

**Cem Kaner, Ph.D., J.D.**

Law Office of Cem Kaner

<http://www.badsoftware.com>

P.O. Box 1200, Santa Clara, CA 95052

[kaner@kaner.com](mailto:kaner@kaner.com)

408-244-7000 (v)

408-244-2181 (f)

## **CONSUMER ISSUES AND ARTICLE 2B**

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**I am submitting this to the ALI on behalf of Todd Paglia of the Consumer Project on Technology and myself.**

**It is our understanding that the ALI is interested in hearing a short list of proposed changes to Article 2B that would make it more palatable to consumers and small business customers. We are submitting this prioritized list in that spirit.**

**We are deeply concerned about Article 2B. We believe that it is seriously flawed, and that little has been done to correct its biases despite strong and detailed opposition from consumer and small business representatives. Our concerns run deeper than the 12 items listed in this memo. We are, for example, fundamentally in opposition to the position taken by the drafting committee that it is desirable to simultaneously recognize the validity and respectability of adhesion contracts and to declare that they should be completely unregulated on the grounds of freedom (for the drafter) of contract. We believe that the committee is giving software publishers significantly more power to set their terms than they have under current law, and we see no public interest in support of this.**

**Here is our list.**

### **1. Consequential damages**

**Article 2B makes it easy for the mass-market software publisher to escape liability for incidental and consequential damages. We understand the policy tradeoffs inherent in this, but protest that this is outrageous in an adhesion contract when it is applied to a defect that was known to the licensor at the time of sale or was not known only because of gross negligence on the part of the licensor.**

**Depending on the balance of the rest of the draft, we are willing to consider a reversal of the default rule for consequentials, eliminating them (unless provided for in the contract) except when the damage was caused by a known defect or a defect that was not known only because of gross negligence on the part of the licensor.**

**We are also willing to see a cap on these non-excludable consequential damages in the mass-market. Kaner has suggested a maximum per license of \$500 or five times the license fee, whichever is greater. This will probably not fully compensate the customer, but it will provide a needed incentive for publishers to fix their more serious defects.**

**We are also willing to see an exclusion of consequentials for a known defect if, at or before the time of contracting, the licensor supplies to the licensee a record that:**

- describes the defect in a way that is understandable to a typical member of the market for this product,
- explains how to work around the defect, in a way that is understandable to a typical member of the market for this product,
- explains how to avoid the defect, in a way that is understandable to a typical member of the market for this product,
- and that explains how to recover from the defect, in a way that is understandable to a typical member of the market for this product.

When dealing with an industry that ships products with known defects as a matter of course, customers should at least be given a fair chance to mitigate their losses.

## 2. Choice of forum

The effect of Article 2B will be to provide small customers with no forum for their disputes with a publisher.

We recommend that if (a) the contract is mass-market and (b) the amount in controversy is within the customer's home state's small claims court jurisdictional limit, then the customer can bring an action in his home state or, if he cannot obtain personal jurisdiction over the defendant in his home state, then anywhere where he can obtain jurisdiction over the defendant. The adhesion contract can specify a choice of forum, and it will be enforced if the amount in controversy (aggregated over all plaintiffs, in a class action suit) is greater than the small claims court jurisdictional limit.

## 3. Express warranty

Statements, descriptions or affirmations of fact in the hard copy or online documentation or on the packaging or in other statements made by the publisher to the public at large should be express warranties, whether or not the licensee was aware of their content at the time of contracting.

Our rationale for including statements made to the public at large is that these are restated in trade publications that circulate widely to the general public. They become part of the basis of the bargain in fact, but the chain from the public statement through the magazine to the customer is too hard to prove.

## 4. Intellectual property

Mass market licenses should not be allowed to include prohibitions against reverse engineering, decompilation, and other similar use restrictions. Nor should they be allowed to declare the observable behavior of the product a trade secret and they should not be able to impose restrictions that conflict with the first sale doctrine.

We agree that a publisher can and should be able to impose restrictions in a license that go beyond those available to a seller of goods (books or merchandise containing patented technology) but it should not be allowed to do so in adhesion-contract-based transactions conducted *in the mass market*. We propose:

A term restricting the use of a mass-market product is not valid in a mass-market license unless it (a) would be an enforceable term in a contract for the sale of the product or (b) is a conspicuous restriction on the number of times the product can be used, the length of time that the product is licensed for, or the

number of people who can simultaneously use the product.

## 5. Incidental damages

Many of the incidental damages involved in mass-market software are imposed by the publisher or as a consequence of delays created by the publisher. For example, the Software Support Professionals Association reports that it takes, on average, 30 minutes for a customer to reach an appropriate person to ask about a problem with a software product. Most of the rest of the time is spent sitting on hold, burning through long distance charges. Many publishers now charge complaining customers a fee per minute or per call and some charge the fee even if the customer is reporting or complaining about a defect that was known to the publisher at the time of the sale.

A mass-market publisher should not be able to exclude incidental expenses that are incurred in reporting the defect, in returning the defective product, or in seeking support from the publisher for the defect or its consequences.

## 6. Consumer protection

Under the Magnuson-Moss Warranty Improvement Act and the associated FTC regulations, customers are entitled to see the warranty of any goods sold for \$15 or more. As the Software Publishers Association's own *Model PC Software License Agreement (and Explanatory Comments)* states (p. 35), "It is reasonable to assume that software purchased for home computer use would be covered by the Act."

Yet software customers are rarely able to see the warranties provided with software until after the sale. This makes it difficult for individuals and reporters to compare the extent to which competing companies will stand behind their products. Article 2B characterizes mass-market sales of software as licenses, which might not be covered by the Magnuson-Moss Act, and blesses the practice of refusing to allow customers to see the contracts until after the sale is complete.

Warranty rules and other consumer protections should be the same for mass market software products and goods. Article 2B should explicitly state that, for purposes of state statutes and other state law concerning contracts for consumer goods, and for purposes of all other consumer protection statutes of the state, a mass market license is a "good." Also, Article 2B should state that the provisions of the Magnuson-Moss Act apply to mass market software, to the extent that other state law does not cover the same area.

## 7. Material breach

A breach should be considered material if it would be material under the Restatement of Contracts or if the breach caused or may cause substantial harm to the aggrieved party, including imposing costs that exceed the contract value.

## 8. Mitigation of damages

2B-707 requires the customer to maintain backup systems just in case of breach of contract by the software publisher. The customer cannot recover compensation for losses that could have been avoided if the customer regularly backed up her data.

There are many ways that any prudent person can protect herself against the possibility of breach of contract by any other party. The point of a contract, though, is that it lays out the duty of the publisher to not breach. The customer should not have

**to spend time, effort and money on defensive steps, before a breach, to minimize the damages that will be incurred if the publisher should happen to breach.**

**It is frequently reported that individuals and small businesses rarely back up their hard disks. At a Law Practice Management session at the August 1997 ABA meeting in San Francisco, only half the attendees reported that they backed up their hard disks. This might not be wise on their part but it is the current situation. Why should the law grant contract-breaching publishers a special deal by requiring a higher standard of self-protective care from customers than customers currently afford themselves today?**

**The requirement in 2B-707 that customers must back up their data should be struck.**

## **9. Internet rules**

**Customers who purchase a product or license over the Internet or through some other electronic transaction shall have the same rights as if they purchased or licensed it by any other means.**

## **10. Electronic Commerce--attribution**

**2b-116(a) unfairly allocates risk of loss onto customers. If the security of the customer's computer is compromised, then messages can be sent that appear to be coming from the customer but do not. The customer has to prove non-negligence to avoid paying for all of the losses caused by the ensuing fraudulent transactions. The overall security of the system, however, is heavily under control of the other parties (see Kaner, Article 2B is Fundamentally Unfair to Mass Market Software Customers, submitted to ALI for the October meeting and available at <http://www.badsoftware.com/ali.htm>). This risk allocation is inappropriate for this emerging technology. Kaner recommends that the presumption that a message came from the apparent sender be very weak, a bursting bubble.**

**A more traditional consumer requirement would be a limit on consumer liability, to \$50 or \$100.**

## **11. Electronic commerce - risk of error**

**2B-117's restriction to consumers is too narrow. The problem is that user errors are heavily determined by the designer of the system, and the system design is fully under the control of the seller. Computer systems are not fully familiar to the average customer, whether that person is a consumer, a lawyer, or another non-software-merchant.**

**2B should provide the seller with reliance damages in the event of an error by the customer, but should otherwise allow the mistake-making customer to escape liability.**

## **12. Arbitration clause**

**A compulsory arbitration clause in a mass market license is not binding if the dispute involves fraud or defects that could threaten the health or safety of customers or the general public.**

**A compulsory arbitration clause in a mass-market license is also not binding unless it provides for arbitration in the home state of the customer.**

**Yours truly,**

**Cem Kaner signing on behalf of himself and Todd Paglia, Esq.**