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September 11, 2000

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

Re: High-Tech Warranty Project – Comment, P994413

By letter dated August 21, 2000, I received an invitation to submit a response regarding the Federal Trade Commission's examination of Warranty Protection for High-Tech Products and Services. I thank you for your letter and am pleased to respond on my own behalf and not on behalf of clients. I will restrict my response to the Uniform Computer Information Transactions Act (UCITA) and would welcome any opportunity to participate on an FTC panel regarding UCITA.

In my personal capacity, I am a partner in the Technology and Intellectual Property Department of my law firm, am a member of the American Law Institute and am included in "An International Who's Who Of Internet And E-Commerce Lawyers" and in the banking law section of "The Best Lawyers in America." I advise clients regarding legal aspects of electronic commerce, consumer regulations and the application of all articles of the Uniform Commercial Code. For over five years I have participated on behalf of clients who are both licensors and licensees of information as to the products they make and licensors as to consumers, in two state law projects: proposed revisions to Article 2 of the Uniform Commercial Code and the drafting of UCITA. Accordingly, I have extensive knowledge regarding the legal and policy debates regarding the issues which are now the subject of the FTC public forum. I respond, however, only as to my personal views and not the views of clients.

I have been a commercial lawyer for my entire legal career. In my view, UCITA is the most honest and impressive piece of commercial law written since Karl Lewellyn wrote Article 2 of the Uniform Commercial Code. I spent quite a few years trying to understand why UCITA was causing such an outcry from those who oppose it because through the eyes of a commercial lawyer, it reflects the finest traditions of commercial law while also accommodating numerous other legal disciplines such as laws regarding intellectual property, secured financing and commercial law consumer protections.

I have listened to commentators criticize phrases or sections as unreadable or awkward, not realizing that the language was intentionally taken verbatim from Article 2 or the Copyright Act so as not to disturb legal concepts that did not need to be disturbed. I have watched those same commentators respond to an invitation to craft better language either not accept the invitation or produce language creating problems that even the drafter acknowledges. I have listened to information managers from large software licensees who sell goods, make speeches about the need to change law to restrict use of standard forms, to regulate contract terms and to provide consumer protections to businesses, while knowing that as sellers of goods those same licensees depend upon standard forms, are free to craft contract terms to meet the needs of their businesses and customers, and are governed by laws such as the U.C.C. which do not extend consumer protections to businesses. I have watched companies seek rules that are not found in U.C.C. Article 2 or the common law, insist without producing illustrative cases, that they are. I have listened to members of intellectual property groups entreat the UCITA drafting committee and now state legislatures to change state contract law to achieve intellectual property result X or Y, knowing that the very same requests made by these groups to Congress have already been rejected by Congress. I have watched members and non-members of the American Law Institute publicly tout purported official positions of the Institute which are not official.

I have watched much more, but none of it explained the heat of the opposition until I realized two things: (1) we've had some of these fundamental debates before and will never resolve them, and (2) this kind of debate takes place every time there is a fundamental shift in our economy. The latter concept is well stated by the President of the Federal Reserve Bank of Dallas in his article entitled "Out On a New-Paradigm Limb:"

> "Paradigm" is a pretty fancy word for a country boy. My understanding of it is illustrated by the familiar recipe for boiling a frog. You don't boil a frog by dropping him into boiling water. He'll jump out. Instead, you drop him in cold water and raise the heat. The frog won't jump because he doesn't realize his paradigm is shifting.
>
> I believe our economy's paradigm has been shifting. But like the frog, many of us haven't noticed because the change has been gradual. Some attribute its improvement to good luck and temporary factors, or "positive supply shocks" in economists' jargon. . . . But we at the Dallas Fed believe there's more to it than that – a lot more.
>
> We believe once-in-century advances in technology are transforming our economy. The computer chip is doing for today's knowledge economy what electricity did for our industrial economy a century ago.

I believe the same. Karl Lewellyn wrote U.C.C. Article 2 because an economy of manufactured goods was being run on laws written for "horses and haystacks." That's simply wrong because one has little if nothing to do with the other and in law, big and little distinctions count. But if all you know is horses who are individually unique and you also know that one would as happily kick you in the teeth while another needs coaxing to come out of the stall, then you are not

immediately going to understand, and are likely to resist, a new law that assumes every horse is essentially the same and interchangeable, i.e., you would have resisted Article 2.

Thus it is understandable that in our current economy, we all feel like the frog – had we known it was changing we might have jumped. But we didn't know, or at least most of us didn't know, and now it's too late to jump even if we wanted to. And thus we are faced with the information age. Instead of attacking UCITA and trying to put the world back to the way we knew it, we should be commending those who had the foresight to see that the paradigm was shifting and to draft the necessary law to accommodate it.

To the contrary, many are still trying to jump or pound the round circle of the information economy into the square peg of laws written for goods. It took over 10 years for U.C.C. Article 2 to be widely adopted. From its introduction in 1949, the first state to adopt it (Pennsylvania) took 5 years and the second (Massachusetts) took 9 years. Then a flurry of states adopted it after 10 years or more. The flurry came because what had been viewed as "wrong" in Article 2 finally became viewed as "obvious." Perhaps it will take that long with UCITA, but one would like to think that we can learn from past mistakes and more quickly adapt old law to new subject matter. There is much disinformation about UCITA, however, so it may follow the path of the last commercial code and take a long time to become obvious. That is unfortunate.

Politics

The question is whether the FTC will try to jump out of the pan or whether it will recognize the new paradigm and take a considered look at the computer information world without using glasses tinted for the goods world. Another questions is whether the FTC can do this without being overly influenced by those who, having not prevailed with NCCUSL over years of debate, now seek to obtain from the FTC what was rejected by NCCUSL as too extreme for a commercial code, as unworkable in real or developing commerce, or as too unbalanced given the needs of *all* parties including licensors and licensees and including consumer licensees. To understand some of the push and pull that occurred in the UCITA debates and to understand some of the agendas that have been imposed upon UCITA that have little to do with it, I invite your review of an article that I wrote in 1999 regarding the politics of licensing law (copy enclosed).[1]

The Scapegoat Issue

The paradigm shift from goods to information has another effect. Critics of UCITA frequently claim that it "deprives" consumers of protections of existing law because it acknowledges the reality that computer information is not a good. Thus they argue, if a

[1] Towle, Holly K., "The Politics of Licensing Law," 36 Houston Law Review 121 (1999). References to "Article 2B" are references to the then draft of UCITA.

consumer protection statute only applies to "goods," then it will not apply to computer information if UCITA is adopted.

The argument is flawed. If UCITA did not exist the same issue would exist. It is nonsense to argue that all consumer protection statues written for goods are intended to apply to computer information – most were written before computer information even existed. So the question is whether consumer protection statutes that apply to "goods" *should be amended,* with or without UCITA, also to apply to computer information. While the answer to that question will sometimes be yes it will often be no. There is no blanket answer and UCITA does not change the equation.

For example, the Magnuson-Moss Warranty Act *already* applies only to *tangible* personal *property* that is acquired by a *buyer*. Why then would it automatically be interpreted as applying to computer information which is intangible, some of which is not property (or at least some so argue), and typically is not sold? A court will answer the question some day but UCITA is completely irrelevant to the question and the answer – the Magnuson-Moss Warranty Act either does or does not apply to computer information that is licensed and UCITA has nothing to do with it. Sometimes UCITA opponents skip over the question of tangibility and go right to the "buyer" requirement, arguing that UCITA removes Magnuson-Moss protection because it requires computer information to be licensed. Again, not so. UCITA doesn't require any particular form of transaction for computer information: it can be sold, it can be licensed, it can be "rented," or anything else that parties legally may dream up. UCITA speaks in terms of licensing because that *is* the overwhelming way in which computer information is distributed; U.C.C. Article 2 speaks in terms of sales of goods because that is how most goods are distributed unless they are leased under U.C.C. Article 2A (which speaks in terms of leasing). If UCITA did not exist the question of whether the Magnuson Moss Warranty Act applies would still exist: computer information is *already* licensed and has been for about 20 years.

As for the question of whether consumer protection statutes *should* be changed to cover goods, that is a legitimate question that would need to be addressed on a case-by-case basis. Again, the Magnuson Moss Act is illustrative. Assuming an implied warranty, *should* computer information implied warranties be made non-disclaimable under the Act if the computer information comes with a written warranty or a service contract? The answer clearly is no. The easiest way to see that is to consider the impact of such a rule on the open source software community (which will increasingly provide service contracts in order to make a commercial market but also requires disclaimer of implied warranties under the foundation license) or upon small developers. I am sure the Commission will receive input on the need to be able to disclaim implied warranties. My point is that the need for computer information is *different* and *greater* than for goods and that those and all other differences need to be considered in any examination of whether a "goods" statute should be applied to computer information. In short, when considering that question the answer cannot be an automatic yes. It must be a nuanced and

thoughtful answer predicated on the provisions of each statute, the differences between goods and information, and the consequences of extending coverage to computer information.

In every case, however, UCITA is irrelevant. UCITA's only relevance is that it expressly preserves consumer protections statute and invites states to review them.

Recycled Debates – Standard Forms and Intellectual Property

My second realization was that these debates are not new.

A. Standard Forms. As I said in my article, we are dancing to tunes that have already been named – we are simply unaware of the titles. For example, many of the FTC questions and the entirely different topics listed in its draft agenda for discussion at the October public forum reflect a debate that raged when Karl Lewellyn wrote U.C.C. Article 2. In my article I refer to this as the mass-market license or contract terms debate and its manifestation in these hearings revolves around the questions concerning shrink-wrap and click-wrap licenses, the power of parties to negotiate contracts or standard forms and the question of whether commercial contract law should continue to honor traditional concepts of freedom of contract or whether the government should impose and regulate contract terms.

The curious thing about this argument is that is has nothing to do with UCITA. Yes, the information industries use contracts but these questions do not pertain only to the information industries and these questions are *not new*. My credit card contract and car rental contract are long standard forms that I cannot and do not want to negotiate. Both our old and new economy *runs* on standard form contracts, adhesion or not. Legal rules and courts have long dealt with them appropriately.

The only new thing about computer information licenses is that they actually *are* the reason that I can get information, i.e., they not only have all of the nonnegotiable terms that consumers would expect in a standard form contract, they are themselves, in a sense, the product. When I paid a consumer price for use of a graphics program to make a family cookbook, I got the same program that graphic artists use. Granted, I didn't need half of its features and didn't even know what they were for, but I used others and was delighted to have access to a program for which commercial artists pay thousands of dollars. Given that I got the same program that they did, the only difference was the price and the *license*, i.e., my license looked different from theirs but the program was exactly the same. My license restricted me to consumer uses and was the way in which I obtained a right to use the program at all or in ways that otherwise would have violated the copyright of the software publisher. As a consumer did I care about all of the nonnegotiable terms that came with that contract? Absolutely not – I knew that I could not change them and that the price I paid depended upon my willingness to take those terms. My alternative was to choose another product, pay the commercial price for more rights or pay an attorney to see if the publisher would be willing to negotiate a non-standard contract with me. I

wasn't interested in doing any of that and was happy to make the standard bargain because my focus is on price and product availability.

Given that contracts are a fact of life for the information economy, then a state law question concerns how consumer contracts are treated in UCITA. I have answered the question in an article that is pending publication, entitled "Mass-Market Transactions in the Uniform Computer Information Transactions Act" (copy enclosed). The answer is that consumers are treated better under UCITA than under the common law and are treated as well under UCITA as they are in U.C.C. Article 2 and are also afforded protections that do not exist in Article 2. UCITA also preserves substantively separate consumer protection statutes. Businesses also are afforded "consumer" protections under UCITA that do not exist in Article 2. Having said that, however, UCITA is not and should not be a consumer protection statute. Like Article 2 it is a commercial code and such codes have an entirely different purpose than consumer protections statutes. The purpose of a commercial code is to facilitate commerce and benefit all of society, including consumers, though a continued expansion of commercial practices that are made uniform through codification. Commercial codes supply legal infrastructures and they are just as important, if not more important, than physical infrastructures.

UCITA does not change, other than to improve, aggregate consumer protections found in commercial codes nor does it invent standard forms or their enforceability. What is puzzling then, are the FTC questions concerning contractual matters not dealing with warranties and which are posed only with respect to the computer information industries as distinct from other industries that rely on contracts. If the U.S. were ever fundamentally to change commercial contract law, the debate leading to any such change should be had with respect to every industry that uses contracts, including the goods industries, the common law service industries and even the government. Contracts are the legal foundation of our economy and to change the rules for any segment either affects other segments or discriminates against the impacted segment. Given the traditional regulation of contract by states and the Constitutional division of powers between states and the federal government, any such debate will also be informed by those principles.

B. Intellectual Property. No debate about the intersection of intellectual property laws and contract law took place when Article 2 was written – that is the reason Article 2 doesn't work for computer information – Article 2 only concerns goods. However, the advent of the information economy has generated raging debates concerning intellectual property that have taken place or are taking place federally and internationally, and those who cannot get what they want from Congress have decided to see if they can get it from UCITA. Thus librarians seek amendments attempting to relieve them from making or managing contracts; proponents of reverse engineering seek amendments banning any contract clause that prohibits reverse engineering; and consumer or other representatives claim that UCITA creates a ban on free speech by failing to state as a matter of state contract law, that X, Y, and Z kinds of statements cannot be controlled by contract.

State contract law has never so provided. State contract law is generic. State contract law currently enforces contracts, including computer information licenses, yet does not contain the requested specific rules against X, Y and Z statements, reverse engineering and libraries. If Congress believes librarians should not make or be bound by contracts then it may say so; in fact it appears to have said the opposite in Section 108(f)(4) of the Copyright Act. If Congress determines that prohibitions on reverse engineering ought to be banned, then it may say that; in fact, the Digital Millennium Copyright Act addresses reverse engineering but does not go that far. And even Congress cannot speak very widely about the Constitutional right of free speech – when it applies both federal and state law fall before it.

For purposes of argument, let's assume that a state law could and should control each of these areas. What then would be the list of new state contract rules? UCITA for the first time in a commercial code, does create a new rule which addresses these concerns in a general way that will stand the test of time. Section 105(b) essentially invites a court to weigh competing fundamental public policies in all of these and other areas against each other, including the right to make contracts (which is also a Constitutional right). UCITA authorizes courts to invalidate particular contract terms if they fail the balancing test. Even though critics may admit that the rule is sufficient to prohibit enforcement of egregious terms, and may admit that the Official Comments almost invite courts to invalidate some of the very clauses which are alleged to be ubiquitous in the computer information industries, their ultimate complaint is that courts will need to decide what X, Y and Z are and that this may take a long time. That is true. It is also true without UCITA. Under the common laws regarding contracts and under U.C.C. Article 2, courts interpret or decide everything. That is our system. If anyone is going to write a statute that dictates a specific result on these federal issues, that body ought to be Congress – and even then courts will interpret what it must have meant.

Conclusion

There is nothing simple about any of the issues being considered by the FTC. UCITA is living proof that the issues are complex and generate strong views from all sides. But UCITA is not the real cause of most of the heat and the source of the strong views: it has simply become the vehicle for discussing larger debates. The FTC could do a great service by helping all sides get past the heat and by providing a platform for a fair and thoughtful examination of what UCITA actually is, a *commercial* code for computer information transactions. Requests to change intellectual property laws should be addressed to Congress. If UCITA is to be the battle

ground for all questions of contract law and for a re-examination of the traditional split between consumer law and commercial law, then more industries need to be involved because any actions taken will affect our entire economy and the well-being of all consumers, not just those who acquire computer information.

Very truly yours,

Holly K. Towle