *Mallin*, 354 So.2d at 1229.

In *Grappo v. Alitalia Linee Aeree Italiane*,[129] the Second Circuit held that a contract for a non-exclusive license to use a customer service training program for which the employee held the copyright was a contract for intangible *personal property*, not a contract for the sale of goods or a contract for services. This was not a contract for the sale of goods, even though it involved the purchase of books, manuals, and other tangibles essential to use the program. The court described its analysis in the following terms:

> Here, "title" to [the program] was hardly "a mere incident" of Grappo's contract with Alitalia; it was its heart and soul. Without a license to use [it] the contract would have been useless to Alitalia. While Grappo may have tailored the program to Alitalia's needs, those efforts were plainly secondary to the contract. As Grappo himself states in his complaint, the contract was for a non-exclusive license to use [the training program]. Indeed, the . . . invoice Grappo sent to Alitalia specified that Alitalia had been granted a "non-exclusive, unlimited license" for . . . .the customized version.
>
> Alternatively, Grappo argues that the contract was not for the sale of personal property . . . but for the sale of "goods" (training manuals and materials) . . . . We reject this argument for the same reason that we reject the proposition that the alleged contract was one for services: the sale of a non-exclusive license for copyrighted material was the core of the contract. The manuals would have been useless to Alitalia absent a legal right to use them.[130]

Even though it used language that an intellectual property lawyer would find awkward (e.g., *sale* of a license and *title* in a license), this court recognized a point made throughout this paper. The dichotomy between goods and services is a false one. Here, the relevant focus was neither goods nor services. It was the right to use the copyrighted information. This being said, the result of the court's analysis is one that intellectual property lawyers would find strange. The license was not governed by Article 2, but by the statute of frauds in Article 1 of the UCC, which applies to the sale of personal property other than goods.[131] The analytical flaw here

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129. 56 F.3d 427 (2d Cir. 1995).

130. *Grappo*, 56 F.3d at 432.

131. *Cf.* Respect Inc. v. Committee on Status of Women, 781 F. Supp. 1358 (N.D. Ill.

was to assume that a license was a sale.

In contrast, a number of courts have held that Article 2 applies to licenses of computer software. Most of these decisions use a predominant purpose test where the transaction involves both hardware and computer software.[132] In these *mixed* transactions, courts seem inclined to follow a goods-centric impulse and incorporate software licenses into law governing the sale of goods. Other cases use Article 2 ideas by analogy.[133]

Beyond this, some cases that approach the issue from a perspective centered on Article 2 apply Article 2 to a software license even if no hardware is involved in the transaction.[134] In most of these cases, the court asks whether the license is for goods or for services.[135] Where there is no software development component, this leads to asking whether obligations to install or maintain software are the predominant purpose, a question with an inevitable and obvious answer. But the answer is obvious only because the framework is wrong. Unlike the courts in *Grappo* or *Cardozo*, these courts fail to recognize that information can be the

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1992) (contract allowing use of a sex education program was a *services* contract governed by the common law statute of frauds and was unenforceable because the writing lacked essential terms; purchase of books as part of the contract did not bring the transaction into Article 2).

132. *See, e.g.*, BMC Indus., Inc. v. Barth Indus., Inc., 160 F.3d 1322 (11th Cir. 1998) (holding that a contract to "design, fabricate, debug/test and supervise Field installation and start up of equipment to automate [production of eyeglass lenses]" was more a contract for goods than one for services because: (1) it was captioned "Purchase Order;" (2) parties were described as "Buyer" and "Seller;" (3) it involved the sale of equipment; and (4) payment was pegged to delivery of the equipment, not to the completion of required services); Apollo Group, Inc. v. Avnet, Inc., 58 F.3d 477 (9th Cir. 1995) (finding that the sale of goods predominated and tort liability was therefore not available); Chatlos Sys., Inc. v. National Cash Register Corp., 479 F. Supp. 738 (D. N.J. 1979), *aff'd* 635 F.2d 1081 (3d Cir. 1980); Synergistic Tech., Inc. v. IDB Mobile Communications, Inc., 871 F. Supp. 24 (D. D.C. 1994); Neilson Business Equip. Ctr., Inc. v. Italo V. Monteleone, M.D., P.A., 524 A.2d 1172 (Del. 1987) (holding that a turnkey hardware and software system was a contract for the sale of goods); Design Data Corp. v. Maryland Cas. Co., 503 N.W.2d 552 (Neb. 1993); Dreier Co., Inc. v. Unitronix Corp., 527 A.2d 875 (N.J. Super. Ct. 1986); Delorise Brown, M.D., Inc. v. Allio, 620 N.E.2d 1020 (Ohio Ct. App. 1993).

133. *See, e.g.*, Angus Medical Co. v. Digital Equip. Corp., 840 P.2d 1024 (Ariz. 1992); Samuel Black Co. v. Burroughs Corp., 1981 WL 138012 (D. Mass. 1981).

134. *See, e.g.*, RRX Indus., Inc. v. Lab-Con, Inc., 772 F.2d 543 (9th Cir. 1985); NMP Corp. v. Parametric Tech. Corp., 958 F. Supp. 1536 (N.D. Okla. 1997); Systems Design & Management Info., Inc. v. Kansas City Post Office Employees Credit Union, 788 P.2d 878 (Kan. Ct. App. 1990); Pentagram Software Corp. v. Voicetek Corp., 1 Mass.L.Rptr. 320 (Mass. Super. 1993); Schroders, Inc. v. Hogan Sys., Inc., 522 N.Y.S.2d 404 (Sup. Ct. 1987); Camara v. Hill, 596 A. 2d 349 (Vt. 1991).

135. *See, e.g.*, RRX Indus., Inc. v. Lab-Con, Inc., 772 F.2d 543 (9th Cir. 1985); Systems Design & Management Info., Inc. v. Kansas City Post Office Employees Credit Union, 788 P.2d 878 (Kan. App. 1990); Camara v. Hill, 596 A.2d 349 (Vt. 1991).

focus of the transaction and that information forms a third element necessary to fill out the false dichotomy of goods-services.

Not all courts make this mistake.[136]

Nevertheless, we have a curious and unsettling conflict. Courts using the Article 2 framework apply Article 2 because software is not "services." On the other hand, courts that approach the issue not tethered to a goods-centric focus typically conclude that common law governs. For example, they would say that ownership of a copy of a computer program is determined by the restrictions a license places on the licensee, while Article 2 would judge title based on delivery of the copy.[137] The question of what is the applicable law, here as elsewhere, is uncertain and grounded in conflicting perspectives.

d. *Data and Data Processing Contracts*

Commercial transactions in data and data processing are an important facet of the information economy; cases dealing with contract issues relating to this subject matter generally do not use Article 2 to determine contract rights. The subject matter is either services or information. It is "not goods."

In *Rosenstein v. Standard and Poor's Corp.*,[138] the contract was a license allowing a commodities exchange to use the Standard & Poor's index as a basis for trading on the exchange. On one day, Standard & Poor's miscalculated the index number. Persons harmed by trading based on that error sued. The issue presented was whether the plaintiffs could bring a claim for economic loss under theories of negligence. Neither side argued that Article 2 applied, but one issue raised by the defendant was that the information (the number) was a "product" and that the concept barring recovery in negligence for economic loss caused by a product precluded the claim. The court rejected this argument, holding that "while [the index is] considered salable products, we do not believe that it sheds its character as information used to guide the economic destinies of others." Given that view, the court held that a cause of action for negligent misrepresentation could exist based on the

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136. *See* Architectronics, Inc. v. Control Sys., Inc., 935 F. Supp. 425 (S.D.N.Y. 1996) (finding that the predominant purpose of a software license was to transfer intellectual property rights, not to sell goods).

137. *See* DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999) (holding that a licensee was not an owner of a copy of a computer program).

138. 636 N.E.2d 665 (Ill. Ct. App. 1993).

claim that the mistake in the index calculation was caused by negligence. However, in this case, that claim was excluded by a contractual disclaimer.

Cases such as *Rosenstein* handle issues of contractual obligation without ever referring to Article 2 concepts. The court looked to tort law to resolve a contract issue, but never seriously asked whether the contract was within the law of sales. This approach is both appropriate and characteristic of many cases involving data and data processing contracts. Thus, the court in *Liberty Financial Management Corp. v. Beneficial Data Processing Corp.*,[139] held that a contract for online data processing was not a transaction in goods.

> In the instant case, Liberty did not bargain for reels of tape containing computer data, but for [the provider's] skill in putting the data on the tapes for transfer to the new Liberty system. This was not a transaction "in goods" as contemplated by Article 2 of the Uniform Commercial Code.[140]

Given this holding, the client could not rely on UCC Section 2-719(2) to void a damages limitation clause. Similarly, courts have consistently held that sales concepts are not appropriate in contracts for the collection and description of survey data.[141]

While this classification (i.e., "not goods") seems clearly correct, it is not followed in all cases. Thus, for example, the court in *Big Farmer, Inc. v. Agridata Resources, Inc.*,[142] held, with little discussion, that a license to use a mailing list was a transaction in goods:

> Since both parties deal in the purchase and sale of mailing lists and demographic information, both parties are merchants as that term is defined in the Uniform Commercial Code. In addition, since the information at issue is moveable and not otherwise precluded from the purview of the Uniform Commercial Code, the information may be considered goods as defined by statute.[143]

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139. 670 S.W.2d 40 (Mo. Ct. App. 1984).

140. *Liberty Financial*, 670 S.W.2d at 47. *See also* Computer Servicenters, Inc. v. Beacon Mfg. Co., 328 F. Supp. 653 (D.S.C. 1970), *affd*, 443 F.2d 906 (4th Cir. 1981); *In re* Community Med. Center, 623 F.2d 864 (3d Cir. 1980).

141. *See, e.g.*, Raffel v. Perley, 327 N.E.2d 1082 (Mass. Ct. App. 1982); WXON-TV, Inc. v. A.C. Nielsen Co., 740 F. Supp. 1261 (E.D. Mich. 1990).

142. 581 N.E.2d 783 (Ill. Ct. App. 1991).

143. *Big Farmer*, 581 N.E.2d at 789.

As a consequence, the court applied UCC Section 2-207 to determine whether a contract had been formed and on what terms the agreement arose.

A similar situation exists in data-processing contracts. If a company delivers information to a data-processing company that processes the information and returns reports, the essence of the transaction is data-processing services, not the tangible report. A services contract is involved.[144] The line is less clear in reported decisions in other situations, such as when the data processing occurs in the client's computer. Even if processing occurs in the licensor's system, the relationship between the software and the service sometimes causes a court to believe that "goods" dominate.

Thus, in *The Colonial Life Insurance Co. of America v. Electronic Data Systems Corp.*,[145] the court held that a contract for development of software and operation of a data processing system over a four year period was a contract for goods. While it recognized that the transaction combined skill, equipment, intangibles and time, the court held that the essence of the entire transaction was for the client to license use (by the provider) of a software system developed for the contract.[146] The warranty and remedy rules applicable to a sale of goods applied to this four year contract. Similarly, in *Hospital Computer Systems, Inc. v. Staten Island Hospital*,[147] the parties accepted the assumption that the UCC applied to a contract to develop software and provide information management systems off-site for the client. This led to an analysis in which a decision to end the long term contract after eighteen months because of performance problems was a proper "revocation" of acceptance of goods under the UCC.

The issue in such cases should not be whether a court can identify some element of goods or services in each deal, but whether the law dealing with the sale of a television set, an automobile, or similar transaction should apply to issues in a multiyear relationship involving review, processing and analysis of data. Most often, when on-going relationships are involved, the sale

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144. *See* Computer Servicenters, Inc. v. Beacon Mfg. Co., 328 F. Supp. 653 (D.S.C. 1970), *aff'd*, 443 F.2d 906 (4th Cir. 1981).

145. 817 F. Supp. 235 (D. N.H. 1993).

146. *Electronic Data Systems Corp.*, 817 F. Supp. at 239.

147. 788 F. Supp. 1351 (D. N.J. 1992). *See also* St. Anne-Nackawic Pulp Co. v. Research-Cottrell, Inc., 788 F.Supp. 729 (S.D.N.Y. 1992) (holding that a contract to design and deliver a pollution control system was a contract for the sale of goods because the "parties contemplated that [the vendor] would get the systems up and running and then [the buyer] would operate it").

of goods model does not provide relevant guidance.

III. THE SCOPE OF UCITA

It should be quite clear from the above discussion that contract law pertaining to information transactions, including transactions in computer information, is a complicated mixture of various areas of contract law that creates both uncertainty and conflicting case law. The Uniform Computer Information Transactions Act ("UCITA") proposes to codify and make uniform part of that disarrayed body of law. The scope of UCITA has been tailored during extended political and substantive discussion to focus on an aspect of the information industry and provide a coherent, codified body of contract law for that aspect of commerce, which is central to the modern information age.

UCITA deals with contracts and not property rights. It thus governs agreements that pertain to computer information on matters addressed by contract law, but does not create or alter property rights law.[148] For transactions to which it applies, UCITA follows the general traditions of the UCC and United States contract law in holding that, with very limited exceptions, the rules in UCITA are background that can be varied by agreement.[149] Within that framework, the Act incorporates various general law concepts such as the doctrine of unconscionability and that

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148. U.C.I.T.A. § 105(a) specifically refers to the obvious point that, when applicable, conflicting federal law preempts any conflicting provision of UCITA. Section 114 provides that various common law doctrines supplement and are not displaced by the Act, including specifically, the law of trade secrecy. The treatment of these and several related issues has been controversial in large part because one aspect of the new economy is that informational property rights law has been moved into the center of economic activity and a number of people are concerned about the relationship between that property law and contract law in the new economy. *See, e.g.*, Lorin Brennan, *The Public Policy of Information Licensing*, 36 HOUS. L. REV. 61 (1999); Raymond T. Nimmer, *Breaking Barriers: The Relation Between Contract and Intellectual Property Law*, 13 BERKELEY TECHN. L.J. 827 (1998); Mark A. Lemley, *The Law and Policy of Intellectual Property Licensing*, 87 CALIF. L. REV. 111 (1999); David Nimmer, et. al., *The Metamorphosis of Contract into Expand*, 87 CALIF. L. REV. 17 (1999); Maureen A. O'Rourke, *Rethinking Remedies at the Intersection of Intellectual Property and Contract: Toward a Unified Body of Law*, 82 IOWA L. REV. 1137 (1997). On the treatment of this issue in modern courts, *see, e.g.*, Alcatel USA, Inc. v. DGI Technologies, Inc., 166 F.3d 772 (5th Cir. 1999); DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999); ProCD Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996).

149. U.C.I.T.A. § 113 (1999). This section lists the only provisions of UCITA the effect of which cannot be modified by agreement; foremost are doctrines of unconscionability, good faith, fundamental public policy invalidation of terms, and protections for the mass-market licensee.

contracts require good faith in performance.[150] It provides sorely needed clarity on questions about choice of law, contract formation and the manner of contracting in the Internet. It provides a blended implied warranty structure which recognizes the idea of merchantability as a warranty applicable to computer programs, but provides tailored treatment for what obligations are incurred with respect to published informational content.[151] It sets out default rules tailored to the idea of information as the subject matter and a license as the primary type of contract, rather than the rules of Article 2 dealing with a model of the sale of tangible goods.

The point of this article is not to focus on substantive rules, but on what body of law applies to computer information transactions. With respect to UCITA, this turns us to the scope of the Act. The scope of UCITA hinges on its definition of "*computer information transaction*" and on application of certain listed exclusions from the scope of the Act.

"Computer information transactions" are agreements that deal with creation, modification, access to, license, or distribution of computer information as the subject matter of the agreement.[152] "Computer information means information in electronic form which is obtained from or through the use of a computer or which is in a form capable of being processed by a computer. The term includes a copy of the information and any documentation or packaging associated with the copy."[153]

The governing principle is that, in a computer information transaction, the transferee seeks the information and the contractual rights to use it. Unlike a buyer of goods, the purchaser (e.g., buyer, lessee, or licensee) of computer information has little interest in the diskette or tape after the information is loaded into a computer unless the information remains on that media and nowhere else. In online use and distribution of computer information, there is often no tangible medium at all. As we have seen, courts dealing with the scope of Article 2 often wrongly

150. U.C.I.T.A. §§ 111, 114 (1999).

151. U.C.I.T.A. §§ 403, 404 (1999). *See also* Winter v. G.P. Putnam's Sons, 938 F.2d 1033 (9th Cir. 1991); Gilmer v. Buena Vista Home Video, Inc., 939 F. Supp. 665 (W.D. Ark. 1996).

152. U.C.I.T.A. § 102(a)(11) (1999). The Act further elaborates that it does not apply to transactions simply because the parties elect or agree to communicate about the contract by means of computer information systems, such as e-mail. The idea here is that the subject matter of the transaction itself must be computer information.

153. U.C.I.T.A. § 102(a)(10) (1999).

assume that the two characteristic types of contracts are a sale of goods or a transaction in services. That dichotomy is not sustainable in the information age, where digital and other information and rights in it are often the main part of the transaction. Some courts have already recognized that this is so.[154] UCITA expressly rejects the idea that one can describe modern commerce in terms solely of goods and services.

A. *Specific Transactions Within UCITA*

UCITA thus deals with a variety of transactions at the center of the modern information economy. It applies when the contractual subject matter is computer information, whether that information entails text, images, data, programs, or other computer information. However, the mere fact that communications about a transaction, such as an application for a loan or employment, are sent or recorded in digital form does not place the transaction within UCITA. Thus, a contract for airplane transportation is not a computer information transaction even though the ticket is in digital form. The subject matter is not the computer information, but the service – air transportation. A contract to create and publish a print book is not a computer information transaction even though the author chooses or is required to deliver the work product on a computer diskette. Yet, there are many types of transactions that are squarely within UCITA.

1. *Contracts to Create or Develop Computer Information*

UCITA applies to contracts to develop, modify, or create software and other computer information, such as a computer database. Except as excluded in Section 103(d), it thus covers all development contracts. As we have seen, what contract law applies to such agreements today is difficult to answer in advance of litigation. UCITA eliminates the uncertainty, by covering the contract whether or not a court might treat the transaction as services or as goods under current case law. Of course, UCITA does not alter copyright rules relating to "works for hire" which determine ownership of the copyright in the work that has been developed.[155]

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154. *See, e.g.*, Architectronics, Inc. v. Control Sys., Inc., 935 F. Supp. 425 (S.D.N.Y. 1996); Stewart v. Lucerno, 918 P.2d 1 (N.M. 1996).

155. This law generally assumes that the copyright ownership remains in the creative developer unless either the work constitutes an employee work for hire, or the written

Some development contracts are excluded, however. These have to do with contracts to develop, create or produce motion pictures, sound recordings, or broadcast programs, or contracts for freelance news reporting.[156] The judgment was that, for these industries, upstream contracts are sufficiently different from transactions in the computer information industries as to suggest that it was not desirable to develop a single, uniform body of default rules that would cover them.[157] The parties to such contracts are able, if they choose, to opt into coverage of their transaction by UCITA.[158]

2. Transactions in Computer Programs

UCITA applies to transactions involving the distribution of, or grant of a right to use, a computer program. These transactions are within the Act whether they involve a license of the program or an unrestricted sale of a copy of a program. The difference between a license and an unrestricted sale of a copy, however, is relevant; as reflected in various provisions of UCITA, a license may involve either a more substantial retention of rights by the licensor, or a greater transfer of rights, than in an unrestricted sale.[159] Most provisions of UCITA apply to both unrestricted sales and licenses, but some are limited solely to licenses.[160]

3. Access and Internet Contracts

UCITA covers "access contracts." Section 102 defines an access contract as: "a contract to obtain by electronic means access to, or information from, an information processing system of another person, or the equivalent of such access."[161] The model is an online Internet or other online service site providing information resources, but the term also includes outsourcing and similar

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contract expressly conveys the copyright to the client. *See, e.g.*, Community for Creative Non-violence v. Reid, 490 U.S. 730 (1989); Aymes v. Bonelli, 980 F.2d 857 (2nd Cir. 1992); MacLean Assoc., Inc. v. William M. Mercer-Meidinger-Hansen, Inc., 952 F.2d 769 (3d Cir. 1991).

156. U.C.I.T.A. § 103(d) (1999).

157. *See generally* Holly K. Towle, *The Politics of Licensing Law*, 36 HOUS. L.REV. 121 (1999).

158. U.C.I.T.A. § 104 (1999).

159. *See, e.g.*, U.C.I.T.A. § 502 (1999) (ownership of a copy in a license). *See also* DSC Communications Corp. v. Pulse Communications, Inc., 170 F.3d 1354 (Fed. Cir. 1999) (holding that a licensee was not an owner when the license placed restrictions that were inconsistent with ownership).

160. *See, e.g.*, U.C.I.T.A. § 816 (1999) (self-help repossession).

161. U.C.I.T.A. § 102(a)(1) (1999).

contracts. It includes systems for access to or use of computer information on a remote information processing system.[162]

Under current law, these contracts are generally governed by common law rules.[163] This common law is underdeveloped, uncertain and non-uniform. A primary goal of UCITA is to provide a coherent template for contracting online. This template includes rules that validate use of electronic signatures and electronic records in lieu of paper records.[164] However, it goes beyond those issues and provides coherent guidance as to how contracts can be formed online and under what circumstances activities of electronic agents can form or perform a contract attributable to the person using the electronic device for that purpose.[165] Detailing these provisions is beyond the scope of this article, but the point is that coverage of this new context for commerce is a central feature of UCITA.

4. *Multimedia Works*

UCITA applies to agreements to create or distribute digital multimedia works. Multimedia products are those which, through digital technology, involve an integration of multiple forms of authorship and multiple types of information into an integrated, often interactive work.[166]

5. *Data and Data Processing Contracts*

As we have seen, case law about what law applies to data and data processing contracts is not consistent.[167] While many courts recognize that data is not equivalent to goods, some apply Article 2. Some courts treat data processing contracts as services agreements, while others view them as transactions in goods, at

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162. UCITA does not cover broadcast or similar distribution of programming, motion pictures, sound recordings or the like. U.C.I.T.A. § 103(d) (1999).

163. *See, e.g.*, Ticketron Ltd. Partnership v. Flip Side, Inc., No. 92-C-0911, 1993 WL 214164 (N.D. Ill. June 17, 1993).

164. U.C.I.T.A. § 107 (1999).

165. An electronic agent is "a computer program, or electronic or other automated means, used by a person to initiate an action, or to respond to electronic messages or performances, on the person's behalf without review or action by an individual at the time of the action or response to the message or performance." U.C.I.T.A. § 102(a)(27) (1999). *See* U.C.I.T.A. § 206 on the effect of using such agents to form a contract.

166. For a discussion of what a multimedia work is, *see* U.S. COPYRIGHT OFFICE, COPYRIGHT OFFICE CIRCULAR (MULTIMEDIA CIRCULAR) (1998).

167. *See supra* notes 126-133 and accompanying text for a discussion of data processing contracts.

least where the agreement involves software provided for the processing service. UCITA resolves this conflicting precedent and applies generally to all contracts for computer information data and for computer data processing.[168]

6. *Distribution Contracts for Computer Information*

Case law on distribution and franchise agreements is split. However, the better reasoned cases exclude distribution agreements from Article 2 when a primary basis of the arrangement lies in a license of intellectual property rights, such as a trademark or a copyright. In contracts for distribution of computer information, whether made explicit or not, allocation of intellectual property rights is frequently a principle underlying feature of the contract. UCITA resolves the conflict, covering all contracts for distribution of computer information within the single law.

B. *Specific Transactions Outside UCITA*

The scope of UCITA is limited by the definitions of "computer information" and "computer information transaction," as well as by the exclusions stated in subsection (d). As a result of these two factors, UCITA leaves unaffected all transactions in the traditional core businesses of non-digital information industries (e.g., print, motion picture, broadcast, sound recordings). Contract rules applicable to print works are outside UCITA, as are the following:

- Sales or leases of goods
- Casual exchanges of information
- Employment contracts[169]
- Compulsory licenses[170]
- Contracts where computer information is insignificant
- Computers, televisions, VCR's, DVD players, or similar goods
- Financial services transactions[171]
- Motion pictures, sound recordings, musical works[172]
- Broadcast or cable programming[173]

Some exclusions arise from the definition of scope that we have already discussed, but several are grounded in specific exclusions

168. U.C.I.T.A. § 102(a)(1)(11)(40) (1999).
169. U.C.I.T.A. § 103(d)(4) (1999).
170. U.C.I.T.A. § 103(d)(3) (1999).
171. U.C.I.T.A. § 103(d)(1) (1999).
172. U.C.I.T.A. § 103(d)(2) (1999).
173. U.C.I.T.A. § 103(d)(2) (1999).

stated in UCITA Section 103(d). These are based on a judgment that rules of UCITA should not apply to transactions in the excluded subject matter unless the parties so agree, because the excluded transactions are different in type from those covered by UCITA or are extensively covered by other contract law or regulations.

1. *Core Financial Functions*

Section 103(d)(1) excludes "financial services transactions."[174] This refers to various core banking, payment, and financial services activities. The affirmative exclusion for these transactions was based on the fact that other, settled law should govern these transactions. Because financial services transactions are similar in many ways to computer information transactions, an explicit exclusion is desirable to avoid confusion and litigation.

While both computer information transactions and financial transactions are often based on digital symbols and share some common legal issues, financial transactions should often be governed by different rules in that, in many cases, the digital subject matter of a financial transaction *is* the value it represents.[175] Also, core financial services practices are subjects of other mature bodies of law.

2. *Core Entertainment and Broadcast*

Section 103(d)(2) excludes certain agreements relating to motion pictures, musical works, sound recordings, enhanced sound recordings, and broadcast and cable programming. The exclusion covers the traditional core activities in these industries. The exclusion includes creation or distribution of these works in digital form. It is comprehensive as to core activities and leaves liability, contract formation, and other issues to general contract law as applicable.

The terms "motion picture," "sound recording," "musical work," and "phonorecord" have the meanings associated with those terms in the Copyright Act and registration system.[176] These distinctions are generally followed in UCITA. For UCITA, the term "motion

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174. U.C.I.T.A. § 102 (1999) (financial services transaction).

175. U.C.C. § 8-501(b)(1) (1998).

176. U.C.I.T.A. also excludes "enhanced sound recordings," a state law contract concept that extends to sound recordings in digital form where the copy of the recording contains a program or other limited material.

picture" focuses on linear works and does not include an interactive computer game, multimedia product, or similar work, nor does it include audiovisual effects within such interactive works.

3. *Voluntary Use of Computer Information*

Under Subsection (d)(5), an agreement is not brought into UCITA merely because one party elects to use computer information to transmit information to the other when not required to do so. For example, an author that contracts to submit an article to a publisher for publication in a print journal and elects to send the submission by e-mail, does not thereby bring the contract into UCITA. A developer required to deliver information in a form other than as computer information, does not bring the transaction within UCITA merely by electing to develop the product using digital systems.

Similarly, if the form of the information as computer information is insignificant, UCITA does not apply. This is a narrow exception applicable only where the form of the information as computer information, as compared to the information itself, is trivial. The exception does not ask a court to compare the cost or value of the computer information to the cost or value of the overall transaction. For the exception to apply, what must be insignificant is the fact that the information is in the form of computer information as contrasted to another form, such as in written form. If the information could not be provided in any other form under the agreement and still fulfill the purpose of the agreement with respect to it, the form can never be insignificant, such as where the computer information is an operating computer program system. This is true even if the operating software is provided as part of a transaction involving goods that in cost far exceed the value of the operating system. To function as an operating system under the agreement, the form can never be insignificant. Similarly, if a party acquires a billion dollar robotics system involving robots and computers along with software that operates each, the fact that the price of the software is small as compared to the billion dollar total deal does not support exclusion under this subsection. Rather, the form of the information as computer information in this transaction is essential to the agreement and not insignificant because the software must be in a form to operate the computer and robots. Insignificance focuses on the particular subject matter and its form, not on the overall deal as a whole.

C. *Mixed Transactions*

As we have seen, an issue in the relationship between sales of goods law and other bodies of contract law focuses on how to deal with so-called mixed transactions. The courts in determining whether to apply Article 2 have struggled with this concept, not always effectively. However, a fact of modern commerce is that virtually all contracts are governed by multiple contract laws. The issue is not whether this will occur, but what law applies. The treatment of this issue is outlined in UCITA Section 103(b) and (c).

1. *Computer Information and UCC Subject Matter*

Although they intermittently disregard it, courts dealing with mixed transactions as an issue of the scope of UCC Article 2 routinely apply the predominant purpose test. We have already discussed the difficulties of applying that test under current law. The salient feature of the test, however, is not simply that it leads to significant uncertainty, but that it always results in applying wrong law to some part of a transaction. That is, the part of the transaction which is different from the part that is the predominant purpose is subjected to rules that are not designed for that type of subject matter.

This is not a generally appropriate rule where both bodies of contract law are stated in a relatively coherent and uniform manner. Instead, UCITA allows each body of law to govern with respect to its own subject matter. Thus, the general rule is that, if a transaction includes computer information and subject matter governed by an article of the UCC, in the absence of contrary agreement, the UCC rules apply to its subject matter and the UCITA rules apply to its subject matter.[177]

Given the background of contract law in reference to information transactions that we have discussed in this article, the primary issue concerns the relationship between UCITA and Article 2 (and Article 2A). The basic rule remains that each law applies to its own subject matter. In general, for goods and computer information, the two sources of contract law do not overlap since computer information and informational rights are not goods.[178] The law

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177. U.C.I.T.A. §§ 103(b)(1), (c), (d)(6) (1999). When there is a conflict between UCITA and Article 9 of the UCC, Article 9 controls.

178. *See, e.g.*, United States v. Stafford, 136 F.3d 1109 (7th Cir. 1998); Fink v. DeClassis 745 F. Supp. 509, 515 (N.D. Ill. 1990) (explaining that trademarks, tradenames, advertising, artwork, customer lists, sales records, unfulfilled sales orders, goodwill, and licenses are not

applicable to an issue depends on whether the issue pertains to goods or to computer information.

There are exceptions to this approach. For purposes of UCITA, the medium that carries the computer information is treated as a part of the computer information and within UCITA, whether it is a tangible object or electronic in nature. UCITA applies to the copy, documentation, and packaging of computer information.[179] These are mere incidents of the transfer of the computer information.

In contrast, in some cases, UCITA excludes coverage of a copy of a computer program if the copy is embedded in, and sold or leased as part of goods, such as a copy of a computer program that controls engine timing in a car.[180] The rules center on the nature of the goods containing the copy and on the importance of the program and access to it in the transaction in those goods.

First: UCITA applies to the copy of the computer program if the goods in which the copy is embedded are a computer or a computer peripheral. A commercial choice to distribute a program in embedded form, rather than in a form that requires loading into a computer or peripheral does not change the applicability of UCITA. For example, the software for a medical imaging device that relies on software capabilities would be within UCITA. Of course, UCITA does not apply to the computer; it only applies to computer information.

Second: In other cases, UCITA applies to the copy of the program only if giving the buyer or lessee of the goods access to or use of the program is ordinarily a "material purpose" of this type of transaction. This standard looks at materiality in an objective sense, centered on transactions of the type, rather than on the subjective goals or intent of the particular parties. Furthermore, materiality focuses on the particular goods in which the program is embedded, rather than the overall transaction as a whole. Thus, the fact that a particular program is contained in and sold or leased as a part of goods that are a small part of a billion dollar transaction involving many other assets does not take it out of UCITA if, as to the particular goods or system containing the program, access to the program is a material aspect of the deal.

In determining whether use of the program is a material purpose

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"goods").

179. U.C.I.T.A. § 102(a)(10) (1999).

180. U.C.I.T.A. § 103(b)(1) (1999). A similar issue is addressed in UCC Article 9, but the resolution there deals with issues about creating and perfecting security interests and is not pertinent to general contract law. It is not adopted in UCITA.

in obtaining the goods, one relevant issue involves between whom the pertinent part of a transaction occurs. If goods are sold by a vendor but the buyer must obtain a license from a publisher, as to the license between the publisher and licensee, the computer information is clearly material. Beyond that, factors pertaining to whether access to or use of the program is material include the extent to which the computer program's capabilities are the dominant appeal of the product, the extent to which negotiation focused on that capability, the extent to which the agreement made the program's capacity a separate focus, and the extent to which the program is or could commercially be made separately available apart from the goods. Materiality is ordinarily clear if the program is separately licensed as part of or as contemplated by the transaction. A separately licensed program for a digital camera that enables the camera to link to a computer is within UCITA. On the other hand, the mere fact that ordinary functions of ordinary goods rely on a program embedded in the goods does not indicate that program is governed by UCITA.

2. *Computer Information and Subject Matter not within the UCC*

If a computer information transaction also involves subject matter not governed by the UCC, the basic rule remains that UCITA applies to the aspects of the agreement concerning the computer information and informational rights, but not aspects involving the other subject matter. However, because we are dealing here with uncodified, often inconsistent common law contract rules, UCITA provides that it covers the other subject matter if the computer information is the primary purpose of the agreement.

As we have seen, variations of this test have been used for years in cases involving goods and services. The test asks a court to consider whether the computer information or other subject matter (e.g., services) is the main focus. In doing so, the court should consider the type of transaction envisioned by the parties. While cases under Article 2 provide guidance on answering this kind of question, it is appropriate to consider additional factors when UCITA is contrasted to common law. Courts should consider the extent to which the transaction as a whole corresponds to the framework involved in computer information transactions, such as: (1) the nature of any underlying intellectual property rights involved, including differences in the rights provided for different types of works; (2) the extent to which regulatory rules outside

UCITA apply to the other subject matter; (3) the extent to which clear allocation of liability risk is a concern; and (4) the extent to which coverage by UCITA of the other subject matter in the transaction will correspond to reasonable expectations of the parties as to how the legal issues should be handled.

D. *Opting in or Opting Out*

UCITA Section 104 follows a general principle that the terms of an agreement govern the relationship of the parties. Consistent with that general rule, UCITA expressly acknowledges that, subject to stated limitations, the parties can agree to apply or to preclude application of UCITA to a transaction if a material part of the transaction involves computer information, or subject matter excluded under Section 103(d)(1) or (d)(2). The materiality requirement does *not* establish a standard that asks a court to determine what is the most significant or the primary part of a transaction, but whether the information has significance to the part of the transaction to which the option applies. Materiality is not met if the computer information is a trivial or otherwise insignificant aspect of the part of the transaction to which the agreement applies.[181]

In determining whether an enforceable agreement to opt-in or out was formed, a court will apply the contract formation rules of UCITA since either a material part of the agreement will involve computer information or the parties may be uncertain regarding the application of an exclusion.

The purpose of the right to agree on the coverage of UCITA is two-fold. One purpose is simply to recognize that, in the modern economy, contract choice is the governing principle. The fundamental idea of contract law is that the parties can control the terms of their own relationship. One way in which they can do so is to determine by agreement what contract law governs their relationship. Except for rules that are clearly regulatory in nature,

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181. U.C.I.T.A. § 103, cmt. 5(f) (1999). The agreement can include opting into, or out of, the contract formation rules of UCITA. "Contract formation" rules are those rules necessary to determine whether an enforceable agreement has been formed, whether actions are attributed to a person, and how terms of the agreement are adopted. The parties may apply the rules of UCITA to part but not all of their transaction if they choose to do so. For example, a company providing financial services may enter into an electronic agreement that enables a customer to access the company's database for the purpose of performing an otherwise excluded transaction. The enforceability of that agreement is determined by UCITA. The same agreement may also indicate terms and conditions regarding computer information not excluded from UCITA. The financial transactions themselves are excluded.

that contract choice should be enforced. In transactions that occur in a mass market, the idea of choice may require some further restriction to provide protection of the person with the lesser leverage. Because of that, UCITA places greater restrictions on mass-market contracts choosing to opt in or opt out of UCITA.[182]

Second, in addition to the basic concept of contract choice, there is a special need in the field of computer information transactions to allow the parties to clarify the source of contract law within which their agreement should be handled. While UCITA provides needed uniformity and coherence for these transactions, there may be cases in which uncertainty arises about when and in what manner it, common law, or Article 2 governs. The ability to contractually choose allows the parties to avoid the cost and uncertainty that would otherwise exist in such cases.

CONCLUSION

In a dynamically changing economy, the ability of basic contract law to support the transactions that drive the change is important. Yet, when the change entails a shift in the nature of the subject matter and the type of transaction involved, the circumstances and the natural tendency of courts and legislators to rely on old, out-dated images and preferences creates a situation in which the ability of underlying contract law to perform its function is compromised.

We have seen in this article the effect of the shift and the complex body of contract law that it produces. Our modern economy is no longer goods-centric, but many of our judicial opinions and academic analyses remain so. We are, instead, in an economy in which information (especially computer information) transactions play a central role. But these transactions are not analogous to transactions involving the sale of goods. Nor are they ordinary services contracts. They are an important, relatively new focus of primary commercial transactions and it is important that contract law shed its prior framework sufficiently to build a body of law that supports this new type of commerce.

One source of such a new framework has been proposed in UCITA. UCITA will not answer all of the important questions in contract law that face us in the information age. But it provides a

182. *See, e.g.*, U.C.I.T.A. § 104(3) (1999) ("In a mass-market transaction, any term under this section which changes the extent to which this [Act] governs the transaction must be conspicuous.").

firm and coherent start that can shift courts and transactional lawyers into a context where the rules and presumptions of contract fit the reality of modern information commerce.