

# UCC TO GOVERN INTERNET TRANSACTIONS: A SUREVY OF PROPOSED CHANGES

By: Shelley M. Liberto, Esq.

From the December 1997 issue of *The Orange County Lawyer*  
Copyright © 1997 by The Orange County Lawyer.  
All rights reserved.

## Introduction

As the Internet continues to gain popularity as a dynamic commercial medium, fundamental tenets of contract formation, performance and enforcement are becoming obsolete. The American Law Institute and National Conference of Commissioners of Uniform State Laws (the "ALI") has therefore been hard at work to keep one step ahead of the cyberspace revolution. The ALI's proposed Article 2B to the UCC, entitled "Licenses", is now in the final stages of the drafting process. It proposes a structure for governing Internet commerce and software licensing by overcoming fundamental assumptions that contracts must be written or oral by abandoning the Statute of Frauds as we know it. Article 2B also creates a double standard for warranties against software viruses as between merchants and the consumer "mass market," rejects the Mailbox Rule as applied to contract formation on the Internet, and acknowledges inanimate computer robots as "agents" of the parties. The following is intended to be an abbreviated survey of the more prominent provisions proposed by the ALI in its new UCC Article 2B.

## Contract Formation by "Attribution" of "Electronic Records"

Contracting on the Internet imposes new problems of the anonymity of parties and the Statute of Frauds requirement of a signed writing. The identity of the parties dealing on the Internet is addressed by Article 2B in terms of "attribution of electronic records." Proposed § 2B-111 defines risk allocation rules that rely on an "attribution procedure" that must be agreed to by the parties before contract formation. An "attribution procedure" is any commercially reasonable procedure adopted by the parties to verify that electronic messages are indeed those of the respective parties, and for detecting errors in the transmission of information. Attribution procedures may, for example, make use of access numbers, codes, or e-mail addresses.

Contractual commitments are attributable to a party in Internet communications if the communication was actually sent by the named party, its human agent, or its "electronic agent." "An electronic agent" is defined as any electronic or automated means used to initiate or respond to electronic messages without review by a person, in other words, a "robot." In the event of communications by an imposter, the communication is nevertheless attributable to the named party if the receiving party complied with the agreed attribution procedure and, in good faith, concluded that it was sent by the other party. This feature holds the transmitting party to its communication even in the event of an erroneous transmission. Risk is also allocated to the purported sender if an imposter transmitted the communication by use of confidential access numbers and codes, obtained as a result of the failure of

the alleged sender to exercise reasonable care. In sum, the receiving party is entitled to attribute the Internet communication, indeed a binding contract, to the named sender as long as the communication complies with the agreed attribution procedure, or the receiver reasonably relies on the result of a breach of security caused by the alleged sender's negligence. No data or hard copy record of the electronic exchange need be retained to be enforceable. The enforcing party need only prove the use of the agreed "attribution procedure" by which an authenticated record must necessarily have been created. Contracts so formed are enforceable notwithstanding the Statute of Frauds.

### Opportunity to Reject Prior to Tender; Right to Refund

Under proposed § 2B-112, the manifestation of assent to the terms of virtual contracts and the right to payment hinge on an offeree's opportunity to review contract terms before manifesting assent. This is the ALI's attempt to solve the problem of post-tender presentation of terms as may occur in electronic Internet exchanges, and in "shrink wrap licenses." In the "shrink wrap" license scenario, a licensee typically pays for the software and then, by the act of opening the package, agrees to previously undisclosed licensing terms which appear inside. If the licensee is given an opportunity to review terms only after paying for the product, he or she is accorded a right of refund if the terms are declined. Likewise, if Internet communications are structured to disclose terms only after acceptance, payment or delivery of the software by Internet download, the offeree is entitled to reject and obtain a refund. This post-assent refund right does not exist in current law.

### Mailbox Rule Rejected

During the course of e-mail exchanges, the parties negotiating a transaction are necessarily confined to the use of their respective Internet Services Providers ("ISP") as a conduit to receive and deliver their e-mail. ISPs are notorious for dispatching and delivering e-mail at different rates of expediency, from a few minutes from transmission, to a few days. Even when e-mail arrives at the recipient's own ISP, the recipient must "log on" to its ISP to effect final delivery of e-mail to his or her own personal computer.

Under the common law Mailbox Rule, a hard copy acceptance of an offer is effective upon dispatch or mailing. Because of the ISP expediency problem, the ALI has opted to reject the Mailbox Rule in proposed § 2B-204 by deeming the acceptance of an offer to be effective upon receipt, rather than upon dispatch. The acceptance is effective even if no individual is aware of its receipt. But the question remains: "Receipt by whom?" Does this mean the manifestation to be bound to a virtual contract is effective when received in the recipient's e-mail box at its local ISP? Or must the e-mail be actually delivered by his or her ISP to the recipient's own personal computer?

"Receipt" is defined in proposed § 2B-102 as taking delivery of information by a system that the recipient has designated for the purpose of receiving records. Furthermore, "delivery" is defined as the transfer of communication to a bailee such as an ISP. These definitions would seem to set up the presumption that delivery to, or receipt by the ISP alone renders an acceptance effective. The ALI does not address the obvious opportunity for the targeted e-mail recipient to avoid receipt by deliberately staying off-line and failing to call for delivery of its e-mail from its ISP. In such a scenario, the proposed recipient could dispatch a withdrawal of its prior offer and cut off the possibility of timely acceptance, simply by neglecting to retrieve its e-mail, even after word of acceptance has been sent.

## Perfect Tender Rule Rejected

Under UCC Article 2 dealing with transactions in goods, even minor defects may allow the rejection of a tender of performance. Under proposed Article 2B, however, the ALI acknowledges the fact that, in theory, all software, whether downloaded over the Internet or sold as magnetic disks, contains "bugs" or potential performance problems. The licensee's duty to pay for the software, therefore, is contingent on the absence of an uncured material breach. Proposed § 2B-108, defines "material breach" as a breach that causes or may cause substantial harm to the aggrieved party including imposing costs that significantly exceed the contract value, or causes the licensee to be substantially deprived of the benefit it reasonably expected under the contract. Article 2B also accounts for the possibility of the cumulative effect of several non-material breaches rising to the level of materiality. Accordingly, a minor defect or "bug" in over-the-counter or Internet downloaded software is not grounds for rejection.

## Anti-Virus Warranties; Disclaimer Double Standard

The proliferation of cyber-vandalism by the unwanted delivery of corrupt data to Internet users can cause serious damage to a computer system and business information. The delivery of "virus" infected software to customers through the Internet has therefore given rise to a duty of the software provider to protect against such injury. Proposed § 2B-313 defines a "virus" as a computer instruction intended to disrupt, damage, destroy or interfere with use of a communications facility or computer without the consent or permission of the owner. Proposed § 2B-313 applies a double standard of warranty against on-line delivery of virus-infected software as between consumers in receipt of a "mass-market" license on the one hand, and merchants on the other hand. Generally, a "mass-market" transaction is a transaction in the retail market directed to the general public as a whole, and involves a software end-user of non-customize software. These would include, for example, widely published business applications, games and utilities.

A software licensor is held to a standard of reasonable care to ensure that its products do not contain undisclosed viruses. A licensor may, however, disclaim all liability to non-consumers only, with language stating that "no action was taken to ensure exclusion of a virus," or that a "risk exists that viruses have not been excluded." In the case of consumer transactions, the reasonable care obligation cannot be avoided by a merchant simply by inclusion of disclaimer language.

## Conclusion

The ALI's ambitious undertaking of revising the Law Merchant to accommodate Internet transactions is necessary and laudable. Proposed Article 2B will remove "virtual contracts" from the traditional legal paradigm applied to goods and services, while maintaining the basic structure of the UCC. The ALI's most current version of proposed Article 2B was published on September 25, 1997. Although completion was originally expected in 1996, challenges to prior drafts by Ralph Nader and Citibank addressing consumer and electronic banking issues have slowed the finalization process. Now is the time for interested parties to voice policy concerns regarding Internet transactions before the ALI concludes. Prior and most

current drafts of proposed UCC Article 2B may be viewed and downloaded from the Internet at <http://www.law.upenn.edu/library/ulc/ucc2>.