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THE ALI'S PRINCIPLES OF SOFTWARE CONTRACTING: SOME COMMENTS & CLARIFICATIONS

Maureen A. O'Rourke*

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I. INTRODUCTION

When I joined Boston University School of Law's faculty in 1993, there seemed to be general agreement among practitioners and academics alike that the time was ripe for some sort of uniform law to address transactions involving software. The debate was over the *form* that law should take rather than whether it should exist at all. More specifically, interested parties were discussing an important structural question—whether software contracts might best be dealt with in the Uniform Commercial Code (UCC) under a "hub and spoke" approach or as a standalone Article. Eventually, drafters focused on a standalone Article, and the National Conference of Commissioners on Uniform State Laws (NCCUSL) and American Law Institute (ALI) worked for a number of years on a new Article 2B that would be incorporated into the UCC. When the joint effort was abandoned, NCCUSL continued the work and promulgated the eventual end product as the Uniform Computer Information Transactions Act (UCITA).

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Debates continue today about whether or not UCITA was successful. One might answer that question through an empirical study of the number of software agreements that adopt UCITA as the governing law and the importance and nature of the software licensed under such agreements. We did not undertake such an empirical study. We did, however, find much to admire in UCITA and drew on it in our own work.

While I cannot speak for the ALI, I believe that the organization felt that the area was ripe for a project which does not restate the law, but rather tries to bring some order to the case law and recommend best practices without hindering the law's adaptability to future developments. In ALI parlance, such a project is conducted as a "Principles" project. Like a Restatement, a Principles project is drafted by "Reporters" who receive input from a group of advisors and ALI members. Advisors are not required to be ALI members, and represent a variety of constituencies. We met over a 5-year period—it did not take that long, however, to discover that serious disagreements existed, and, in some cases, we would need to make hard choices that would likely satisfy very few. In other words, our experience was not unlike that of UCITA's drafters and the criticisms we received often recalled the debates over UCITA.

I will not attempt here to mount a defense of either the advisability of the project in the first place[1] or to justify all of its provisions. Rather, I am writing here for two reasons—first, to

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[1] The consensus for the need for a uniform law for software contracting that ostensibly existed at the time of the UCC Article 2B effort may have eroded over time as technology advanced, contracts became more sophisticated, and courts addressed disputes over agreements involving software under either common law contract or the UCC.

express my gratitude to Suffolk University Law School for conducting the day-long program on the Principles; and second, to focus on just three areas that arose in our discussion during that program. For those who are interested, I would recommend reading the Principles in their entirety and drawing your own conclusions.[2]

II. SOME COMMENTS & CLARIFICATIONS

A. Contract Formation – Standard Forms

At the conference, panelists objected to our provisions addressing standard form contracts. They read the relevant sections to require electronic standard forms to be presented as clickwrap agreements. This is not, however, the Principles' approach.

We drafted provisions on contract formation against the backdrop of a number of relevant facts. First, we recognized that software vendors license their products in a variety of ways—from negotiated, signed agreements to standard forms presented as shrinkwrap, clickwrap or browsewrap agreements. Second, we believed that courts, using common law contract and the UCC, had begun addressing the legitimacy of different modes of contract formation in the best sense of the common law tradition. Their decisions illustrate, unsurprisingly, that the standard form context presents the most challenges for classical contract law. Finally, we appreciated that, as in many areas of the Principles, the underlying issue - contract formation particularly in an online environment—is by no means unique to software.

[2] The text of the Principles is available from the ALI. Readers may also find interesting Volume XX of the Tulane Law Review, a symposium devoted to the Principles.

In § 2.02, we address questions of contract formation in the context of standard form transfers of generally available software. We define such a transaction as:

> A transfer using a standard form of
> (1) a small number of copies of software to an end user; or
> (2) the right to access software to a small number of end users
> if the software is generally available to the public under substantially the same terms.[3]

In § 2.02(b), we adopt traditional contract law—the Restatement test—as the overriding governing principle: "A transferee adopts a standard form as a contract when a reasonable transferor would believe the transferee intends to be bound to the form."[4] This standard gives the courts room to continue developing the common law as they address new modes of contract formation.

We sought, however, to enhance certainty by offering transferors a safe harbor. The safe harbor is exactly that—a standard that, while not required, offers the parties the certainty of legitimacy in contract formation. As a matter of interpretation, the safe harbor is effectively an *example* of when the test of § 2.01(b) is satisfied; it is not the *only* way to satisfy § 2.01(b).[5]

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[3] ALI Principles § 1.01(l). Section 1.01(k) defines standard form as "a record regularly used to embody terms of agreements of the same type."
[4] *Id.* § 2.02(b).
[5] *Id.* cmt. c. ("Subsection (c) prescribes best practices and constitutes a safe-harbor provision for transferors. Compliance with subsection (c) should as-

The safe harbor is met when:

(1) the standard form is reasonably accessible electronically prior to initiation of the transfer at issue;

(2) upon initiating the transfer, the transferee has reasonable notice of and access to the standard form before payment or, if there is no payment, before completion of the transfer;

(3) in the case of an electronic transfer of software, the transferee signifies agreement at the end of or adjacent to the electronic standard form, or in the case of a standard form printed on or attached to packaged software or separately wrapped from the software, the transferee does not exercise the opportunity to return the software unopened for a full refund within a reasonable time after the transfer; and

(4) the transferee can store and reproduce the standard form if presented electronically.[6]

The safe harbor, then, essentially validates clickwrap agreements, providing a strong incentive for their use. It does not, however, *require* providers to use clickwraps as a condition of enforceability. In particular, as we note, there are occasions, including in transactions involving open source software, in which established custom counsels against requiring the click-

sure a transferor of the enforcement of the standard form, but failure to comply does not absolutely bar a transferor from otherwise proving transferee assent.") Comment c does, however, also note that "[I]n many instances, failure to comply with the [safe harbor] should mean that the standard form will not be enforceable because it fails the reasonable-transferor test of subsection (b)." *Id.*

[6] *Id.* § 2.02(c).

wrap.[7] The general test of § 2.02(b) suffices for these transactions and, in many cases, will find that a contract has been formed.

B. Express Warranty – Creation and Disclaimer

Some commentators at the conference expressed concern about § 3.02 on the creation of express warranties as well as how that section is to be interpreted consistently with § 3.06 on disclaimers. Specifically, some questioned why the Principles do not require a showing of actual reliance for an express warranty to exist. They also asked how § 3.06, which provides that disclaimers of express warranties are not enforceable, works with contract interpretation principles. That is, they raised the question whether we intended courts to incorporate statements the transferee did not rely on into a fully integrated agreement in which the parties indicated the exclusive sources on which they were relying.

Section 3.02 on the creation of express warranties is quite similar to UCC Article 2-313.[8] Like 2-313, § 3.02 states that an

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[7] *Id.* § 2.02 cmt. b.

[8] U.C.C. § 2-313 states that:

> (1) Express warranties by the seller are created as follows:
>
> (a) Any affirmation of fact or promise made by the seller to the buyer which relates to the goods and becomes part of the basis of the bargain creates an express warranty that the goods shall conform to the affirmation or promise.
>
> (b) Any description of the goods which is made part of the basis of the bargain creates an express warranty that the goods shall conform to the description.
>
> (c) Any sample or model which is made part of the basis of the bargain creates an express warranty that the whole of the goods shall conform to the sample or model.

U.C.C. § 2-313 (2011).

express warranty can be created by an affirmation of fact or promise, a description, or a demonstration.[9] Unlike 2-313, § 3.02 does not require that the affirmation, description, or demonstration form a part of the basis of the bargain. Rather, an express warranty is formed if the assertion is one on which a reasonable transferee *could* rely.[10]

As we discuss at length in the Principles, the UCC's basis of the bargain test has proven difficult for courts to understand and apply and has been at issue in many cases.[11] The UCC's comments state that 2-313 was not intended to require particular reliance, leaving it to courts to attempt to discern what the term "basis of the bargain" in the black letter was intended to mean.[12] We believe that our formulation is consistent with both what the UCC's drafters intended and courts have in fact been doing.

It is not the case that express warranties may not be disclaimed under the Principles. Under § 3.06(a), "A statement intending to exclude or modify an express quality warranty is unenforceable if a reasonable person would not expect the exclusion or modification."[13] Thus, a disclaimer is enforceable if a reasonable person would expect it. If (as in the hypothetical

[9] ALI Principles, § 3.02(b) (explaining the ways in which a transferor might make an express warranty); UCC Art. 2-313 (listing the ways in which someone might make an express warranty).
[10] *Id.* § 3.02(b). Comment b expressly states that the "basis of the bargain" test is omitted from Section 3.02.
[11] *Id.* § 3.02 cmt. B (stating that the "basis of the bargain test" is "foggy" and has caused much litigation).
[12] *See* U.C.C. § 2-313 cmt. 2. Comment 2 state that, beyond the brief discussion provided, "the matter is left to the case law with the intention that the policies of this Act may offer useful guidance in dealing with further cases as they arise." *Id.*
[13] ALI Principles § 3.06(a).

raised at the conference) a party agrees that they are relying on only a limited number of representations, a court should find that a reasonable person in that context could not rely on other representations or, in other words, would expect the disclaimer.

C. Contracting Around the Principles

Another question that arose at the conference was whether parties could opt out of the Principles as the governing law in their agreement. For example, the parties might agree to a provision that states something akin to "The Principles of the Law of Software Contracts shall not provide the rule of decision for matters arising under this agreement."

Of course, the Principles are not the law within a jurisdiction unless and until a legislative body adopts them as law or a court looks to them to provide guidance, adopting a particular rule set forth in the Principles as part of the common law. To date, courts have generally decided software contracting cases under either the Restatement or the UCC. To the extent that we have simply reiterated rules that would apply in the absence of the Principles—e.g., unconscionability, public policy—the parties effectively cannot avoid the Principles by agreement. We are unsure why they would wish to. In such areas, we have collected the then current cases and provided illustrations that we believe would be helpful to both the parties and courts in determining outcomes.

Of course, both the Restatement and UCC leave gaps. For example, the Principles contain a section on automated disablement,[14] a topic that neither the Restatement nor the UCC express-

[14] *Id.* § 4.03 (granting a specific remedy to transferors of software).

ly addresses. In such cases, as well as ones in which the Principles modify what the other sources of law would provide, parties are free to provide that the Principles do not govern. Keep in mind, however, that to the extent that a court finds the Principles' approach to better state fundamental public policy, contracting around the Principles would have no effect.

Our suggestion is that lawyers should familiarize themselves with the Principles before making a judgment counseling a client to avoid them. In fact, there may be a number of places in the Principles where we have taken positions that may prove useful to a client in a particular context.

III. CONCLUSION

I am grateful to Suffolk University Law School and the conference organizers for the chance to present the Principles to a diverse audience. I also appreciate the opportunity to clear up some confusion and misperceptions regarding their content. The three areas discussed above do not, unfortunately exhaust the items which have raised questions. A common misconception that seems to exist is that we have departed from traditional contract law and required that all on-line agreements be characterized by a click-wrap license requiring assent at the end. We hope, however, that most answers will be found in a careful reading of the Principles themselves.