



23.6.2016

## **WORKING DOCUMENT**

on the directive of the European Parliament and of the Council on certain aspects concerning contracts for the supply of digital content

Committee on the Internal Market and Consumer Protection, Committee on Legal Affairs

Rapporteurs: Evelyne Gebhardt, Axel Voss

## **The Commission Proposal and its Objectives**

As part of the implementation of the Digital Single Market Strategy, the European Commission adopted in December 2015 two proposals on harmonised rules for certain aspects concerning contracts for the supply of digital content ('Digital Content Proposal') and contracts for the online and other distance sales of goods ('Goods Proposal'). The proposals contain common objectives and are therefore designed for a coherent and comprehensive legal interpretation.

The Digital Content Proposal draws on the experience acquired during the negotiations on a Common European Sales Law. Instead of introducing an optional contract law regime, the Commission intends to harmonize certain aspects of the contract law rules on business-to-consumer contracts for the supply of digital content.

The Digital Content Proposal aims at addressing a gap in European and national legislation by creating a standard set of consumer and contract law rules and preventing the rise of divergent national ones that would hamper cross-border trade, consumer confidence and the growth of the Digital Single Market.

## **Preparatory work of the Committees**

The proposal was referred to IMCO and JURI as joint committees under Rule 55 of the Rules of Procedure. On February 17<sup>th</sup> 2016, JURI organised a workshop on "New rules for contracts in the digital environment". On April 27<sup>th</sup> 2016, IMCO and JURI held a joint committee meeting during which the European Commission presented the proposal. On May 24<sup>th</sup> 2016, IMCO and JURI organised a joint public hearing with the title "Contractual Relations and Consumer Remedies in the Digital Sphere". The panels were comprised of representatives from academia, consumer organisations and different business branches.

## **Guiding principles of the Co-Rapporteurs**

The Co-Rapporteurs have agreed to base their work on the following key principles:

- Clear, simple and balanced contract law rules for the supply of digital content. This implies future-proof solutions which are as open to new technical developments as possible;
- Coherence in relation to existing Union legislation, while clarifying the relationship with other relevant legislation;
- Alignment with the Goods Proposal as far as possible and with Union rules applying to the offline world, in order to avoid different levels of consumer protection as a consequence of different distribution channels;
- Balanced result which would benefit consumers and businesses alike.

## **Reflections on the Proposal**

### **Definition of digital content**

The Co-Rapporteurs welcome the extension of the definition of “digital content” in Article 2 vis-à-vis the definition of “digital content” in the Consumer Rights Directive. However they both consider the option to clarify between the two legal regimes by introducing a category of digital services in order to explicitly include in the scope video, audio, applications, digital games and any other software (Article 2(1)(a)) as well as cloud services (Article 2(1)(b)) and social networks (Article 2(1)(c)), without confusing the existing terminology which has been transposed into national laws only recently. This approach, according to which the Digital Content Proposal covers all digital content and services, may represent a future-proof solution for covering all types of digital products and contracts in the coming years. However, since the legal category of the contract (lease, sale, service) is not specified, it requires the transposing Member States to either create a new type of sui generis contract or alternatively to integrate the provisions in the existing contract types, according to the respective national legislation.

## Scope

Attention will have to be paid to Article 3 and recitals 11, 12, 13 and 17. Committee Members, stakeholders and academia widely approve of the fact that the Digital Content Proposal covers supply of digital content regardless whether the contractual relation has been concluded online or offline and irrespective of the delivery mode of the digital content (digital content on a carrier or supplied by download, streaming or any other provision of access). However, considerable criticism has been levelled at the Commission’s decision to exclude from the broad scope embedded software. This is particularly problematic in view of goods with embedded digital content which fall under the category of smart products like connected cars, mobile phones or Smart TVs etc. Recital 11 of the Digital Content Proposal and Recital 13 of the Goods Proposal both state that the Goods Directive shall apply to digital content integrated in goods, such as household appliances or toys, where the digital content is embedded in such a way that its functions are subordinate to the main functionalities of the goods and it operates as an integral part of the good. In practice, this distinction would lead, for instance, to the consequence that embedded software of a hybrid product such as a connected car would fall under the regime and remedies of the Goods Proposal while the separately obtained connected car software would fall under the Digital Content Proposal regime. The discussions within both Committees have shown that the aforementioned “functionality test” may be difficult to apply for consumers and traders alike and may moreover have a subjective component, which could evolve over time (is the main functionality of a smart phone making phone calls, or serving as a carrier for apps, pre-installed or not?). The subjective component of the functionality test leaves doubts of interpretation especially regarding the products of the *Internet of Things* which may fall outside the scope of the Digital Content Proposal (recital 17).

This controversy has compelled the Rapporteurs to consider different ways how to clarify the scope of the proposal, *including*:

- a) Improving the definition of goods with embedded digital content, which would fall under the Goods Proposal;
- b) “Location of the defect” approach: The applicable remedies’ regime would depend on what is broken. If the defect is in the software, then the digital content regime applies; if the defect relates to hardware (including CDs), then the goods regime applies. The “location of the

defect” approach widely corresponds to the suggestion to focus on mixed purpose contracts. The proposal on digital content indeed seems to accept in its Article 3(6) that a contract may include elements for the supply of digital content and elements of other contracts, e.g. sales contract. This provision could be further developed in order to properly catch such mixed contracts. The recently introduced Consumer Rights Act 2015 in the UK covers in its section 1(4) mixed contracts with the consequence that for both rights and remedies it is necessary to look at the relevant elements of the mixed purpose contract;

c) “Digital content” approach: It could be considered to submit smart goods to the Digital Content Regime (with its remaining differences and additional digital rights), and model after the approach taken by the Commission on CDs and DVDs, which already fall under the Digital Content regime;

d) “Tangible versus intangible” approach: A single set of remedies applies, depending on whether one can touch the object of the contract, e.g. smartphones, CDs, etc. (goods remedies apply), or not, e.g. downloading apps (digital content remedies apply). This approach has the benefit of enhanced simplicity and would be easy to apply by consumers: only one set of remedies applies to one contract. No distinction is made between types of embedded digital content, because all embedded digital content would fall under the Goods Proposal, whether subordinate to the main functionalities of the good or not. CDs, DVDs would then be treated as goods, unlike the Commission’s proposal.

All four approaches show advantages and disadvantages. For instance, the application of a single set of remedies to a mixed situation such as embedded digital content, (as in approaches a) and d) outlined above), may have the effect that remedies that are otherwise logical for the subordinate/non-instrumental element of the contract are not available. Hence, if embedded software causes economic damage to the consumer’s digital environment, the specific remedy laid down in Article 14(1) of the Digital Content Proposal may not be available, since the Online Sales regime applies.

### **Data as Counter-performance and coherence of the proposal with the EU data protection framework**

The proposal introduces the notion of counter-performance other than money in the form of data. Today, data is being collected in very diverse ways, such as voluntary disclosure in social network settings or by tracking when users reveal their intention to purchase through multiple searches on the internet. Increasingly, online services are advertised and labelled “for free” when in reality consumers are providing their data as a counter-performance and moreover consent to process those data under the General Data Protection Regulation (‘GDPR’). This trend has been accelerated by digitalisation. The Co-Rapporteurs will ensure coherence with the GDPR, and would welcome the introduction of a provision, for instance in Article 3(8), stating that this Directive is without prejudice to the General Data Protection Regulation (EU) 2016/679.

The Digital Content Proposal stipulates that suppliers and consumers enter synallagmatic contractual relationships where the supplier provides digital content in exchange for money, actively supplied personal data or any other data (Article 3(1)). The declared reason behind the use of both the terms “personal data” and “any other data” appears to be that the Digital Content Proposal should not anticipate the interpretation of the term “personal data” as used in the GDPR. The notion of “any other data” could however be clarified further.

Stakeholders and scholars have expressed serious concerns as to the exact scope of Articles 3(1) and (4), since they merely encompass “actively” provided data. Often, personal data is nonetheless gathered through indirect means of data collections (tracking) which, pursuant to recital 14, do not fall under the Proposal. This gives rise to the question whether this provision does not inevitably narrow the scope of application and encourages the creation of loopholes by content providers. The Co-Rapporteurs will also need to elaborate on the meaning of the term “strictly necessary” in Article 3(4) in relation to justified data processing according to the GDPR.

Furthermore, the Co-Rapporteurs would like to see a clarification of the consequences of a withdrawal of consent to the processing of personal data under the GDPR for the contractual relationship (contracts in exchange for personal data). The rules on termination of the contract and the obligations and consequences for both supplier and data subject/consumer may have to be clarified as well in order not to impair the balance of the contractual relationship based on data as counter-performance.

### **Conformity of digital content**

The rules on conformity are subdivided in this Proposal into a subjective criteria test (Article 6(1)) and an objective criteria test (Article 6(2)). Article 6(1) provides that digital content must comply with the description given by the supplier. Only to the extent that the contract does not stipulate such requirements, the digital content must be fit for the purposes for which goods of the same type are normally used (Article 6(2)). In sum, conformity is being assessed first and foremost through the individual stipulations of the respective contract. This marks a departure from the previously universally endorsed model of an objective conformity test as contained in the Consumer Sales and Guarantees Directive.<sup>1</sup> Only if and when the contract is “insufficient or intransparent” with regard to the requirements of digital content (Article 6(2); Recital 25), objective criteria can be utilised in order to ascertain whether the digital content is conform or defect.

Committees’ Members, stakeholders and scholars have however questioned whether this approach is appropriate. On several occasions and also during joint committee meetings, representatives of the European Commission have argued that conventional conformity rules are insufficient with regard to digital content as supplier might be restricted by intellectual property rights which have to be transferred on to the consumer. In turn it can be argued that the conformity test of Article 2 of the Consumer Sales and Guarantees Directive<sup>2</sup> offers the required openness which is necessary with regard to the uncertainty what the consumer may reasonably expect from digital content. The Co-Rapporteurs also see the need to further critically evaluate whether this subjective/objective conformity test does satisfy the needs of consumers and businesses as well as transposing Member States.

---

<sup>1</sup> Directive 1999/44/EC. See Martin Schmidt-Kessel et al, “Die Richtlinienentwürfe der Kommission zu Digitalen Inhalten und Onlinehandel-Teil I“ GPR/ 1 (2016) p. 65.

<sup>2</sup> Conformity is presumed if the good complies with the seller’s description, is fit for any purpose for which it is required, is fit for purpose for which the good is normally used or shows the quality and performance which is normal in goods of the same type and which the consumer can reasonably expect.

## **Burden of Proof**

The Co-Rapporteurs note that Article 9 of the Digital Content Proposal does not restrict the reversal of the burden of proof to six months as established in the Consumer Sales and Guarantees Directive or two years as stipulated in the Goods Proposal. The burden of proof of conformity of digital content with a contract rests with the supplier, with regard to non-conformity existing at the time of supply. The reversal of the burden of proof of conformity (in favour of consumers) can be reversed by suppliers if they show that the “digital environment of the consumer is not compatible with interoperability and other technical requirements of the digital content, and where they had informed the consumer about such requirements” prior to the contract's conclusion. Furthermore, the burden of proof of a defect returns to the consumer if the latter fails to cooperate with the supplier “to the extent possible and necessary to determine the consumer's digital environment”, used by the consumer.

In relation to the lack of a guarantee period in the Digital Content Proposal, the Co-Rapporteurs have to consider the following: In Recital 36 the Commission argues that “digital content is not subject to wear and tear” and thus no time limit for bringing claims in case of non-conformity is required. By juxtaposing tangible goods and digital content this reasoning might be compelling on the surface because it presumes the longevity of digital content. However, this hypothesis is by all means not proven. The Co-Rapporteurs have to consider whether the approach taken by the Commission to prescribe different guarantee periods for digital content and tangible goods is sensible. The problem becomes even more evident when one takes into account the diverging prescription periods in Member States, which preclude consumers from raising claims, on expiry of a limitation period.

Questions thus remain regarding the extent of information which suppliers should be able to request before the conclusion of the contract as well as the permanent nature of the reversal of burden of proof. In particular with regard to the latter an alignment with the Goods Proposal could be considered.

## **Remedies**

In relation to remedies, the Digital Content Proposal retains the same system of hierarchy of remedies as under the Consumer Sales and Guarantees Directive, which in contrast followed the minimum harmonisation approach, and the Goods Proposal. In case of non-conformity consumers have to seek first cure and only in the second step are entitled to termination and subsequently refund. The consumer's right to terminate is nonetheless excluded if the non-conformity does not impair the functionality, interoperability or “other main performance” features of the digital content, according to Article 12(5), while the burden of proof lies with the supplier. In cases where the consumer purchased the digital content in exchange for money and is entitled to termination because of non-conformity, she can instead choose partial reduction in the price paid (Article 12(3)-(4)). Such a price reduction shall be in proportion to the reduced value of the digital content actually supplied in comparison to the digital content which would have conformed to the contract.

Several Committee Members and stakeholders criticise the proposal for retaining the system of hierarchy under a full harmonisation approach, as this would trigger changes to well-established national consumer protection rules. Under some EU jurisdictions the consumer can terminate the contract if the breach of contract is sufficiently serious. The Co-Rapporteurs will need to further assess the system of a fully harmonised hierarchy of remedies.

In any case, in order to avoid the creation of two completely different sets of rules, the remedies of the Digital Content Proposal and the remedies of the Tangible Goods Proposal should be as coherent as possible. The starting point for such adjustments would be the existing rules, i.e. the Consumer Sales and Guarantees Directive, and the Goods Proposal. Only where the specificities of digital content so dictate, would there be additional consumer remedies specific to digital content (economic damage to digital environment, retrieval of data after termination, etc.).

This “aligning remedies” approach could entail a further discussion on a possible alignment of several aspects of the proposals, such as:

- Relationship between objective and subjective conformity criteria
- Length of guarantee periods and burden of proof
- Termination of contracts (minor defects etc.)
- Right to compensation for economic damages to the digital environment (also for embedded digital content)
- Provisions on commercial guarantees (also for digital content)
- Provisions on supply
- ...

In combination with the “aligning remedies” approach, the demarcation criteria mentioned under Scope could be used to determine to what extent remaining specific rules for digital content would have to be applied.

## **Damages**

The Co-Rapporteurs consider the newly introduced rule on economic damage to the consumer’s digital environment in Article 14 of the Proposal worthy of in-depth discussion. Article 14 provides that the supplier of digital content is liable for economic damage to the digital environment caused by faulty digital content or by failure to supply digital content. However, several open questions need to be answered. For instance, due to the fact that the Digital Content Proposal geared towards full harmonisation, it is unclear if all other grounds for damages are excluded or not. In fact it appears plausible that all conceivable other cases of damages, most importantly to the non-digital environment, are further regulated by the Member States and no harmonisation of tort law in general was intended. For those reason the Co-Rapporteurs have to consider whether they see the need to add language which clarifies that Article 14 does not exclude liability to damages to the non-digital environment and which clarifies the concrete meaning of the term “digital environment”.

## **Other issues**

### **Level of harmonisation**

One further fundamental question that will need to be addressed is the level of harmonisation. Article 4 of the Digital Content Proposal states that Member States shall not maintain or introduce provisions diverging from those laid down in this Directive. As a consequence Member States could be barred from retaining or introducing more or less consumer-friendly rules than prescribed by the Digital Content Proposal. However the Co-Rapporteurs have to agree on a future-proof and technologically-neutral approach and thus have to take into account the difficulty to foresee today what kind of problems, requiring legislative intervention in favour of consumers and businesses, may arise in the near future. Whilst maximum harmonisation is certainly suitable for creating a level-playing field for businesses across Europe, it must not be forgotten that the relevant rules implementing the directive will be scattered across 28 legal systems, and, more importantly, they will be closely linked with the remaining part of the private law of each Member State. The proposal addresses only selected issues, and the bulk of rules affecting the validity, content and interpretation of a digital content contract will remain at national level. Therefore, the advantages for businesses will be at least partly outweighed by the divergence of general contract laws. A political choice therefore has to be made between, on the one hand, achieving maximum protection of consumers, and the relative advantage of having a (supposedly) level-playing field for businesses.

### **Conclusion**

Experts have identified additional issues which have not been, but potentially could be, addressed by this Directive. These could include, for instance, consumers' rights to multiple downloads, to make copies, to re-sell digital content and to receive essential updates and maintenance, as well as the issues of optional guarantees, immediate supply, joint liability and specific unfair contract terms in contracts for the supply of digital content. The Co-Rapporteurs intend to work together with the Shadow Rapporteurs towards a balanced and fair final text which is coherent with already existing EU legislation and which meets the needs of businesses and consumers alike.