

**'Out of the Box'**

David Andrew Poyton

**“Dematerialised Goods and Liability in the Electronic Environment: the truth is,**

**“there is no ~~spoon~~ box”**

David Andrew Poyton<sup>1</sup>

ABSTRACT

*This paper considers the rights and potential liabilities which may, or may not, arise in relation to contracts for ‘dematerialised’ or ‘intangible’ items. Such contracts are increasingly entered into and performed via an electronic form of communication making this a potentially significant issue for parties engaging in electronic commerce. The issues raised naturally lead to the examination of the legal arguments associated with that most infamous ‘intangible’; computer software. It is argued that in disputes relating to computer software and in particular when the issue of its classification as ‘goods’, ‘services’ or ‘something else’ have been raised, there has been a tendency to overstate the ‘unique’ nature of computer software and lose focus of the real issue of what rights and liabilities should be attached to contracts relating to these items. When other dematerialised or intangible items are considered, an unacceptable dichotomy in relation to rights and potential liabilities, often overlooked when discussing computer software, is highlighted. It is concluded that as the law stands the method by which an item is delivered may dictate the rights and obligations attached to that contract adversely discriminating against the customer using electronic commerce.*

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**First: An Explanation**

As is often the case when the imagination is released unfettered the resultant ‘great idea’ requires some explanation. References can appear obscure and the link made by a conference participant to the conference theme or title may seem tentative to say the very least. From the feedback received from my colleagues,<sup>2</sup> my title requires some words of explanation.

The quotation in the title comes from the technological masterpiece of cinematography of the late nineties – ‘The Matrix’. The obscure reference relates to *perception* and its effect on the understanding and consequent analysis of a thing or situation. In the film (for those who have not had the good fortune of seeing it) a young boy is using, what at first appears to be, telekinesis to make a spoon bend and mutate in ways that would make Uri Gellar blush. Our hero, Neo, attempts the same with little success and the enlightened child tells him:

“Do not try and bend the spoon. That’s impossible. Instead only try to realise the truth. . . There is no spoon.”

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<sup>2</sup> I must add, feedback which was very gratefully received! Particular thanks to Ruth Atkins for her comments on the paper.

Thus illustrating that Neo's perception of what he is seeing, or believes that he is seeing, is determining what he can and cannot do. The 'truth' will allow him to gain a real understanding of what appears in front of him.

Perceptions are based upon the information we are provided with and previous experience. Our perception can shape our understanding and analysis of something 'new' and there is a tendency to try to fit the 'new' into our understanding of the 'old' and at times this can lead to a failure to appreciate the true nature of what we are seeing.

The hypothesis, tentatively linked to this piece of cinema, is that perhaps our understanding of 'intangibles', 'dematerialised goods' or 'data products' has been adversely affected by our perception of what they *should* be rather than what they *are* and as a result the legal analysis of these 'things' has been flawed. Although the law is often necessarily preoccupied with categorisations and definitions the desire to 'bend the spoon' and fit something new into an existing category can distract from a true analysis. It is submitted that this has occurred with the analysis of the most prevalent intangible, computer software, in the context of contractual rights and liabilities. It is also argued that such analysis may have an unacceptable consequence for other 'dematerialised goods' regularly transferred via electronic commerce. As a result we have been left without a tested and reliable way to predict the risk associated with the supply and purchase of such items, to the detriment of the e-commerce user.

In the title of this paper the 'spoon' is replaced by a 'box' and the following analysis considers how the removal of the physical boxes may require some reconsideration of existing, well-established 'legal boxes'.

### **The Physical Boxes**

The truth is, with technological developments there are actually no boxes anymore and as technology advances and we, or more probably future generations, become accustomed to these developments there will be less and less need for these physical carriers. It must be asked whether this removal of the 'physical' boxes has had an effect upon the rights and liabilities of sellers and consumers and equally, whether such removal *should* have any effect. This naturally leads to the question: if there is an effect, what should it be? However, before these questions are addressed some consideration of the actual items and their place in the commercial environment is necessary.

### **Dematerialised Goods?**

To an extent this phrase encapsulates the problems associated with the classification of these 'intangible' items. 'Dematerialised', suggests some incredible vanishing trick, which is not the case, and the word 'goods' in this context has significant legal overtones. The variety of phrases used to describe these items adds further uncertainty; 'dematerialised goods', 'data products', 'intangibles' and even 'information products' are all phrases used to refer to what is essentially a discernible group of commercially transferable items with identifiable characteristics. The term employed may inadvertently or sometimes deliberately associate with, or disassociate the item from, a particular legal definition and corresponding obligations. In this paper the phrase 'digital product' defined as; something in digital form created, developed or refined for sale, will be used to encompass all of these items unless otherwise stated.

In essence, and in the context of this discussion, we are concerned with items that by their very nature do not require a physical carrier medium, although previously they have been or can be delivered in such a way. Books, computer programs or software, feature

films, music, ring tones and other entertainment media have been variously ‘sold’ on CD’s, DVD’s, magnetic tape or other storage medium.<sup>3</sup> Some of these items have been delivered without a physical carrier medium before, down analogue telephone lines for example, but the utility of such methods was restricted by the speed and reliability of such communications. Only with the advent of modern communication technologies has it been possible to transfer products of this nature with any commercial level of reliability and viability. With the technology have come ‘new’ products which, whilst often available on a physical carrier as well, are more usually purchased and delivered electronically, mobile telephone utilities are one example. All of these items can now be readily downloaded to the electronic device – a computer hard-drive, portable device, mobile telephone or digital television. Such digital products are now truly ‘out of the box’ but nevertheless legal debate necessarily has to focus upon whether they fit into an existing legal definition or ‘box’.

### **The Legal Boxes**

In relation to rights and liabilities the law has some familiar ‘boxes’ or legal definitions. Subject matter transferred in the commercial environment has traditionally been placed in one of two ‘boxes’; goods or services. A contract may also be for a combination of both goods and services.<sup>4</sup>

To lawyers and legislators these little boxes are vital because the boundaries of legal definitions usually define legal rights and liabilities. Being able to identify those boundaries and hence corresponding obligations and risk is vital for advisers and businesses alike.

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<sup>3</sup> Or should I say a *copy* of an ‘original work’ has been sold.

<sup>4</sup> See the approach adopted by the House of Lords to a contract for the building and delivery of a ship in *Hyundai Heavy Industries Co. v. Papadopoulos and Others* [1980] 2 All E.R. 29.

## **What Rights and Potential Liabilities?**

At this point it is useful to consider some of the rights and potential liabilities referred to many times above. The most common provisions discussed in this context relate to the standards expected in relation to performance and quality; specifically the terms implied by the Sale of Goods Act 1979 (SGA) and the Supply of Goods and Services Act 1982 (SGSA).<sup>5</sup> These provisions only apply to contracts for items falling within the definitions of 'goods' or 'services' associated with the relevant legislation.<sup>6</sup> However, historically the courts have implied similar terms into contracts of a particular type where such implication was felt necessary.<sup>7</sup>

In addition to the implied terms found in the SGA and SGSA there are a number of other provisions whereby the protection afforded is dependent upon the contract being one for 'goods' or 'services'. For example; consumer guarantees and remedies,<sup>8</sup> product liability, consumer safety and misleading price indications,<sup>9</sup> false trade descriptions<sup>10</sup> and the provisions relating to distance contracts<sup>11</sup> all provide valuable rights and potential liabilities in a variety of circumstances. In relation to these obligations, intervention or equivalent implication by the courts is less likely or may not be possible. So an important starting point would be to establish *what* the parties are contracting for and whether it fits into one of the existing categories.

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<sup>5</sup> That goods sold 'match their description', are of 'satisfactory quality' and are 'fit for their purpose or purposes' (s.13 – 15 SGA). That services are performed with 'reasonable care and skill' (s.13 SGSA)

<sup>6</sup> This is considered in more detail in the next section.

<sup>7</sup> See *Trollope & Colls Ltd v. N.W. Metropolitan Regional Hospital Board* [1973] 1 W.L.R. 601 and *Liverpool CC v Irwin* [1976] 2 All ER 39. The main difference between the terms implied by statute and the terms implied by the courts is that the latter are implied subject to a contrary express term and are also susceptible to being excluded or limited by an exemption clause. The statutory implied terms are also protected by s 6 Unfair Contract Terms Act 1977. The protection is absolute where one party 'deals as a consumer' with exemption clauses rendered automatically ineffective and subject to the requirement of reasonableness where neither party deals as consumer.

<sup>8</sup> The Sale and Supply of Goods to Consumers Regulations 2002 (Statutory Instrument 2002 No. 3045).

<sup>9</sup> Consumer Protection Act 1987, s 1.

<sup>10</sup> Trade Descriptions Act 1968, s 1 and Consumer Protection Act 1987, s 20.

<sup>11</sup> Consumer Protection (Distance Selling) Regulations 2000 regulations 3, 11 and 12.

The approach adopted by the courts in determining rights and liabilities must now be considered and this begins with the identification of *what* we are actually contracting for.

### **What are we contracting for?**

Some guidance in this search can be found in the case law relating to the distinction between a contract for ‘the sale of goods’ and a contract for the ‘supply of a service’.<sup>12</sup> The distinction is directly relevant to this discussion because in the majority of cases it has been necessary to decide this issue in order to apply the appropriate standards of performance. When considering the true nature of a contract the courts have traditionally looked at the ‘dominant element’ of the transaction or the ‘substance of the contract’, on its proper construction.<sup>13</sup> Significant to this assessment is whether you are contracting for the ‘skill and labour’ of the other party, or for the ultimate ‘result’ or ‘end product’ of that skill and labour.<sup>14</sup>

So what is the ‘substance’ of the contract when the subject matter involved is a ‘digital product’? It is submitted that with all of the ‘dematerialised’ items discussed above, you contract for the use, utility, enjoyment or entertainment value obtained from a copy of an author’s or creator’s work, whether it be a book, film, music album or computer game. However, this simple proposition has apparently not found favour and there are strong counter arguments, particularly in relation to computer software. When computer

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<sup>12</sup> As will be seen below, this question has already been considered in cases involving one of the intangible items mentioned previously – computer programs and software. It will however be suggested that the analysis and arguments considered in those cases have done little to clarify the situation. Nevertheless, useful analogies can be drawn.

<sup>13</sup> *Robinson v Graves* [1935] 1 KB 579; *Cammell Laird & Co Ltd v Manganese Bronze and Brass Co Ltd* [1934] AC 402; *c.f. Lee v Griffin* (1861) 1 B & S 272.

<sup>14</sup> It is also relevant to note that the courts have appeared willing to treat a complex contract as a combination of both rather than either /or where it appears appropriate. See *Hyundai Heavy Industries Co. v. Papadopoulos and Others* [1980] 2 All E.R. 29 and some supporting comments by Lord Penrose in *Beta Computers (Europe) Ltd v Adobe Systems (Europe) Ltd* [1996] FSR 367 at p 396.

software is purchased it has been argued that you are actually contracting for a 'licence' to use a copy of the software, making the 'licence' the 'real substance' of the contract.<sup>15</sup> Arguably, this analysis caters more to the empowerment of computer software producers than to logic. The real 'substance' of the contract is a copy of the software, the 'necessary' licence to use the software is ancillary to that.<sup>16</sup> In the same way, when a DVD, CD or book is purchased, it is the content – a copy of the written word, the movie or the music, which is the purpose and 'substance' of the transaction. A great deal of skill and labour will have been put into the production of that item, and you may require a licence to do certain things with it, but in most cases the contract is for the end product.<sup>17</sup>

To this point Professor Michael Landau<sup>18</sup> made a wonderfully illustrative observation in what I shall call the 'coffee cup analogy', paraphrased here:

The coffee machine at work dispenses coffee in a little plastic cup. The subject matter of the contract is a cup of coffee. If the plastic cup is removed and replaced with the customer's own mug, what is the contract for then? The 'carrier' has been removed, or changed, but few would argue that the contract is no longer for a cup of coffee; the 'substance of the contract' remains the same.

The analogy is clear. If a copy of the latest Eminem album, Steven Spielberg movie or computer game is purchased in a box, from a high street store or downloaded without a

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<sup>15</sup> For example D Bainbridge *Introduction to Computer Law* 5<sup>th</sup> edn, Longman, 2004 at p 193.

<sup>16</sup> The necessity of such licences has been debated, see M Sherwood-Edwards 'Seven degrees of separation: the Software Directive and UK implementation' *Computer Law and Practice* Vol 9, No 5, pp 169-175, 1993 and G Smith 'EC Software Protection Directive – an attempt to understand article 5(1)' *Computer Law and Security Report* Vol 7, No 4, pp 148-151, 1991.

<sup>17</sup> This surely remains the case, even if the item you have purchased requires continual updating to amend and correct faults and flaws in the product sold. A practice common to certain software suppliers.

<sup>18</sup> At the BILETA 2004 conference. If I am incorrect and my memory has failed me I apologise and would be happy to re-attribute the anecdote to its rightful owner.

box from an online store, the substance of the contract remains the same. It defies logic and common sense to conclude otherwise.

However, when considering legal rights and obligations the question remains whether what you are contracting for falls within one of the existing definitions and statutory regimes.

### **'Goods'**

A definition of 'goods' can be found in Section 61 of the Sale of Goods Act 1979.<sup>19</sup>

““goods” includes all personal chattels other than things in action and money”

This well-established definition distinguishes a 'chose in possession' from a 'chose in action'; the former may fall within the definition of goods whereas the latter will not. Halsbury's Laws of England provides the following definition of a chose or thing in possession:

“... all things which are at once tangible, moveable and visible, and of which possession can be taken, for example animals, household articles, money, jewels, corn, garments, and anything else that can properly be put in motion and transferred from place to place.”<sup>20</sup>

It would appear that to fall within the statutory definition of 'goods' an item must be capable of being considered a personal chattel or personal property, of which possession

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<sup>19</sup> This definition is also applied to the Consumer Credit Act 1974, the Unfair Contract Terms Act and the Supply of Goods and Services Act 1982.

<sup>20</sup> 4th edn, Vol 35, at 1205.

can be taken. The definition also appears to require that the item has some physical manifestation because it must be moveable, visible and tangible.

### **Services**

Statute provides a definition of a “contract for the supply of a service” as a “contract under which a person (“the supplier”) agrees to carry out a service”.<sup>21</sup> However, no definition of ‘a service’ is provided. Black’s Law Dictionary provides a definition which conforms to a common sense understanding of the word:

“. . .The act of doing something useful for a person or company for a fee. . .A person or company whose business is to do useful things for others. . .An intangible commodity in the form of human effort, such as labour, skill, or advice <a contract for services>”<sup>22</sup>

‘Service’ in this context clearly refers to a process, activity or procedure rather than an end result (although there will usually be an end result). Such activity is usually undertaken by another party exercising skill, labour or human effort but it may equally be performed by an automated system designed to provide a service. The ‘human effort’ exists in the setting up and maintenance of such a system.

### **‘Digital Products’: As a ‘service’?**

This point will be dealt with first because the analysis is arguably more straightforward when compared with the analysis relating to the definition of ‘goods’. Without being distracted by discussions about tangibility or intellectual property the application of the

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<sup>21</sup> The Supply of Goods and Services Act 1982 s 12.

<sup>22</sup> B Garner (ed) *Black’s Law Dictionary* 7<sup>th</sup> edn, West Group, 1999.

principle discussed above is all that should be required; i.e. what is being contracted for and what is the 'substance' of the contract?

In relation to computer software it has been suggested that:

“...the predominant nature of the contract is the provision of a service, the function of the software being the service in question.”<sup>23</sup>

It is respectfully submitted that such arguments defy common sense, even when bespoke software is considered. There may be elements of the nature of a service involved, including the development of the software, the delivery or downloading of the software and ongoing support. However, the software transferred is an end product, it may not be a 'perfect' end product, and it need not be, but what that end product actually *does* can hardly be called the provision of a service.<sup>24</sup>

To once again take a step back from computer software and change perspective. If a copy of a movie or pop album is downloaded would the 'function' that it performs (i.e. entertaining the purchaser) ever be called a service?

It is submitted (and will be discussed further below) that computer software demonstrates more similarities with other 'digital products' than differences. Only when this fact is recognised does the illogical nature of some of the arguments surrounding this topic become apparent.

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<sup>23</sup> D Bainbridge *Introduction to Computer Law* 5<sup>th</sup> edn, Longman, 2004 at p 196.

<sup>24</sup> Such a conclusion could lead to some very interesting debates about whether the last time my software failed and dumped files from my hard drive, downloaded a virus, or allowed a hacker to gain access, it was performing its duties with reasonable care and skill??

### **'Digital Products': As Goods?**

The digital products referred to in the introduction to this paper, must now be considered in the light of the statutory definition of 'goods'. To date the only 'intangible' item tested against this definition in the courts is computer software. While it appears to be generally accepted that when software is supplied on a physical carrier medium it may be classified as goods<sup>25</sup> (or an integral part thereof)<sup>26</sup> it would appear equally clear that when the program is downloaded or transferred without that medium it cannot be classified as goods.<sup>27</sup> That said, it is useful to examine some of the arguments put forward in relation to computer software to consider the effect of their application to other 'dematerialised' goods. If nothing more, this analysis should illustrate the futility of trying to fit these new items into this dated definition.

### **The Computer Software Debate**

Computer programs and software are regularly contracted for, and delivered in, the electronic environment and as such they are a significant commodity in the electronic commerce economy. They can be purchased with or without a physical carrier medium, downloaded or carried out of a retail outlet in a box, in a carrier bag. At this stage it is important to note that movies, music albums, books, ring tones and other media can be purchased and delivered in much the same manner. Much of the debate surrounding computer software has focused on the differences between computer software and other items available in the market place; its unique nature and need for special or individual treatment. Whilst this is a justifiable focus in a number of contexts, in this particular context it is submitted that the focus should be on the 'similarities' computer software

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<sup>25</sup> In the case of 'off the shelf' software at least.

<sup>26</sup> Treating the software as the 'instructions' for the hardware for example.

<sup>27</sup> See *St Albans City and District Council v. International Computers Ltd* [1997] F.S.R. 251 per Sir Iain Glidewell at pp 266.

has with many other items, particularly those which lend themselves to 'dematerialisation'.

The predominant arguments against computer software being classified as 'goods' are: that it is 'intangible' and by its nature 'mere information' and therefore not a 'personal chattel' or personal property. It has also been argued that software is 'intellectual property' and hence a 'thing in action' and therefore specifically excluded by the definition in s 61 SGA.<sup>28</sup>

*Computer software is 'intangible' and therefore cannot be goods*

This argument is based upon s 61 of the SGA, its interpretation and the traditional definition of personal chattels. The definition refers to a physical and visible form of property, capable of being 'owned' and possession being taken thereof. It is argued that intangible items do not have a physical form recognised as 'property' in law.<sup>29</sup>

A number of points can be made in relation to this argument. First, the definition of chose in possession derives from an era before intangibles of the nature under discussion could be envisaged and therefore the appropriateness of its application in this context must be questioned. Secondly, it must be asked whether, regardless of the appropriateness of the definition, the items under discussion can be shown to satisfy the requirement that possession be taken of some physical form.

It is submitted that if it is indeed necessary for there to be a physical manifestation which can be 'owned' or possessed, the requirement can be satisfied by a more detailed analysis of the subject matter of the contract. It is suggested above that the real substance of the

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<sup>28</sup> A 'chose in action' is a proprietary right *in personam*, in contrast with a 'chose in possession'.

<sup>29</sup> The only form of property recognised in computer software and other intangibles is 'intellectual property' which is non-physical and beyond the scope of the definition and usually not transferred under the contract and hence 'ownership' is not taken of it.

contract is a copy of the software, movie, book or other item. It could therefore be argued that it is this copy which is possessed after purchase and download. If analysed at a detailed and microscopic level it can be seen that this copy also has a physical form to the extent that its presence has a physical effect on the storage medium to which it is downloaded.<sup>30</sup>

*Computer software is 'information' and therefore not 'goods'*

Scott<sup>31</sup> puts forward the argument that as software is simply coded information<sup>32</sup> it is “altogether different in nature to personal property”.<sup>33</sup> The English authorities, culminating in the House of Lords decision in *Boardman v Phipps*<sup>34</sup> suggest that information “is not property in any normal sense”<sup>35</sup> and is therefore incapable of being personal property or a personal chattel. In *Oxford v Moss*<sup>36</sup> it was held that an undergraduate student could not be convicted of theft of confidential information, under the Theft Act 1968, because such information did not fall within the definition of property under s 4. The ‘value’ of information is recognised in law but in general the rights over information relate to the control over its use and are not, as such, based upon any notion that it constitutes personal property. Scott concludes that “Information, and therefore software, cannot be considered ‘goods’ under s 61” of the SGA.<sup>37</sup>

This would appear to be an accurate technological analysis and if this analysis is correct then it is submitted that all digitally and magnetically recorded media is simply coded

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<sup>30</sup> For example, the variation in reflective and non-reflective pits on a CD or the altered orientation of the magnetic particles on a magnetic disc by the presence of the program. See *St Albans City and District Council v. International Computers Ltd* [1997] F.S.R. 251 at 265 per Sir Iain Glidewell.

<sup>31</sup> A Scott ‘Software as ‘goods’: nullum simile est idem.’ *Computer Law and Policy* Vol 3, No 4, pp 133-136, 1987.

<sup>32</sup> As indeed a movie or music album may be when downloaded.

<sup>33</sup> *Op cit* note 29 at p 135.

<sup>34</sup> [1967] 2 AC 46.

<sup>35</sup> *Ibid* per Lord Upjohn at p 128.

<sup>36</sup> [1978] 68 Cr App R 183.

<sup>37</sup> *Op cit* fn 39 at p 136.

information.<sup>38</sup> Therefore, the content contained on DVD's, CD's and magnetic tape cannot be considered goods, but the tangible transfer medium can be. This analysis places too great an emphasis on the method of transferring the material in question in the determination of the rights and liabilities of the parties.

However, this argument can be met, in relation to computer software, if the functional effect of the software is considered. This 'functional' argument relates to the fact that as the software "interacts directly, with the hardware",<sup>39</sup> it is not mere information because it has a direct effect on its surroundings, the hardware. Reference has been made to the US case *Winter v G P Putnam*<sup>40</sup> in which the judge felt that whilst the information contained within an instruction manual could not be a 'product' for the purpose of product liability laws, he felt that software could be a product because it was more than 'just information'. Here, a distinction was made between the analysis of the sale of a book and the sale of computer software. Professor Atiyah explains this distinction by reference to the difference in the *effect* that books and computer software may have upon their physical environment. The software may be capable of causing damage or harm to the system it enters, whereas all but the most woodworm infested book is unlikely to have an effect upon its surroundings.<sup>41</sup> A further distinction can be identified due to the fact that the effect of the software on the hardware may be automatic, giving the user no opportunity to exercise his own judgement to identify any defects or unwanted results.

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<sup>38</sup> DVD's and CD's essentially contain a series of 'bumps' or 'gaps' interpreted by the reader as binary 1's and 0's. This information is simply translated into its recognisable form by the technology or software in the computer, DVD or CD player. On a magnetic tape or disc the arrangement of the magnetic particles is interpreted by the player/reader.

<sup>39</sup> P S Atiyah et al, *The Sale of Goods* 10<sup>th</sup> edn, Longman, Pearson Education, London 2001, at pp 66-71.

<sup>40</sup> 938 F 2d 1033 (9<sup>th</sup> Cir 1991).

<sup>41</sup> *Op cit* note 37 at p 68.

An analogy with certain types of books has also been used in relation to the supply of computer software and hardware together.<sup>42</sup> Where computer software is sold in a package with the hardware<sup>43</sup> it has been suggested that the sale is analogous to many other contracts falling within the SGA because the software is akin to ‘instructions’ telling the hardware what to do. In the Australian case *Toby Constructions Products v Computer Bar Sales Pty Ltd*<sup>44</sup> a computer system comprising of software and hardware was described thus:

“By itself hardware can do nothing. The really important part of the system is the software. Programs are the instructions or commands that tell the hardware what to do.”<sup>45</sup>

By employing this description it is possible to draw an analogy with decided cases falling within the SGA where misleading ‘instructions’ included with goods led to a finding of a breach of the implied terms as to quality or fitness for purpose.<sup>46</sup> However, this line of reasoning only equates to a breach of implied terms in relation to the hardware (clearly ‘goods’) rather than supporting an argument that the software or ‘instructions’ are goods, in their own right. This renders this particular argument ineffective for items not integrated into something else which has a physical form.

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<sup>42</sup> Although the ‘physical’ argument discussed above could be of equal application.

<sup>43</sup> As is becoming increasingly common with Microsoft’s domination of the software market.

<sup>44</sup> [1983] 2 NSWLR 48.

<sup>45</sup> *Ibid* at 51. This description was adopted in the *St Albans* case by Scott-Baker J.

<sup>46</sup> s 14. See *Wormell v RHM Agriculture Ltd* [1986] 1 All ER 769, a decision reversed by the Court of Appeal [1987] 3 All ER 75, but on the ground that the instructions were not misleading. The Court did not suggest that misleading instructions could not amount to a breach.

Professor Atiyah believes that the analysis in the *Wormell* case is far from satisfactory, especially when applied to computer software.<sup>47</sup> He explains that software being described as a ‘set of instructions to a computer’<sup>48</sup> is a false analogy because:

“A computer cannot ‘understand’ in any epistemological sense: it is a machine, and simply follows instructions. It would be a very stupid person who followed an instruction in a *recipe* for a fish dish to ‘cook under the gill’, but a computer would do exactly that. This would argue for a more ‘mechanical’ finding of liability in the case of defective software.”<sup>49</sup>

There has been some debate regarding books and their content, distinguishing the liability associated with the book’s manufacture (the pages and printing etc) from the words contained within the pages. The predominant position in relation to books is that whilst the pages, binding and printing should be subject to the stricter standards of the implied terms in the SGA as to quality and fitness for purpose, the content or information printed on those pages should only be subject to the standards of due care and skill under the SGSA.<sup>50</sup>

“A book would certainly be regarded as goods but information or advice therein would be subjected to a due care standard.”<sup>51</sup>

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<sup>47</sup> *Op cit* note 37, at p 69, n 18.

<sup>48</sup> Citing E Macdonald ‘The council, the computer and the Unfair Contract Terms Act 1977.’ *Modern Law Review*, Vol 58, No 4, pp 585-594, 1995 at p 590.

<sup>49</sup> *Op cit* note 39.

<sup>50</sup> In a transaction for the purchase of a book from a shop, a distinction is made between the liabilities of the shop or publisher and the author. The former may be liable under the SGA for missing pages or poor manufacture but not liable in respect of erroneous information contained within the book. See M G Bridge *The Sale of Goods* Oxford University Press, Oxford, 1998 at p 31.

<sup>51</sup> *Ibid.*

Whilst this is an entirely logical analysis when considering works of fiction or those containing the author's opinions and commentary, there is an equally logical argument that the content of instruction manuals and 'do-it-yourself' books should be subject to the stricter standards implied by the SGA. Professor Lloyd makes a convincing case for this suggestion.<sup>52</sup> He concludes that a work that is intended to be functional and instructional in nature is providing information in the sense that it is 'a material representation of some objectively verifiable fact', and should therefore be open to a claim that it is unfit for its intended purpose if it contains errors. An analogous argument can be made for computer software to the extent that the software as a 'work' is intended to be functional and instructional and therefore should be subject to the requirement that it is fit for its purpose. However, this line of reasoning tends to support an argument relating to *which* standards should apply, rather than to the categorisation of the items as 'goods'.<sup>53</sup>

*Computer software is intellectual property and therefore not goods*

Where computer software is involved in a dispute there has been a tendency to focus upon the intellectual property embodied in the software. Intellectual property rights are 'things in action'<sup>54</sup> and as such are excluded from the definition of goods in s 61 SGA. However, intellectual property rights themselves, in particular copyright, are not usually the subject of the common transactions under discussion here. The transaction will usually be for a copy of the protected work, with a licence, express or implied, to use or get the enjoyment and benefit from that copy. The software, movie, text or music are not in themselves 'copyright'; they are *protected* by copyright in that the copying,

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<sup>52</sup> See I Lloyd 'A rose by any other name' *Journal of Business Law* Jan, pp 48–54, 1993.

<sup>53</sup> This line of reasoning is returned to below. It is submitted that this is the approach that *should* be taken in relation to dematerialised goods.

<sup>54</sup> *Torkington v Magee* [1902] 2 K.B. 427 at p 430: " 'choses in action' is a known legal expression used to describe all personal rights of property which can only be claimed or enforced by action, and not by taking physical possession."

distribution of the work and certain other activities are prohibited without the permission of the rights owner.<sup>55</sup> One of the prohibited activities is of course the copying of the material – an act generally necessary to enable the use of a piece of software on a purchaser’s system, in contrast to other works protected by copyright, such as movies, music or books where no copying is necessary to obtain the benefit from the purchase. However, the fact that a computer program, a movie, a pop album or a book may be protected by intellectual property rights should not preclude it from being ‘goods’. The definition in the SGA excludes transactions for the transfer of the ownership in ‘things in action’. In the normal course of events the ownership rights in proprietary software are not transferred, merely licensed and the contract is not one for intellectual property, but rather for a copy of the protected work. In the US this point was recognised by Weiss J in *Advent Systems Ltd v Unisys Corp*:<sup>56</sup>

“That a computer program may be copyrightable as intellectual property does not alter the fact that once in the form of a floppy disk or other medium, the program is tangible, moveable and available in the marketplace.”

This statement however returns the emphasis to the physical carrier medium as a key to classification and associated rights.

Nevertheless, the problem remains that without examining the ‘substance’ of the transaction at the microscopic level, when the subject matter of the contract is a ‘data product’, no ‘tangible’ items, in the traditional sense, pass. Even if the argument that the contract is for the supply of ‘mere information’ can be defeated, it is at least uncertain

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<sup>55</sup> In the computer software context this was recognised by Steyn J in *Eurodynamics Systems v General Automation Ltd* (1988) unreported 6<sup>th</sup> September LEXIS.

<sup>56</sup> 925 F 2d 670 (1991).

whether digital products can be defined as ‘goods’ within s 61. For this reason some members of the judiciary and academic commentators have adopted a pragmatic approach to the analysis.

### *Pragmatism*

Professor Bridge suggests that software should be treated in the same way as books, with the “seller being strictly liable only for the physical materials on which the program is written”.<sup>57</sup> However, Napier argues that such a conclusion, in relation to software, would offend common sense and defeat a purchaser’s expectations.<sup>58</sup> In the *St Albans* case, Scott-Baker J adopted a pragmatic approach to the question of whether a computer program supplied on a physical medium could be classified as goods. Concluding that software probably was goods within the Act, he stated:

“If the supply of software is not a supply of goods, it is difficult to see what it can be other than something to which no statutory rules apply, thus leaving the recipient unprotected in the absence of express agreement.”<sup>59</sup>

Napier explains that as “structured and coded information” computer software in isolation cannot be goods for the purpose of s 61 SGA and continues:

“...when software is captured on a physical medium do we have, by *specificatio*, creation of a new thing, capable of constituting a ‘good’ ...? If the answer is ‘yes’, as some have suggested then it might be objected that we have allowed the

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<sup>57</sup> M G Bridge *The Sale of Goods* Oxford University Press, Oxford, 1998 at p 31.

<sup>58</sup> B Napier ‘The future of information technology law’ *Cambridge Law Journal*, Vol 51, No 1, pp 46 – 65, 1992, at pp 55-57.

<sup>59</sup> *St Albans City and District Council v. International Computers Limited* [1995] F.S.R. 686 at 699.

physical medium to dictate the legal message. But if we say ‘no’ we face a much greater evil...’’<sup>60</sup>

That greater evil being the exclusion of the ‘software’, in a package, from the implied terms of the SGA, whilst at the same time making the physical discs and documentation subject to the requirements as to quality and fitness.

Although the comments of Scott-Baker J are commendable on the grounds that they emphasise the need to protect purchasers, his reasoning ignores two issues. First, his approach only extends to situations where the software is embodied on a disc or some other medium, ignoring the possibilities of transfer via a non-tangible medium.<sup>61</sup> Second, the statement is not necessarily correct, in that the protection afforded by statute may be provided by equivalent terms being implied at common law.<sup>62</sup>

Fitting computer software and other digital products into an existing legal category does have the advantage of being convenient and creating some certainty. Although computer programs do not fit easily into the traditional definition of goods, it would be appropriate for them to be covered by the same statutory regime. Common transactions by which they are acquired are undoubtedly of the type, and involve the parties, that the legislation was intended to encompass.

The Sale of Goods Act 1893 was introduced to codify the principles of law derived from the existing body of case law and as such reflected commercial activity and the legal concepts of the 19<sup>th</sup> century. It has been continually updated and ‘patched’ by later

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<sup>60</sup> *Op cit* note 56 at p 55.

<sup>61</sup> Direct down loading from the Internet for example.

<sup>62</sup> See *St Albans City and District Council v. International Computers Ltd* [1997] F.S.R. 251 at 265. However, certain measures including unfair terms legislation and distance selling provisions are more difficult for the common law to emulate.

legislation in order to accommodate and adapt to 20<sup>th</sup> century commercial activity. The implied terms as to description, quality and fitness, with only minor amendments since the Acts introduction,<sup>63</sup> provide minimum basic standards which a buyer might reasonably expect. In the 19<sup>th</sup> century the courts became willing to imply terms into sale of goods contracts as a need to modify the well established ‘caveat emptor’ approach was recognised. Professor Bradgate suggests that:

“Such an approach might be justifiable in an age where goods were generally simple and were normally traded at markets, where buyers had the opportunity to examine goods before buying. However, the industrial revolution led to great changes in the number and complexity of goods sold, to the involvement of many more individuals in the purchase of complex items, and, with improvements in transport and communication, to different ways of doing business”<sup>64</sup>

Hence, the individual buyers ability to ‘beware’ when contracting in the new mass market of consumables had been considerably eroded. The terms implied by the courts were an attempt to redress the imbalance created and make sellers legally responsible for the quality of their products directly rather than relying on market forces to provide sufficient protection for buyers. The justifications for this approach remain relevant today and have become a matter of policy in the United Kingdom and European Union. It would appear therefore, as a matter of policy, that a mass produced and marketed item which the buyer may not be able to examine in any meaningful way before purchase must be subject to the minimum standards prescribed in the implied terms. This should be the case the product can ‘technically’ be called ‘goods’ or not.

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<sup>63</sup> For example; the much criticised ‘merchantable quality’ terminology remained until 1994.

<sup>64</sup> R Bradgate *Commercial Law* 3<sup>rd</sup> edn Butterworths, London, 2003, at p 273.

It has been argued that computer software differs in many ways when compared with other 'goods', it would not be the first time that computer software was perhaps labelled inappropriately because an existing statutory regime is considered most appropriate to accommodate it. Computer software was initially protected 'as a literary work' for the purposes of copyright protection, even though it was considerably different to existing literary works. However, the long term effect of such an approach may be undesirable, leading to over-complex technical argument and further uncertainty. Professor Macdonald suggests that although, to an extent, computer software is akin to books, music CD's and videos, the 'functional' nature of computer software (see above) makes it sufficiently different from those types of goods not to be included in the same category. In addition, the categorisation is too linked to the medium used to transfer the software, 'inappropriately divorcing' programs transferred on a physical medium from those which are not.<sup>65</sup> The same could be said of music, films or electronic books. This line of reasoning follows the approach adopted by Lord Penrose in the Scottish case *Beta v Adobe*.<sup>66</sup> In his *obiter* comments he suggested that treating software supplied on a physical carrier, such as a disk, as goods was an unattractive proposition because

"It appears to emphasise the role of the physical medium, and to relate the transaction in the medium to sale or hire of goods. It would have the somewhat odd result that the dominant characteristic of the complex product, in terms of value or of the significant interests of parties, would be subordinated to the medium by which it was transmitted to the user in analysing the true nature and effect of the contract."<sup>67</sup>

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<sup>65</sup> E Macdonald and D Rowland *Information Technology Law*. 2<sup>nd</sup> edn, Cavendish, London 2000, at p 185.

<sup>66</sup> *Beta Computers (Europe) Ltd v. Adobe Systems (Europe) Ltd* [1996] FSR 367.

<sup>67</sup> *Ibid* at p 376.

He continued to criticise the view that where software is supplied on a physical medium it should be regarded as physical property like a book or a record,<sup>68</sup> and the views expressed by Steyn J in *Eurodynamics Systems plc v General Automation Ltd*<sup>69</sup> that the transfer of software is a transfer of a product. However, it is submitted that although different in nature, a computer software package is sufficiently similar to other goods to be so classified.

*Common sense / reasonable expectations.*

If computer software and other intangibles purchased via electronic contracts do not fit comfortably into existing categories, and it is submitted that in many cases they will not, perhaps they should not be ‘shoe-horned’ inappropriately into an existing category for convenience. This was certainly the opinion of Lord Penrose in *Beta v Adobe*.<sup>70</sup>

“...the supply of proprietary software for a price is a contract *sui generis* which may involve elements of nominate contracts such as sale, but would be inadequately understood if expressed wholly in terms of any of the nominate contracts.”<sup>71</sup>

Although this conclusion is convenient, to the extent that it avoids the difficult issues raised by attempting to force computer software into one of the existing categories, it does raise difficulties of its own. In *St. Albans City and District Council v. International Computers Ltd*<sup>72</sup> Scott-Baker J was concerned that if computer software fell outside the definition of goods the purchaser would find himself ‘unprotected’ by any statutory

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<sup>68</sup> *Ibid.* See also, C Reed and J Angel *Computer Law* 4<sup>th</sup> edn Blackstone Press Limited, London, 2000 at p 44.

<sup>69</sup> 6<sup>th</sup> September 1988 (unreported) LEXIS.

<sup>70</sup> *Op cit* note 63.

<sup>71</sup> *Ibid.*

<sup>72</sup> [1995] FSR 686.

regime.<sup>73</sup> On the same basis Napier concludes that if computer software is not categorised as goods then the ‘legal analysis’ would defeat purchasers ‘common sense expectations’.<sup>74</sup> In addition to these fears it can be argued that by treating software as *sui generis* the law lacks certainty and allows for too much flexibility in judicial decisions. However, some of the criticisms of this approach can be answered, and a level of ‘protection’ found, by looking at other statutory provisions in force and the possible common law implication of terms of quality and fitness.

The first relevant statute to consider is the Unfair Contract Terms Act 1977. Sections 2 and 3 of the Act remain relevant and subject any contractual terms excluding or limiting liability for negligence or breach of contract in general, to the test of reasonableness.<sup>75</sup> There would, however, appear to be no statutory implied terms relating to the quality of goods or standards of service, that a purchaser could expect from a supplier. Hence, it would appear that to this extent, the purchaser is indeed ‘unprotected’.

It has been suggested that there would be no reason why a court could not imply equivalent terms, to those found in the SGA, into the parties’ contract at common law.<sup>76</sup> Previously, where a transaction was not included in a statute, the judiciary have demonstrated a willingness to imply equivalent terms to those found in the relevant statute, where appropriate. For example, in *Dodd v. Wilson*<sup>77</sup> the contract concerned did not fall within the Sale of Goods Act 1893, nevertheless an equivalent term was implied at common law. The implication of a term can be based on the intentions of the parties,

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<sup>73</sup> *Ibid* at 699.

<sup>74</sup> *Op cit* note 56.

<sup>75</sup> Defined in s 11. Where the contract is between a supplier and a consumer the Regulations on Unfair Terms in Consumer Contracts 1999 would also remain relevant.

<sup>76</sup> See, E Macdonald and D Rowland *Information Technology Law*. 2<sup>nd</sup> edn, Cavendish, London, 2000 Ch 4, pp 185-186.

<sup>77</sup> [1946] 2 All ER 691.

(in fact), or alternatively as a matter of law because of the type of contract being entered into. Further support for this suggestion can be found in the *obiter* comments of Sir Iain Glidewell in *St Albans City and District Council v. International Computers Ltd*,

“In the present case if, contrary to my view, the matter were not covered by express terms of the contract, I would hold that the contract was subject to an implied term that [the software] was reasonably fit for, that is, reasonably capable of achieving, the purpose specified.”<sup>78</sup>

Although these comments were *obiter* they clearly state the approach adopted by the courts when faced with questions of liability and the implication of terms. It would appear that if a contract for the supply of computer software were to be treated *sui generis*, the purchaser is perhaps not as ‘unprotected’ as originally perceived by Scott-Baker J.

However, there are some significant gaps in the protection which can be afforded by the courts implying terms at common law<sup>79</sup> and such terms are subject to express contrary terms and exemption clauses to a greater extent than their statutory counterparts.<sup>80</sup>

## **Conclusions**

From the issues raised in this paper a number of points can be highlighted. The traditional definitions of goods and services appear inappropriate when ‘digital products’ are considered. A detailed and technical analysis can be formulated to accommodate these items into existing definitions but this is undesirable because it would result in even more uncertainty in the law and lead to unhelpful technical debate in the courts.

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<sup>78</sup> *Op cit* note 60 at pp 266 – 267.

<sup>79</sup> For example, the protection afforded the consumer under the Consumer Protection (Distance Selling) Regulations 2000.

<sup>80</sup> For example the protection afforded by s. 6 of the Unfair Contract Terms Act 1977.

A number of the arguments relating to computer software place a disproportionate emphasis on an otherwise unimportant piece of plastic, the carrier medium, to the extent that the presence of this increasingly superfluous carrier can dictate the rights and obligations associated with the contract. Arguably, one cause of this over-emphasis is the antiquated definition of 'goods' in the statute being a decisive factor in relation to liability and obligations.

It is submitted that the standards applicable to items considered 'goods' in the physical world must be applied equally to the items when they are 'dematerialised' and they become 'digital products' because the 'substance' of the contract remains the same. If they are not, then parties involved in electronic commerce may be unjustifiably discriminated against because of their chosen method of supply.

The interesting solution proposed at present is to take our contracts for 'digital products' back to the 19<sup>th</sup> century with the courts dictating, subject to the parties' express contrary provision, which rights and potential liabilities should apply. Whilst this is an eminently pragmatic solution to the problem it is respectfully submitted that it is one which has the potential to omit a century of policy making and lead to uncertainty.

It would appear that the only effective solution would be a clarification of the legal standing of these contracts by the legislature based upon the same policy considerations that led to the introduction of the regulatory measures referred to above. A logical solution would appear to be the addition of 'digital products' to the existing definition of 'goods'. A contract for the download of a 'digital product' such as a movie may then be treated as a composite of sale and service, with the download requiring the standard of

reasonable care and skill and the 'digital product' transferred being given equivalent standing to physical 'goods'. This approach would have the same outcome as the approach advocated by Sir Iain Glidewell in *St Albans* but would have the added advantage of ensuring that the other provisions relating to 'goods' would apply with the same levels of protection for the purchaser, without the unhelpful debate as to whether they will fit into the traditional definition of 'goods'.

Finally, as a more general point, the courts have appeared uncertain and uncomfortable when dealing with issues raised by our increasingly digital world, particularly when they are required to apply outdated and inappropriate definitions and presumptions. Perhaps it is time that the legislature gave more consideration to the potential difficulties which may arise in relation to traditional definitions, when the law has to regulate commercial activity in the 21<sup>st</sup> century.