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Gloria Molina

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PROPOSED LEGISLATION

ASSEMBLY BILL NO. 1507: A LEGISLATOR'S PERSONAL PERSPECTIVE

Assemblywoman Gloria Molina*

I. INTRODUCTION

In March of 1985, I introduced Assembly Bill No. 1507(AB1507)¹ to address the issue of warranty protection for buyers of computer products. This measure requires computer manufacturers and sellers to guarantee their products. A buyer would have the right to return the product for up to six months after sale if it is proven that it did not perform according to advertisements or instructions accompanying the product. The impetus for the introduction of this bill stemmed from a \$10,000 computer which I purchased from a leading computer manufacturer. I later learned the computer system never had the hardware capability or the software capability to perform the tasks I expressly bought it for and needed for my office operations.

After a year of promised updates, and the hiring of computer consultants to decipher the new program which had innumerable bugs, I realized this computer system would not deliver as promised, and I began asking for redress. It was at this point that I became aware of the lack of warranties in the computer industry. There was no reasonable recourse, except expensive litigation, and I discovered that there were not even customer service departments in many of these major computer companies.

One would think that a \$10,000 business purchase would have adequate warranty standards so that an individual or business

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* The author is the former Deputy Director of Personnel under the Carter Administration and former Director of Intergovernmental and Congressional Affairs for the Department of Health and Human Services. She presently serves as a member of the California Assembly from the 56th district for East Los Angeles. She also chairs the subcommittee on Mental Health and Developmental Disabilities. First elected to the Assembly in 1982, Assemblywoman Molina was the first Hispanic woman elected to the California Legislature.

1. See Appendix A for a copy of Cal. A.B. 1507, 1985-86 Regular Sess., proposed CAL. CIV. CODE §§ 1797.7 (West 1986).

would not lose on a major equipment investment. For example, the automobile industry commonly provides buyers with some type of warranty which protects the buyer against defects and product "bugs." After further research, it became apparent to me that other consumers were encountering a certain lack of responsibility by the computer industry in the area of product warranties.

II. STATEMENT OF THE PROBLEM

During the past year, computer buyers, engineers, publishers and dealers have called and written my office supporting AB1507. The most common complaint received by my office concerns "as-is" sales. The lack of adequate product testing before marketing has led to computer products with numerous "bugs" and an increased use of "as-is" sales. Computer industry representatives continue to espouse the notion that no program is "bug-free" and, with that caveat, the buyer is warned and the company is off the hook. The race to the marketplace has been cited as the major reason for inadequate testing of products. The practice of getting a product to market first overrides quality control.

Another often cited complaint centers on "truth in advertising." The bulk of advertising in the computer industry often misleads the buying public regarding the ease of use of computers and the present capabilities of a product. Consumers repeatedly tell horror stories of the "elusive update." Usually, the computer system's capability is described in the product's advertisement. After purchase, the buyer discovers that the advertised capability is not there and calls the company. The computer company tells the buyer that the capability will be included in the next update which will be sent to the buyer "soon." The buyer normally has to pay for the update, thereby paying again for what she thought she was getting in the beginning. This cycle is particularly unconscionable to the buyer and extremely harmful to the integrity of the computer industry as a whole.

With errors in the computer program or the documentation, or both, buyers need to get corrections. But where do they get them from? If they go back to the store where they purchased it, the dealer will point out the "as-is" warranty disclaimer which states that nothing is guaranteed but the medium. If the product does not have the capability it was sold for, what is the redress? Again, the "as-is" warranty disclaimer precludes consumer satisfaction.

The lack of consumer redress or customer service in the computer industry is noticeable at the onset of the problem. Eventually,

the buyer is given a long-distance phone number to call for corrections. This may involve lengthy and expensive telephone calls, and again the buyer pays the expense even when it is the manufacturer's error.

The honeymoon era between the computer industry and the buyer is beginning to wane. With increased numbers of small businesses purchasing computer products to gain a competitive edge and move into the technological age, the new purchaser is a different breed of consumer. Generally, a small business which purchases a computer system will have a specific use in mind. Consumers now want guarantees, truth-in-advertising, adequate testing of products, and adequate remedies.

Every buyer who has contacted my office initially wanted the product fixed rather than their money back. However, when the manufacturer, publisher or dealer could not or would not correct the problem, the buyer wanted his or her money back. Buyers are no longer willing to support the mere glamorized image of computerization. They expect products to work and perform with the capabilities for which they were purchased.

III. PRESENT LAW

The computer industry, in its opposition to warranty legislation, claims there is adequate protection for buyers under present law, citing the Song-Beverly Act² and the Uniform Commercial Code (U.C.C.).

The Song-Beverly Act applies primarily to those products purchased for personal, family and household uses. In addition, the computer industry has taken the "as-is" portion of this buyer oriented section of the Song-Beverly Act and made it their industry standard.³ This was clearly not the intent of the Act. By utilizing the "as-is" disclaimer, adequate protection for the buyer of computer products has again been diluted.

The U.C.C. is also cited by the computer industry as giving buyers adequate protection. As has been pointed out to me over and over again, the U.C.C. does not give adequate protection to the small businessperson. The U.C.C. was designed to facilitate commercial sales by allocating risks between the parties to a transaction so that their bargaining positions are more equal, not to protect the unsophisticated consumer. However, in the area of computer prod-

2. Song-Beverly Consumer Warranty Act, CAL. CIV. CODE §§ 1790 *et seq.* (West 1986).

3. CAL. CIV. CODE § 1792.5 (West 1985).

ucts, the bargaining positions between the seller and the buyer are very disparate due to the manufacturer's superior knowledge in this rapidly changing technological field. For example, it has been held that a computer manufacturer who made statements to a buyer regarding the capabilities of a system was liable for misrepresentation, notwithstanding the fact that the buyer was an expert in computer technology.⁴ In *Accusystems, Inc. v. Honeywell Information Systems, Inc.*,⁵ the court held that the consumer had reasonably relied on Honeywell's representations given the dynamic character of the computer industry.

In September of 1985, the Ninth Circuit Court of Appeals decided the case of *RRX Industries, Inc. v. Lab-Con, Inc.*,⁶ which was an action for breach of contract based on defects in computer software. The Ninth Circuit affirmed the trial court's holding that the manufacturer/distributor had breached its contract by providing the buyer with defective software packages. Lab-Con's failure to correct the defects and properly train the buyer's staff was cited as evidence of the breach.⁷ In addition, the court affirmed an award of consequential damages.⁸

Again, the gap between the seller and buyer creates unequal bargaining positions, leaving the buyer unprotected in a business sale. The protection provided by the U.C.C. in these situations is extremely questionable. The U.C.C. allows its own provisions to be disclaimed. Thus, the buyer is not given reasonable time to test the performance of a given product. This disparity in bargaining positions will leave many cases to be resolved by the courts for those who can afford sometimes lengthy litigation. In its present state, however, the legal system is too onerous and expensive to be of much help to a typical buyer.

IV. EXPLANATION OF AB1507

AB1507, as amended, states that every sale or lease of a new computer hardware or software product, or part thereof, shall be accompanied by certain express and implied warranties.⁹ First, if the product is sold by a dealer with respect to products of that kind, there is an implied warranty by the manufacturer and the seller that

4. *Accusystems, Inc. v. Honeywell Info. Sys., Inc.*, 580 F. Supp. 474 (S.D.N.Y. 1984).

5. 580 F. Supp. 474 (S.D.N.Y. 1984).

6. 772 F.2d 543 (1985).

7. *Id.* at 546.

8. *Id.* at 546-47.

9. Cal. A.B. 1507, 1985-86 Regular Sess., proposed CAL. CIV. CODE § 1797.7(a) (West 1986).

the product is merchantable.¹⁰ Second, if at the time of contracting, the manufacturer or seller has reason to know any particular purpose for which the product is required, and that the buyer is relying on the skill or judgment of the manufacturer or seller to select or furnish a suitable product, there is an implied warranty that the product is fit in all material respects for that particular purpose.¹¹ Third, there is an express warranty by the manufacturer or seller that the product conforms in all material respects with the description of the technical specifications and performance capabilities of the product as set forth in advertisements of that product.¹²

While both the manufacturer and the seller are obligated to furnish a product that conforms with the implied warranty of merchantability, the implied warranty of fitness for a particular purpose is only the obligation of the party on whose skill and judgment the buyer has relied in selecting a suitable product. The express warranty, that the product conforms to the technical specifications and performance capabilities as advertised, is only the obligation of the party who advertised the product.¹³

For a product to be "merchantable," it must satisfy the same minimum standards that are set forth in the California Commercial Code.¹⁴ The product must at least meet the following requirements:

- (A) Passes without objection in the trade under the contract description.
- (B) Is fit for the ordinary purposes for which the product is used.
- (C) Is adequately contained, packaged, and labeled.
- (D) Conforms to the promises or affirmations of fact made on its container or label.¹⁵

Not all advertising gives rise to an express warranty. The term "advertising" is defined broadly to include "a commercial message in a newspaper, magazine, leaflet, brochure, flyer, manual or catalog, on radio or television or in any other telecommunications medium, or in any other medium, that promotes, directly or indirectly, the sale or lease of the product."¹⁶

An advertisement shall not constitute an express warranty "unless it is of a kind on which prospective buyers normally rely, and then only if the advertisement is one of the contributing causes

10. *Id.* at § 1797.7(a) (1).

11. *Id.* at § 1797.7(a) (2)-(3).

12. *Id.* at § 1797.7(a) (4)-(5).

13. *Id.* at § 17.97.(a) (2)-(5).

14. CAL. COM. CODE § 2314 (West 1986).

15. Cal. A.B. 1507, 1985-86 Regular Sess., proposed CAL. CIV. CODE § 1797.7(e) (4).

16. *Id.* at § 1797.7(e) (1).

of the sale."¹⁷ The term "advertising" is defined to exclude "a written or oral statement to an individual buyer that is merely an expression of an individual sales agent's own viewpoint, or recommendation," if it has not been set forth in an advertisement.¹⁸

At the same time, this bill states that the burden of proving that the statement does not constitute an advertisement is on the person on whose behalf the statement is made.¹⁹ The person on whose behalf the advertisement is made also has the burden of proving that the advertisement, once made, does not constitute an express warranty.²⁰

In order to give meaning and effect to these warranties, this legislation specifically states that the warranties "may not be disclaimed or modified, that their duration may not be limited," and that any purported disclaimer, modification or limitation in violation of this proposed statute is void.²¹

In the event of a breach of the express or implied warranties, the buyer shall have the remedies provided for in the California Commercial Code,²² subject to two qualifications. First, if the manufacturer or seller limits the buyer's remedies, and if this limitation fails to promptly cure a breach of the warranty, "the buyer's remedies shall also include the right to reject or revoke acceptance of the product."²³ Second, the buyer must give notice of his election to revoke acceptance within a reasonable time after she discovers or should have discovered the grounds for it.²⁴ The bill creates "a rebuttable presumption that notice has been given within a reasonable time if it is communicated to the manufacturer or the seller or its agent within six months after the purchase or installation of the product, whichever occurs later."²⁵

Where the buyer rightfully rejects or justifiably revokes acceptance of a substantially nonconforming product, she "may cancel the sale and recover from the seller so much of the price as has been paid, and from the manufacturer any other damages to which the buyer is entitled."²⁶

17. *Id.* at § 1797.7(d).

18. *Id.* at § 1797.7(e) (1).

19. *Id.*

20. *Id.* at § 1797.7(d).

21. *Id.* at § 1797.7(f).

22. CAL. COM. CODE § 11065 (West 1986).

23. Cal. A.B. 1507, 1985-86 Regular Sess., proposed CAL. CIV. CODE § 1797.7(g) (1).

24. *Id.* at § 1797.7(g)(2).

25. *Id.*

26. *Id.* at § 1797.7(h).

Willful neglect by a manufacturer or seller in accepting a buyer's rightful rejection or justifiable revocation of acceptance within a reasonable time after receiving the buyer's notice may result in a civil penalty of up to two times the buyer's actual damages.²⁷

If it is necessary for the buyer to enforce any liability and she prevails, the buyer is entitled to reasonable attorneys' fees, based on the actual time expended and any other reasonable expenses incurred in connection with the litigation.²⁸

Any action, however, must be commenced within four years after the cause of action has incurred.²⁹

The rights and remedies provided to a buyer under this bill are intended to be cumulative and are in addition to any other procedures, rights, or remedies available to a buyer under other provisions of law.³⁰

If either the seller or the manufacturer sustains any liability or loss as a result of any wrongful act or omission of the other, including a breach of an implied or express warranty, the party sustaining the liability or loss has a right of recourse against the other.³¹

This legislation extends to all situations in which there is a significant relationship between the sale or lease and the State of California, including:

- (1) A sale or lease that is entered into in this state.
- (2) A sale or lease that is made to a buyer whose mailing address, or whose business or residence address, is within this state.
- (3) A sale or lease of a product that is, or is agreed to be, installed or delivered to the buyer in this state.³²

The computer industry's customers, and perhaps the industry itself, may be helped if manufacturers and sellers are held to more of their promises and other statements made in their advertisements.³³

The advertiser is protected against dubious claims by buyers. This bill limits statements made by manufacturers and sellers to the descriptions of a product's technical specifications and performance capabilities,³⁴ advertisements on which prospective buyers normally

27. *Id.* at § 1797.7(j).

28. *Id.* at § 1797.7(i).

29. *Id.* at § 1797.7(n).

30. *Id.* at § 1797.7(m).

31. *Id.* at § 1797.7(k)-(l).

32. *Id.* at § 1797.7(b).

33. *Id.* at § 1797.7(a) (4)-(5).

34. *Id.* at § 1797.7(a) (5).

rely,³⁵ and advertisements that are a contributing cause of the particular sale.³⁶ A sales agent's statements that merely repeat the contents of an advertisement are excluded,³⁷ and the product need only conform to the warranties "in all *material* respects."³⁸

This bill attempts to make the basic rights given by the U.C.C. have more legal meaning by prohibiting warranty disclaimers.³⁹ When certain express and implied warranties are made, they will be enforceable in court if the manufacturer or seller neglects to honor them. This bill, however, attempts to *discourage* court actions. This is achieved by upgrading the buyer's non-court remedies, and by providing the manufacturer and the seller with an incentive to resolve their disputes outside of court.

Existing U.C.C. provisions that allow a manufacturer or seller to limit a buyer's remedies to repair or to replacement of defective parts are followed.⁴⁰ This bill, however, makes it clear that the buyer also has a right to revoke acceptance of the product and cancel the purchase and recover any payments made, if the limited repair or parts replacement remedy does not *promptly* cure the manufacturer's or seller's breach.⁴¹

Manufacturers and sellers are not required to offer their own written warranties for their products.⁴² The only change in the law that applies to written warranties is that the remedies of rejection and revocation of acceptance will be available to the buyer in cases where the written warranty has failed to promptly remedy the problem.⁴³

A manufacturer or seller can continue to issue a warranty that requires the buyer of a defective product to use the warrantor's service and repair facilities to resolve any problem, and that also excludes other remedies, including the right to reject or revoke acceptance, and the right to recover incidental and consequential damages.⁴⁴

California's present Commercial Code rule is followed, and the bill permits the warrantor to exclude these other remedies *only* if

35. *Id.* at § 1797.7(d).

36. *Id.*

37. *Id.* at § 1797.7(e) (1).

38. *Id.* at §§ 1797.7(a) (2) and 1797.7(a) (5).

39. *Id.* at § 1797.7(f).

40. CAL. COM. CODE § 2719(1) (a) (West 1986).

41. Cal. A.B. 1507, 1985-86 Regular Sess., proposed CAL. CIV. CODE § 1797.7(g) (1).

42. *Id.* at § 1797.7(a).

43. *Id.* at § 1797.7(g) (1).

44. *See* CAL. COM. CODE § 2719 (West 1986).

the limited remedy *works*—that is, permits the buyer to reject, revoke acceptance and recover damages in any situation in which the circumstances cause the limited remedy of repair or replacement of parts to fail its essential purpose.⁴⁵ Where the manufacturer or seller is honest and competent, where all representations and promises are fulfilled, and where any product defects or other breaches of warranty are promptly cured, the buyer's remedies for breach of warranty can be limited to those set out in the written warranty.⁴⁶

The buyer will have approximately six months in which to give the manufacturer or seller notice of her decision to revoke acceptance and cancel.⁴⁷ This will benefit both sellers and buyers by giving them some breathing space in which to resolve the problem by cooperating with each other.

The present rule that parties must both observe and enforce warranties and other contractual obligations in *good faith* is not altered by this bill. Under present law, a seller is not penalized for simply refusing to resolve the problem after informal attempts to resolve the problem have failed and the buyer decides to revoke acceptance and cancel the contract.⁴⁸ Also, a manufacturer or seller who is aware of the unsuitability of its product, but does nothing hoping the buyer will cave in and abandon her claim for a return of the purchase price, is not deterred under present law. In that situation, the manufacturer or seller loses nothing by inaction.

This bill attempts to resolve these problem by penalizing the manufacturer or seller for not promptly acting to cure any breach of warranty. If the manufacturer's or seller's informal attempts to remedy the breach of warranty do not succeed, and the buyer gives notice of revocation of acceptance and cancels the purchase, the manufacturer or seller, or both, will incur a civil penalty if no steps are taken to honor the buyer's decision to back out of the transaction.⁴⁹ Of course, if the buyer does *not* have a legitimate basis for revoking acceptance—for example, where there is no breach of warranty, or where the breach does not substantially impair the value

45. *Id.* at § 2719(2).

46. Courts also may allow recovery of consequential damages when the breach of warranty results in personal injuries, or when, under the circumstances, the language limiting the buyer's remedies is unenforceable on the basis that it is unconscionable, e.g., CAL. CIV. CODE §§ 1670.5 and/or 1770 (West 1986), or on some other legal ground.

47. Cal. A.B. 1507, 1985-86 Regular Sess., proposed CAL. CIV. CODE § 1797.7(g) (2).

48. See CAL. COM. CODE § 2713 (West 1986).

49. Cal. A.B. 1507, 1985-86 Regular Sess., proposed CAL. CIV. CODE § 1797.7(j).

of the product to the buyer⁵⁰ — there will be no legal basis for canceling, and no penalty. The amount of the penalty will be determined by the court, and it shall not exceed two times the buyer's actual damages.⁵¹

As a practical matter, it is not likely that a penalty will be imposed on a manufacturer or seller who is not both legally and morally at fault. But no manufacturer or seller will be able to stonewall a buyer who has a complaint without risking a major increase in the buyer's award, should the buyer be forced to take legal action. And where the buyer *does* take legal action, the buyer will also be entitled to recover reasonable attorneys' fees and any other litigation expenses, if she prevails.⁵² While attorneys' fees awards never equal or exceed a buyer's actual legal costs, they do help to offset a portion of those costs, to the extent that the court deems it reasonable.

There are usually at least three parties to the sale of a product — the manufacturer, the seller, and the buyer. This bill recognizes this and if the buyer has a right to cancel because of the product's failure to conform to a warranty made by the manufacturer, it is clear that the seller must also honor the buyer's election to cancel.⁵³

This bill also takes into account the seller's need to look to the manufacturer for reimbursement for its losses if the buyer cancels the sale because of a wrongful act or omission by the manufacturer. The seller is given a statutory right of indemnity against the manufacturer.⁵⁴ And if the manufacturer suffers a loss because of a wrongful act or omission by the seller, or by one of his employees, the manufacturer is given a similar right of indemnity against the seller.⁵⁵

This bill applies to cases of sales and leases of computer products.⁵⁶ Since some courts already apply the Commercial Code rules to both sales and leases, the proposed codification of this principle will not change present law.

In essence, this bill requires that those who merchandise computer products act honestly and competently, level with prospective buyers in describing the technical specifications and performance capabilities of their products, and live up to their promises.

50. CAL. COM. CODE § 2608(1) (West 1986).

51. Cal. A.B. 1507, 1985-86 Regular Sess., proposed CAL. CIV. CODE § 1797.7(j).

52. *Id.* at § 1797.7(i).

53. *Id.* at § 1797.7(h).

54. *Id.* at § 1797.7(k).

55. *Id.* at § 1797.7(l).

56. *Id.* at § 1797.7(a).

V. CONCLUSION

The attention given to Assembly Bill No. 1507 and the issues it raises indicates that there are consumer problems in the computer industry that need to be resolved. As trade publications analyzed and followed this legislation, buyers began to send their complaints and "horror stories" to my offices. If this legislation had not struck a chord of truth, it would have quietly died due to lack of support. However, this is clearly not the case. Legislators across the country are considering similar measures because their constituents are indicating that this is an important consumer issue.

AB1507 does not proclaim the "as-is" standard and is not the only solution to the buyer's identified problems. What AB1507 is designed to do is give protection and equal bargaining power to the buyers of computer products. It is a first step in addressing the lack of consumer rights and recourse in this quick-paced technological frontier.

My first preference is that the computer industry be its own regulator and set its own equitable standards for both sellers and buyers. However, if there is reluctance to have more than an "as-is" standard and a disclaimer of all warranties for the buyer, then I believe this legislation will pass. The main thrust of consumer legislation is to provide adequate remedies and keep the buyer out of court.

The initial measure I introduced required a simple disclosure statement from the manufacturer or dealer because I think that it is important that the buyer assume equal responsibility in a transaction. If a manufacturer or dealer openly discloses the product's capabilities, the type of warranty available and whether the product has been tested or not, then the buyer can intelligently decide whether or not to purchase the product with full knowledge of its limits at the outset. This still remains a viable solution to the previously mentioned problems.

The issues presented here are not going to disappear. Dialogue needs to be established between government and industry. Promoting solutions and working with legislatures will assure a reasonable, equitable process, and reasonable, equitable laws. No industry can afford to have its reputation be its worst element. A balanced solution must come from a cooperative effort, not an adversarial one.

