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Contractual Liability Of Suppliers Of Defective Software: A Comparison Of The Law Of The United Kingdom And United States

*Stephen E. Blythe**

I. INTRODUCTION

The common law of contracts has its roots in medieval England. Traditional contract law, evolved from the age of feudalism, focused on “hard copy” documents and their authentication. Today, we frequently find ourselves entering into virtual, digital contracts. Instead of signing the written document with a seal, we merely type in our name on the computer screen and click on “I accept.”

Should contract law be changed to accommodate the digital nature of the modern contract and, if so, to what extent should it be changed? A traditionalist may contend that there is no need to completely overhaul contract law because the law pertaining to the basic elements of a contract—offer, acceptance, etc.—is still relevant. Nevertheless, most countries and international organizations have modified their contract law somewhat in order to adjust to the peculiar nuances of virtual, digital agreements.¹ The law of digital contracts is emerging worldwide at a rapid pace. This evolution of contract law is a wholesome and natural phenomenon and is another illustration of the beauty of the law. Contract

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¹ *E.g.*, U.N. GAOR, Comm. on Int'l Trade Law, UNCITRAL Model Law On Electronic Commerce, With Guide To Enactment, G.A. Res. 51/162, U.N. Doc. A/51/628, (1996); Council Directive 2000/31/EC, 2000 O.J. (L 178); Electronic Commerce Act, 2000 (Eng.); UNIF. ELEC. TRANSACTIONS ACT, 7A U.L.A. 20 (Supp. 2000). *See generally* Christopher T. Poggi, *Electronic Commerce Legislation: An Analysis of European and American Approaches to Contract Formation*, 41 VA. J. INT'L L. 224 (2000); Michael Dessent, *Click-Wraps, Browse-Wraps and Cyberlaw: Our Shrinking (Wrap) World*, 25 T. JEFFERSON L. REV. 1 (2002).

law, and the law in general, is never static. Rather, it is always dynamic, responding and adapting to new inventions and occurrences.

Software consists of computer programs which, when written and used properly, will enable the user to accomplish a specific objective. A contract to purchase software is inherently different from contracts to purchase most other items because it is debatable as to whether software is a "good" or a "service." The purchaser of software is often unable to determine whether a defect exists until the software is used; the defect is not easily recognizable or easily ascertained. Software must often be custom-ordered to fit the specifications and objectives of the purchaser; the supplier of the software often does not have an intimate knowledge of what the purchaser really wants to accomplish. Furthermore, the divergence of knowledge between the supplier and the purchaser is often great; the supplier is hired as an expert and is entrusted by the purchaser to provide a set of programs which will hopefully enable the purchaser to realize specific objectives. Indeed, more than in most purchases, the purchaser is at the mercy of the software supplier's ability, expertise, and integrity.

Moreover, software is seldom perfect. Defective software frustrates the purchaser's objectives and may cause the purchaser to incur monetary damages. Business purchasers, government entities, and even private individuals may pursue litigation because of defective software. In the past decade, more and more suppliers of defective software have been sued for damages caused by defects in the software. The United States and the United Kingdom have experienced a significant amount of litigation pertaining to suppliers' liability for defective software. Furthermore, the two nations account for a significant amount of the world's production of software. A comparison of the drawbacks and the benefits of the laws of the two nations for contractual liability for defective software will illustrate how the laws in both nations might be improved. This article compares U.K. and U.S. law pertaining to the following aspects of contractual liability for defective software: (1) reasonableness/unconscionability; (2) express warranties; (3) implied warranties; (4) limitation of remedies; and (5) standard form contracts (including shrink-wrap licenses). Using the results from the comparisons, this article draws conclusions and makes recommendations for changes to the laws of both countries.

II. OVERARCHING CONSIDERATIONS

Among the aspects of contractual liability to be discussed, the distinction between the reasonableness test in the U.K. and the unconscionability doctrine in the U.S. provides the backdrop for many of the differences in the two nations' laws. It is more common for a U.K. court to find a situation unreasonable than it is for a U.S. court to find a situation unconscionable. It takes a more extreme situation to trigger the

unconscionability doctrine than it does to trigger the reasonableness test.

A. United Kingdom: The Reasonableness Test

In the United Kingdom, an unreasonable contract will not be enforced.² The Unfair Contract Terms Act of 1977 (“1977 Act”) requires the court to consider the following factors in making a determination of reasonableness: whether the goods were purchased in a special order by the customer; the relative amount of bargaining power between the parties; the degree of the customer’s understanding of the terms contained in the standard form contract and whether he should have understood them; whether the customer received an inducement to agree to the terms of the contract; and, if the contract limits liability if a specific condition is not complied with, whether it was reasonable at the time of the agreement to expect that compliance with that condition would be practicable.³

B. United States: The Unconscionability Doctrine

In the United States, an unconscionable contract will not be enforced.⁴ The test of unconscionability is whether the contract is so one-sided as to be unconscionable under the circumstances existing at the time the contract was entered into.⁵ The doctrine seeks to prevent one party from using oppression and unfair surprise against the other.⁶

The doctrine does not seek to alter the parties’ relative allocation of risks created by one party’s superior bargaining power;⁷ this is one of the significant differences between the U.K. and U.S. positions. Accordingly, weak negotiating parties in the United Kingdom are better off than their U.S. counterparts.

The Uniform Computer Information Transactions Act (“UCITA”) is a model statute written in an attempt to achieve greater consistency in the laws of the fifty states of the United States.⁸ U.K. law does not have a comparable “computer-specific” statute.⁹ UCITA is applicable to “standard software licenses, contracts for the custom development of computer

² Unfair Contract Terms Act, 1977, c. 50, §§ 2(2)–(3) (Eng.).

³ *Id.* § 112; *Photo Production Ltd. v. Securicor Transport Ltd.*, [1980] A.C. 827, 843 (appeal taken from Eng. C.A.).

⁴ U.C.C. § 2-302(1) (2003).

⁵ *Id.*

⁶ *Id.*

⁷ *Id.*; RESTATEMENT (SECOND) OF CONTRACTS § 211 (1979).

⁸ NAT’L CONFERENCE OF COMM’RS ON UNIF. STATE LAWS, UNIFORM COMPUTER INFORMATION TRANSACTIONS ACT (Proposed Official Draft 1999), available at <http://www.law.upenn.edu/bll/ulc/ucita/citaam99.pdf> [hereinafter UCITA].

⁹ University of Strathclyde School of Law, Glasgow, Scotland (U.K.), Course: Liability in the Information Society, Notes for Theme Two (Software Contracts and Quality), page 23.

programs, licenses to access online databases, website user agreements, and agreements for most Internet-based information.”¹⁰ UCITA section 803(d) states that a disclaimer of consequential damages for personal injury in a consumer contract for software is *prima facie* unconscionable; this provision does not apply, however, to non-consumer contracts.¹¹

III. EXPRESS WARRANTIES

In both countries, if the seller promises to provide a specific result—either in terms of performance of the software, or its suitability to the customer—the existence of an express warranty will be recognized.¹² The promise may have been made within the agreement itself or outside of it.¹³ An important consideration is whether it was reasonable for the buyer of the software to rely on the statements of the supplier.¹⁴ If it is determined that a contract contains an express warranty, the next consideration is whether the warranty has been qualified or disclaimed.¹⁵

A. United Kingdom

1. Categories of Promises: Result vs. Process

The case law often distinguishes result-oriented promises and process-oriented promises.¹⁶ The former pertains to warranties concerning the achievement of positive outcomes for the buyer of the software.¹⁷ The latter pertains to warranties related to how the work is to be done, e.g., the degree of expertise of the personnel assigned to carry out the installation of the software.¹⁸

a. Result-Oriented Promises

A classic example of a case with explicit, result-oriented warranties is *St. Albans City v. International Computers, Ltd.*¹⁹ The city, as the plaintiff,

¹⁰ Sandy T. Wu, Comment, *Uniform Computer Information Transactions Act: Failed to Appease Its Opponents in Light of the Newly Adopted Amendments*, 33 SW. U. L. REV. 307, 308 (2004).

¹¹ UCITA., *supra* note 8, § 803(d).

¹² Jeffrey C. Selman, et al., *Steering the Titanic Clear of the Iceberg: Saving the Sale of Software from the Perils of Warranties*, 31 U.S.F. L. REV. 531, 542 (1997).

¹³ Noriko Kawawa, *Contractual Liability for Defects in Information in Electronic Form*, 8 U. BALT. INTELL. PROP. L.J. 69, 124 (1999).

¹⁴ Unfair Contract Terms Act, 1977, c. 50, §§ 112 (Eng.).

¹⁵ *Id.*

¹⁶ Kawawa, *supra* note 13, at 125.

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *St. Albans City & District Council v. Int'l Computers Ltd.*, [1996] 4 All E.R. 481 (Eng.).

entered into an agreement with defendant software supplier.²⁰ The software was required to be capable of maintaining a reliable database of the names of the city's taxpayers, i.e., it had to be reasonably fit for its intended purpose.²¹ However, the defective software underestimated the number of taxpayers in the community, causing the city to charge each taxpayer less than it should have, resulting in a loss of tax revenues to the city coffers.²² Since the computer program was not fit for its intended purpose, the software provider was held liable for the amount of the lost revenue.²³

b. Process-Oriented Promises

Salvage Association v. Cap Financial Service Ltd. recognized that a supplier's promise to use specially-trained personnel must be kept.²⁴ Cap Financial Service had expressly warranted that each person assigned to the project would exercise skills appropriate to that of a competent person.²⁵ Cap failed to assign sufficiently competent personnel to the project and breached its contract when it failed to deliver a proper computer system and thus, Salvage Association was entitled to termination of the contracts.²⁶

2. Disclaimer Clauses

Disclaimer clauses are often added to contracts by negotiating parties in an attempt to avoid or limit obligations.²⁷ Express warranties are difficult to disclaim, however, if they pertain to the fitness of the software for its intended purpose.²⁸

a. Statutory Controls

Several U.K. statutes limit the effect of disclaimer clauses in software contracts;²⁹ U.S. law has relatively less statutory control over disclaimer clauses. The 1977 Act requires that, where a party is a consumer or relies on the other's written standard terms of business, the contract must satisfy the requirement of reasonableness if it attempts to limit liability for breach

C.A.).

²⁰ *Id.* at 686.

²¹ *Id.* at 691.

²² *Id.* at 686.

²³ *Id.* at 704.

²⁴ *Salvage Association v. Cap Financial Service Ltd.*, [1995] F.S.R. 654.

²⁵ *Id.* at 654.

²⁶ *Id.* at 656.

²⁷ Daniel T. Perlman, Comment, *Who Pays the Price of Computer Software Failure?*, 24 RUTGERS COMPUTER & TECH. L.J. 383, 393 (1998).

²⁸ *Id.* at 389.

²⁹ *E.g.*, Unfair Contract Terms Act, 1977, c. 50, §§ 112 (Eng.).

of contract.³⁰

b. Integration Clauses

The purpose of an integration clause is to invalidate any representations made outside of the written contract.³¹ In *Mackenzie Patten & Co. v. British Olivetti Ltd.*, an integration clause excluded all other liabilities, obligations, warranties, and conditions.³² Applying the reasonableness test, the court held that it was not reasonable to allow the supplier to exclude liability for breach of contract.³³ The reasonableness test trumped the supplier's attempted disclaimer using an integration clause.³⁴

B. United States

American law does not require express warranties to be contained within the "four corners" of the contract; they may be oral.³⁵ Express warranties may be created by any affirmation of fact, a promise, or a description of goods which becomes part of the bargain; this may include affirmations made in brochures or in demonstrations.³⁶

1. Case Law Recognizing Express Warranties

In *USM v. Arthur D. Little Systems, Inc.*, the supplier of a computer system made an express warranty that the system would have no design defects and would have acceptable response time.³⁷ The actual response time, however, was substantially greater than the time promised by the supplier and the express warranty was held to have been breached.³⁸

2. Disclaimer of Express Warranties

a. Relevant Statutes

It is an "uphill battle" to disclaim an express warranty because it is

³⁰ *Id.*

³¹ Perlman, *supra* note 27.

³² *Mackenzie Patten & Co. v. British Olivetti Ltd.*, (Q.B. 11 Jan. 1984) *unreported*, 1 C.L.&P. 92 (1984); 48 M.L.R. 344 (1985).

³³ *Id.*

³⁴ *Id.*

³⁵ U.C.C. § 2-313 (2003). See generally Joel R. Wolfson, *Express Warranties and Published Information Content Under Article 2B: Does the Shoe Fit?*, 16 J. MARSHALL J. COMPUTER & INFO. L. 337 (1997).

³⁶ U.C.C. § 2-313.

³⁷ *USM v. Arthur D. Little Systems, Inc.*, 546 N.E.2d 888, 890 (Mass. App. Ct. 1989).

³⁸ *Id.* at 895.

ordinarily considered to incorporate the “essence of the bargain.”³⁹ Section 2-316 of the Uniform Commercial Code (“UCC”) states that “words or conduct relevant to the creation of an express warranty and words or conduct tending to negate or limit warranty shall be construed whenever reasonable as consistent with each other.”⁴⁰

b. Inconsistency

Inconsistency between the express warranty and the disclaimer clause often leads courts to rule against the applicability of the disclaimer.⁴¹ In *Consolidated Data Terminals v. Applied Digital Data Systems, Inc.*,⁴² the court held that very specific language contained in an express warranty prevailed over a general disclaimer of warranty liability.⁴³ The computer equipment manufacturer made an express warranty in its brochure that the computer terminals would operate at high speed and were reliable.⁴⁴ The court held that the express warranty was breached because the terminals were not high-speed and were unreliable. The disclaimer clause had stated: “There is no warranty, express or implied, other than a ninety-day guarantee covering materials and workmanship.”⁴⁵

c. Integration Clauses

U.S. courts sometimes find that a written contract was not meant to be a complete statement of the terms of the agreement. In these cases, the written contract may be supplemented by the parties’ course of dealing, usage of trade, course of performance, or evidence of consistent additional terms.⁴⁶ Some courts have stated that a written disclaimer clause combined with a written integration clause may be enough to override the existence of an express warranty not based on the writing within the contract.⁴⁷

Before considering anything outside the written contract, the threshold question is whether the parties intended the writing to be the complete statement of their agreement.⁴⁸ All of the documents must be considered by

³⁹ U.C.C. § 2-316.

⁴⁰ *Id.*

⁴¹ *Kawawa*, *supra* note 13, at 133.

⁴² *Consolidated Data Terminals v. Applied Digital Data Systems, Inc.*, 708 F.2d 385 (9th Cir. 1983).

⁴³ *Id.* at 398.

⁴⁴ *Id.* at 388.

⁴⁵ *Id.* at 396.

⁴⁶ U.C.C. § 2-202 (2003).

⁴⁷ *E.g.*, *Jaskey Fin. & Leasing v. Display Data Corp.*, 564 F. Supp. 160, 163 (E.D. Pa. 1983).

⁴⁸ *E.g.*, *L.S. Heath & Son, Inc. v. A.T. & T. Info. Sys., Inc.*, 9 F.3d 561 (7th Cir. 1993).

the court.⁴⁹ In *Sierra Diesel Injection Service v. Burroughs Corp.*, the court determined the validity of the integration clause.⁵⁰ The Burroughs Corporation (“Burroughs”) sent a letter to Sierra Diesel Injection Service (“Sierra”) containing an express warranty regarding computer performance.⁵¹ Sierra was not knowledgeable about computers and relied upon Burroughs’ representations.⁵² The sales contract was on a pre-printed form prepared by the seller and presented to the buyer without negotiations.⁵³ The contract contained an integration clause but the court ruled it was invalid because it was overridden by the express warranty in the letter.⁵⁴

d. Parole Evidence Rule

The parole evidence rule may prevent the admission of any of the supplier’s representations made in a prior agreement or in a contemporaneous oral agreement.⁵⁵ In *Jaskey Finance & Leasing v. Display Data Corp.*, the defendant sold a computer to the plaintiff.⁵⁶ The seller had orally represented in advertisements that the computer and software would only require routine maintenance and was suitable for plaintiff’s type of business.⁵⁷ The written sales contract, however, did not make these representations.⁵⁸ At trial, the court ruled that the oral evidence was inadmissible, holding that admitting the evidence would violate the parole evidence rule.⁵⁹

3. UCITA’s Treatment of Express Warranties

UCITA allows a licensor to create an express warranty to a licensee with an affirmation or a promise which may be part of an advertisement.⁶⁰ Samples, models, or demonstrations may also become the basis of express warranties.⁶¹ Language pertaining to an express warranty and language attempting to disclaim an express warranty must be construed, whenever

⁴⁹ *Id.* at 164.

⁵⁰ *Sierra Diesel Injection Service v. Burroughs Corp.*, 656 F. Supp. 426 (D. Nev. 1987), *aff’d*, 874 F.2d 653 (9th Cir. 1989), *amended by* 890 F.2d 108 (9th Cir. 1989).

⁵¹ *Sierra*, 890 F.2d at 110.

⁵² *Id.* at 111.

⁵³ *Id.* at 112.

⁵⁴ *Id.*

⁵⁵ *Kawawa*, *supra* note 13, at 136.

⁵⁶ *Jaskey*, 564 F. Supp. at 161.

⁵⁷ *Id.* at 163.

⁵⁸ *Id.* at 162.

⁵⁹ *Id.* at 164.

⁶⁰ UCITA, *supra* note 8, § 402.

⁶¹ *Id.* § 402(a)(3).

reasonable, as consistent with each other.⁶²

IV. IMPLIED WARRANTIES

Warranties may be express or implied. Express warranties, as discussed above, are relatively more straightforward and explicit. On the other hand, implied warranties are relatively more subtle and less straightforward. The natural result is that implied warranties are more likely to lead to confusion, misunderstanding, and potential litigation between the parties.

A. United Kingdom

1. Reasonable Care & Skill Required

Section 13 of the Supply of Goods and Services Act of 1982 (“1982 Act”) provides that a business supplying a service must do so “with reasonable care and skill.”⁶³ This is an implied warranty, but it is subject to a reasonableness test. In *Salvage Association*, the court found that the supplier had the obligation to carry out its service with reasonable care and skill.⁶⁴

2. Software Quality Must Be “Satisfactory”

In 1994, the Sales of Goods Act of 1979 and the 1982 Act were amended to require the quality of software provided to be “satisfactory.”⁶⁵ The following factors should be taken into account when determining the quality of goods: fitness for purposes for which the goods are commonly supplied, appearance and finish, freedom from minor defects, safety, and durability.⁶⁶

3. Fitness For Intended Purpose

In *St. Albans City*, the court held that, in the contract, there was an implied term that a software program would be reasonably fit for its intended purpose because the supplier knew of the necessity of the program to achieve a specific function.⁶⁷ In *Saphena Computing Ltd. v. Allied*

⁶² *Id.* § 406(a).

⁶³ Supply of Goods and Services Act, 1982, c. 29, § 13 (1994) (Eng.).

⁶⁴ *Salvage*, [1995] F.S.R. at 655.

⁶⁵ Sale of Goods Act, 1979, c. 54, § 14(2) (1994) (Eng.); Supply of Goods and Services Act, 1982, c. 29, § 4(2) (1994) (Eng.).

⁶⁶ Sale of Goods Act, 1979, c. 54, § 14(2)(b) (1994) (Eng.).

⁶⁷ *St. Albans City*, [1996] 4 All E.R. at 691.

Collection Agencies Ltd.,⁶⁸ the court held that the contracts contained a term of implied fitness for the intended purpose because the buyer had communicated the purpose to the seller.⁶⁹ However, the court also recognized that it is not a breach of warranty *per se* to deliver software with defects; rather, a reasonable period of time must be given to cure the defects.⁷⁰

4. Disclaimer of Implied Warranties

Compared to the United States, the reasonableness test makes it more difficult to exclude implied warranties in the United Kingdom.⁷¹

a. Relevant Statutes

In a sale to a consumer, the implied conformity of goods with a description or sample, or to their quality of fitness for a purpose, cannot be overridden by reference to a disclaimer.⁷² In a sale to a non-consumer, any attempt to override the same implied warranties is subject to the reasonableness test.⁷³

The Sale of Goods Act of 1979 states that an implied obligation can be “negated or varied by express agreement.”⁷⁴ It also states that “an express term does not negative an implied term unless inconsistent with it.”⁷⁵ Likewise, the Supply of Goods and Services Act of 1982 allows an implied term to be overridden or changed by express agreement.⁷⁶

b. Inconsistency

In *Salvage Association*, the court ruled that the seller had successfully disclaimed implied terms of merchantability and fitness for purpose, but not the implied term pertaining to reasonable care and skill.⁷⁷ The court found that the latter term was not inconsistent with the express terms in the contract to carry out the service with reasonable care and skill.⁷⁸

⁶⁸ *Saphena Computing Ltd. v. Allied Collection Agencies Ltd.*, [1995] F.S.R. 616 (Eng. C.A. 1988).

⁶⁹ *Id.* at 650.

⁷⁰ *Id.* at 652.

⁷¹ Unfair Contract Terms Act, 1977, c. 50, § 6(3) (Eng.).

⁷² *Id.* § 6(2).

⁷³ *Id.* § 6(3).

⁷⁴ Sale of Goods Act, 1979, c. 54, § 14(2) (1994) (Eng.).

⁷⁵ *Id.* § 55(2).

⁷⁶ Supply of Goods and Services Act, 1982, c. 29, § 16(1) (1994) (Eng.).

⁷⁷ *Salvage*, [1995] F.S.R. at 657.

⁷⁸ *Id.*

B. United States

1. Implied Warranty of Merchantability

If a seller is a merchant in goods of a particular kind, there is a mandatory implied warranty of merchantability.⁷⁹ The UCC establishes standards for determining whether goods are merchantable; for example, if the goods will: 1) pass without objection in the trade; 2) be fit for ordinary purposes; 3) be of a certain kind, quality and quantity per unit; 4) be adequately packaged and labeled; 5) be in conformity with the label's specifications; and 6) as fungible goods, be of fair average quality.⁸⁰ In *Neilson Business Equipment Center v. Monteleone*,⁸¹ the court found an implied warranty that the computer system be "merchantable" and held that the warranty was breached because the computer system was not fit for the ordinary purpose for which it was intended.⁸²

2. Implied Warranty of Fitness for a Particular Purpose

This warranty attaches at the time of sale if the seller has reason to know of any particular purpose intended for the goods and the buyer relies on the seller's expertise to provide suitable goods.⁸³ In *Neilson Business*, the court found such a warranty because the buyer depended on the seller to provide a suitable computer.⁸⁴ This case is comparable to the U.K. cases of *St. Albans City*⁸⁵ and *Saphena Computing*.⁸⁶

3. Exclusion of Implied Warranties

Compared to U.K. law, it is easier for a U.S. seller to disclaim implied warranties because there is no reasonableness test.⁸⁷

a. Relevant Statutes

In order to exclude the implied warranty of merchantability, the UCC mandates that the word "merchantability" must be mentioned, and, if in

⁷⁹ U.C.C. § 2-314 (2003). See generally Robert W. Gomulkiewicz, *The Implied Warranty of Merchantability in Software Contracts: A Warranty No One Dares to Give and How to Change That*, 16 J. MARSHALL J. COMPUTER & INFO L. 393 (1997).

⁸⁰ *Id.*

⁸¹ *Neilson Business Equipment Center v. Monteleone*, 524 A.2d 1172 (Del. 1987).

⁸² *Id.*

⁸³ U.C.C. § 2-315.

⁸⁴ *Neilson*, 524 A.2d at 1173.

⁸⁵ *St. Albans City*, [1996] 4 All E.R. at 691.

⁸⁶ *Saphena*, [1995] F.S.R. at 643.

⁸⁷ Unfair Contract Terms Act, 1977, c. 50, § 6(3) (Eng.).

writing, it must be conspicuous, so that an oral exclusion will be allowed.⁸⁸

Exclusion of an implied warranty of fitness for a particular purpose must be in writing and it must be conspicuous.⁸⁹ The *Jaskey* court found the following clause sufficient to exclude all implied warranties of fitness: "There are no warranties which extend beyond the description on the face hereof."⁹⁰

4. Treatment of Implied Warranties Under the UCITA

UCITA provides that a licensor merchant of a particular kind of software supply a product which is "fit for the ordinary purposes for which such computer programs are used."⁹¹ The software is not required to be completely free of defects, but it must meet average standards for programs having a particular type of use.⁹² UCITA also recognizes an implied warranty of fitness for a particular purpose.⁹³ The requirements for disclaiming warranties are comparable to those of the UCC and facilitate easy disclaimer.⁹⁴

V. LIMITATION OF REMEDIES

There are four methods of limiting remedies: 1) limitation of the situations in which a seller's obligation will be incurred; 2) limitation of the cures to which the buyer is entitled; 3) limitation of the types of damage for which compensation is payable; and 4) limitation of the total amount payable upon breach.⁹⁵

A. United Kingdom

In the United Kingdom, if suppliers attempt to limit damages to a fixed maximum, the court will determine whether that amount is reasonable.⁹⁶ In evaluating the validity of monetary damages, U.K. courts take various factors into account, such as insurance coverage of the parties⁹⁷ and relative degree of bargaining power.⁹⁸ Ordinarily, courts award damages based on

⁸⁸ U.C.C. § 2-316.

⁸⁹ *Id.*

⁹⁰ *Jaskey*, 564 F. Supp. at 162.

⁹¹ UCITA, *supra* note 8, § 403.

⁹² *Id.*

⁹³ *Id.* § 405.

⁹⁴ *Id.* § 406.

⁹⁵ Kawawa, *supra* note 13, at 154.

⁹⁶ Unfair Contract Terms Act, 1977, c. 50, §112 (Eng.).

⁹⁷ *St. Albans City*, [1996] 4 All E.R. at 687-88.

⁹⁸ *Id.*

what was foreseeable when the contract was created.⁹⁹

In *Salvage Association*, the contract restricted the cure, the damage for which compensation was payable, and the total amount payable upon breach.¹⁰⁰ The court held that the limitation of damages to £25,000 was unacceptable under the reasonableness test.¹⁰¹

In the United Kingdom, lost profits are not considered a part of consequential damages, but rather they are treated as a loss flowing directly and naturally from a breach.¹⁰² This differs from U.S. law, which treats lost profits as consequential.¹⁰³

B. United States

U.S. suppliers can limit remedies more easily because they need not contend with the reasonableness test.¹⁰⁴ American courts tend to accept the amount of liquidated damages agreed to by the parties.¹⁰⁵ A plaintiff may pursue all available remedies whenever circumstances cause an exclusive remedy to fail in its essential purpose.¹⁰⁶ Contractual limitations on consequential damages are acceptable, unless the limitation is unconscionable.¹⁰⁷ UCITA sections 803(b) and 803(d) are comparable to their respective UCC provisions.¹⁰⁸

In *Fargo Machine & Tool Co. v. Kearney & Trecker Corp.*,¹⁰⁹ the contract limited the buyer's remedy to either repair or replacement of defective parts and excluded consequential damages. The court held that the remedy was invalid because it failed in its essential purpose since the repairs would not cure all defects. The court awarded the buyer damages.¹¹⁰

⁹⁹ *Hadley v. Baxendale*, 9 Ex. 341 (1854).

¹⁰⁰ *Salvage*, [1995] F.S.R. at 657.

¹⁰¹ *Id.*

¹⁰² *Kawawa*, *supra* note 13, at 158; *British Sugar Plc. v. NEI Power Projects Ltd.*, 14 Const. L.J. 365 (Eng. C.A. 1998).

¹⁰³ *Kawawa*, *supra* note 13, at 158 (treating lost profits as consequential makes them relatively more difficult to win in the U.S.); *see, e.g., Consol. Data Terminals v. Applied Digital Data Sys.*, 708 F.2d 385 (9th Cir. 1983).

¹⁰⁴ Unfair Contract Terms Act, 1977, c. 50, §112 (Eng.).

¹⁰⁵ *See, e.g., Colonial Life Ins. Co. v. Elec. Data Sys. Corp.*, 817 F. Supp. 235 (D.N.H. 1993).

¹⁰⁶ U.C.C. § 2-719(2) (2003).

¹⁰⁷ *Id.* § 2-719(3).

¹⁰⁸ *Id.* § 2-719(2)-(3).

¹⁰⁹ *Fargo Machine & Tool Co. v. Kearney & Trecker Corp.*, 428 F. Supp. 364 (E.D. Mich. 1977).

¹¹⁰ *Id.*

VI. STANDARD FORM CONTRACTS

Both countries have statutes designed to offer protection for contracting parties who are offered a standard form contract on a “take it or leave it” basis.¹¹¹ Such situations are often characterized by unequal bargaining power between the parties.¹¹² Both nations resolve any ambiguity in the contract against the party who wrote it.¹¹³ This rule is especially important for standard form contracts.¹¹⁴

A. United Kingdom

1. *Unfair Contract Terms Act of 1977*

The 1977 Act protects both consumers and any business that is not computer-related.¹¹⁵ The seller’s implied warranties pertaining to conformity of goods, or to their quality of fitness for a particular purpose, cannot be disclaimed in a standard form contract.¹¹⁶ The reasonableness requirement applies to every situation involving a standard form contract, even if both parties are business firms.¹¹⁷

2. *Unfair Terms in Consumer Contracts Regulations of 1999*

This act implemented the Council Directive on Unfair Terms in Consumer Contracts.¹¹⁸ Unlike the 1977 Act, the 1999 Regulations only apply to consumers, not to firms making business purchases.¹¹⁹ Standard form contracts are “unfair” if they are not written in good faith, but instead “cause a significant imbalance in the parties’ rights and obligations arising under the contract, to the detriment of the consumer.”¹²⁰

B. United States

Unlike the 1977 Act, the UCC and the Magnuson-Moss Act¹²¹ allow implied warranties to be disclaimed in consumer transactions in some situations. However, the Magnuson-Moss Act restricts disclaimers in

¹¹¹ Leo L. Clarke, *Performance Risk, Form Contracts and UCITA*, 7 MICH. TELECOM. TECH. L. REV. 1, 20 (2000).

¹¹² *Id.*

¹¹³ RESTATEMENT (SECOND) OF CONTRACTS § 211(1) (1979).

¹¹⁴ *Id.*

¹¹⁵ Unfair Contract Terms Act, 1977, c. 50, §12 (Eng.).

¹¹⁶ *Id.* § 6(2).

¹¹⁷ *Id.*

¹¹⁸ Council Directive 93/13/EEC, 1993 O.J. (L 095).

¹¹⁹ UCITA, *supra* note 8, § 406.

¹²⁰ *Id.* §§ 5(1)–(2).

¹²¹ 15 U.S.C. § 2308 (2001).

contracts for the purchase of “consumer products,” defined as “any tangible personal property that is distributed in commerce and which is normally used for personal, family, or household purposes.”¹²²

VII. A SPECIAL TYPE OF STANDARD FORM CONTRACT: THE SHRINK-WRAP LICENSE

The shrink-wrap license is a standard form contract that may be delivered with software. Its purpose is to protect the intellectual property rights of the owner of the software.¹²³ Typically, the agreement is on the outside of the software’s package, and its purpose is to achieve implied acceptance of the agreement if the package is opened.¹²⁴ The license terms may limit liability, use, the warranty, or designate the law which governs the contract.¹²⁵ Since it is a standard form contract offered on a “take it or leave it” basis, it is debatable whether the person opening the package has entered into a contract.¹²⁶ In both the United Kingdom and the United States, all terms in a shrink-wrap license are enforceable if the terms are clearly readable, and the person accepted them before buying the software.¹²⁷

A. United Kingdom

Warranty disclaimers in shrink-wrap licenses are subject to the statutory control of the 1977 Act.¹²⁸ The terms of the agreement must pass the reasonableness test.¹²⁹ Any attempt to later change the terms of the license after the date of its creation will ordinarily fail.¹³⁰

B. United States

Case law exists to support the notion that opening a shrink-wrap package is usually considered to imply acceptance of the license

¹²² *Id.* § 2301(1).

¹²³ Batya Goodman, Note, *Honey, I Shrink-Wrapped the Consumer: The Shrink-Wrap as an Adhesion Contract*, 21 CARDOZO L. REV. 319, 320 (1999).

¹²⁴ *Id.*

¹²⁵ David L. Hayes, *Shrinkwrap License Agreements: New Light on a Vexing Problem*, 9 No. 9 COMPUTER LAW. 1, 2 (1992).

¹²⁶ Garry L. Founds, Note, *Shrinkwrap and Clickwrap Agreements: 2B or Not 2B?*, 52 FED. COMM. L.J. 99, 101 (1999).

¹²⁷ Clive Gringas, *The Validity of Shrink-Wrap Licenses*, 4 INT’L J.L. & INFO. TECH. 77 (1996).

¹²⁸ Kawawa, *supra* note 13, at 172 (citing Unfair Contract Terms Act, 1977, c. 50, §§ 3, 6(2) (Eng.)).

¹²⁹ *Id.* (citing *Thorton v. Shoe Lane Parking Ltd.*, [1971] 2 Q.B. 163, 169).

¹³⁰ *Id.*

agreement.¹³¹ Pursuant to the UCC, a purchaser must agree to any proposed changes to an existing contract.¹³² UCITA differs from the UCC on this point, however. UCITA allows new, modified terms proposed after the commencement of performance to become enforceable, if the party had reason to know at the time of purchase that such new terms might be proposed and later assents to them.¹³³ In the case of mass-market licenses, however, the requirements imposed for later changes are more stringent.¹³⁴ A number of commentators have severely criticized UCITA for allowing later modifications to the agreement.¹³⁵ Only a few have defended UCITA.¹³⁶

VIII. CONCLUSIONS

The two nations take different approaches in statutory control of contractual terms. U.K. law has the more potent reasonableness test; U.S. law has the less stringent unconscionability doctrine. U.K. courts offer more automatic statutory protection when the buyer has significantly less bargaining power than the supplier. By contrast, U.S. law does not accept disparity in bargaining power as a default and does not attempt to protect a weak party. U.S. law is more seller-oriented and focuses on whether the buyer had sufficient sophistication to understand the terms of the contract and to evaluate the quality of the software. If the buyer had an understanding of the terms of the agreement and the degree of the software's quality, the buyer will be held accountable for the bargain entered into, regardless of the lack of bargaining power the buyer had when entering into the purchase agreement.

Suppliers often make express warranties regarding the suitability of the software for the buyer's needs. Under U.K. law, any terms in the contract that seek to disclaim express warranties are subject to the reasonableness

¹³¹ *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447 (7th Cir. 1996); see also Joseph C. Wang, Note, *ProCD, Inc. v. Zeidenberg and Article 2B: Finally, the Validation of Shrink-Wrap Licenses*, 16 J. MARSHALL J. COMPUTER & INFO. L. 439 (1997).

¹³² U.C.C. § 2-209(2) (2003).

¹³³ UCITA, *supra* note 8, § 208(2).

¹³⁴ *Id.* § 209(a) & cmt. 2a (2001) (if the licenses are for a "mass-market," the licensee must be told the potential terms, to be modified no later than the initial use of the information, and the licensee is given a right of refund if he/she refuses to accept).

¹³⁵ E.g., Roger C. Bern, "Terms Later" Contracting: *Bad Economics, Bad Morals, and a Bad Idea for a Uniform Law*, *Judge Easterbrook Notwithstanding*, 12 J.L. & POL'Y 641 (2004); Jean Braucher, *Amended Article 2 and the Decision to Trust the Courts: The Case Against Enforcing Mass-Market Terms, Especially for Software*, 2004 WIS. L. REV. 753 (2004); Ajay Ayyappan, Note, *UCITA: Uniformity at the Price of Fairness?*, 69 FORDHAM L. REV. 2471 (2001).

¹³⁶ E.g., Erika E. Schinler, Comment, *Trouble at the Sausage Factory: Has the Uniform Computer Information Transactions Act Been Unjustly Stigmatized?*, 75 TUL. L. REV. 507 (2000).

test, making it more difficult to disclaim an express warranty. Moreover, an express warranty of fitness for the buyer's intended purpose is especially difficult to disclaim. In the United States, express warranties are also difficult to disclaim, since the express warranty and the disclaimer must be construed as being consistent with each other. However, U.S. law does not subject disclaimers to a reasonableness test and is therefore more seller-oriented.

Both countries have statutes that create implied warranties for the quality of the software and its fitness for the buyer's purpose. The actual impact of implied warranties, however, depends upon whether the law allows them to be disclaimed by agreement of the parties. U.K. law offers more protection for the buyer of the software because the reasonableness test applies to any attempt by the supplier to disclaim implied warranties. On the other hand, U.S. law under both the UCC and UCITA ordinarily permits easy disclaimer of implied warranties, so long as the specific language and format requirements are met.

The two countries also differ in terms of limitation of remedies. In the United Kingdom, the reasonableness test is used to assess the appropriateness of the limitation. If monetary damages are to be restricted, a relevant factor is whether the user of the software could have obtained insurance coverage. In some cases, limitation of damages to the amount of the contract price has been considered reasonable. In the United States, liquidated damages clauses are generally held to be valid if the language and conspicuousness requirements are met. However, courts may rule that the limitation of remedies is invalid if the remedy fails in its essential purpose or is unconscionable.

The United Kingdom is relatively less tolerant of standard form contracts and has more statutory control of contractual terms. By comparison, the United States is more accepting of standard form contracts, provided that the buyer had an opportunity to attain an understanding of the agreement and that the contract terms were conspicuous and noticeable. Similarly, U.K. shrink-wrap license law provides more protections for the buyer of the software by making it more difficult for suppliers to disclaim express or implied warranties, or limit remedies. By comparison, UCITA allows a shrink-wrap license to be modified by the supplier during the middle of the contract period.

IX. RECOMMENDATIONS

A. United States: Needs More Consumer Protections

The United States can learn from the United Kingdom's greater protections for consumer rights. As a long-time supporter of consumer empowerment, this author finds that U.S. law is deficient in its consumer

protections. Shrink-wrap agreements are too one-sided in favor of the supplier.¹³⁷ For example, to protect buyers, UCITA could be amended by adding a clause comparable to one found in the U.S. Restatement (Second) of Contracts, which provides that: "Where the other party has reason to believe that the party manifesting such assent would not do so if he knew that the writing contained a particular term, the term is not part of the agreement."¹³⁸ This would provide additional protection for the buyer who hurriedly purchases software online without bothering to read an often lengthy agreement containing legalese.¹³⁹

B. United Kingdom: Should Consider a UCITA-style Statute

Perhaps the United Kingdom should consider adopting a computer-specific statute comparable to UCITA, but modified to incorporate more consumer rights and protections. UCITA is flawed in its present form, but it is a work-in-progress that is still being amended. Over time, more U.S. states are expected to embrace it. We have entered the digital millennium; contract law needs to be modified to accommodate the unique aspects of electronic contracting and the sale and lease of software. Adoption of a UCITA-style statute would be a good first step for the United Kingdom to update its laws to the contract law challenges of the digital millennium.

¹³⁷ One commentator has described shrink-wrap agreements grounded in state contract law as "unconscionable" and has called for their preemption by federal copyright law. See Nathan Smith, Comment, *The Shrinkwrap Snafu: Untangling the "Extra Element" in Breach of Contract Claims Based on Shrinkwrap Licenses*, 2003 B.Y.U.L. REV. 1373, 1406-07, 1410-18 (2003) (arguing that copyright law would better preserve the rights of both software sellers and purchasers, affording copyright protections for the sellers and the related rights of fair use for the purchasers).

¹³⁸ RESTATEMENT (SECOND) OF CONTRACTS § 211(3) (1979).

¹³⁹ This portion of the Restatement was used by Nathan Smith as one argument for the federal preemption of shrink-wrap agreements by copyright law. Citing Section 211(3), Smith states that "[i]t is reasonable to believe that prospective licensees would not enter into shrink-wrap agreements if they understood that entering into such constituted a waiver of their federal rights." Smith, *supra* note 137, at 1405; *but see* Founds, *supra* note 126, at 107 (opining that shrink-wrap agreements are enforceable under contract law, notwithstanding the impact of Section 211(3) and adhesive qualities, after considering the entirety of Section 211 because "contracts of adhesion usually are enforced as an implied agreement between the parties.")