Report on the Uniform Computer Information Transactions Act

Alvin C. Harrell, Oklahoma City University School of Law
Charles Cheatham, et al.

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Report on the Uniform Computer Information Transactions Act (UCITA)

By Charles Cheatham, Peter Dillon, Paul Foster, Albert J. Givray, Sarah E. Hansel, Alvin C. Harrell, Tom Holland, Neal R. Kennedy, Robert Luttrell, D. Kent Meyers, Fred H. Miller, Donald A. Pape, Ross Plourde, and Tamara Wagman

I. Introduction and Background

As a result of the decision of the Executive Committee of the National Conference of Commissioners on Uniform State Laws (NCCUSL) in July, 1995 to separate the licensing of computer information from the law dealing with transactions in goods due to a growing appreciation of the differences in transactions and practices, a separate drafting committee was appointed to develop an Article of the Uniform Commercial Code (UCC) dealing with computer information transactions, which was designated UCC Article 2B.

The Article 2B Drafting Committee held its first meeting in January, 1996 and subsequently held many additional meetings. In addition, the Chair and Reporter met with NCCUSL's Committee on Style and the UCC Article 1 Drafting Committee, which was revising that Article. There also were special harmonization meetings to make sure provisions borrowed from UCC Article 2, which itself was in the process of amendment, were not inconsistent, except as required by the differences in transactions and practice. There were meetings with a wide range of interested groups to review provisions of various interim drafts. More than 60 organizations and other interested groups were represented at drafting committee meetings. A draft of proposed Article 2B was considered at length at the NCCUSL 1997 and 1998 Annual Meetings.

Notwithstanding all of this, the draft still remained controversial. Much of the controversy stemmed from the fact that the draft dealt with many issues about which there was no settled law. While this fact, and the accelerating pace of widely diverse legislation and case law results in response, demonstrated a need for a product like the draft, it also demonstrated that the provisions of the draft were quite different from the provisions of the UCC which, in the main, codified and refined developed law. Accordingly, and anticipating that further debate at the drafting stage would produce little gain but that further debate during the actual enactment process was likely to and could produce significant non-uniform amendments representing acceptable political compromises, a decision was made to remove the act from the UCC and continue it as the Uniform Computer Information Transactions Act (UCITA or the Act).

The same reasoning that led to the removal of UCITA from the UCC led to its promulgation by NCCUSL in 2000, even though consensus had not been reached on a number of issues. Even so, UCITA was rapidly enacted in Virginia and Maryland, as these states perceived the obvious economic benefit from embracing clear legal rules for an area of the economy that already was overshadowing others in economic consequence.

The enactment efforts in Virginia and Maryland did produce some of the anticipated significant non-uniform amendments to the versions of UCITA passed in those states. Moreover, the accompanying debates disclosed areas of controversy where official adjustments to the uniform act not only might improve it substantively but might make it more acceptable to various organizations and interest groups. Accordingly, the standing committee reviewed the situation and came up with a number of proposals. It then convened a meeting in the fall of 2001 in Washington, D.C., to which its previous American Bar Association advisors and representatives of the organizations and other interested groups who

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1. Originally, UCITA was described as a "spike" in the UCC, which would leave the Article 2 provisions on sales of goods as another spike.

2. The balance of this report reemerges to add a note by Fred H. Miller, Alvin C. Harrell, Charles Cheatham, Paul Foster, Robert Luttrell, D. Kent Meyers, Donald A. Pape, and Ross Plourde describing developments subsequent to the redrafting of Article 2B to UCITA, including UCITA amendments through 2002. It also updates the original Oklahoma report and abbreviates it to some extent. This revised report, except for some changes but also because of the review by others of the original Oklahoma report and by other members of the Subcommitte, is as follows:

3. See UCITA, Prefatory Note.

4. In the NCCUSL process, the drafting committee, once its draft is promulgated by NCCUSL, consists on an ongoing basis of those who drafted and revised the draft and who were involved in its enactment, so that the final adoption of the act in a particular state must itself be understood in that context (Continued from previous columns)


(Continued in next column)
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had participated in the drafting process were invited, to gather comment on the proposals and to consider any additional proposals that might seem to have merit.

Meanwhile, on the side, the Committee of the American Bar Association (ABA) that for some reason had not directly participated in the drafting of the Act, under the chairmanship of the ABA appointed a task force, a sort of long-standing arrangement between the AIA and NCCUSL, with the drafting committee from the beginning, and had both been on the advisory panel's side of the debate and had transferred to the drafting the reactions of such parts of the AIA as had taken the time to respond to that. The next working group was invited and did attend the 201 Washington meeting, and thereafter prepared a report with a dozen.

The Standing Committee took the information and recommendations prepared under consideration and after extensive discussion, including the work of a subcommittee whose sole focus was to make recommendations for improvement in the "clarity" of the Act, proposed thirty-eight amendments to the Act. A number were only "style," but were designed to address the "clarity" objection to the Act, but a number also were quite substantive. At its annual meeting in 2002, NCCUSL adopted all of the amendments. Thus, at the time the Act was once again UCITA was proposed for adoption by the states in the 2003 legislative sessions.

II. Computer Information Transactions: Scope of UCITA, Other Law, and Controls on Contracts

The scope of UCITA encompasses computer information transactions. At its core, UCITA basically applies to the licensing of "computer information," or its creation, modification or transfer. It applies to support agreements. This is a broad scope. However, there are specific limitations and exclusions. UCITA Article 9 controls over UCITA in the event of conflict when the computer information is collateral: Article 2 or 2A may apply to the goods in a transaction including computer information and goods, and UCITA does not apply to the subject matter of UCC Articles 3 through 8.12

Section 103 of UCITA further clarifies that the Act is not applicable to a variety of contracts, or other agreements. It is the dominant characteristic of which is to create or obtain rights to create a motion picture, or an agreement to create, perform in, or in other ways related to a motion picture or audio or visual recording, a sound recording, musical work, non-fictional work for hire, a service of a professional services or insurance services transactions; or a compulsory license; an employee contract; a contract where the computer information is insignificant or not required; or to a transaction involving regulated telecommunications services or products. Nor does UCITA apply to sales or leases of goods; cash exchanges of information; computers, televisions, VCR's, CD players, or similar goods; or contracts for prints, books, magazines, or newspapers.

Transactions involving trademarks, trade names, trade dress, patents, copyrights, or other intellectual property rights are not within the scope of UCITA, nor is any transaction of goods in the course of law.7

We are not dealing with a simple contract, but a statute, and a statute's foreknowledge and purpose are not to be overlooked in determining the scope. The purpose of UCITA is a vast one, and it is not simply to regulate and enforce agreements in the marketplace, but to control and enforce agreements electronically. Recognizing that, the purpose of UCITA is "to achieve the objects set forth" in the Act, the Act is not limited to the transactions and agreements that it regulates, but is to be understood as having a broader purpose.

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or performance, or otherwise the later terms should be considered as proposals for modification of an existing contract. The fact is mandating all significant terms "upfront" is neither feasible in all cases, nor necessarily good policy. It is not required in a number of other contexts, and most courts under current law enforce contract terms that are presented and asserted to be after initial agreement under circumstances required by UCTA. Further, UCTA provides even more protection on this issue than current law, e.g., in section 209 for a mass market transaction and in section 114 for internet transactions.

UCTA section 115 provides that, except as otherwise provided in UCTA, the parties to an agreement may change the effect of the rules of UCTA. Eleven "mandatory" rules are listed, which unenforceable rules include restrictions on choice of law agreements, agreed choice of forum, requirements for manifesting assent and opportunity to review, limitations on enforceability against mass market licensees, the consumer electronic defense, and various other provisions including the limitations on self-help possession, in addition to remedies for unscrutability and the controls of fundamental public policy, good faith and due care.

UCTA section 116 contains a proviso like UCC revised section 1-204(b), which allows UCTA to be supplemented by another applicable law, but is more specific on what other law is not displaced, and imposes a general obligation of good faith.

III. Contract Formation, Terms, Construction and Interpretation

UCTA rather closely follows UCC Article 2 in incorporating provisions dealing with the formation of a contract for computer information. There is a statute of frauds, and the rules on formation are similar except as updated for electronic commerce. In addition, there is a special rule on releases, and elaboration on rules on attribution and electronic errors. UCTA also follows UCC Article 2 in other respects, including a para evidence rule, and rules on modifications or rescission. By the same token, where the nature of a computer information transaction requires a different or additional rule as compared to a sale or lease of goods, UCTA supplies the rule. For example, section 304 provides for continuing initial contract terms for successive performances, an issue not dealt with explicitly in either UCC Article 2 or Article 2A (on leases of goods).

By the UCTA provisions to those in UCC Articles 2 and 2A in this context, UCTA, like those UCC provisions:

- contains a para evidence rule;
- has a provision on course of performance;
- has a provision on modification and rescission; and
- provides gap fillers where performance standards are left open.

However, UCTA also has additional provisions peculiar to the type of transaction subject to UCTA, as follows:

- UCTA sets out what a license grants about more specific terms in it;
- UCTA and suppliers for assessment of performance to a party's satisfaction.

Enactment of UCTA would clarify the law of most states to these matters in particular, since, absent UCTA, statutory law and (little) significant case law relating to computer information transactions except some rules of questionable application borrowed from UCC Article 2.

1. To the extent that general statutes are applicable to these transactions, such as the provisions on contracts in the

Oklahoma statutes, those more general provisions would be superseded by the special computer provisions in UCTA in the same manner that similar provisions in UCC Articles 2 and 2A superseded such provisions.

IV. Viruses and Warranties

The warranty structure of UCTA in many ways resembles that for goods contained in UCC Article 2. However, there are adjustments to reflect the differences in the transactions and practice. For example, disclaimers and limitations of remedy are allowed, and there are rules similar to those of Article 2 concerning causation, explanation, and privacy.

One major debate during the development of UCTA was responsibility for a virus. A virus is any instruction to a computer that materially damages, destroys, or infects information, or is inappropriately interacts with the use of a computer or communications facility, without the consent or permission of the owner and in a manner otherwise unauthorized.

A vendor of software who distributes disks is most likely the source of a virus. This is obvious but not necessarily the only way viruses get introduced. It is more frequent for licensees to introduce viruses in their provided on-line systems, or for licensees to inject viruses when accessing on-line systems, or for third-party strangers to introduce a virus. Viruses introduced into distributed software products and data on diskettes or in a computer are yet another source of viruses. Criminal law makes a virus a very liable offense, for knowledge (though not negligently introducing a harmful code or virus into the computer system of another person. For the contractual situation, there is virtually no case law yet on how to allocate risk for viruses. Absent UCTA, the implied merchantability warranty in UCC article 2-314 would probably be applied in some cases. In that context, courts would probably ask two questions:

- Does the 'extraneous code' fall within normal expectations regarding the particular type of software or features, or is it by analogy to cases dealing with food products?
- Was an implied warranty disclaimer? Implied warranties generally can be disclaimed by specific formulations.

Arguably, this would be an example of an inappropriate application of a rule formulated for a different context. As UCTA does not directly address the virus issue because the law is not sufficiently developed to codify and the circumstances perhaps too diverse to make any codification feasible. Thus, UCTA leaves the matter to case law development. Licensees (and perhaps licensees) nonetheless may be well advised to consider that a court could create a warranty. If so, such a warranty probably could be overridden by contract.

As UCTA as well as UCC Article 2 allows warranties to be disclaimed. Under UCTA, generally warranties may be disclaimed by words like "as is;" and a disclaimer is also disclaimable by specific language, but to be effective the language must be conspicuous. UCTA also provides that a disclaimer good under Article 2 or Article 2A is good for Article 2B. If the disclaimer is blocked by some consumer law, nothing in UCTA (or Article 2 or 2A) would interfere with such a block.

Absent UCTA and if a court does not apply Article 2 (and the difference between the Article 2 and UCTA rules in this area suggest Article 2 should be applied), a software developer providing development services is probably under the common law rules of reasonable and workmanlike care in performance of services. But this standard has never been litigated for a virus, and the rules on disclaiming this UCTA would probably apply without authorization.

Some factors to consider are:

- Is there a high rate of new viruses being found? Reasonable testing will suffice even if one or more viruses slip through.

- May it depend on whether it is IBM scanning viruses in major software that IBM licenses from a third party and then passes on to a licensee or to others in the market, or a consumer scanning a software diskette that the consumer acquired from Crazy Eddie's.

Should the "reasonable care" obligation be satisfied by a simple "I didn't check for viruses" warning? It would not seem appropriate in a mass-market transaction where a mass-market license involves delivery of a copy on a tangible medium like a diskette, where the user might claim the license is defective and the mass-market transactions, the licensor should be able to satisfy the "reasonable care" obligation by giving one of two warnings in the contract:

1. See, e.g., 80.104 (Officer of Board of Trade and Margarine trade practice) to the effect that "an officer of a board of trade or a trade association or association of dealers dealing in margarine or any other similar goods or materials, acting in his official capacity or as a member of any such board of trade or association or association of dealers, shall be guilty of a breach of the peace if he commits any breach of the peace within the meaning of this section, and the person injured by the breach of the peace may have the right to recover from him any damages sustained, and the court shall, in its discretion, award such damages as shall be found by the jury to be just compensation for such injury."
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1. I took no action to ensure exclusion of viruses.
2. A risk exists that viruses have not been excluded.

Beyond the issue of viruses, the warranty structure of UCITA deserves some discussion since it has been subject to some criticism. The warranty of non-infringement has three parts; the first states that a licensor warrants that no one holds a claim that arose from an act or omission of the licensor that will interfere with the licensee's rights. The licensor's second warranty arises when the licensor grants an exclusive right in information; here the licensor warrants two things -

• that patent rights being transferred are valid and exclusive to the best of the licensor's knowledge; and
• in all other cases the licensed information is valid and exclusive (in other words, no third party has the right to grant a similar license; there are no prior assignees, no joint inventors, and no co-authors in whom might also grant a right that might compete with the rights granted by licensor to licensee). 32

The third warranty is given when the licensor is a merchant who regularly deals in the kind of information involved; here the merchant licensor warrants that the information is delivered free of the right of claim of any third party by way of infringement. Now that this warranty only says that delivery does not infringe the rights of any third party that exist at the time of the delivery; this warranty pertains to the delivery as delivered and it says nothing about the information used. If the licensor issues a warranty that the use that will be made does not infringe, the licensor needs to test this warranty as part of the contract or service performance obligation. The warranty exists whether or not the information is included in or created by a computer. A computer of obligated individual is carefully limited to persons who not only are in the business of providing such information but also in the business of more than that - of providing a relationship of reliance (i.e., on a custom-tailored, not a mass-marketed basis). The focus of this warranty is solely on the accuracy of the process by which the information is provided, not on its aesthetic quality or market appeal, and there is an exclusion for published informational content. The concept is derived from the Restatement (Second) of Torts section 552 and has no UCC antecedent.

UCITA section 405 imposes two further implied warranties. The first of these is that information provided under consulting, data processing, and information content contracts will be fit for the licensor's particular purpose. The class of obligated individuals is comprised of the licensor or its agent, regardless of whether a merchant or not, who at the time of contracting has reason to know of not only such purpose but also the licensor's reliance on the licensor's knowledge as an interest in the development, and furnishing the information. The focus of this warranty is on the quality of the "result" delivered. On the other hand, section 405 requires a performance level of fitness for the licensor's particular purpose whereas section 403 requires fitness for the ordinary, industrial, or trade-accepted purpose. The second of the implied warranties imposed by section 405 is one of system integration. There is an exception for excessive market appeal and published informational content. Finally, except for published informational content, section 409 extends a licensor's liability to those third parties which the licensor must have known and clearly intended to have been effected by the transaction. The possible liability is further broadened in the consumer contract to the immediate family or household of the licensee if the provision reasonably expected that such an individual would rightfully use the information. The loss may be either personal injury or economic loss. A contractual provision excluding or limiting third-party beneficiary claims will be effective unless applied by and at the option of the consumer. Disclaimers or modifications of warranties or remedies which are effective against the licensee are equally effective against third parties. This essentially tracks the UCC Article 2 and 2A rules, depending on the alternative a state may have adopted when Article 2 or 2A was enacted, and the case law interpreting the alternative.

V. Transfers of Interests

Part 5 of UCITA covers issues relating to the ownership and transfer of informational rights in computer software. Section 501 allows the contract to control and, absent agreement, if the contract is silent, the conveyance of ownership that ownership will be transferred as soon as the contract becomes enforceable if the rights are existing and identifying and the licensor acquires an interest in the intellectual property or data processing and furnishing the information. The focus of this warranty is on the quality of the "result" delivered. On the other hand, section 405 requires a performance level of fitness for the licensor's particular purpose whereas section 403 requires fitness for the ordinary, industrial, or trade-accepted purpose. The second of the implied warranties imposed by section 405 is one of system integration. There is an exception for excessive market appeal and published informational content. Finally, except for published informational content, section 409 extends a licensor's liability to those third parties which the licensor must have known and clearly intended to have been effected by the transaction. The possible liability is further broadened in the consumer contract to the immediate family or household of the licensee if the provision reasonably expected that such an individual would rightfully use the information. The loss may be either personal injury or economic loss. A contractual provision excluding or limiting third-party beneficiary claims will be effective unless applied by and at the option of the consumer. Disclaimers or modifications of warranties or remedies which are effective against the licensee are equally effective against third parties. This essentially tracks the UCC Article 2 and 2A rules, depending on the alternative a state may have adopted when Article 2 or 2A was enacted, and the case law interpreting the alternative.

VI. Performance and Remedies

The performance and remedy structure of UCITA is in Part 6 and Part 7 of the Act. The performance provisions, section 601 through 701, UCTA couples the statutory model on UCC Article 2. However, there are special sections to deal with matters particular to the subject matter of UCITA, for example sections 602 (use to enable use), 603 (submissions of information); 604 (immediately completed performance); 605 (electronic regulation of performance through automatic restraints to enforce limitations on the use information, but not as a remedy for breach); 611 (on accounts); 612 (on correction and support contracts) and 613 (on contracts involving publishers, dealers, and end users). Note also that the "perfect tender rule" is modified in UCITA section 619(b) and thus, while refusal and cancellation are allowed, adjustments have been made as called for by the different nature of the transaction. Refusal and cancellation are not permitted for each and every defect, but only where there is an unexcused material breach (defined in section 701) unless a mass-market license is involved, where the "perfect tender rule" is employed as more "consumer friendly." The remedy provisions of UCITA are in sections 801-816. In general, the remedy structure also is modeled after the familiar UCC Article 2 on sales of goods and UCC Article 2A on leases of goods. For example, section 801 provides that an aggrieved party has several remedies provided by statute and contract.

Comparing the UCITA remedies to those in Articles 2 and 2A, UCITA:

• grants a right of cancellation (section 802);
• permits contractual modification of statutory remedies (section 803);
• provides for liquidation of damages (section 804);
• allows for rejection of the goods (section 801).
sets out a statute of limitations (section 805);

- accords a remedy for fraud (section 806);

- provides general damages rules (section 807);

- provides alternative damage remedies for the licensor, akin to either lost profit or the seller's action for the price or a lessor's action for the rent (re-license not being a rational measure given the nature of the subject matter) (section 808);

- provides a damage remedy for the licensee for: (a) for licensor non-performance, in the amount of the contract-market difference (cover being essentially impossible due to the nature of the transaction); and (b) for defective performance, in the amount of the difference in value (section 809);

- allows recoupment (section 810);

- allows specific performance (section 811);

- permits a licensor to complete performance to reduce loss (section 812);

- allows a licensee faced with a breach to continue to use the information under certain conditions (section 813); and

- furnishes remedies to the licensor roughly akin to a right to repossess and, given the nature of the transaction, a right to stop use (sections 814 and 815), but there is no right to electronic self-help for breach (section 816).

VII. Conclusion

Part 9 of UCITA contains provisions on effective date, savings of prior law for vested rights, repeal of inconsistent prior law, and a statement of relation to the federal E-SIGN Act. In our opinion, enactment of UCITA without question would clarify state law since, absent the statute, there is virtually no expressly relevant statutory law, and virtually no case law relating to computer software contracts in relation to performance and remedies. To the extent general state statutes are applicable to these transactions, such as a provision on liquidated damages and the statute of limitations, those more general provisions are less than clear or appropriate in application and would be superseded by the more particular provisions of UCITA in the same manner that similar specific provisions in UCC Articles 2 and 2A superseded more general provisions of law. Also in the opinion of the authors who have followed the development of UCITA, with the adoption of the latest amendments to UCITA, most valid concerns have been addressed. We believe that any remaining objections largely are the result of misunderstanding of what UCITA does or of what the law without UCITA does, or represent a desire for UCITA to do more than it should reasonably do, or to do what it cannot. In short, UCITA is a balanced statute ready for enactment to improve state law, and, if it is not enacted as state law, the need for statutory guidance is acute enough that this area of law is likely to slip into the federal sphere, where not only might the rules be far more regulatory but there would be the added complexity of coordinating new federal law with the underlying state contract law in an already complex area, which would only raise the legal costs associated with the "new commerce," to the benefit of no one.

Nonetheless, opposition to UCITA continues; it failed of enactment in Oklahoma in 2003 without a legislative committee hearing being afforded. In the long run, however, since courts have begun to look to UCITA as the best guidance for shaping the common law in the absence of legislation, its influence may be substantial notwithstanding the opposition to its enactment.

69. Nevertheless, use of computer services without authorization due to breach of the license may constitute a serious crime (see, e.g., 21 Okla. Stat. § 1953), and may subject the user to civil liability. 21 Okla. Stat. § 1955. See generally Paul C. Bello, The Theft and Sales of E-Commerce, 53 Consumer Fin. L. Q. Rep. 259 (1999).


71. For example, some opponents apparently fail to recognize that electronic self-help is not prefaced or regulated in reference to losses of goods and security interests, but is for the subject matter of UCITA. Some oppose UCITA on the ground they now can contract safely without carefully examining licenses, but would be at risk under UCITA, a position that ignores the lack of specific present controls on standard form contracts and that UCITA provides even more explicit protection in this regard.

72. To illustrate, some advocates want UCITA to revise consumer protection laws to define unfair or deceptive practices in electronic commerce rather than stand on those laws unchanged, or desire to have UCITA defer federal intellectual property law, which obviously state law cannot do. See supra notes 22 and 23.

73. See, e.g., Specht v. Nucor Corp., 306 F.3d 17 (2d Cir. 2002).

ARTICLES SOLICITED

The Quarterly Report is seeking submission of manuscripts, for possible publication, on the following subjects: consumer protection and litigation; Truth in Lending and Regulation Z; access to consumer financial services (including fair housing, CRA, and equal credit opportunity); electronic commerce; credit and debit cards; credit insurance; mortgage lending; auto finance; UCC case law and revisions; banking law; debt collection; and bankruptcy. If you would like to contribute to an article or research project, please contact the Editor of the Quarterly Report.

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