

# ALERT

TECHNOLOGY / LONDON OFFICE

November 1999 Number 4

## Software Licensing – Changes in U.S. Laws may Affect U.K. Practice

A recent law in the United States may soon begin to affect the way in which software is licensed and distributed in the rest of the world. The Uniform Computer Information Transactions Act ("UCITA") introduces significant protections for software owners. Given the fact that much of the world's software is either owned or licensed by United States companies, or is distributed in the U.S., the effect of UCITA may be to change the terms under which all software - whether or not owned and licensed by a U.S. company - is licensed.

### What is UCITA?

UCITA is based on Article 2(b) of the Uniform Commercial Code - the U.S. equivalent of the UK Sale of Goods Act. UCC Article 2(b) deals primarily with the sale of tangible goods. UCITA is intended to cover the licensing of intangible goods such as information and software which, at the moment, is dealt with under a range of disparate state laws.

It is important to realise that UCITA is a uniform code. It is not itself legally binding in any state until that state has formally adopted UCITA into its laws. Companies located in a particular state - or companies selling software in a particular state - will only be affected as and when that state's legislature has approved and adopted UCITA. Obviously, adoption in key states such as New York and California will heavily influence the practice of major national software vendors. If adopted across the entire country, UCITA will provide a large degree of uniformity in software licensing laws in the United States. UCITA was approved by the national body responsible for generating it on 30 July 1999. U.S. state legislatures are expected to implement the Act in states across the U.S. over the next 12 months.

Although the bill initially faced strong opposition from many of the states (a total of 25 state attorneys general opposed the bill), it was eventually passed in a vote of 43 to 6, with 2 states abstaining. UCITA was primarily backed by software publishers, and was widely opposed by software developers, consumer advocacy organisations, software buyers,

librarians and newspaper and magazine publishers. The American Computer Society, America's premier IT professional body, came out strongly against the bill, as did the U.S. Federal Trade Commission which considers it to be an unnecessary risk for consumers engaging in e-commerce.

### Key Provisions

UCITA will introduce into U.S. law a range of rights and restrictions that are alien to English contract law. These include:

- the express right for software owners to disable their software remotely (e.g., by using "time bombs") if they believe that a breach of contract has occurred;
- the ability for software owners legally to disclaim their statutorily implied warranty to sell products that function properly;
- the right for software owners to prevent the transfer of software sold under "shrink-wrap" or "click-wrap" licences;
- a provision in UCITA allows software owners to enforce "shrink-wrap" or "click-wrap" licences as soon as a user unwraps a piece of software or clicks the "I accept" button - regardless of whether the terms have been read.

Perhaps not surprisingly, UCITA has been heavily influenced by the strong U.S. software vendor lobby. The Consumer's Union in the U.S. opposes UCITA because it believes that the Act authorises software owners to use and enforce unfair contract terms and practices. Some software user organisations have proclaimed UCITA a "parade of horrors". They say it marks a shift away from policies to protect software transfer, competition and innovation. Large software customers have voiced their opinion firmly against the ability of vendors, under UCITA, to shut down user software remotely, without a court order. Several large corporations are believed to have rejected shrink-wrap products based purely on their licensing terms, due to the spectre of UCITA.

## Application of the Act in the UK

UCITA's broad scope, covering all "information transactions", means that its potentially harmful reach extends beyond software licensing. It includes access to databases, electronic works such as books as well as compiled information - all of which are the bedrock of e-commerce.

UCITA will apply in all cases where the law of any U.S. state applies (obviously, only if that state has adopted UCITA) if the contract between an owner and a licensee is silent on any point covered by the Act. So, although contracts can be negotiated to exclude the UCITA-approved provisions (by expressly stating provisions to the contrary), if the contract is silent UCITA will apply as a matter of course.

Any users of U.S.-source software are potentially at risk. This is particularly the case in transatlantic deals where either English or U.S. law could potentially apply, and in e-commerce transactions when customers generally pay less attention to terms and conditions because they believe that there is little or no chance of negotiating with a vendor to deviate from their standard term contracts.

## Costs to Customers and Vendors

The cost of enforcing the new law and educating users is likely to be significant.

The provisions setting out the scope of the Act, limitations on enforceability and the ability to override or exclude operation of the Act are complex and little guidance has been given on how they might apply. UCITA will, therefore, increase procurement costs as lawyers will need to be engaged to scrutinise shrink-wrap licenses bought on a large scale as well as bespoke arrangements.

Some pundits argue that legal uniformity and certainty is necessary for e-commerce to prosper, and UCITA promotes neither. To start with, it establishes a bargaining position favoring the licensor, which is contrary to concerted efforts in most jurisdictions to enhance protection for consumers in electronic transactions. It also leaves many questions unanswered: for example, it is stated to apply to "computer information transactions", but it is not altogether clear what this means.

The Act creates further uncertainty because although its scope at first appears to be wide, there are actually several common types of e-commerce

transactions that are specifically excluded. These include financial services transactions and contracts dealing with audio or visual programming, motion pictures, sound recordings, musical works. The inconsistent treatment of these transactions may impact heavily on the finance and entertainment industries that are currently investing millions in the burgeoning push to make their products 'go digital'.

## Recommendations

In order to be certain to avoid the application of UCITA, software licensees should ensure that contracts are concluded under English law. This may be easier in a negotiated deal between parties that are familiar with multinational transactions. It will be more difficult where standard form contracts are used without being amended, or where transactions are concluded via the Internet using standard form or shrink-wrap style licences.

In bespoke agreements that must be governed by a U.S. state law, the parties must expressly state that certain clauses are at variance to UCITA. For example, a contract may say: "Notwithstanding any contrary provision in UCITA or any other law or regulation governing software licensing or other computer information transactions, the parties agree ..".

Software owners in the UK who licence their software in the United States need to be aware of the effects of UCITA and, potentially, to take its provisions into account in their contracts. They should also consider the use of remote disablement devices in their software distributed in the U.S. since, presumably, the use of such devices may become more common in the light of UCITA.

## About Shaw Pittman

Shaw Pittman's technology group advises on all types of software and e-commerce licensing contracts. Lawyers in the firm's London office have represented both customers and suppliers in many such contracts and regularly advise on the issues raised by this Alert. For further details about Shaw Pittman's expertise in relation to licensing contracts, or in relation to the issues covered in this Alert, please contact Margaret Harvey (020.7337.9463) or Anita Smith (020.7337.9469).

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