

NOT.COM: COMMERCIAL LAW AT THE CROSS-CODES?

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In a 1970 speech at Ohio State University, Grant Gilmore famously declared contract dead. See GRANT GILMORE, *THE DEATH OF CONTRACT*, vii (Ohio St. 1974). Although rumors of contract's death have proved to be greatly exaggerated, it nevertheless remains fashionable to ask whether various commercial subjects have much life left. Thus, we have a robust literature on the putative demise of, among others, secured lending, negotiability and liability in general. It is perhaps no coincidence that the title of this conference takes the Blues' symbol for mortality – The Crossroads.

This essay is not quite so morbid. I suggest that commercial law is not threatened with extinction, but is instead changing in subtle yet profound ways. Commercial law is not dead, but may be at a crossroads – or perhaps a “cross-codes” -- formed by the distinct, increasingly incompatible roles that information plays in commerce.

On the one hand, information – *e.g.*, data, intellectual property -- is increasingly the *subject* of commerce. As Rochelle Cooper Dreyfuss has observed, “information, like time, is money.” Rochelle Cooper Dreyfuss, *Warren and Brandeis Redux: Finding (More) Privacy Protection in Intellectual Property Lore*, 1999 STAN. TECH. L. REV. 8. As such, it is governed by its own “codes,” *e.g.* intellectual property law and similar rules. On the other hand, efficient information production has long been an *object* of “our” code, the UCC.

These roles of information (and their codes) conflict in at least two ways. First, the law of information – and in particular the law of intellectual property – has uncertain preemptive force. For a variety of doctrinal reasons, it is not always clear whether the law of information (*e.g.*, copyright) or the UCC will govern commercial transactions involving information. Second, information transactions are often governed by pure contract, and not the UCC (or other uniform, mandatory rules). In either case, the rules and norms of information law will increasingly displace the rules and norms of the UCC. Yet, while these other rules and norms may *involve* information – they may, for example, govern a license of copyrights – they will not necessarily *produce* information with the rigid efficiency that has been a hallmark of the UCC.

The thesis of this essay is therefore that the law of information may, paradoxically, erode rules and norms in commercial law that foster the production of information needed to contract in a fair and efficient way. By displacing the UCC, the rules and codes of the “dot.com” world may, if we are not careful, produce an informational void, a “not.com.”

I. One Code – The UCC and Informational Efficiency

We don't usually talk about it this way, but the UCC is in its essence a set of rules about information. Its success is due at least in part to its ability to solve difficult

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problems in the production and distribution of information needed to contract. Although this is apparent in a number of ways, consider two just examples – the development of the negotiable instrument and the UCC-1 financing statement.

A. The Negotiable Instrument

Those of us who teach payments often struggle to explain Article 3’s rigid, seemingly senseless, rules on negotiable form. How, for example, do we justify hoary words of negotiability in a world where most important payment transactions won’t involve paper, much less words like “bearer” or “order?”

One way to understand the development of the negotiable instrument rules is informational. In order to create liquidity in the 18th and 19th centuries, commercial law had to make it possible for remote purchasers of paper to know cheaply and with great certainty the payment rights they were obtaining. Commercial law solved this problem by forcing – “merging” – the relevant legal information into the instrument itself, in a standardized form. “[T]he idea [was],” Gilmore explained “that the piece of paper on which the bill was written or printed should be treated as if it – the piece of paper – was itself the claim or debt which it evidenced.” Grant Gilmore, *Formalism and the Law of Negotiable Instruments*, 13 CREIGHTON L. REV. 441, 448-49 (1979). Negotiable instruments became “couriers without luggage” (*Overton v. Tyler*, 3 Pa. 346, 347 (1846)) because negotiability “facilitate[d] commercial transactions by minimizing the administrative burdens of processing information about property rights.” Jane Kaufman Winn, *Couriers Without Luggage: Negotiable Instruments and Digital Signatures*, 49 S.C. L. REV. 739, 740 (1998).

B. The Article 9 Security Interest

We can tell a similar story about the development of the UCC-1 financing statement. The financing statement swept away the many complex, cumbersome notice devices that preceded it under the many different security statutes prior to the UCC. “The typical pre-Code pattern,” Gilmore explained, “included separate filing systems for chattel mortgages, for conditional sales, for trust receipts, for factor’s liens, and for assignments of accounts receivable.” See 1 GRANT GILMORE, *SECURITY INTERESTS IN PERSONAL PROPERTY* (1965), at § 15.1, p. 463.

Like the rules on negotiable form, the rules on perfecting a security interest simplified and standardized the production of information. If you wanted to borrow money, you had to execute a piece of paper that set forth the important payment rights that anyone might have against you (and little else). If you wanted to take a security interest in the borrower’s collateral, you had to make sure that simple notice of this was given. The UCC made both possible on a standardized and nationwide basis.

I don’t mean to oversell this informational point. Commercial law has also developed in response to many other concerns, including questions of efficiency, fairness, and (sometimes crass) politics. But we should remember that some of the most important mandatory rules in the UCC developed as a means of generating and standardizing information needed to promote the underlying goals of commercial law, *i.e.* “to simplify, clarify and modernize the law governing commercial transactions.” UCC § 1-103(a)(1).

II. Other Codes: The Law and Reality of Information as Commodity

The problem, of course, is that the UCC's rules developed in response to a world with vastly different economies, technologies and rules. If we started today with a clean slate, we probably wouldn't choose the same rules on negotiable form or financing statements because information technologies would perform (or render obsolete) many of these functions. The question would then be whether these new technologies and their rules ("codes") deal with information production – information as object – as well as or better than the UCC. My instinct is to believe that they do not, at least not yet.

A. Intellectual Property – The Problem of Preemption

Consider first the problem of preemption. At the risk of gross oversimplification, information law is largely the law of intellectual property, which is sometimes (but not always) federal law. *See, e.g.*, 17 U.S.C. § 301(a) (1994) (Copyright Act preempts state law). Until recently, copyright law – arguably the most important, since it protects rights in software -- swept the field. The *Peregrine* case, for example, held – to much chagrin – that the Copyright Act preempted Article 9's notice-filing rules, even where copyrights were not registered. *See Nat'l Peregrine, Inc. v. Capitol Fed. Sav. & Loan Ass'n of Denver (In re Peregrine Entm't Ltd.)*, 116 B.R. 194 (C.D. Cal. 1990). More recent case law, however, holds that the Copyright Act will preempt the UCC only if the underlying copyright was registered with the Copyright Office. *See Aerocon Eng'g v. Silicon Valley Bank (In re World Auxiliary Power Co.)*, 303 F.3d 1120 (9th Cir. 2002).

Preemption undermines informational efficiency in at least two ways. First, to the extent that the Copyright Act governs the creation and perfection of security interests, its rules and norms on information production and standardization will displace those of the UCC. The problem is that the informational architecture of the Copyright Office is organized around designating and protecting rights in works of authorship. It only incidentally (and grudgingly) deals with liens. This "systemic asymmetry" adds information costs. *See* Jonathan C. Lipson, *Financing Information Technologies: Fairness and Function*, 2001 WIS. L. REV. 1067, 1104-22.

Second, and more subtly, we do not really know when the federal rules will preempt the UCC. This is due partly to the fact that preemption doctrine is "muddled *in general*". *See* Caleb Nelson, *Preemption*, 86 VA. L. REV. 225, 233 (2000) (emphasis in original). It also reflects the difficulty we have in categorizing "mixed" goods, *e.g.* copyright-protected software embedded in goods. *See, e.g.*, Ann Lousin, *Proposed UCC 2-103 of the 2000 Version of the Revision of Article 2*, 54 SMU L. REV. 913, 913 (2001).

B. Pure Contract

Even if federal law does not control, we must also contend with the expanding role of pure contract, chiefly in the form of the license. The license – an agreement not to sue for infringement -- is the dominant contractual form for transactions in software and other informational rights. Yet, unlike sales of goods (or negotiations of instruments or perfection of security interests, or anything else which the UCC governs), no standard (or helpful) set of informational rules applies to licenses.

Consider, for example, the *ProCD* case. *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447 (7th Cir. 1996). There, the Seventh Circuit Court of Appeals concluded that a "shrinkwrap"

license was binding on the purchaser of a CD-ROM, even though the terms could not be seen until after the disk was purchased. The Uniform Computer Information Transactions Act (UCITA) similarly envisions what Maureen O'Rourke characterizes as "pay now, terms later" contracts. See Maureen A. O'Rourke, *Progressing Towards a Uniform Commercial Code for Electronic Commerce or Racing Towards Nonuniformity?*, 14 BERKELEY TECH. L.J. 635, 651 (1999).

The problem with these forms of "private legislation" is informational. These contracts are "valid against the world" even though neither the "world" -- nor even all parties -- necessarily know their terms. See J.H. Reichman & Jonathan A. Franklin, *Privately Legislated Intellectual Property Rights: Reconciling Freedom of Contract with Public Good Uses of Information*, 157 U. PENN. L. REV. 875, 911 (1999). While it may be possible to discover the contract terms (assuming no fraud), it will require much greater investigation than merely reading a promissory note or financing statement. See Jonathan C. Lipson, *Remote Control: Revised Article 9 and the Negotiability of Information*, 63 OHIO ST. L. J. 1327, 1404-1409 (2002).

The rise of contract also has a theoretical impetus. Debates about the role and scope of contract have long dominated commercial law scholarship. See Jonathan C. Lipson, *Secrets and Liens: The End of Notice in Commercial Finance Law*, 21 EMORY BANKR. DEV. J. 419, 473-482 (forthcoming 2005) (discussing debates). Those who support contract in its strongest form dismiss the problem of information costs. Alan Schwartz, for example, has suggested that contracting parties would (at least in theory) prefer a world in which a "true first in time" priority could be conferred exclusively by contract, without any need for notice. See Alan Schwartz, *A Theory of Loan Priorities*, 18 J. LEGAL STUD. 209, 219 (1989).

These informational problems -- preemption and contract -- are not limited to security interests and licenses involving intellectual property. They also drive the increasing fragmentation of payments law. For all its shortcomings, the negotiable instrument is highly efficient, informationally speaking. Increasingly, however, payments will be governed by a patchwork of complex federal, state and contract rules, including the Truth in Lending Act (credit cards), the Electronic Funds Transfer Act (debit cards), and the Automated Clearinghouse rules (wire payments). Parties to these transactions can certainly learn their rights, but it will be a more costly and cumbersome informational endeavor than simply reading within the four corners of a note.

III. At the Cross-Codes

Does this matter? It can, for our teaching and our scholarship.

A. Teaching

We can bring the informational transformation of commercial law into the classroom in at least two ways. First, it creates incentives to approach commercial law from a transactional perspective. If the license is going to become the proto-commercial contract, perhaps we should introduce a form of it in commercial classes early and often.

Second, this problem helps us explore Professor Gilson's claim that business lawyers are (or should be trained to be) "transaction cost engineers," whose job in life is to produce and verify information that promotes efficient and fair contracting. See

Ronald J. Gilson, *Value Creation by Business Lawyers: Legal Skills and Asset Pricing*, 94 YALE L. J. 239 (1984).

B. Scholarship

This can also inform scholarship. First, and most obviously, there is the burgeoning field of cognitive theory, which explores whether our law adequately accounts for the ways we process information. *See generally* BEHAVIORAL LAW AND ECONOMICS (Cass Sunstein ed., 2000); *Symposium: Empirical Legal Realism: A New Social Scientific Assessment of Law and Human Behavior*, 97 NW. U. L. REV. 1075 (2003); Larry T. Garvin, *Small Business and the False Dichotomies of Contract Law*, 40 WAKE FOREST L. REV. 295 (2005); Russell Korobkin, *Bounded Rationality, Standard Form Contracts, and Unconscionability*, 70 U. CHI. L. REV. 1203 (2003).

Second, there is plenty of empirical work to do. While we may have theories about the role information plays in commercial contracting, we have very little data about what really happens. Who actually uses the financing statement system? What other information systems are developing to manage commercial contracting? We can still add to the long and important tradition of empirical legal work in this context. *See, e.g.*, Lisa Bernstein, *Opting Out of the Legal System: Extralegal Contractual Relations in the Diamond Industry*, 21 J. LEGAL STUD. 115 (1992); Lisa Bernstein, *Merchant Law in a Merchant Court: Rethinking the Code's Search for Immanent Business Norms*, 144 U. PA. L. REV. 1765 (1996); Lisa Bernstein, *Private Commercial Law in the Cotton Industry: Creating Cooperation Through Rules, Norms, and Institutions*, 99 MICH. L. REV. 1724 (2001); Stewart Macaulay, *Non-Contractual Relations in Business: A Preliminary Study*, 28 AM. SOC. REV. 55 (1963); Ronald J. Mann, *Explaining the Pattern of Secured Credit*, 110 HARV. L. REV. 625 (1997); Ronald J. Mann, *Secured Credit and Software Financing*, 85 CORNELL L. REV. 134 (1999).

IV. Conclusion

Our commercial law developed in response to the radical 19th century transformation from an economy in which value was stored largely in land and agriculture, to one in which value was increasingly found in personal property. An analogous transformation is under way, from tangible personal property to intangible information. The question will not be whether commercial law survives. It will survive, but in a much different form. Rather, the important question is whether this new code – the law of information – will absorb and reflect the information-forcing rules and norms of the old code -- commercial law. As we prepare to leave the crossroads, will we know where we want to go and how – indeed, whether -- maps should be drawn?