

## AN ESSAY ON ARTICLE 2'S IRRELEVANCE TO LICENSING AGREEMENTS

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### I. INTRODUCTION

There must be an old saying to cover the circumstances ignored in many articles. While that old saying escapes me, the circumstances are quite obvious: Article 2 of the Uniform Commercial Code (UCC) is fading in commercial and theoretical importance. Today, most important contract law theory developments and practice innovations occur outside the realm of Article 2. The recent and largely failed effort to revise Article 2 sought to reclaim center stage for that statute, but has failed of enactment and has very little new content relevant to the modern context.<sup>1</sup> A proliferation of state and federal laws overrides Article 2 in consumer, franchise, and other fields, such as electronic commerce.<sup>2</sup> New forms of commercial subject matter and transactions that lie outside the ambit of Article 2 have emerged and receive little relevant guidance from the goods-centric themes of Article 2.<sup>3</sup>

Indeed, in my experience, very few lawyers or law academics hold themselves out as specializing in Article 2. On the other hand, there are many who claim special expertise in other types of contracting, such as consumer law, licensing law, labor law, entertainment law, real estate, franchising, electronic commerce, and

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1. Even if that draft is ever enacted, it will most likely be in a highly modified form from the promulgated "official" revision of Article 2, reflecting little more than a copy-editing exercise. See Gregory E. Maggs, *The Waning Importance of Revisions to U.C.C. Article 2*, 78 NOTRE DAME L. REV. 595, 597 (2003) ("The proposed revisions . . . make minor corrections and adjustments but otherwise avoid significant substantive changes.").

2. See RAYMOND T. NIMMER & JEFF M. DODD, *MODERN LICENSING LAW* ch. 2 (Thompson West 2d ed. 2006).

3. *Id.*

so forth. These other areas are where important commercial and policy decisions are being made. They, not Article 2, are where the “action is” in modern commerce and law.

In this setting, the question is not should one be able to contract around or out of Article 2. Rather, the question is whether Article 2 has, or should have, any relevance beyond (1) its narrow original boundaries, and (2) some of its general rules that have been incorporated into the common law of most states (for example, good faith, and unconscionability). The answer in most cases is *no*. Indeed, that is the answer most lawyers and courts reach when they address Article 2’s relevance in reference to transactions in real estate, intellectual property, services, and other types of contracts.<sup>4</sup>

In part, the reason for this lies in the fact that Article 2 fails to ask or answer many of the most important issues present today in contract law. This is true whether one focuses on theoretical questions or on practical commercial questions. Most of what is contained in Article 2 has long since been asked and answered, and most of what is being asked today in contract law falls outside of Article 2.<sup>5</sup> In addition, most of what is answered in Article 2 is grounded in assumptions and practices that are not relevant to other areas of commercial contract law, including licensing, services, and online contracting.<sup>6</sup>

There has been a troubling reaction to the increased marginalization of Article 2 sales’ core. It is predicted by Karl Llewelyn’s comments about the original reaction to Article 2 and to what he saw as a transition from an agricultural economy to a manufactured goods economy:

Mercantile capitalism yields to industrial capitalism . . .  
industrial yields again to financial capitalism: and the  
dye-woods, cloves . . . and simple textiles . . . are pushed

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4. See Raymond T. Nimmer, *Through the Looking Glass: What Courts and UCITA Say About the Scope of Contract Law in the Information Age*, 38 DUQ. L. REV. 255, 267–268 (2000) (discussing several general rules in Article 2 having relevance beyond the sales of goods); see also Caroline Edwards, *Article 2 of the Uniform Commercial Code and Consumer Protection: The Refusal to Experiment*, 78 ST. JOHN’S L. REV. 663 (2004) (describing the limitations to Article 2 and its strict adherence to sales of goods transactions).

5. See Maggs, *supra* note 1, at 598 (“[T]he recent growth of electronic commerce actually tends to diminish the importance of Article 2’s present contract formation rules because it removes many sales transactions from the coverage of those rules.”).

6. See Nimmer, *supra* note 4, at 265, 287–91.

out of dominance by chemicals . . . ; you follow iron . . . ; you meet sewing machines sold to householders on the installment plan, you meet locomotives sold on the “same” plan to an equipment trust . . . , you find “choses-in-action,” which means here stocks and bonds, excluded from the Uniform Sales Act. You wake up then to the fact that the throne your subject matter once occupied is overshadowed . . . .<sup>7</sup>

You wake up and your throne is overshadowed. Vested interests—whether grounded in economics, academics, or mere personal preferences—resist a loss of status, and act to block or divert recognition that their once-protected position is being eroded. We are seeing this in reference to Article 2 and a focus on goods transactions in contract law. Indeed, there was fierce resistance from some against explicitly excluding information transactions from Article 2. That resistance testifies to a reluctance of some to cede position to new areas and subject matter of commerce. However, that resistance is wrong—information is simply not goods.<sup>8</sup>

This essay juxtaposes Article 2’s sales rules to contract law and practice associated with licensing of informational assets. Licensing intellectual property and digital information today is one of the most important commercial transaction formats in commerce.<sup>9</sup> We live in an information age, an expression that signals both the importance of informational assets and the widespread commercial dissemination of information and tools for processing, analyzing, and using information based on digital and modern communications systems as a commercial enterprise.<sup>10</sup> In most instances, Article 2 sales rules are, and should be, irrelevant to licensing, except for the broad themes of Article 2 that have already been incorporated into the common law.<sup>11</sup>

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7. See Karl N. Llewellyn, *Across Sales on Horseback*, 52 HARV. L. REV. 725, 725–27 (1939).

8. See *infra* notes 98–99.

9. See, e.g., NIMMER & DODD, *supra* note 2, at 1.

10. Thomas A. Stewart, *Welcome to the Revolution*, FORTUNE, Dec. 13, 1993, at 66.

11. When I refer to Article 2, I mean Article 2 working in combination with the relevant provisions of Article 1 applicable to Article 2.

## II. IMAGES: ARTICLE 2'S SALES RULES

Not all of Article 2 is of the same nature. There are various ways to describe Article 2's themes, but the framework that best fits what I am discussing includes three categories:

- The first involves Article 2's reaffirmation (with some limitations) that the express terms of an agreement control the contours of the bargain, and that most provisions on presumed obligations and risk allocation are subject to contract agreement.<sup>12</sup> This was not an innovation of Article 2 but a reflection of traditional U.S. law.<sup>13</sup> The continued dominance of this theme is not an indication of Article 2's current relevance.
- The second refers to the general themes set out in Article 2 or Article 1 that are not tailored to the specific facets of sales of goods transactions. These include the obligation of good faith,<sup>14</sup> the requirement of practical construction of an agreement,<sup>15</sup> and the judicial power to avoid unconscionable terms.<sup>16</sup> Although not all states have adopted these doctrines into general laws, they have fared well.<sup>17</sup> Article 2, in its early years, was part of the then-current movement to embed these themes into general contract law.<sup>18</sup> Its impact is unquestionable but historical, rather than current. In most states, these general doctrines are now part of contract law, whether or not Article 2 applies to a transaction.<sup>19</sup>
- The third category consists of the tailored rules regarding sales transactions. These rules reflect typical transactions as they occurred in the 1940s and 1950s

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12. U.C.C. § 2-303 (2003).

13. *See, e.g.*, Edwards, *supra* note 4, at 696.

14. U.C.C. § 1-203 (2000) (amended 2003).

15. U.C.C. §§ 1-205, 2-208 (1998) (amended 2003).

16. U.C.C. § 2-302 (2003).

17. *See, e.g.*, Edwards, *supra* note 4, at 664 n.5.

18. *See id.*, at 696.

19. *See, e.g.*, Carol B. Swanson, *Unconscionable Quandary: UCC Article 2 and the Unconscionability Doctrine*, 31 N.M. L. REV. 359, 362 & n.29 (2001) (discussing this concept with regards to unconscionability).

when Article 2 was adopted.<sup>20</sup> Questions about the relevance of Article 2 or of contracting around it in modern commerce most often focus on these tailored issues. The question is whether the old images of contracting in hard goods are relevant to modern contracts in goods or other subject matter.

This essay deals with the contemporary relevance of this third category as it exists in enacted Article 2.

#### A. *Category-Three Tailored Default Rules*

When we look at category-three tailored rules, we need to identify what images are reflected in these sales-tailored rules and their relevance in modern commerce. Article 2's tailored default rules operate in the absence of contrary agreement and reflect the drafters' image of what should be an appropriate or normal starting point in understanding the meaning of a particular transaction.<sup>21</sup>

There are many ways to describe the images that underlie category-three rules. One thing we know is that all of the images reflect the commercial and legal environment of the 1950s and earlier.<sup>22</sup> In addition, the rules are connected to a transaction in which there is a single delivery of tangible goods on immediate payment, where the focus of the agreement and remedies for its breach center on the particular goods.<sup>23</sup> Few provisions of Article 2 address commercial agreements involving numerous deliveries of goods over time.<sup>24</sup> Only those provisions associated with breach,<sup>25</sup> and those referring the parties to Article 9 for guidance on credit transactions,<sup>26</sup> provide any guidance for obligations that might be owed after goods have been delivered and accepted.

Delivery of the subject matter accompanied by restrictions on its

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20. See Edwards, *supra* note 4, at 689–700.

21. See Steven J. Burton, *Default Principles, Legitimacy, and Authority of a Contract*, 3 S. CAL. INTERDISC. L.J. 115, 116 (1993); Dennis Patterson, *The Pseudo-Debate Over Default Rules in Contract Law*, 3 S. CAL. INTERDISC. L.J. 235, 237 (1993).

22. See Edwards, *supra* note 4, at 689–700.

23. See, e.g., U.C.C. §§ 2-307, 2-503 (2003).

24. See Nimmer, *supra* note 4, at 266 (“Many of sales rules are not pertinent to leases of goods, which have become a major type of commercial contract.”); see, e.g., U.C.C. §§ 2-306, 2-307, 2-311, 2-612 (1998) (amended 2003).

25. See, e.g., U.C.C. § 2-607 (2003).

26. See, e.g., U.C.C. §§ 2-401 to -403, 2-607, 2-703, 2-711 (2003).

use is not otherwise addressed, despite being one of the most common and commercially important forms of transaction today. The world was simpler then and, most importantly, did not involve the broad involvement of digital information and intellectual property rights as a valuable form of commercial subject matter. In addition:

- The images and reality of electronic commerce are not addressed in Article 2 (although they are dealt with in the non-enacted revisions).
- Doctrines of consumer protection are largely absent from Article 2 and are left for federal regulation and nonuniform state regulation.<sup>27</sup>
- Personal property leasing is covered elsewhere, requiring a separate Article 2A of the U.C.C. and various leasing acts in the several states.<sup>28</sup>
- Licensing and other forms of transactions in information are not discussed.

Indeed, in all of these areas, law (including contract law) and practice (including commercial practice) have developed outside of Article 2 and should continue to do so.<sup>29</sup>

### *B. Nature of Default Rules*

Why are the images that generate tailored rules important? One could argue—weakly, I believe—that they are not. This argument would focus on the fact that, in large part, the tailored rules connected to sales are subservient to the express agreement of the parties.<sup>30</sup> Thus, if the parties are aware of rules tailored inappropriately for the particular transaction, they can change the rule by agreeing to a different rule. The express bargain controls over the “default” or “gap-filler” rules.<sup>31</sup> However, the situation is not so simple.

The potential of parties to know and address all relevant issues

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27. See Edwards, *supra* note 4, at 699 (“[T]he notion of ‘consumer rights’ is found only in a few provisions of current Article 2.”); Nimmer, *supra* note 4, at 273–74.

28. See U.C.C. § 2A-101 (2003).

29. See Gerald T. McLaughlin, *The Evolving Uniform Commercial Code: From Infancy to Maturity to Old Age*, 26 *LOY. L.A. L. REV.* 691, 695 (1993).

30. See Burton, *supra* note 21, at 116.

31. See Patterson, *supra* note 21, at 237.

in a transaction is suspect, and even to the extent that discovering and solving all issues were possible, doing so would generate substantial costs.<sup>32</sup> On the other hand, if the express agreement does not address an issue, the default rule governs.<sup>33</sup> Wrong images then produce wrong results in court and in the parties' ability to match their agreements to their core expectations.

While a debate exists about whether default rules should articulate an appropriate outcome for a particular type of transaction or should impose a rule that forces one party to produce information to avoid an inappropriate rule,<sup>34</sup> no argument supports default rules that are simply wrong because they reflect the wrong image of a transaction type. Unfortunately, this is what happens if the sales-related rules of Article 2 are applied to different subject matter or to types of transactions other than those for which they were originally intended.

Default rules supply a contract term to deal with aspects of the contractual relationship not covered by the express agreement of the parties.<sup>35</sup> They also provide a background against which the agreement is understood and interpreted.<sup>36</sup> A default rule must be developed in reference to a benchmark. As a result, substantial academic debate has developed around competing theories of the appropriate benchmark to be used.<sup>37</sup> Some argue for so-called penalty default rules in some circumstances, while others argue for rules in all cases that reflect the agreed terms hypothetical,

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32. Ian Ayres & Robert Gertner, *Strategic Contractual Inefficiency and the Optimal Choice of Legal Rules*, 101 YALE L.J. 729, 733 (1992) (“[I]nefficiencies that can be caused by strategic bargaining under conditions of asymmetric information . . . depend upon, and can be exacerbated by, the costs of contracting around a given default rule.”); Nimmer, *supra* note 4, at 262 (Default “[r]ules that are not so tailored increase costs because parties must negotiate to eliminate their effect.”).

33. See Patterson, *supra* note 21, at 237; see also Burton, *supra* note 21, at 154.

34. See Patterson, *supra* note 21, at 238.

35. See *id.* at 237.

36. See *id.*

37. See generally Ian Ayres & Robert Gertner, *Majoritarian vs. Minoritarian Defaults*, 51 STAN. L. REV. 1591 (1999) (describing advocates of the penalty default approach as taking a majoritarian approach and advocates of the other perspective as having a minoritarian perspective); Burton, *supra* note 21, at 133; Patterson, *supra* note 21, at 252.

reasonable parties would have adopted had they specifically addressed the issue.<sup>38</sup>

The penalty perspective regards a proper function of default rules as manipulating the bargaining process. Penalty default rules provide a term that would *not* have been the choice of the parties had they contemplated the issue.<sup>39</sup> The theory is that such rules create incentives for the party hurt by the rule to take steps to avoid its adverse effects. This arguably promotes disclosure and negotiation associated with the covered issue.<sup>40</sup>

The penalty theory, however, works only in an abstract world. When real world influences, incentives, negotiation, and asymmetrical information are put into play, the idea that a penalty default rule will predictably cause such results in complex bargaining or market conditions is too simplistic.<sup>41</sup> Actual bargaining processes are far more complex than can be easily influenced in a direct manner by arcane and relatively weak contract law rules that are often unknown to either party.<sup>42</sup> Even if the projected disclosure or bargaining effects often occur, there are still costs and inevitable failures.<sup>43</sup> The idea of a complete contract that expressly covers all contingencies with one clear rule is a myth, not achievable in practice.

In contrast to the penalty default concept, many argue that default rules should be fashioned to supply a term and yield the result parties would most likely have agreed upon had they contemplated the particular contingency at hand.<sup>44</sup> One court commented that this

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38. See Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87, 91–92 (1989).

39. See *id.* at 91.

40. *Id.*; see generally Ayres & Gertner, *supra* note 32, at 729 (discussing the extent to which theory can predict response in bargaining via default rules that are intended to shape contracting behavior); Jason Scott Johnston, *Strategic Bargaining and the Economic Theory of Contract Default Rules*, 100 YALE L.J. 615, 616 (1990).

41. See Barry E. Adler, *The Questionable Ascent of Hadley v. Baxendale*, 51 STAN. L. REV. 1547, 1548–54 (1999) (lauding penalty default rules for economic efficiency, but questioning whether such rules can be practically imposed in actual marketplaces).

42. See *id.* at 1550–51.

43. See *id.*

44. See UNIF. COMPUTER INFO. TRANSACTIONS ACT, Prefatory Note (Nat'l Conference of Comm'rs of Unif. State Laws 1999) ("The best source of substantive rules lies not in a theoretical model, but in commercial and trade practice. . . . It stems from the reality that we may not know how law interacts with contract practice, but decisions about

approach involves “[giving] the parties what they would have stipulated for . . . if at the time of making the contract they had complete knowledge of the future and the costs of negotiating and adding provisions to the contract had been zero.”<sup>45</sup> Formulating a default rule is not an academic exercise. Default rules have commercial consequences.<sup>46</sup> Hence, these rules should be founded upon general commercial practices, regardless of whether those commercial practices fit within academic preconceptions of what the “best” outcome should be.

Since default rules function as surrogates for commercial terms, they should be developed by lawmakers in a manner that is relevant and fitted to the particular type of commercial context. Thus, the default rule should correspond to the type of resolution parties generally would expect in similar transactions under similar circumstances, without reflecting the specific bargaining balance associated with the specific parties.<sup>47</sup> It is, in effect, a commercially sensible and balanced bargain in light of ordinary images regarding risk allocation, issues specific to the type of transaction and reasonable participants in such agreements.<sup>48</sup>

This is not about what the specific parties would have accepted but about what terms reasonable parties in similar positions generally would adopt. This cannot be asked or answered about individual parties but from balancing the outcome from the respective perspectives of transacting parties generally involved in such transactions. Due to the function of the default rules, it is important

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contract law will continue to be made. In those decisions, we should refer for guidance to the accumulation of practical choices made in actual transactions. The goal is a congruence between legal premise and commercial practice so that the transactions between contracting parties achieve commercially intended results.”); Patterson, *supra* note 21, at 254.

45. *Mkt. St. Assocs. Ltd. P’ship v. Frey*, 941 F.2d 588, 596 (7th Cir. 1991); *see also* Burton, *supra* note 21, at 134.

46. *See* Patterson, *supra* note 21, at 237; *see generally* Charles J. Goetz & Robert E. Scott, *The Limits of Expanded Choice: An Analysis of the Interaction Between Express and Implied Contract Terms*, 73 CAL. L. REV. 261, 264–265 (1985).

47. *See* Goetz & Scott, *supra* note 46, at 266; Randy E. Barnett, *The Sound of Silence: Default Rules and Contractual Consent*, 78 VA. L. REV. 821, 829 (1992) (“[D]efault rules that reflect the conventional or commonsense understanding existing in the relevant community . . . are likely to reflect the tacit . . . agreement of the parties and thereby facilitate the social functions of consent.”).

48. Goetz & Scott, *supra* note 46, at 266; *see* Patterson, *supra* note 21, at 237.

that they are developed in statute and by courts in a manner that is relevant and fitted to the particular *type* of context. Grant Gilmore expressed this idea in the following words:

The principal objects of draftsmen of general commercial legislation . . . is to assure that if a given transaction . . . is initiated, it shall have a specified result; they attempt to state as a matter of law the conclusion which the business community apart from statute . . . gives to the transaction in any case.<sup>49</sup>

The goal in judicial development of background rules should be similar—it should achieve congruence between legal premise and commercial practice so that transactions adopted by commercial parties attain commercially intended results.

Default rules also provide a framework for interpretation and a context for negotiation.<sup>50</sup> The rules may come to characterize the type of transaction involved. Thus, for example, according to most courts, a nonexclusive license is a mere covenant not to sue the licensee.<sup>51</sup> That characterization shapes a court's approach to interpreting matters such as license grant language, the transferability of the license, and the existence or nonexistence of infringement warranties.<sup>52</sup>

Writing in 1939, Llewellyn commented:

[If] the *stock* intellectual equipment [(image)] is [in]apt, it takes extra art or intuition to get proper results with it. Whereas *if* the stock intellectual equipment is apt, it takes extra ineptitude to get sad results with it. And the work of the artist, accomplished with poor intellectual equipment, is not clearly intelligible to the inept reader. It does not talk to him, it does not provide him tools, it does not help him focus issues.<sup>53</sup>

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49. Grant Gilmore, *On the Difficulties of Codifying Commercial Law*, 57 YALE L. J. 1341, 1341 (1948).

50. See Ayres & Gertner, *supra* note 38, at 91.

51. See *Spindelfabrik Suessen-Schurr Stahlecker & Grill v. Schubert & Salzer Maschinenfabrik Aktiengesellschaft*, 829 F.2d 1075, 1081 (Fed. Cir. 1987), *cert. denied*, 484 U.S. 1063 (1988).

52. See *id.* at 1081.

53. Karl Llewellyn, *The First Struggle to Unhorse Sales*, 52 HARV. L. REV.

As the economy evolves, it is important that modern default provisions and the stock intellectual equipment they embody aptly reflect modern commerce.

### III. IMAGES AND THEMES: LICENSING LAW

In asking about the relevance of category-three default rules in Article 2 to licensing or other transactions, we must ultimately compare the images and resulting rules that exist in law and practice in each context. As we have seen, the Article 2's image is grounded in the sales practices of an old era that emphasizes transactions involving a single delivery, where payment is required at the time of delivery in exchange for the full rights to use the particular item sold.<sup>54</sup> While these arrangements can be altered by agreement,<sup>55</sup> and there is passing coverage of multi-delivery contracts in Article 2,<sup>56</sup> this simple model sets the base for most category-three default rules.

What are the attributes of a license of information? License contracts allocate rights and set limitations on the use of *informational or intellectual property*.<sup>57</sup> As one court commented, '[A] license . . . is a transfer of limited rights, less than the whole interest which might have been transferred.'<sup>58</sup> The following is another definition of a license:

A license is an agreement that deals with, and grants or restricts, a licensee's contractual right, power privilege or immunity with respect to uses (including allowing access to) information or rights in information made available by a licensor. The agreement includes a focus on what rights, immunities, or uses are given or withheld in reference to use of the information as well as what the licensee has

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873, 876 (1939).

54. U.C.C. § 2-106(1) (2003) (A sale is "the passing of title from the seller to the buyer for a price.").

55. *See, e.g., id.* §§ 2-209, 2-507.

56. *See, e.g., id.* § 2-307.

57. *See Icee Distribs., Inc. v. J & J Snack Foods Corp.*, 325 F.3d 586, 597 (5th Cir. 2003).

58. *Exxon Corp. v. Oxxford Clothes, Inc.*, 109 F.3d 1070, 1076 (5th Cir. 1997) (citing *Acme Valve & Fittings Co. v. Wayne*, 386 F. Supp. 1162, 1165 (S.D. Tex. 1974) (alteration in original)).

agreed to do or not to do with respect to the information.<sup>59</sup>

This definition is broader than definitions grounded in intellectual property law that view a license as a mere covenant not to sue or enforce intellectual property rights against the licensee.<sup>60</sup>

As this indicates, a rich diversity exists in how courts and parties characterize a license in commercial practice. This diversity is grounded in two core considerations. First, a license focuses on rights and limitations in information, rather than on ownership or possession of goods. Second, a license is a limited transfer, while a sale of goods conveys ownership of the goods. There are few more explicit differences in contract law than the competing observations that a sale of goods passes title to the goods for a fee, while a license represents a transfer of limited permissions or a mere covenant not to sue.

Properly understood, the images and default rules that these very different transactional expectations engender are quite different in content. In practice, some view a license as passive, while others may view the license as more active with respect to granting the licensee's use of the informational assets.<sup>61</sup> The two views coexist but yield very different implications in licensing law and practice.

A passive view tends to dominate in agreements arranged by lawyers and practitioners schooled in intellectual property law (particularly patent law).<sup>62</sup> Under this view, licenses are mere

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59. NIMMER & DODD, *supra* note 2, at ch. 1; *cf.* UNIF. COMPUTER INFO TRANSACTIONS ACT § 102(a)(41) (2000) ("License" means a contract that authorizes access to, or use, distribution, performance, modification, or reproduction of, information or informational rights, but expressly limits the access or uses authorized or expressly grants fewer than all rights in the information, whether or not the transferee has title to a licensed copy. The term includes an access contract, a lease of a computer program, and a consignment of a copy. The term does not include a reservation or creation of a security interest to the extent the interest is governed by [Article 9 of the Uniform Commercial Code].).

60. *See, e.g.,* Gen. Talking Pictures Corp. v. W. Elec. Co., 304 U.S. 175, 181 (1938) (characterizing a patent license as "a mere waiver of the right to sue." (citing De Forest Radio Tel. Co. v. United States, 237 U.S. 236, 242 (1927))); Spindelfabrik Suessen-Schurr Stahlecker & Grill v. Schubert & Salzer Maschinenfabrik Aktiengesellschaft, 829 F.2d 1075, 1081 (Fed. Cir. 1987), *cert. denied*, 484 U.S. 1063 (1988).

61. *See Exxon*, 109 F.3d at 1076-78.

62. *See, e.g.,* Wang Labs., Inc. v. Mitsubishi Elecs. Am., Inc., 103 F.3d 1571, 1580 (Fed. Cir. 1997) ("[A]n implied license merely signifies a patentee's waiver of the statutory right to exclude others from making, using, or selling the patented invention."); *Wokas v. Dresser Indus., Inc.*, 978 F. Supp. 839, 847 (N.D. Ind. 1997) ("[A]

covenants not to sue: the license waives the licensor's right to sue the licensee for specified, otherwise infringing actions but does no more than that.<sup>63</sup> The products of this view can be seen throughout licensing law and practice. Under this view, for example, the licensor provides no implicit warranty or assurance of the licensee's right or ability to actually use the licensed subject matter, whether as to the information's quality or usefulness or as to the existence of third-party rights to prevent such use.<sup>64</sup> The license merely provides that the property owner (licensor) will not sue for infringement as long as the licensee does not go beyond the scope of the license.<sup>65</sup>

In a frequently cited quotation, the Federal Circuit Court of Appeals stated, "[A] patent license agreement is in essence nothing more than a promise by the licensor not to sue the licensee . . . [e]ven if [the promise is] couched in terms of '[L]icensee is given the right to make, use, or sell X.'"<sup>66</sup> This language reads into the transaction a passive relationship as to the use of the patented subject matter, even though the contract language might suggest a more active connotation—for example, a licensed "right" to use the subject matter.

This view explains important aspects of modern licensing law and practice. Consider, for example, the way in which many courts treat the "rights" of a nonexclusive licensee. A license is a mere waiver of the right to sue for infringing conduct and a nonexclusive license does not give the licensee assurance that the same waiver will

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license . . . was in essence only a right not to be sued for manufacturing items contained in the 485 patent.").

63. See *Exxon*, 109 F.3d at 1074–77. "Phase-out agreements," which allowed those who were allegedly infringing or diluting the Exxon mark to discontinue the use of their offending marks over a period of time, were not "naked licenses" that invalidated the underlying mark. The district court found that these agreements were not licenses at all since they were not designed to permit "third parties to continue misleading uses of Exxon's mark" but were rather meant to halt "such activities" without litigation. The Fifth Circuit focused not on the motivation for the transaction but on whether, in the absence of the agreement, an infringement would occur. A consent-to-use agreement could be employed (without quality controls) where there would be "no likelihood of confusion in the marketplace," otherwise a licensee had to be employed. *Id.*, (citing *In re Mastic, Inc.*, 829 F.2d 1114, 1116 (Fed. Cir. 1987); see also *In re Mastic* 829 F.2d at 1116–17 (asserting that a license is a permission to use is granted so that the licensee does not infringe on the property owner's rights).

64. *Spindelfabrik*, 829 F.2d at 1081; See *United States v. Studiengesellschaft Kohle*, 670 F.2d 1122, 1127 (D.C. Cir. 1981).

65. *Spindelfabrik*, 829 F.2d at 1081; *Studiengesellschaft*, 670 F.2d at 1127.

66. See *supra* note 60.

not be granted to other persons. Thus, it is easy to see why the courts hold that a nonexclusive license conveys far less than a property right and is little more than a personal agreement not to enforce rights against the licensee.<sup>67</sup> From this perspective, a nonexclusive license provides the licensee with the barest assurance possible, and no vested right that can be transferred to anyone or exercised without risk of third-party claims.

As transactions in information have become more important in commerce, many want to treat a license as an active, commercial relationship that entails reciprocal performance obligations.<sup>68</sup>

However, while parties from different backgrounds may emphasize the passive or active nature of licenses differently, neither view completely dominates today. Licenses span a continuum of increasing complexity in the relationships they create. At one end of the continuum lies a “pure” license, which may involve no more than a promise not to sue.<sup>69</sup> At the other end are complex commercial relationships involving commitments to provide services, goods, information, support, and a grant of rights to use technology or other information. While all licenses share a fundamental structure and focus, the farther apart on the continuum the transactions lie, the farther apart are the default rules that should govern.

Under either view, a license is a conditional, limited transfer.<sup>70</sup> In commerce, a rights owner has numerous options for how to commercialize the informational property. One option is to sell all

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67. See *In re CFLC, Inc.*, 89 F.3d 673, 677 (9th Cir. 1996); *MacLean Assocs., Inc. v. William M. Mercer-Meidinger-Hanson, Inc.*, 952 F.2d 769, 778 (3rd Cir. 1991) (stating that a nonexclusive license is not a transfer of ownership); *Harris v. Emus Records Corp.*, 734 F.2d 1329, 1333 (9th Cir. 1984) (copyright license); *In re Patient Educ. Media, Inc.*, 210 B.R. 237, 240 (Bankr. S.D.N.Y. 1997) (copyright license).

68. See *MacLean*, 952 F.2d at 779 (A licensor can bring a suit for copyright infringement if the licensee’s use goes beyond the scope of the nonexclusive license, demonstrating that any action taken beyond that of an ordinary commercial relationship can result in legal repercussions.).

69. See Raymond T. Nimmer, *Licensing in the Contemporary Information Economy*, 8 WASH. U. J.L. & POL’Y 99, 119 (2002) (“In many transactions, licenses entail complex agreements, while in others they merely waive the right to sue.”); see also *Gen. Talking Pictures Corp. v. W. Elec. Co.*, 304 U.S. 175, 181 (1938).

70. Nimmer, *supra* note 69, at 119 (“Under this definition, a license authorizes limited or conditional access to or use of information.”); see UNIF. COMPUTER INFO. TRANSACTIONS ACT § 102(a)(41); *MacLean*, 952 F.2d at 778–79.

rights in it. Traditional terminology describes this as an “assignment.”<sup>71</sup> The more normal commercial alternative is to conditionally grant some rights or privileges to use the property. It is to this type of transaction that the term “license” applies.<sup>72</sup>

Thus, a copyright owner might grant licenses that allow licensees to publicly perform the licensed work (in a theater, for example) but not permit modifying the works. Alternatively, the owner may grant licenses that allow making a single copy but no others. In both cases, the withheld rights are within the scope of the intellectual property involved; going outside the scope of the license both breaches the contract and infringes the copyright. Similarly, patent owners may grant licensees the right to use a patented printer cartridge once but no more. The right to control use of a patented invention is one of the patent owners’ rights.<sup>73</sup>

A license of intellectual property gives the licensee a contractual right or privilege to engage in actions that would otherwise constitute infringement, but the licensor maintains rights in the intellectual property and with respect to any copy that it delivers to the licensee.<sup>74</sup> In a license, the licensees do not receive the right to do whatever they please with respect to the informational asset or copy.<sup>75</sup> The license is not a full conveyance of rights in the information.<sup>76</sup> The scope of the rights given defines what value or product is being conveyed.<sup>77</sup> To understand this, consider the difference between a license to make a single copy of a computer program for personal use and a license to make 10,000 copies for distribution. In this illustration, the initial copy delivered to the

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71. See *Hudson Props. Co., Inc. v. Governing Bd.*, 168 Cal. App. 3d 63, 72 (1985) (stating that “an assignment is the ‘transfer of title to any kind of property,’” requiring “‘manifestation to another person by the owner of the right indicating his intention to transfer, without further action or manifestation of intention’” (citation omitted)).

72. See generally Nimmer, *supra* note 69, at 119–24; see, e.g., *Exxon Corp. v. Oxxford Clothes, Inc.*, 109 F.3d 1070, 1076 (5th Cir. 1997).

73. See Nimmer, *supra* note 69, at 127; 35 U.S.C. §§ 101–04 (2000).

74. See *United States v. Studiengesellschaft Kohle*, 670 F.2d 1122, 1127 (D.C. Cir. 1981) (“[A] licensee waives [the patentee’s] right to judicial relief against what, but for the license, would be an infringement.”).

75. See, e.g., *MacLean* 952 F.2d at 778.

76. See *id.*

77. See Nimmer, *supra* note 69, at 130 (“The license, if any occurs, reflects the parties’ bargain about the scope of the rights conveyed, the conditions on which they are given, and of course the price.”).

licensee would be the same program, but the value each licensee receives (and pays for) is very different.

The use of a “license,” however, does not depend on a property-rights base. Rather, it depends on how parties handle valuable information by contract and what restrictions or permissions are established with respect to that information.<sup>78</sup>

Licensing law is the product of interaction between contract rights, property rights, and public policy.<sup>79</sup> Contract law dominates, but the doctrines and issues generated by this interaction are different in kind and content than those related to transactions involving the sale of ordinary goods (as are the commercial transactional needs of the parties). While saying that an issue involves “contract law” suggests homogeneity, that superficial impression masks a body of remarkably diverse law and doctrine. Embodied in contract law are widely divergent clusters of applicable legal principles. The principles relevant for one transaction type may not be wholly relevant to other transactions.<sup>80</sup>

As with most commercial contracts, licenses absorb unique qualities from various sources. These include the commercial contexts in which they are used, the relationships they create, their underlying subject matter, and the intersection among legal doctrines and public policy considerations.<sup>81</sup> In this regard, licensing law reflects a pattern found in numerous other areas of contract law.

In a license of intellectual property rights, the contract terms defining the scope of the license delineate a boundary between two areas: the area in which the licensor may enforce its rights regarding the licensee’s use of the information, and the area in which it may not do so, as long as the license exists.<sup>82</sup> This is not the only

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78. *See, e.g., Register.com, Inc., v. Verio, Inc.*, 356 F.3d 393, 399–400 (2d Cir. 2004); *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447, 1454 (7th Cir. 1996) (involving a contract that limits use of a database to consumer purposes); *Siedle v. Nat’l Ass’n of Secs. Dealers, Inc.*, 248 F. Supp. 2d 1140, 1141–45 (M.D. Fla. 2002).

79. *See* Nimmer, *supra* note 69, at 113–18.

80. *See, e.g.,* U.C.C. § 2-102 (2003) (Article 2 “does not apply to any transaction which although in the form of an unconditional contract to sell or present sale is intended to operate only as a security transaction.”).

81. *See* Karl Llewellyn, *On Philosophy in American Law*, 82 U. PA. L. REV. 205, 205 n.\* (1934) (“‘One system of precedent’ we may have, but it works in forty different ways.”).

82. *See, e.g., Sun Microsystems v. Microsoft*, 188 F.3d 1115, 1122 (9th Cir.

influence that property or information law doctrines exert on licensing transactions. Indeed, intellectual property law may influence such transactions in at least five general ways:

- property rights may comprise part of the consideration for the contract;<sup>83</sup>
- property rights may provide background rules that, in part, define the parties' relationship where the agreement is silent;<sup>84</sup>
- property rights provide noncontractual remedies for some breaches of the license;<sup>85</sup>
- property rights law sometimes imposes certain specific requirements for an effective transaction (e.g., writing, quality controls, etc.);<sup>86</sup> and
- property rights may provide a basis under which a licensor or licensee can assert rights against third-parties who were not participants in the license agreement.<sup>87</sup>

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1999) (“The enforcement of a copyright license raises issues that lie at the intersection of copyright and contract law, an area of law that is not yet well developed.”).

83. *See, e.g.,* Swannell v. Wilson, 400 Ill. 138, 140–41 (1948) (finding that a “plaintiff’s right to take full title upon survivorship was a valuable property right which was part of the consideration in the property settlement [contract]”).

84. *See supra* note 60; *see infra* note 89.

85. *See* Brennan’s Inc. v. Dickie Brennan & Co., 376 F.3d 356, 368 (5th Cir. 2004) (noting that “trademark law provides more numerous and generous remedies than contract law”).

86. *See infra* note 97.

87. This point reflects an important distinction between intellectual property licensing and commercial transactions involving the sale of goods. One test for the presence of property rights is whether restrictions on permitted uses of the putative property extend vertically through a chain of transfers to third parties without a contractual framework. *See* RESTATEMENT (THIRD) OF PROP.: SERVITUDES, at xxiii–xxvii, § 2.2 cmt. (Tentative Draft No. 1, 1989); RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 1.1 cmts. a, b, d (Tentative Draft No. 7, 1998) (defining property by reference to survival after transfer).

With narrow exceptions, in intellectual property law, there is no rule that protects a bona fide purchaser of a license. *See* Rhone-Poulenc Agro, S.A. v. DeKalb Genetics Corp., 284 F.3d 1323, 1331 (Fed. Cir. 2002) (noting that neither copyright law nor patent law protects a bona fide purchaser). As a result, an upstream transaction in a distribution system that violates the contract and intellectual property rights of a license allows the licensor to assert an infringement claim against a third party who, even in good faith, acquires the license from an unauthorized vendor. *See, e.g.,* Microsoft Corp. v. Grey Computer, 910 F. Supp. 1077 (D. Md. 1995); Microsoft Corp. v. Harmony Computers & Elecs., Inc., 846 F. Supp. 208 (E.D.N.Y. 1994).

As these examples illustrate, while property rights are not essential to a contractual license, when they are part of the license package, actions outside the granted scope of the license may invoke both contract remedies and property rights remedies.

Property rights also shape expectations about the contractual relationship. As we have seen, a license often takes the form of a covenant not to sue (in other words, a waiver or release), rather than an affirmative grant.<sup>88</sup> In many patent licenses, for example, the licensor merely grants to the licensee an immunity from suit for infringement of the licensor's specified patent rights, whether expressly stated or not.<sup>89</sup> This formulation traces to the nature of patent rights: a patent does not give affirmative rights to the patent owner. Rather, patents merely give a right to preclude others from certain actions involving the patented subject matter.<sup>90</sup> In fact, patents are often subject to blocking patents—that is, one party's use of its own invention might be blocked by a third-party patent owner whose patent would be infringed by that use.<sup>91</sup> Thus, the patent holder may be able to exclude unauthorized use by others but does not have the power to use the invention itself if doing so would infringe upon the rights of another person.<sup>92</sup> Given this background, viewing patent licenses as mere covenants not to sue (or immunity from suit) is supported by the property right itself.

Since licensors are assumed to merely agree not to assert claims, the general theory is that they provide no implicit assurance that the licensees' use of the invention will not infringe the rights of others.<sup>93</sup>

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88. *See supra* note 60.

89. *Id.*; *see, e.g.*, *Cohen v. Paramount Pictures Corp.*, 845 F.2d 851 (9th Cir. 1988) (holding that a license for use of musical composition in film conferring right to exhibit film "by means of television" did not include the right to distribute videocassettes of the film for home viewing).

90. 35 U.S.C. § 271(a) (2000).

91. *See Standard Oil Co. v. United States*, 283 U.S. 163, 171 n.5 (1931) ("A patent may be rendered quite useless, or 'blocked,' by another unexpired patent which covers a vitally related feature of the manufacturing process. Unless some agreement can be reached, the parties are hampered and exposed to litigation."); *CCPI Inc. v. Am. Premiere, Inc.*, 967 F. Supp. 813, 819 n.13 (D. Del. 1997) (Blocking patents occur "when two or more patents seem to be closely related, and none of the title holders can use its rights under the patent without fear of treading on the rights of the title holders of the other related patents.").

92. *See supra* notes 90–91.

93. *See Spindelfabrik Suessen-Schurr Stahlecker & Grill v. Schubert & Salzer Maschinenfabrik Aktiengesellschaft*, 829 F.2d 1075, 1081 (Fed. Cir. 1987), *cert. denied*, 484 U.S. 1063 (1988)

A different rule would implicitly convey an assurance to licensees that the licensors may not themselves possess. That assurance can be expressly given,<sup>94</sup> but it should not be presumed. Thus, property rights shape how the terms of a license are constructed and at least substantial parts of patent licensing practice.

As this suggests, there is an interaction between contractual default rules and intellectual property norms. However, the nature of the underlying rights in reference to intellectual property law differs significantly from the assumptions about ownership and control associated with the sale of goods. It is not that the intellectual property rights control or dictate the scope of contractual freedom.<sup>95</sup> Rather, the point is that contract law default rules or assumptions may borrow from the terms of the underlying property rights law.

The same point can be made for other types of intellectual property licensing. For example, in a trade-secret license, should a presumption about confidentiality be adopted as a default rule? Retaining confidentiality of the licensed information is relevant to retaining the property right itself.<sup>96</sup> A presumption of confidentiality may be appropriate. A similar question can arise in trademark licensing. In that context, the issue is whether a court or the parties should presume that the licensor retains the right to control the quality of the licensee's performance, since quality controls may be central to avoiding abandonment of the mark itself.<sup>97</sup>

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94. See U.C.C. § 1-102(3) (1998) (amended 2003).

95. See *Davidson & Assocs., Inc. v. Jung, Inc.*, 422 F.3d 630 (8th Cir. 2005) (holding an end user license effective to preclude reverse engineering of software); *Bowers v. Baystate Techs., Inc.*, 320 F.3d 1317 (Fed. Cir. 2003), *cert. denied*, 539 U.S. 928 (2003) (holding shrinkwrap license effective to preclude reverse engineering of software).

96. See RAYMOND T. NIMMER, *THE LAW OF COMPUTER TECHNOLOGY: RIGHTS, LICENSES, LIABILITIES* § 3.3 (3d ed. 1997 & Supp. 2006).

97. See *Stanfield v. Osborne Indus., Inc.*, 52 F.3d 867, 871 (10th Cir. 1995) ('Naked (or uncontrolled) licensing of a [trade]mark occurs when a licensor allows a licensee to use the mark on any quality or type of good the licensee chooses.');

*Barcamerica Int'l USA Trust v. Tyfield Imps., Inc.*, 289 F.3d 589, 596 (9th Cir. 2002) (stating that uncontrolled or naked licensing may result in the owner being estopped from enforcing the mark); *Exxon Corp. v. Oxxford Clothes, Inc.*, 109 F.3d 1070, 1075 (5th Cir. 1997); *Moore Bus. Forms, Inc. v. Ryu*, 960 F.2d 486, 489 (5th Cir. 1992); *Gorenstein Enters., Inc. v. Quality Care-USA, Inc.*, 874 F.2d 431, 435 (7th Cir. 1989) ("The owner of a trademark has a duty to ensure the consistency of the trademarked good or service. If he does not fulfill this duty, he forfeits the trademark. The purpose of a trademark, after all, is to identify a good or service to the consumer, and identity implies consistency and a correlative duty to make

## IV. COMPARISON

As even this limited overview indicates, licensing consists of a body of practice and law that differs significantly from the underlying assumptions in Article 2. The primary subject matter, property rights, commercial practices, and presumed allocation of risk are very different. The difficult questions in licensing are not addressed in sales law or, if addressed, are dealt with in a manner that does not fit licensing practice. This is because information<sup>98</sup> is not goods.<sup>99</sup> Metaphysical considerations should not be used to equate a license of information to a sale or other transaction in goods. Sales law occupies its separate space, and so does licensing law.

A. *Points of Comparison*

Let us take a brief look at a few points of mismatch between the idea of a sale of goods in Article 2 and the idea of a license of information.

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sure that the good or service really is of consistent quality, i.e., really is the same good or service.” (citations omitted)); *Dawn Donut Co. v. Hart’s Food Stores, Inc.*, 267 F.2d 358, 366 (2d Cir. 1959) (The Lanham Act “places an affirmative duty upon a licensor of a registered trademark to take reasonable measures to detect and prevent misleading uses of his mark by his licensees or suffer cancellation of his federal registration.”).

98. See UNIF. ELEC. TRANSACTION ACT § 2(10) (1999) (“‘Information’ means data, text, images, sounds, codes, computer programs, software, databases, or the like.”); 15 U.S.C. 7006(7) (2000); *Green v. Am. Online (AOL)*, 318 F.3d 465, 471 (3d Cir. 2003) (Section 230 barred a claim that AOL was negligent in failing to prevent a third party from using a so-called “punter program” that briefly shut down the plaintiff’s computer. The program was within the definition of “information.”).

99. See, e.g., *Specht v. Netscape Commc’ns Corp.*, 306 F.3d 17, 29 n.13 (2d Cir. 2002); *United States v. Stafford*, 136 F.3d 1109 (7th Cir. 1998); *Architectronics, Inc. v. Control Sys., Inc.*, 935 F. Supp. 425, 432 (S.D.N.Y. 1996) (finding that the predominant purpose of the software license was a transfer of intellectual property rights, not goods); *Fink v. DeClassis*, 745 F. Supp. 509, 515 (N.D. Ill. 1990) (“[T]radenames, trademarks, logos, advertising, artwork, customer lists, sales records, unfulfilled sales orders, goodwill, and licensing agreements” are not “goods.”); see also U.C.C. § 2-103(1)(k) (2003).

1. A sale conveys title to  
the goods when the seller completes  
what is required for delivery, but a license  
is a conditional or limited grant of rights or permissions

Article 2 defines a “sale” as a transaction that transfers title of goods to a buyer for a price.<sup>100</sup> In contrast, a license involves a limited transfer of rights privileges to use information.<sup>101</sup> The two engage very different transactional assumptions. Even where the license involves delivery of a tangible copy of information, a license splits possession and ownership rights in a manner analogous to a lease, but with the focus on the privileges to use the information or intellectual property rights in it, not the copy.<sup>102</sup>

In licensing practice, however, circumstances exist in which the licensee’s ownership of a tangible copy might affect the transferee’s noncontractual, intellectual property privileges. This occurs in connection with the so-called “first sale” or “exhaustion” doctrine.<sup>103</sup> Under these intellectual property doctrines, an owner of a copy of a copyrighted work or a patented invention obtains certain limited privileges to use or transfer that copy in ways that would otherwise infringe on the transferor’s intellectual property rights.<sup>104</sup>

In some transactions, a question arises as to whether the licensee is an owner of the copy.<sup>105</sup> Several courts have asked whether the UCC’s rules on title should apply.<sup>106</sup> The answer is no—a license is not a sale, and the default rule regarding ownership of a licensed copy does not hinge on Article 2. For example, the Ninth Circuit held that a licensee is not the owner of a copy simply because it was

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100. U.C.C. § 2-106(1) (2003).

101. *See* UNIF. COMPUTER INFO. TRANSACTIONS ACT § 102(a)(41) (2002).

102. *See id.* § 102 cmt. 37.

103. “[T]he first sales doctrine provides that where a copyright owner parts with title to a particular copy of his copyrighted work, he divests himself of his exclusive right to vend that particular copy. While the proprietor’s other copyright rights (reprinting, copying, etc.) remain unimpaired, the exclusive right to vend the transferred copy rests with the vendee . . . .” *United States v. Wise*, 550 F.2d 1180, 1187 (9th Cir. 1977).

104. *See* 17 U.S.C. § 109 (2000); *Monsanto Co. v. McFarling*, 302 F.3d 1291 (Fed. Cir. 2002), *cert. denied*, 537 U.S. 1232 (2003).

105. *See infra* notes 107–108.

106. *See, e.g.,* *Novell, Inc. v. Network Trade Ctr., Inc.*, 25 F. Supp. 2d 1218, 1230 (D. Utah 1997), *vacated in relevant part by* 187 F.R.D. 657 (D. Utah 1999) (U.C.C. applies); *Applied Info. Mgmt., Inc. v. Icart*, 976 F. Supp. 149, 154 & n.2 (E.D.N.Y. 1997) (U.C.C. applies); *United States v. Drebin*, 557 F.2d 1316, 1330 (9th Cir. 1977) (U.C.C. does not apply).

a licensee.<sup>107</sup> The Court of Appeals for the Federal Circuit concluded that whether the licensees become owners depends on the terms of the license and whether those terms restrict the licensees' use of the information in ways inconsistent with them being owners.<sup>108</sup> The Uniform Computer Information Transactions Act (UCITA) adopts the same view.<sup>109</sup>

The default rules are different because the transaction is different. A license does not routinely entail an intent by the licensor that it is transferring unrestricted title and use to the licensee. Quite the contrary, the expectation is that the copy is a mere conduit for providing the information<sup>110</sup> and that rights or privileges to use the information are controlled by the terms of the contract.<sup>111</sup>

2. Article 2 provides that,  
in a sale, any reservation of title in the seller  
is limited to a security interest, while licensing law  
and practice give effect to contract terms on retention of title

Article 2's treatment of a reservation of title in a sale is consistent with the practice in goods industries regarding conditional sales. That is, they are governed under the security interest law in Article 9 because a retained title in a sale is typically part of a financing arrangement.<sup>112</sup>

In licensing, however, retaining title to the copy is not associated with financing. Instead, it is typically related to a package of terms that sets control of the use of the licensed information.<sup>113</sup> In short, it

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107. See *MAI Sys. Corp. v. Peak Computer, Inc.*, 991 F.2d 511 (9th Cir. 1993), *cert. denied*, 510 U.S. 1033 (1994) (finding that a license, by its nature, does not transfer ownership of an underlying copy of a program).

108. See *DSC Commc'ns Corp. v. Pulse Commc'ns, Inc.*, 170 F.3d 1354 (Fed. Cir. 1999); see also *Krause v. Titleserv, Inc.*, 402 F.3d 119 (2d Cir. 2005); *Microsoft Corp. v. Grey Computer*, 910 F. Supp. 1077 (D. Md. 1995); *Microsoft Corp. v. Harmony Computers & Elecs., Inc.*, 846 F. Supp. 208 (E.D.N.Y. 1994).

109. UNIF. COMPUTER INFO. TRANSACTIONS ACT § 502 (2002).

110. See *id.* § 102 cmt. 37.

111. See *supra* notes 107–109.

112. U.C.C. § 2-501 (2003).

113. See *Mallinckrodt, Inc. v. Medipart, Inc.*, 976 F.2d 700, 704–05 (Fed. Cir. 1992) (“The patentee may grant a license ‘upon any condition the performance of which is reasonably within the reward which the patentee by the grant of the

is a substantive part of the transaction.

Courts that have addressed this question in licensing agreements give effect to the retention of title.<sup>114</sup> In doing so, they are recognizing the nature of the transaction as a limited or conditional permission to use information or intellectual property rights that are controlled by the licensor.

3. Article 2 provides that, in a sale,  
the seller warrants that the goods are not infringing  
as delivered, while in licensing, the presumption is that  
no assurances of non-infringement are given unless expressly made

The Article 2 statutory warranty of non-infringement is consistent with the premise that a seller of goods undertakes several implicit obligations about the quality and usability of the goods *as delivered*.<sup>115</sup> The assumption is at odds with the assumption in licensing that a licensor does not give any assurance that use of the licensed information will not violate third-party rights. Instead, a nonexclusive license is a mere covenant not to sue the licensee for actions within the scope of the license that would otherwise infringe the licensor's rights.<sup>116</sup>

There are indeed two very different types of transactions. Obviously, in a sale, a seller can disclaim the warranty, and in a license, a licensor can expressly warrant noninfringement. However, the point is that the two transactions start with diametric premises.

4. Under Article 2, contract rights  
can be assigned unless the assignment would  
materially harm the other party, while in licensing,  
a non-exclusive license cannot be assigned by the licensee without  
the licensor's permission

The Article 2 rule on transferability of contract rights parallels general common law and also reflects the presumptive context in which the rule operates.<sup>117</sup> Basically, transfers of rights are

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patent is entitled to secure.” (quoting *United States v. Gen. Elec. Co.*, 272 U.S. 476, 489 (1926)); *Monsanto Co. v. McFarling*, 302 F.3d 1291 (Fed. Cir. 2002), *cert. denied*, 537 U.S. 1232 (2003).

114. *See supra* note 113.

115. U.C.C. §§ 2-312, 2-314 (2003).

116. *See supra* note 60.

117. U.C.C. § 2-210 (2003).

presumptively effective in the absence of potential harm to the other party.<sup>118</sup> That potential of harm will seldom occur where the contract is assigned by the buyer to a third-party since the buyer's only remaining performance is accepting and paying for the goods. It is potentially more problematic where the assignment is by a seller with special skills or circumstances important to the buyer.<sup>119</sup>

The default rule in nonexclusive licenses is that assignment of the license by the licensee is ineffective unless the licensor consents.<sup>120</sup> There are numerous reasons for this rule. Historically, the rule was grounded in the idea that a covenant not to sue is a personal right, presumptively nontransferable.<sup>121</sup> However, the rule is also grounded in the nature of information assets and licensed intellectual property rights.<sup>122</sup> Effectively, given the nature of informational rights, licensees could otherwise become limited competitors with their licensors.<sup>123</sup> The Ninth Circuit phrased the matter in the following way:

The fundamental policy of the patent system is to “encourage the creation and disclosure of new, useful, and non-obvious advances in technology and design” by granting the inventor the reward of “the exclusive right to practice the invention for a period of years.” Allowing

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118. *Id.*

119. *Id.*

120. *See In re CFLC, Inc.*, 89 F.3d 673, 679 (9th Cir. 1996) (holding that as a matter of federal policy, nonexclusive licenses cannot be transferred without the consent of the licensor.); *Gilson v. Rep. of Ireland*, 787 F.2d 655, 658 (D.C. Cir. 1986) (“It is well settled that a non-exclusive licensee of a patent has only a personal and not a property interest in the patent and that this personal right cannot be assigned unless the patent owner authorizes the assignment or the license itself permits assignment.”); *Harris v. Emus Records Corp.*, 734 F.2d 1329, 1334 (9th Cir. 1984) (copyright license not transferable without consent); *PPG Indus., Inc. v. Guardian Indus. Corp.*, 597 F.2d 1090, 1093 (6th Cir. 1979), *cert. denied*, 444 U.S. 930 (1979); *Unarco Indus., Inc. v. Kelley Co.*, 465 F.2d 1303, 1306 (7th Cir. 1972), *cert. denied*, 410 U.S. 929 (1973); *Rock-Ola Mfg. Corp. v. Filben Mfg. Co.*, 168 F.2d 919, 922 (8th Cir. 1948), *cert. dismissed*, 335 U.S. 855, and *cert. denied*, 335 U.S. 892 (1948) (“The mere granting of a license . . . does not confer upon the licensee the right to transfer his license unless the patentee has consented thereto.”); *In re Patient Educ. Media, Inc.*, 210 B.R. 237 (Bankr. S.D.N.Y. 1997) (nonexclusive copyright license in photographs not transferable without consent).

121. *See In re CFLC, Inc.*, 89 F.3d at 677; *Gilson*, 787 F.2d at 658; *Harris*, 734 F.2d at 1334; *PPG Indus., Inc.*, 597 F.2d at 1093; *Unarco Indus., Inc.*, 465 F.2d at 1306; *In re Patient Educ. Media Inc.*, 210 B.R. at 240.

122. *See In re CFLC, Inc.*, 89 F.3d at 679.

123. *See id.*

states to allow free assignability . . . of nonexclusive patent licenses would undermine the reward that encourages invention because a party seeking to use the patented invention could either seek a license from the patent holder *or* seek an assignment of an existing patent license from a licensee. In essence, every licensee would become a potential competitor with the licensor-patent holder in the market for licenses under the patents.<sup>124</sup>

Restricting transferability reflects the unique character of intellectual property: it is an asset that does not lose value or condition from use. Accordingly, allowing the licensee to transfer rights under a license would allow the licensee to compete with its licensor on exactly the same work or product that the licensor offers. The policy that precludes this covers patent, copyright, and software licenses.<sup>125</sup>

### B. The Broader Picture

There are more illustrations of the mismatch between assumptions in Article 2 and those governing licensing of informational assets. This should not be a surprise. Different subject matter, different industries, different time frames, and different commercial objectives combine to provide an environment in which default rule assumptions should be far different than the world of commerce in the sale of goods. Given those differences, it would be a mistake to claim that the assumptions built around the sale of goods should be transported to the world of licensing.

However, beyond wrong answers or assumptions in Article 2, there are also many things that Article 2 does not address that are important in licensing. Briefly, let me focus on one general principle: since it presumes a transaction involving a sale and transfer of full title to the buyer, Article 2 provides no guidance or assumptions about postdelivery uses of the goods (except in reference to handling defective products<sup>126</sup>). This corresponds to the assumption that the new owners of the goods can do what they will

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124. *Id.* (citations omitted).

125. *See id.* (patent license); *Harris*, 734 F.2d 1329 (copyright license); *In re Patient Educ. Media, Inc.*, 210 B.R. 237 (debtor in bankruptcy could not assign its nonexclusive license in photographs used in videotapes without the copyright owner's consent).

126. *See, e.g.*, U.C.C. § 2-601 (2003).

with those goods.<sup>127</sup> What this means, however, is that Article 2 does not even vaguely address the many issues important to licensing contracts related to enforcing (or interpreting) restrictions on the use. Such ongoing restrictions are increasingly important in modern commerce.<sup>128</sup>

The point is not that Article 2 rules are wrong as to the ongoing obligations (unless one assumes that the silence of Article 2 means such restrictions are ineffective), but that it offers no guidance on important issues in licensing.

## V. CONCLUSION

Let us return to the perspective with which this piece began. To ask questions about the need to contract around Article 2 or the right to do so assumes that Article 2 has and should continue to have some broad influence beyond its own limited scope and perspective. That may be relevant as to the basic premise that express agreements control, and to the general themes that Article 2 helped make part of modern law. However, when looking at the sales-related rules of Article 2 and their potential application to modern areas of contemporary commerce, that assumption is simply wrong.

As we have seen, the sale-bias rules of Article 2 are a poor match with the commercial context of licensing. The simplistic sales model that lies at the heart of Article 2 (at least as to the category-three rules) bears little relationship to the commercial expectations and background law applicable to modern licensing relationships. Attempting to force licensing arrangements into that older framework would be an exercise in futility and a fundamental mistake. The world of transactions in the sale of goods remains important in commerce, but it has and will continue to cede its once-dominant position to the world of transactions in information and intellectual property rights.

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127. *See id.*

128. *See Jazz Photo Corp. v. United States*, 439 F.3d 1344 (Fed. Cir. 2006); *Ariz. Cartridge Remfrs. Ass'n v. Lexmark Int'l, Inc.*, 421 F.3d 981, 988 (9th Cir. 2005) (holding contract terms enforceable because company's use of restrictive contract and technology did not violate California's "unfair competition" or "false ad" laws); *Monsanto Co. v. McFarling*, 302 F.3d 1291 (Fed. Cir. 2002).