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February 5, 2003

Members of the House of Delegates
American Bar Association

Re: Uniform Computer Information Transactions Act

Dear Delegate:

I am currently the chair of the Computer Law Section of the Delaware State Bar Association (“DSBA”), and I also served as the chair of a Joint Task Force of the DSBA to study UCITA when it was first promulgated in 1999. After months of study, the Joint Task Force recommended passage of UCITA in Delaware as a significant improvement over existing law by providing predictable and reasonable rules for transactions that are critically important to our economy. The Executive Committee of the DSBA reviewed our report and officially endorsed UCITA. Attached is a copy of the report issued by the Joint Task Force on January 5, 2000.

Since the date of our report, the drafters of UCITA have continued discussions with UCITA’s opponents, and have introduced amendments to UCITA in an attempt to meet the critics’ concerns. While these amendments have not been necessary in my view, they have served the beneficial function of making UCITA more widely acceptable,¹ and, more importantly, they have not detracted from UCITA’s principal value. UCITA clarifies and codifies existing law and practices in the area of information licensing, creating a framework for these transactions in the same way that UCC Article 2 created a framework for the sale of goods.

As a member and later vice-chair of the Business Law Section’s Subcommittee on Information Licensing, the only BLS subcommittee focusing on the substance of UCITA, I attended numerous UCITA drafting committee meetings, and heard many of the same arguments in those meetings that now are being presented to the ABA House of Delegates. All of these arguments were considered in depth by the drafting committee, and I doubt they will ever be resolved; however, this kind of debate takes place every time there is a fundamental shift in our

¹ For example, by amendment, UCITA now prohibits the licensor’s use of electronic self-help. Today, there is no restriction over a software manufacturer’s right electronically to repossess software on a licensee’s computer. UCITA as originally drafted had provided significant restrictions to that right, protecting licensees of software.

economy that necessitates a shift in law. Karl Lewellyn wrote UCC Article 2 because an economy of manufactured goods was being run on laws written for “horses and haystacks.” The UCC faced the same resistance and the same prospect of non-uniform enactment (which prospect was realized as states did enact it non-uniformly). Today, we have transitioned to an information economy. Therefore, instead of attacking UCITA and trying to pretend existing law works, we should commend those who had the foresight to see that the paradigm was shifting and to draft law to deal with it.

Instead, issues that were endlessly debated and positions that were not adopted for good policy reasons are being repeated for the House of Delegates. A recent iteration is a letter dated January 27, 2003 from The Association of Life Insurance Counsel (ALIC). It is an example of why this process has been frustrating: it is not wholly inaccurate but it leaves so much unsaid that it does not create a fair reflection of UCITA or existing law or considered policy choices. For example:

1. It implies that all software publishers are massive conglomerates dealing with sympathetically small and defenseless customers. However, in 1999, 64.5% of software companies had only 1 to 15 employees, with 22% of that percentage being companies comprised of 1 to 2 employees. The picture created by ALIC does not reflect reality.

It is true that insurance companies use software and often rely on one vendor for unique software, such as a product to automate assessment of reimbursement requests from doctors. The software developer retained to write such a program is likely much smaller than its customer insurance company and the bargaining leverage is with the insurance company licensee, not the software licensor. Even if that were not so, a tenet of U.S. commercial contract law is that parties are deemed equal – they are allowed to allocate risks among themselves. Contract law does not purport to resolve the difference except as reflected in special, regulatory statutes such as consumer protection laws and franchise acts. ALIC gives itself too little credit – most commercial lawyers would not lose sleep worrying whether life insurance companies are able to protect themselves in the tides of contract law. ALIC also knows that anti-trust laws continue to apply in addition to contract law, including UCITA.

2. ALIC claims that “delayed boilerplate” should always be available to customers when they make acquisition decisions. However, at the web site of Pacific Life Insurance Company, the employer of the President of ALIC (at least according to a Google search), there were descriptions of products available to buy, all subject to contract terms (according to the Prospectus, which only purported to summarize the terms). But the terms of those contracts were not available to review until after an order for an annuity or other product was placed.

It is no answer to pretend that all of the Contract terms and language are regulated and, therefore, that insurance companies are completely different from the numerous industries that use “delayed boilerplate” distribution channels. The insurance industry is competitive, including as to policy language which has sufficient variance among companies to have created a

wealth of case law interpreting the actual insurance contract. Insurance commissioners review policies and do require some terms, but they do not, typically, write the policies or dictate every clause or its wording. As the Pacific Life prospectus says, it is important to read the actual contract.

Further, insurance companies or their affiliates do not confine themselves to one type of contract. In fact, and as explained by the Seventh Circuit,² the insurance industry exemplifies the “delayed boilerplate” distribution channel, yet ALIC argues for its elimination for computer information industries, while retaining it for their contracts, including credit card contracts. There is nothing wrong with the pay-now, terms-later channel: it allows distribution of sophisticated products by efficient means and is used by many industries. Protections are in order, however, and UCITA provides them. Under UCITA I would be entitled to get my money back if I did not like the Pacific Life Contract terms once I order my annuity and the Contract is finally delivered. I doubt insurance law requires that. Under UCITA I would be entitled to see contract terms before agreeing to them; yet NCCUSL has been provided with examples of insurance credit card products requiring customers to agree to the credit card contract before they ever see it.

3. ALIC states that the ABA Working Group feared “coffee pots, blood pressure monitors, or even automobiles” would be subject to UCITA. The ABA Working Group did not fear that because it read UCITA. UCITA clearly provides that the coffee pot, the car and the monitor, i.e., the good, are never part of UCITA. The only “scope” debate has been over how appropriately to treat any software such as licensed software that is in and provides aspects of a magnetic resonance imaging machine. Yes, some contend that law designed to cover the rollers and the bed, or even the large plastic casing, is completely adequate for the software. The ABA Working Group did not pretend that and neither does UCITA. The ABA Working Group did suggest a way to handle that software, but the suggestion did not solve or address the many, many issues that were detailed and debated in the public hearings regarding UCC Article 2 or UCITA. So it is quite understandable that the suggestion was not adopted. It was not adopted for UCC Article 2 either.

4. ALIC exemplifies a classic pattern in the UCITA debate: it criticizes UCITA for something it does not do and then requests a result that is, in fact, already provided by UCITA. ALIC portrays a circumstance where independent automobile repair services “become subject to a UCITA-like prohibition on reverse engineering.” This is simply an

² See *ProCD, Inc. v. Zeidenberg*, 86 F3d 1447, 1451 (7th Cir. 1996):

Transactions in which the exchange of money precedes the communication of detailed terms are common. Consider the purchase of insurance. The buyer goes to an agent, who explains the essentials (amount of coverage, number of years) and remits the premium to the home office, which sends back a policy. On the district judge's understanding, the terms of the policy are irrelevant because the insured paid before receiving them. Yet the device of payment, often with a "binder" (so that the insurance takes effect immediately even though the home office reserves the right to withdraw coverage later), in advance of the policy, serves buyers' interests by accelerating effectiveness and reducing transactions costs.

incredible statement. UCITA has no provision “prohibiting” reverse engineering. None. Period.

The 1999 version of UCITA³ (the version enacted in Maryland and Virginia) allows a court to refuse enforcement of a contract term that violates a fundamental public policy, and Official Comment No. 3 strongly suggests that a term prohibiting reverse engineering for interoperability would be an ideal candidate for such invalidation. The 2002 version of UCITA goes further to do what ALIC wants but still criticizes: Section 118 invalidates a contract term that prohibits reverse engineering for interoperability, and also allows continued use of the fundamental public policy section in case more is appropriate. Indeed current law allows contracts to prevent reverse engineering while UCITA prohibits such contracts. That was confirmed as recently as January 29, 2003 by the Court of Appeals for the Federal Circuit.⁴ While one can fairly criticize UCITA for inappropriately giving ALIC what it wants, clearly it is nonsensical for ALIC to do so.

5. ALIC criticizes UCITA for failing to require computer information licensors to “permit the transferability of licenses, even in the case of a sale, merger, or acquisition.” When ALIC or its affiliates seek amendment of state insurance statutes to require the same thing as to all insurance policies, that demand will have some credibility. Currently, most state insurance statutes allow insurers to make their policies nontransferable for any reason, including mergers and acquisitions. The irony here is twofold. Not only do ALIC members have statutory protection that they seek to deny to others, but ALIC asks NCCUSL to do this despite federal law that says NCCUSL (actually, states), may not do so. Under a line of patent and copyright cases, non-exclusive licenses may not be transferred without the consent of the licensor. Just as there are good policy reasons to allow insurance companies to make their policies non-transferable, so are there good policy reasons for this federal rule for licenses.⁵

ALIC worries about two law firms that merge but cannot transfer their licenses to the successor: federal intellectual property law dictates that exact result and UCITA cannot rewrite federal law. Indeed, while ALIC ignores this, UCITA provides that, except as mandated by other law, licenses are presumptively transferable unless the transfer would materially harm the interests of the other party. UCITA also honors contracts prohibiting transfers and ALIC’s contracts are afforded that same treatment by insurance laws. Commercial lawyers know that reviewing leases, loans, insurance policies and licenses are a primary component of standard due diligence in mergers and acquisitions.

The other claims made by ALIC and similar claims made by the Society for Information Management, AFFECT and other opponents are addressed in various of the

³ Section 105(b)(1999).

⁴ *Bowers v. Baystate Technologies, Inc.*, -- F.3d -- (Fed Cir., 2003), original opinion entered August 20, 2002, *Bowers v. Baystate Technologies, Inc.*, 302 F.3d 1334 (Fed. Cir. 2002).

⁵ See e.g., *Everex Sys., Inc v. Cadtrak Corp.* (In re CFLC, Inc.), 89 F.3d 673 (1996).

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materials prepared by NCCUSL, Professor Raymond T. Nimmer, Professor Richard Epstein and numerous other respected academics and ABA members, so I will not address them. Those materials can be reviewed at http://www.nccusl.org/nccusl/ucita/UCITA_Standby_Comm.htm.

I do agree with one comment implied by ALIC, however, and that is that no law should be unreasonable or favor the position of only one party. UCITA is not such a law. But such a law will be created if the suggestions made by ALIC, AFFECT, SIM and others are adopted.

UCITA would be good for our information economy, in that it would create a legal environment, in which both licensors and licensees of information could transact business efficiently and at lower cost. I have not heard or read anything in the past three years that in my opinion would change the Delaware State Bar Association's support for UCITA.

Respectfully,

William R. Denny

Enclosure

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