

ELECTRONIC CONTRACTS:
AN ANALYSIS OF THE LAW
APPLICABLE TO ELECTRONIC
CONTRACTS IN ENGLAND AND
WALES AND ITS ROLE IN
FACILIATING THE GROWTH OF
ELECTRONICS

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Abstract

Electronic commerce has been described as unique, in the opportunities it creates for economic growth and its potential to revolutionise the way business is done. Although initial expectations and predictions have proven rather optimistic, it must nevertheless be accepted that electronic commerce has firmly established its place in the economies of the United Kingdom and European Union.

Although considerable work and discussion has surrounded the creation of a regulatory framework for electronic commerce, insufficient attention has been given to the most fundamental element – the legal regime applicable to electronic contracts. Electronic contracts form the basis of electronic commerce.

Parties have been contracting electronically for some time. However, electronic contracts have unique qualities and attributes making them sufficiently 'different' to contracts entered by more 'traditional' means to raise questions of the applicability and appropriateness of existing legal principles. This work is an examination of the legal environment within which electronic contracts are made. If electronic commerce is to reach its economic potential there must be a stable and predictable legal environment for electronic contracts. In this thesis the existing common law and regulatory principles are analysed, in the context of electronic contracts, to examine whether their application has the potential to create a stable legal environment. It is argued that a combination of; uncertainty in the common law; dated concepts in regulatory measures; and the introduction of new regulation without sufficient consideration of the nature of the electronic environment, has resulted in a lack of clarity in the law applicable to electronic contracts.

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I

Preliminary Issues

Introduction

1.1 Electronic Contracts

Contract *n.* 1. An agreement between two or more parties creating obligations that are enforceable or otherwise recognisable at law <a binding contract>.¹

Electronic → adjective 1 (of a device) having or operating with the aid of many small components, especially microchips and transistors, that control and direct an electric current.

...

3 relating to or carried out using a computer or other electronic device, especially over a network: *electronic shopping*.²

Two relatively well established and reasonably well understood definitions. Put simply, electronic contracts are contracts entered into via, or facilitated by, electronic forms of communication.³ Parties have been contracting electronically for some time. However, electronic contracts have unique qualities and attributes that are sufficiently *different* to contracts entered by more 'traditional' means to raise questions of the applicability and appropriateness of existing legal principles. This work is an examination of the legal environment within which electronic contracts are made.

1.2 Electronic Commerce and Legal Certainty

Electronic commerce has been described as "a unique opportunity to create economic growth, a competitive European industry and new jobs."⁴ It also has "the potential to revolutionise the way business is done and improve the competitiveness of

¹ Blacks Law Dictionary 7th edition. West Group 1999.

² The New Oxford Dictionary of English, Oxford University press 1998.

³ It is accepted that the phrase 'electronic communications' can encompass many of the older and more basic forms of communication such as fax, conventional telephones and even telex. Here, the phrase is used to refer to the more 'modern' forms of communication, including e-mail, mobile-phones and the Internet, unless otherwise stated.

⁴ Proposal for a European Parliament and Council Directive on certain legal aspects of electronic commerce in the internal market. (COM(98) 586 final); (OJ C30, (05.02.99)) at p.3.

British industry.”⁵ Although initial expectations and predictions have proven rather optimistic, it must nevertheless be accepted that electronic commerce has firmly established its place in the economies of the United Kingdom and European Union.

Trust and confidence in the electronic environment and in entering electronic contracts has a significant role to play in the development of electronic commerce. The legal regime applicable to electronic commerce must not only be consistent and predictable but must also foster an environment of trust and confidence, particularly for weaker parties such as consumers.

Contracts created and often performed in the electronic environment form the basis of electronic commerce. A contract is required; to access the electronic environment (a contract with an Internet Service Provider (ISP) for example); to create a presence in that environment (contracts for domain names, hosting and e-mail services); and most obviously contracts to transact with customers and participate in the e-commerce economy, an economy worth 14,572 billion US dollars⁶ and an estimated 172 billion Euro⁷ in 2001.

A stable and predictable legal environment for electronic contracts is therefore essential for the growth of electronic commerce. The European Commission has indicated that:

“electronic commerce will not fully develop if concluding online contracts is hampered.”⁸

The Commission also identified key elements required to provide an appropriate legal environment to promote electronic commerce and facilitate the use of electronic contracts. The essential elements are:

- 1) the removal of legal ‘barriers’ to the use of electronic contracts;
- 2) a non-discriminatory or medium neutral approach to contracts formed and performed by electronic means; and

⁵ Department of Trade and Industry. *Building Confidence in Electronic Commerce – A Consultation Document*. 5th March 1999 URN 99/642 at p.1.

⁶ U.S. Census Bureau. ‘E-Stats’ 2001. Available at; www.census.gov/estats.

⁷ Eurostat ‘E-Commerce in Europe’ 2000/2001 Available at; <http://europa.eu.int/comm/enterprise/ict/studies/lr-e-comm-in-eur-2001.pdf>.

⁸ *Op cit* fn. 4 at p. 4.

- 3) the creation of legal certainty in the principles and legislation applicable to contractual relationships created in the electronic environment.⁹

It is often said that business parties prefer a 'light touch' approach to the regulation of commercial activity, allowing for party autonomy wherever possible. However, it is equally important in many areas (particularly those considered in this thesis) for there to be a sufficient level of legal certainty to enable businessmen to order their affairs. As Professor Roy Goode states:

"A recurrent theme in the development of English commercial law is the importance attached to predictability. As our judges have said again and again over the past 300 years, it is better that the law should be *certain* than that in every case it should be just."¹⁰

Legal certainty in this context is required to provide a predictable and stable legal environment within which a business party can ascertain the potential risks, liabilities and responsibilities which may arise from a particular venture. Whilst legal certainty is desirable for commercial activity in general it is particularly important for electronic commerce because the activity is new to those participating and a lack of legal certainty may undermine the confidence required to take steps into this 'new' territory. There is a general consensus that if electronic commerce is to reach its potential then a consistent and predictable legal environment must be created:

"The pace and the extent to which Europe will benefit from electronic commerce greatly depends on having up-to-date legislation that fully meets the needs of business and consumers"¹¹

The needs of the business community in relation to legal certainty and predictability can be seen in the report for the Organisation for Economic Cooperation and Development (OECD) chaired by Mr. John Sacher in 1997. In the report it is asserted that:

⁹ *Ibid* at p. 7, 8, and 11.

¹⁰ Goode, R. *The Hamlyn Lectures: Commercial Law in the Next Millennium*. (Sweet & Maxwell: London, 1998) p.14. *Emphasis* added.

¹¹ "A European Initiative in Electronic Commerce" COM(97)157 at p.12.

“Commerce depends on confidence. For the electronic market-place to flourish in both its customer and enterprise dimensions, buyers and sellers alike must have at least the level of confidence in the outcome of Electronic Commerce as they have in more traditional kinds of transactions.”¹²

and

“As a matter of urgency, governments need to clarify the legal definitions, practices and structures that pertain to commercial activities in an electronic environment”

The report identifies a number of key issues. In particular the fact that an increased level of legal certainty, when compared to traditional commercial activity, is not necessarily required but rather that the nature of electronic commerce and associated technological developments challenge existing legal provisions, principles and definitions creating a potentially detrimental degree of uncertainty. This is illustrated by reference to the nature of the electronic environment and the prevalence of contracts for intangible products in electronic commerce. The report concludes that governments should “adjust existing laws and regulations so that they apply to “intangible” as well as “material” product environments.”¹³

For consumers the need for ‘legal certainty’ relates to the protection they are afforded when entering transactions with parties via electronic commerce, particularly parties in other states. Consumers are becoming increasingly aware of their rights through the media and the availability and dissemination of information promoted by the European Union and implemented by the Office of Fair Trading. Electronic commerce is relatively new and an unknown quantity to consumers and the EU and other interested bodies¹⁴ have recognised that uncertainty as to what legal protection consumers are afforded in cross border electronic contracts may lead to a lack of confidence. The Council of the European Union identified particular concerns including the legal regime

¹² OECD Report of the Group of High-Level Private Sector Experts on Electronic Commerce. *Electronic Commerce: Opportunities and Challenges for Government (The Sacher Report)*, OECD, August 1997 p.16 & 42.

¹³ *Ibid.* This issue is considered in below in chapter 3 and in detail in the context of implied terms in chapter 13.

¹⁴ The European Consumer Law Group and the National Consumer Council for example.

applicable to consumer contracts and contractual terms, liabilities and responsibilities.¹⁵ The European Consumer Law Group (ECLG) focus on this crucial issue in their report on consumer transactions on the Internet in 2000:

“The development of the Internet as a shopping channel can be of great benefit to consumers. It can lead to lower prices, a more varied range of choices of delivery and more flexible payment solutions. But still there is a long way to go before consumer protection is sufficient and business attitudes serious enough to develop a thriving market. Today many consumers lack confidence in this new technology.

This report deals with four important issues related to the Internet: contract conclusion, payment, privacy, and jurisdiction/applicable law. These are the areas of major importance, and concern, for consumers. Without a good legal framework and a high level of consumer protection in these areas consumers will not use the Internet as a shopping channel and the Internet will not develop to its potential.”¹⁶

One of the main benefits associated with the electronic environment is the ability to conveniently and quickly conclude contracts with parties in another State. This factor must also be introduced into any discussion of the legal environment applicable to electronic contracts. Although cross-border trade is not a new phenomenon, the extent to which it is now possible, and the accessibility of cross-border trade to the ordinary consumer, is a unique attribute of electronic commerce

The law then has a dual role, to facilitate and promote the use of electronic contracts by providing legal certainty and to create an environment of trust and confidence for electronic commerce.

So to the purpose of this research: Can the law applicable to contractual relationships in England and Wales, as influenced by legislation from the European Community, fulfil these requirements and adequately accommodate electronic contracts?

¹⁵ See; “The Consumer Dimension of the Information Society”- Council Resolution (3.XI.1998. Adopted at the 2128th Council meeting on “Consumer Affairs”, Brussels, 3 November 1998. Article 4 (d, g & h).

¹⁶ Report of the European Consumer Law Group (ECLG) “Consumer Transactions on the Internet” (ECLG/194/2000) at p.2.

The approach adopted in this thesis is to assess the existing common law and regulatory principles to establish,

- 1) Whether they can be applied? (Does the terminology used or basis of the approach adopted make it impossible to apply a particular principle to electronic contracts?)
- 2) What the likely consequences are of the application of the existing principles?
 - a. Is the result absurd, unwelcome or contrary to the purpose or function of the principle or legislation?
 - b. Could the result have a detrimental impact upon the use of electronic contracts and correspondingly electronic commerce?

In addition, a number of regulatory provisions have been implemented because of concerns that existing principles and legislation may not be able to accommodate electronic contracts successfully. These developments will be examined and analysed against,

- a. the problems perceived with the existing law;
- b. the objectives of the new regulation; and
- c. whether the new regulation has or is likely to achieve those objectives.

From this analysis it is possible to assess whether existing law permits, facilitates, or deters the use of electronic contracts.

An important *caveat* to be remembered when considering the electronic environment and electronic contracts was highlighted by Professor Goode in his 1997 Hamlyn Lectures:

“In debates concerning the legal implications of an electronic business environment there is an unfortunate tendency to over-emphasise the technology and to assume that it automatically changes everything so far as legal relationships are concerned. This is a myth which I am anxious to dispel.”

He continued to pose a fundamental question:

“... it is necessary to ask why, if the message is broadly the same, its legal significance should be affected by the medium through which it is sent.”¹⁷

The Professor's comments emphasise the resistance that should meet any discriminatory treatment of contracts formed and performed by electronic means of communication. It follows that, *a fortiori*, the communication medium used to create a contract and the media employed to deliver the subject matter of that contract should not dictate a party's rights. The technology must not be allowed to conceal the fact that an electronic contract is after all just a contract.

1.3 The 'Thesis'

This thesis then is an argument that although considerable work and discussion has surrounded the creation of a regulatory framework for electronic commerce, insufficient attention has been given to the most fundamental element – the legal regime applicable to electronic contracts. It is submitted that although the common law in England and Wales is sufficiently flexible and adaptable to accommodate electronic contracts, regulatory guidance is needed to create a predictable, consistent and favourable environment with sufficient legal certainty to promote the use of electronic contracts and hence, electronic commerce. It is further submitted that where measures have been introduced with the objective of accommodating new methods of communication and electronic contracts, insufficient consideration has been given to the nature of the electronic environment to produce regulation which is sufficiently clear to provide the legal certainty and favourable legal environment desired.

1.4 The Structure of this Work

The research focuses on the law of England and Wales and applicable legislative instruments emanating from the European Community. Where relevant reference is also made to other sources helpful in the analysis of electronic contracting, including the United Nations Commission on International Trade Law (UNCITRAL). The research was concluded on September 1st 2002. However, where possible developments after that date have been included in the text. In the text, words importing the masculine gender include the feminine and vice versa.

¹⁷ Goode, R. *The Hamlyn Lectures: Commercial Law in the Next Millennium*. (Sweet & Maxwell: London, 1998) p.96.

This work is divided into five sections intended to be a progressive examination of the law and electronic contracts. In Section I this introduction is followed by a brief examination of Electronic Data Interchange (EDI) which can be politely referred to as 'the old man' of electronic commerce. Its relegation to a brief discussion is in no way a reflection of its significance to electronic commerce, responsible as it is for the majority of electronic contracting worldwide, but rather a reflection of the nature and environment within which that particular type of electronic commerce takes place. Chapter 3 contains a discussion of issues fundamental to the rest of this work, the nature of the electronic environment and of electronic contracts. This chapter illustrates the important elements of electronic commerce and in particular the significantly different nature of many electronic contracts and their subject matter, compared to their more traditional counterparts.

In Section II the issues relevant to the cross-border potential of electronic commerce and specifically electronic contracts are examined. For the European Community the facilitation of cross-border trade is a fundamental principle of the Single Market. Electronic communications create an unprecedented opportunity for the development of cross border trade between businesses and with consumers throughout Europe. Chapter 4 contains a detailed examination of the rules relating to the adjudicative jurisdiction of the courts in a contractual dispute. The discussion includes an analysis of the Brussels Convention¹⁸ and its recent replacement, the 'Brussels Regulation',¹⁹ introduced to accommodate modern forms of communication and clarify the interpretation of certain provisions contained in the 1968 Convention. The provisions contained in these instruments are analysed in the context of electronic contracts to examine whether they provide the legal certainty and subsequent confidence required to promote the use of electronic contracts. In chapter 5 the same approach is adopted in the examination of the rules for determining the governing or applicable law of the contract. The provisions of the Rome Convention²⁰ form the basis of this analysis and the significance of the lack of a modernising, at present, is considered. The section is concluded with an assessment of whether the specific rules relating to cross border contractual activity are sufficiently clear when applied to the electronic environment to promote the desired confidence in the use of electronic contracts.

¹⁸ The Convention on jurisdiction and the enforcement of judgments in civil and commercial matters, signed at Brussels, 27 September 1968, (OJ L299/32).

¹⁹ Council Regulation (EC) No 44/2001 of 22 December 2000, on 'jurisdiction and the recognition and enforcement of judgments in civil and commercial matters' (OJ L 12/1 (16.1.2001)).

²⁰ The 1980 Rome Convention on the Law Applicable to Contractual Obligations (OJ L 266).

Section III is concerned with the creation of electronic contracts. Chapter 6 highlights the potential problems created by the 'anonymity' of the electronic environment and the difficulty in identifying the party you are communicating with. This situation creates two potential problems for electronic contracts, a lack of confidence in entering a contract with a party with whom you are communicating electronically and the creation of a contract with a party other than the one with whom you were intending to contract. The practical solutions to the first problem and the common law response to the second are considered. The issues raised in this chapter also highlight the need for transparency in electronic commerce and the importance of the provision of information about business parties contracting in the electronic environment. Statutory information requirements have been introduced to address this issue and help promote trust and confidence in electronic commerce and these are also considered in the discussion. Chapter 7 focuses on the potential problems created for electronic contracts by formal legal requirements such as 'writing' and 'signature'. Requirements of this nature, developed and adopted in a paper-based society, are often considered to be potential 'barriers' to the development of electronic commerce. Their potential to act as 'barriers' to the use of electronic contracts and the regulatory solutions to this perceived problem are discussed. The chapter also contains an analysis of formal requirements specifically introduced for the electronic environment. The risks associated with the introduction of such requirements and the potential creation of additional barriers to the use of electronic contracts by the use of inappropriate terminology is highlighted. In chapter 8 the formation of electronic contracts is analysed. The final chapter in this section is devoted to a discussion of the application of traditional contract formation principles to the electronic environment and the potential difficulties associated with this application. There is an inherent flexibility in the common law which allows for the accommodation of new technology and changes in society. Unfortunately the corollary of this flexibility can be legal uncertainty, which may have a detrimental effect on electronic contracting because of the difficulty predicting how existing principles will be applied to electronic contracts. Of particular importance in the electronic environment is the question of when and where a contract is actually formed. To address this issue the common law rules on contractual offer and acceptance must be considered, including the inevitable debate surrounding the postal rule and the point at which an electronic acceptance is effective.

In Section IV the contents, or terms of electronic contracts are the focus. The analysis begins in chapter 9 with an examination of the traditional common law principles relevant to the incorporation of terms and the application of those principles to electronic contracts. Chapters 10, 11 and 12 are concerned with the regulatory control of contractual terms, in particular the Unfair Contract Terms Act 1977 and the Unfair Terms in Consumer Contracts Regulations 1999. This legislation may be particularly important to the development of consumer confidence in participating in electronic commerce. The background and objectives of these pieces of legislation are considered with the substantive elements to examine whether the objectives can be achieved in the electronic environment. The section is concluded with a consideration of the implication of terms into contracts at common law and by statute in chapter 13. Here, a particular issue is raised by the increasing occurrence of 'dematerialised' or intangible items as the subject matter of electronic contracts and the appropriate terms to be implied as to the standards of performance required. The issue has been raised briefly in the courts in relation to computer software and whether the implied terms as to quality in the Sale of Goods Act 1979 should apply to contracts for its supply. As computer software and other intangible items are common subject matter in electronic contracts this issue is of particular importance and uncertainty in the matter may have detrimental effects on electronic commerce.

Section V concludes the work with a re-examination of the initial proposition that the present legal environment applicable to electronic contracts does not provide the legal certainty, consistency and predictability required to promote confidence in the use of electronic contracts and the development of electronic commerce.

The topics considered in this thesis were chosen on the basis of their significance to electronic contracting in the United Kingdom and cross border trade in general within the European Union. From the preliminary research it was clear that the areas identified would pose a significant challenge to existing legal rules. The subject matter chosen also broadly reflects the issues which have been prominent in regulatory developments and policy discussions concerning electronic commerce at an International, European and National level.

A discussion of the nature of the electronic environment and electronic contracts is an essential starting point. However, before that discussion, brief consideration must be given to a particular form of electronic commerce and a well established form of electronic contracting, Electronic Data Interchange (EDI).

Electronic Data Interchange

At this point a brief discussion of Electronic Data Interchange (EDI) is required. Electronic Data Interchange (EDI) is one of the oldest and hence, most established forms of electronic commerce. In the banking and airline sectors EDI has been in use since the 1960's.¹ Its function is primarily the transfer of data between users, whether on a floppy disc delivered by a courier or via a direct computer link. The purpose of such data can range from simple information exchange to facilitating complex stock management and payment systems. The UNCITRAL Model Law on Electronic Commerce defines EDI as,

“the electronic transfer from computer to computer of information using an agreed standard to structure the information.”²

EDI and its associated technology were the focus of early discussions of the legal issues now commonly discussed under the broader mantle of ‘electronic commerce’. The shift in focus from EDI to Electronic Commerce can be attributed to two main factors.³ The first has been the rapid development of technology and the widespread availability of that technology, making EDI only one element in the electronic commerce phenomenon. This move is reflected in one of the earliest attempts to guide the regulation of electronic commerce, the UNCITRAL Model Law. The Model Law began life, and its key principles were developed, under the auspices of an investigation of the legal issues raised by EDI. Identifying the need to encompass a broader range of communications used in electronic commerce the UNCITRAL sought to provide,

¹ See, Lloyd, I. *Legal Aspects of the Information Society* (London: Butterworths, 2000) at, p. 233.

² Article 2(b) of the UNCITRAL Model Law on Electronic Commerce (1996). General Assembly Resolution 51/162 of 16 December 1996. Available at; <http://www.uncitral.org/english/texts/electcom/ml-ecomm.htm>.

³ See *op cit* fn.1 at p. 233.

“a general framework that would identify the issues and provide a set of legal principles and basic legal rules governing communication through electronic commerce.”⁴

indicating that the issues under consideration had a much broader sphere of application.

The second factor is the pre-formulated structure within which EDI takes place. EDI can produce considerable savings in human and paper resources and increase speed and efficiency.⁵ However, in order to obtain these benefits the system put in place must be highly structured with appropriate safeguards to reduce the risks associated with electronic systems.⁶ In order to achieve this, the transactions between the parties usually take place within a highly structured regime, agreed upon in advance. The potential for disputes arising due to legal uncertainties is considerably reduced. The parties will make provision for a variety of these issues before any transactions take place. These provisions are usually found in an Interchange Agreement. In the agreement the parties will generally prescribe technical specifications, formats and protocols; security, confidentiality and archiving procedures; dispute resolution and legal forum provisions; and importantly, detailed provisions relating to contract formation.

In line with the approach adopted by other multinational bodies⁷ in 1994 the European Community introduced a Model Interchange Agreement as guidance to parties seeking to take advantage of EDI.⁸ Rather than prescribing the content of Interchange agreements it provides a structure highlighting the key issues, for parties to customise to their own particular needs. Its form and structure is indicative of many such agreements in use by commercial parties. The Model Agreement deals with contract formation as follows:

3.1. The parties, intending to be legally bound by the Agreement, expressly waive any rights to contest the validity of a contract effected by the use of EDI in accordance with the terms and conditions of the Agreement on the sole ground that it was effected by EDI.

⁴ Guide to Enactment of the UNCITRAL Model Law on electronic Commerce (1996) at para 131.

⁵ *Op cit* fn 1.

⁶ Such as system failure and errors in transmission to unauthorised access, and resultant liabilities.

⁷ In particular the UN/ECE, 1990-03, definition of UN/EDIFACT: United Nations rules for Electronic Data Interchange for Administration, Commerce and Transport. They comprise a set of internationally agreed standards, directories and guidelines for the electronic interchange of structured data, and in particular that related to trade in goods and services between independent, computerised information systems

⁸ EC Model Interchange Agreement – 94/820/EC OJ L338/98 (28.12.1994).

3.2. Each party shall ensure that the content of an EDI message sent or received is not inconsistent with the law of its own respective country, the application of which could restrict the content of an EDI message, and shall take all necessary measures to inform without delay the other party of such an inconsistency.

3.3. A contract effected by the use of EDI shall be concluded at the time and place where the EDI message constituting acceptance of an offer reaches the computer system of the offeror.⁹

An agreement of this nature commits the parties to recognising the validity of contracts entered into via EDI and specifies the time and place of contract formation.¹⁰

By employing the regular, structured format of the interchange agreement, the parties will deal with many of the key legal issues themselves to ensure a smooth operation and the minimum risk of conflict due to legal uncertainty. The existence of such a structured and pre-meditated approach to EDI means that at present, e-mail, web-based and other forms of electronic commerce, where there is no pre-existing relationship between the parties, raise the more significant legal issues for electronic contracting and hence this thesis. However, the substantial economic significance of EDI and its impact on e-commerce as a whole must not be overlooked because,

“Business-to-Business (B2B) activity, which depends critically on Electronic Data Interchange (EDI), dominates e-commerce.”¹¹

Therefore where the issues discussed below have a bearing on EDI or EDI agreements they are incorporated into the discussion.

⁹ Article 3. Validity and formation of contract.

¹⁰ Although phrases such as ‘reaches the computer system of the offeror’ have the potential to create difficulties. See the discussion of ‘receipt’ of electronic communications below chapter 8.4.

¹¹ U.S. Census Bureau. ‘E-Stats’ 2001. Available at; www.census.gov/estats. (March 2003).

3

The Nature of the Electronic Environment and Electronic Contracts

As was indicated in the introduction, the electronic environment, within which electronic contracts are formed, demonstrates a number of unique characteristics. As a consequence many elements of the contractual process and contractual relationships formed in that environment are also unique. It is important to consider these characteristics independently before any detailed analysis is undertaken because the unique characteristics of the electronic environment and electronic contracts have potential implications for many of the legal issues discussed below. In this section the 'nature' of the electronic environment, the contractual process, the contracting parties and the subject matter of electronic contracts will be considered. This analysis, focussing on some well known issues, is essential to the following discussion.

3.1 The 'Nature' of the Electronic Environment

Electronic contracting takes place in the electronic environment, via electronic forms of communication and is an integral element of electronic commerce.

3.1.2 Electronic Communications

Electronic communications involve the exchanging of information by electronic means and can encompass a wide variety of methods, techniques and technology, many of which have been in existence for some time. Section 15 of the Electronic Communications Act 2000 defines "electronic communication" as,

"a communication transmitted (whether from one person to another, from one device to another or from a person to a device or vice versa)-

(a) by means of a telecommunication system (within the meaning of the Telecommunications Act 1984); or

(b) by other means but while in an electronic form

On this broad interpretation electronic communications can encompass any communication transmitted by connecting a device to a telecommunication network. This could be a telephone, a fax machine, a personal computer, a laptop or a Personal Data Assistant (PDA). Electronic contracts are most commonly associated with computer-based forms of communication and Electronic Data Interchange ('EDI' – discussed above) can probably claim to be the oldest form of computer based electronic contracting.¹ Here, the communication is automated, and contractual messages are sent and received directly between computers, often without any human intervention. However, it is the accessibility and expansion of the Internet and the World Wide Web which has been responsible for the establishment and growth of most electronic commerce based business and hence, electronic contracting. For the majority of electronic contracts on open networks, e-mail and interactive websites are the chosen form of communication. A personal computer or laptop is connected to the Internet or some other network and parties communicate using electronic mail protocols (e-mail) or web-based communications, such as websites. Websites can take a variety of forms and the form adopted not only dictates the function performed by that website but may also have an influence on a number of legal issues.

3.1.2.1 Websites – 'Passive' or 'Interactive'

Websites can be used in a number of ways and they can be broadly classed as 'passive' or 'interactive'. Here the phrase 'passive' is used to describe sites that merely provide information to the viewer, such as advertisements, product ranges and price lists, and contact names and addresses. The phrase 'interactive' describes those sites which allow greater user interaction such as the placing of orders. This may include the sending of automated responses to confirm the receipt of orders, the tracking of orders, and in many cases the automated provision of the service, information or data product ordered. The site may also provide a 'personalised' shopping experience with the use of cookies² to store individual user information and allow the site software to target advertising to

¹ "The most mature form of electronic contracting is electronic data exchange (EDI), which permits trading partners to exchange commercial documents electronically." Baum, M.S. & Perritt, H. *Electronic Contracting, Publishing and EDI Law* (Wiley Law Publications: New York, 1991) p. 2.

² According to 'Netscape', cookies are a "general mechanism which server side connections can use to both store and retrieve information on the client side of the connection." Essentially, cookies are small data files written to your hard drive by web sites when you view them in your internet browser software. These data files contain information the site can use to remember such things as passwords, items in your 'virtual shopping basket' and lists of pages you have visited, to save time on subsequent visits.

the user's profile, such as suggesting linked purchases. Some service providers have co-operated to create 'virtual shopping malls' with 'virtual shop assistants' to guide you around the site with a human face, providing the user with a more familiar shopping experience.³

However, it is important to remember that while this may be one of the most popular methods of electronic contracting at present, the technology involved is constantly developing and there are likely to be significant changes in the future.⁴

3.1.2.2. The 'nature' of electronic communications

The 'nature' of electronic forms of communication also means that it is often difficult to assess 'when' they are sent and 'where' they are sent from. The law often requires, or searches for, some physical manifestation of the subject matter, the parties' presence or the contract itself. The physical concepts of time and place have little meaning in the electronic environment, but many legal concepts are predicated upon the location of a certain thing at a particular time. At the simplest level, it makes the ascertaining of the point at which a contractually significant communication is effective problematic. This characteristic also has the potential to create difficulties when ascertaining the appropriate legal forum, or jurisdiction, and the proper law of a contract.⁵

Communications via the Internet, a mobile phone or a PDA are ephemeral in nature and their presence on a piece of equipment may be transient unless steps are taken to store or print the communication. Even if a message is stored, the electronic data can often be easily altered without leaving a trace of the interference. This raises evidential questions as to the existence and reliability of an electronic communication if, for example, a contractual dispute arises as to the existence of a contract or the terms and conditions of a contract.

³ See Shop@AOL.CO.UK; <http://www.shopping.aol.co.uk>.

⁴ Even 'sci-fi' based gadgets, such as a pair of spectacles through which the wearer can gain access to the networks including the Internet, which are operated by voice command or even eye movement, are technologically on the horizon (Tomorrows World, BBC June 2001). Science of fiction? See <http://www.hackwriters.com/futureofnetworks.htm>; <http://www.phys.uni.torun.pl/~dych/ref/01-future/> If nothing more, this serves to illustrate that care must be taken when adopting legal approaches to regulate this area, not to base the concepts too heavily on current technology.

⁵ Considered below in chapter 5.

3.1.3 Electronic Commerce (e-commerce)

Rapid advancements in communications technology and its availability, combined with the expansion of communications networks, have been responsible for the phenomenon known as electronic commerce (e-commerce). A well known phenomenon it may be, but defining it can be more problematic.⁶ The definitions proposed tend to be unspecific and very broad:

“Electronic commerce is a broad concept that covers any commercial transaction that is effected via electronic means and would include such means as facsimile, telex, EDI, internet and telephone.”⁷

A broad and flexible definition is probably appropriate in light of the constant technological change associated with communications technology. However, an overly broad and flexible definition can result in uncertainty regarding its boundaries and the legal principles applicable to the activity.⁸

The ‘e-commerce revolution’, although not quite yet reaching the heights predicted in the nineties, is nevertheless responsible for a significant sum, if not a significant percentage of retail sales and it is the potential for growth which drives Government and business interest. The statistics vary, in reliability and more importantly in what they actually measure, with the difficulty in defining e-commerce being a contributory factor to what often appear to be statistical anomalies. For example, the Office of National Statistics in the UK reported that £56.6 bn worth of goods and services had been sold over the internet in 2000, but on closer examination it became clear that this figure was closer to £11 bn once share trading and other financial trading had been taken out. Nevertheless, this is no small sum for an industry in its infancy, and sales of goods and services via the Internet are predicted to reach £300 bn in the UK by 2005.⁹ It is the environment of electronic commerce within which electronic contracts play a leading role.

⁶ See the comments in paras 7 & 8 of the Guide to Enactment of the UNCITRAL Model Law on electronic Commerce (1996). General Assembly Resolution 51/162 of 16 December 1996, UNCITRAL Model Law On Electronic Commerce. Available at, <http://www.uncitral.org/english/texts/electcom/ml-ecomm.htm>.

⁷ Report of the Electronic Expert Group to the Attorney General (Australia). *Electronic Commerce: Building the Legal Framework*, 1998. <http://www.law.gov.au/aghome/advisory/eceg/ecegreport.html>

⁸ It can also mean that e-commerce activity is not measured consistently in the statistical reports.

⁹ David Metcalf, analyst at Forrester research, quoted in McAuliffe, W. “Government e-Commerce figures ‘massaged’” (2001) *ZDNet UK News* 13/09/2001 at <<http://news.zdnet.co.uk/story/0,,t269-s2095133,00.html>> (Last accessed 24/03/2003).

3.1.4 Mobile Commerce (m-commerce)

One predicted, but nevertheless still awaited development, is the 'boom' in 'm-commerce'. The name represents a form of electronic commerce entered into via a mobile phone.

"m-commerce is essentially e-commerce conducted via mobile phone or Personal Digital Assistant (PDA) and includes subscription based services such as news and information delivered to your mobile device"¹⁰

Not only does this form of communication have portable convenience, it has a potentially enormous market, with some figures suggesting that up to two thirds of Britons own a mobile phone with 80% of households having at least one mobile phone.¹¹ M-commerce also has the potential to open the commercial market to the under 18's, who do not have access to credit cards, but do constitute a large proportion of mobile phone ownership. The economic potential of m-commerce is highlighted by the fact that commercial communications and 'spam' to mobile phone technology is becoming common place.¹²

3.2 The 'Nature' of Electronic Contracts

Although electronic contracts exhibit more similarities to their non-electronic counterparts than differences, the differences that do exist have been the focus of considerable debate. The distinguishing characteristics of electronic contracts are attributable to the technological developments associated with the 'new' forms of communication discussed above. The new methods of communication in the electronic environment, the automated systems developed to send and receive those communications and the 'new' products forming the subject matter of electronic contracts have all contributed to a level of legal uncertainty.

¹⁰ Scroggs, C and Nugent, R. "M-commerce: Payments and Security". [2003] Feb/March *Computers and Law* at p 19.

¹¹ However, it has been suggested that the figure may be somewhat overstated due to 'double counting'. See "Vodafone says figures overstate mobile ownership" Thursday 15th March 2001 Reuters. Available at <http://news.zdnet.co.uk/story/0,,t269-s2085035,00.html>>. The 80% figure includes both adult and child users see "Key trends in fixed and mobile telephony, and Internet: Residential consumers" OFTEL 17 June 2002. Available at <http://www.oftel.gov.uk/publications/research/2002/trenr0602.pdf>.

¹² 'Spam' is the common phrase used to describe unsolicited commercial communications, originally developed in reference to e-mail.

3.2.1 The Methods of Communication

Communication, in the electronic environment, by whatever means, is fast, convenient and can be automated to a greater extent than most non-electronic forms of communication. Electronic communications, in particular the Internet, also have the advantage of 'scale' providing a potentially massive, readily accessible global market for businesses for minimal expense. For marketing purposes electronic communications are a goldmine, a mass audience with minimal costs. For the individual, the business party and governments internationally, this has meant unsolicited commercial communications, or 'spamming', the invasion of privacy and the 'jamming' of networks.¹³

Access to the electronic environment brings with it potential risks and liabilities whether entering contracts electronically or simply marketing goods and services. While the electronic environment itself is not a respecter of geographical or political boundaries the business or service provider must be, to avoid incurring civil or criminal liability imposed by national law to regulate 'activity' within state borders or with citizens of that state.¹⁴

For the consumer, electronic communications bring the promise of increased competition, better value and lower prices. However, once again there are inherent disadvantages created by the very factors responsible for the potential benefits. Cross-border contracts create the potential for confusion and uncertainty as to the level of consumer protection available, which in turn can reduce trust and confidence in entering cross-border electronic contracts.

With the benefits associated with electronic forms of communications come the inevitable risks of a communication containing errors or being sent in error. The complete failure of a communication is also a realistic possibility. While the law has dealt with this type of occurrence previously, the issue will have to be considered again in the light of the numerous potential problems which may arise with electronic communications. For example electronic mail has a habit of being lost or delayed en-route, or becoming scrambled and nonsensical because of the packet switching

¹³ See Department of Trade and Industry "Building Confidence in Electronic Commerce – A Consultation Document" (1999) URN 99/642. at p. 15 para. 28 et seq.

¹⁴ For example defamatory comments 'published' in the US but accessible in Australia have attracted liability, see *Dow Jones & Company Inc v Gutnick* [2002] HCA 56 (10 December 2002). Also see nua.com "Publish and be damned" December 16, 2002 available at <http://www.nua.ie/surveys/analysis/weekly_editorial.html>.

technology used.¹⁵ Equally possible is an inadvertent click on a 'send' button or icon instantaneously delivering an unintended, contractually significant message. Faulty software may result in the delivery of inaccurate communications to large numbers of customers, or the acceptance of an offer which would not have been contemplated by the supplier. In each situation the court will be left to decide where liability should fall and the issue may even be complicated further because the contracting 'parties' may not be quite what they seem.

3.2.2 Contracting Parties

In the electronic environment the contracting parties will generally be the same parties who enter non-electronic contracts. Individuals may enter contracts with one another, in much the same way as in regular private sales. However, the popularity of online 'auction' sites, such as eBay, has increased the opportunities for this type of contract and electronic communications have introduced individuals to the possibility of entering private contracts with individuals in other states, previously a comparatively rare occurrence.

Many businesses have been using electronic communications to enter contracts with their trading partners for some time. EDI has been particularly popular with business parties with an established relationship who enter contracts with one another on a regular basis. Business to business (B2B) electronic contracts account for the largest section of electronic commerce both in number of transactions and value with the latest figures suggesting that B2B contracts constitute 93% of all e-commerce transactions in the US.¹⁶ In the European Union the total value of Internet e-commerce in 2001 was estimated at 172 billion Euros with B2B transactions constituting 87% of the total.¹⁷

However, the status of B2B e-commerce may be challenged for 'total value', by the growth in business to government (B2G) procurement contracts being tendered electronically. Governments in the EU and the UK government in particular, have been keen to embrace the new electronic media, emphasising the benefits to citizens of living in the information society and setting ambitious goals for access and use. In the UK, the goal championed by the 'Office of the eEnvoy', is to ensure that those who want it have Internet access by 2005, and to make all government services available electronically by

¹⁵ For a more detailed discussion of 'packet-switching' see Reed, C. *Internet Law: Text and Materials* (Butterworths: London, 2000) at p. 10-14.

¹⁶ U.S. Census Bureau. 'E-Stats' 2001. Available at; <http://www.census.gov/estats>.

¹⁷ European Information Technology Observatory (EITO) 2002, 10th edition <http://www.eito.com>.

the same year.¹⁸ Some of the services available will introduce a consumer to Government (C2G) category of electronic commerce.

The consumer sector is accounting for increasing numbers of electronic contracts and business to consumer (B2C) contracts are seen as one of the major areas for growth in electronic commerce the future. The global nature of electronic communications has also led to the increased possibility of cross-border consumer activity. While this has occurred previously, the scale of this activity may increase due to easy access to wider markets, greater competition and hence better value. The consumer entry into cross-border trade has highlighted the need to ensure that consumer protection measures are in place, providing a 'base level' of protection for consumers to help promote trust and confidence.¹⁹

3.2.2.1 'Electronic Parties'

A development 'unique' to the electronic environment and the Internet in particular, is the creation of automated systems controlled by complex computer software. Often called 'electronic agents' they make the contracting process more convenient and less time consuming for consumers and suppliers. By using electronic systems, such as electronic agents, the need for human interaction can be minimised, creating greater transactional opportunities and reducing costs. This factor has been exploited by those using EDI for some time, drastically cutting the labour costs associated with stock level maintenance and improving cash-flow by facilitating 'last minute ordering'.

The point of legal significance here is the fact that at least one of the 'human parties' to the contract will often have no conscious role in the entering, and sometimes performance of the contract particularly where so-called 'intelligent' electronic agents have been used.

¹⁸ 'Modernising Government' White Paper March 1999, <http://www.archive.official-documents.co.uk/document/cm43/4310/4310.htm>. For example, registering and licensing vehicles. Services currently available can be found at, [http://www.e-envoy.gov.uk/oeo/oeo.nsf/sections/about-servicetransformation-dooline/\\$file/citizens.htm](http://www.e-envoy.gov.uk/oeo/oeo.nsf/sections/about-servicetransformation-dooline/$file/citizens.htm).

¹⁹ Organisation for Economic Co-operation and Development (OECD) 'Recommendation of the OECD Council Concerning Guidelines for Consumer Protection in the Context of Electronic Commerce.' (1999) at 1. Available at < <http://webnet1.oecd.org/pdf/M00000000/M00000363.pdf>>.

3.2.2.2 Electronic Agents²⁰

'Electronic agents' are software programs instructed to undertake particular tasks, for example finding particular goods or services, tracking down the best prices and even concluding transactions on behalf of the user. As a technology they are in their infancy but they are considered by many to be tools that will revolutionise electronic commerce by making shopping on the Internet less time consuming for the consumer and providing sellers with vital information about their customers.²¹ As with most recent advancements in information technology there has been initial resistance to their use, because of security fears and concerns about privacy and data protection, particularly in relation to 'customer profiling'.²²

There are also concerns, voiced by sellers and service providers, that the use of electronic agents will 'strip away' their 'brand image' because they often remove the need to visit the vendor's website. For this reason some online businesses have blocked access to their websites by 'shopping agents' to avoid being ranked solely on price.²³ The ability of suppliers to rely on the terms and conditions available on their website may also be compromised if electronic agents are used. If the supplier uses a 'click wrap' licence to ensure that purchasers review his terms, an electronic agent will automatically proceed through, or completely bypass the terms page with no consideration for its contents with the user having no opportunity to even be aware of its existence.²⁴

As the technology develops and the concerns are addressed, the use of electronic agents will become an integral and necessary part of electronic commerce.²⁵ For the purpose of this discussion it is their role in the contractual process and the legal significance of that role which is of interest.

²⁰ Also referred to as 'intelligent agents', 'software agents', 'software robots', or 'softbots'. A comprehensive review of this technology is beyond the scope of this work, but for a very informative insight see Gonzalo, S. "A Business Outlook Regarding Electronic Agents" (2001)9 *International Journal of Law and IT* 189.

²¹ Weitzenboeck, E. M. "Electronic Agents And The Formation Of Contracts" (2001)9 *International Journal of Law and IT* 204.

²² Issues of privacy and data protection are beyond the scope of this work, but for a consideration of those issues in the context of electronic agents see, Bygrave, L. A. "Electronic Agents And Privacy: A Cyberspace Odyssey 2001" (2001)9 *International Journal of Law and IT* 275.

²³ Levi, S. & Sporn, R. "Can Programs Bind Humans To Contracts?" (1997) *The National Law Journal* B09. Available at <<http://www.ljextra.com/internet/0113shrink.html>> (last accessed 22/06/1999).

²⁴ *Ibid.* However, this may not affect incorporation of the terms at common law, see the discussion below in chapter 9.

²⁵ It is suggested that they will become 'necessary' for e-commerce because as the networks and their use expands the vast number of users and amount of information available will make it more time consuming to find the product or service desired, at the best price. The increased size of the market and corresponding increase in competition is perceived as one of the main advantages of electronic commerce, but to fulfil its potential the market must be readily accessible and convenient to use.

The most recent electronic agents demonstrate artificial intelligence and can, arguably, be seen to behave autonomously, determining their behaviour by reference to their own experiences.²⁶ To this extent it can be seen that the direct intervention of a human being is not necessary for its operation. In relation to electronic contracts, electronic agents raise questions of capacity, intent, participation and liability, because as Weitzenboeck indicates,

“In such a situation, the question that naturally arises is whether a contract that has been generated and conducted by an intelligent agent without any direct human intervention, is legally binding and on whom.”²⁷

It must be noted at this point that, at common law, an ‘electronic agent’ is unlikely to be treated as an ‘agent’ for the purpose of the law of agency.²⁸ Agency at common law necessarily requires the consent of two distinct parties, the ‘principal’ and the ‘agent’, to the extent that ‘one person, the agent, has the power to change the legal relations of the other, the principal.’²⁹ It would require a very imaginative approach to apply the concept of ‘consent’ to electronic agents, comprising of computers and computer software. It would be equally difficult to describe the user and the electronic agent as two ‘distinct parties’.

It has been suggested that one way to deal with the activities of intelligent electronic agents would be to confer ‘legal personality’ on them in the same way that limited companies are given legal personality once they are incorporated.³⁰ In this way they would have the legal capacity to enter contracts. However, such an approach has been questioned, because of the inherent uncertainty in the definition and identification of electronic agents and the need for some form of registration system, akin to the registration system for companies, for this approach to be workable. This is seen as an

²⁶ See Russell, S. & Norvig, P. *Artificial Intelligence: A Modern Approach*. (Prentice Hall: New Jersey, 1995).

²⁷ Weitzenboeck, E. M. “Electronic Agents And The Formation Of Contracts” (2001)9 *International Journal of Law and IT* 204.

²⁸ Nevertheless, there have been suggestions that this approach should be adopted. See Fischer, J.P. “Computers as Agents: A Proposed Approach to Revised U.C.C. Article 2” (1997) 72 *Ind. L. J.* 545; and Kerr, I. “Providing for Autonomous Electronic Devices in the Uniform Electronic Commerce Act” (2000) *Uniform Law Conference of Canada*, available at <http://www.law.ualberta.ca/alri/ulc/current/ekerr.pdf>.

²⁹ Guest, A. G. (General Editor) *Chitty on Contracts*, Vol 2 – Specific Contracts, 28th ed. (1999) (Sweet & Maxwell: London), para 31.

³⁰ Allen, T. & Widdison, R. “Can Computers Make Contracts?” (1996) 9 *Harvard Journal of Law & Technology* 25.

unnecessary expense which would be unwelcome and superfluous to the requirements of those engaging in electronic commerce.³¹

Allen & Widdison consider the implications of treating computers, and by analogy electronic agents, as 'mere machines', or simply communication tools or conduits, through which certain acts are performed by the user. In this way the activities of the machine or software are treated as coming directly from the person controlling or instructing them (the user). This approach is often considered as something of a 'legal fiction' because it ignores the involvement of the software altogether and in particular the fact that the software may make, what appear to be, autonomous decisions. This approach can be criticised because it has the potential to produce unfair results by being unnecessarily harsh on the party using the software. Allen & Widdison ask the question,

"Is it fair, or even commercially reasonable, to hold the human trader bound by unexpected communications just because it was theoretically possible that the computer would produce them?"³²

And Weitzenboeck highlights the potential for

"disastrous consequences that could ensue from an electronic bug, from an error of calculation or a programming fault"³³

However, it can be argued that the only party who has any level of control over the activities of an electronic agent is the party who chose to use it, and therefore the risks and liabilities associated with that use can only be borne by him.³⁴

At common law the refusal of the courts to allow parties to 'snap up' offers clearly made in error would also serve to mitigate the harshness of this approach.³⁵ If an electronic agent makes an erroneous offer, which the other party knew or reasonably ought to have known, was incorrect the courts are unlikely to allow him to enforce

³¹ *Op cit* fn. 22.

³² *Op cit* fn.31.

³³ *Op cit* fn.22.

³⁴ He will usually have the opportunity to foresee such risks and adopt contingencies, such as insurance or passing liability on to the supplier of the service or software. However, as indicated by Allen & Widdison there are some occurrences which may be completely unforeseeable by the user. The risks for consumers in the European Union are reduced by virtue of the Electronic Commerce Directive to the extent that they cannot be bound to a contract unless they have had the opportunity to correct any errors. See below in chapter 8.4.

³⁵ See *Hartog v Colin & Shields* [1939] 3 All ER 566; *Scriven Bros & Co v Hindley & Co* [1913] 3 KB 504; and *Centrovincial Estates plc v Merchant Investors Assurance Co Ltd* [1983] Com LR 158.

obligations entered into under that agreement. This approach would certainly accommodate some of the more 'disastrous consequences' envisaged from an error such as the shifting of a decimal point a couple of places to the left in the price of a product.³⁶

The use of automated machines to enter contractual relationships on behalf of their owner has long been accommodated by the courts of England and Wales because of the objective approach adopted to agreement. This issue was famously discussed in *Thomton v Shoe Lane Parking*³⁷ where Lord Denning was in no doubt that the offer is made by the proprietor of the machine when he holds it out as being ready to receive the customer's money.³⁸ The activities of the machine are deemed to be those of the proprietor and he is bound by his apparent 'intention to be bound' to the actions of that machine. When a user introduces an electronic agent into the electronic environment, usually the Internet, with instructions to enter a contract with a party or parties satisfying pre-programmed criterion, an analogy can clearly be drawn with the use of any automated machine and hence, Lord Denning's analysis of the contractual process.

The attribution of communications generated by electronic agents, to the person instructing them would appear to be the approach adopted in the UNCITRAL Model Law on Electronic Commerce.³⁹ In Article 13(2) it states that,

"As between the originator and the addressee, a data message is deemed to be that of the originator if it was sent:

...

(b) by an information system programmed by, or on behalf of, the originator to operate automatically."⁴⁰

In the European Union the importance of electronic agents and related systems was recognised in the development of the Electronic Commerce Directive. However, their consideration was limited to the preliminary materials wherein it was stated that Member States should "not prevent the use of certain electronic systems such as

³⁶ Interesting discussions of this nature followed a pricing error on the Argos website. See Azim-Kahn, R. & MacQueen, H. L. "The Argos Free TV Debacle: Two Legal Opinions" (1999)1(9) *Electronic Business Law* 9-10.

³⁷ [1971] 2 Q.B. 163

³⁸ *Ibid* at p 169.

³⁹ General Assembly Resolution 51/162 Of 16 December 1996 available at; <<http://www.uncitral.org/english/texts/electcom/ml-ecomm.htm>>

⁴⁰ A number of States have introduced legislation based upon the UNCITRAL Model Law. For example Singapore's Electronic Transactions Act 1998, section 13 but cf Australia's Electronic Transactions Act 1999 section 15 which focuses upon the concept of 'authority' to send messages.

intelligent electronic agents”.⁴¹ Electronic agents do not feature in the final directive and this complex issue will ultimately fall to be considered by the courts or legislators in each Member State.

3.2.3 Subject Matter

The subject matter of electronic contracts is a combination of familiar goods and services and ‘new’ subject matter capable of challenging the law and existing presumptions and definitions. Some of these definitions go to the root of contractual liability dictating the implied terms in a particular contract and hence the rights and liabilities of the parties.⁴²

3.2.3.1 Traditional Goods & Traditional Services

Many of the contracts entered into electronically are for traditional goods and services. In the B2B market it may be components, outsourced services, and of course, traditional goods. In the B2C market, books, CD’s, DVD’s, chocolates, flowers, wine, computers and other technology, and clothes are all purchased online. Even the weekly grocery shop can be concluded online with the food delivered to your door.⁴³ The service industries involved with travel, finance and even dating have all made themselves at home in the electronic environment.

3.2.3.2 Information Services

Information of all kinds is available in the electronic environment and the Internet in particular is often called the ‘information superhighway’. A large amount of information is freely available but the majority of useful or valuable information is only available for a price. It is not surprising that a large number of electronic contracts relate to access to information, including access to national statistics, product reviews, television listings and other databases. It has already been noted that the online availability of information about Government services is targeted to be complete by 2005.

⁴¹ Proposal for a European Parliament and Council Directive on certain legal aspects of electronic commerce in the internal market’ COM(1998) 586 final, [1999] OJ C30/42.

⁴² In particular the implied terms found in the Sale of Goods Act 1979 and the Supply of Goods and Services Act 1982. See the discussion below chapter 13.2.

⁴³ As ‘Tesco’ has been keen to inform us, however, for obvious reasons the e-commerce grocery market is somewhat geographically restricted.

However, for businesses the most important information available is information about their customers, or potential customers. As in the 'real world' the sale of data about consumers and their interests is an industry itself. In the electronic environment this information is readily and rapidly accumulated and distributed. This activity has raised serious issues in relation to privacy and data protection.⁴⁴

3.2.3.3 'New & Novel' Subject Matter

With the evolution of electronic communications there has been a corresponding need created for contracts relating to associated subject matter. In particular there are contracts for services directly involved with the electronic communications industry such as service contracts with ISP's, contracts for domain name registration and web-hosting facilities. Developments in technology capable of 'dematerialising' traditionally supplied goods and making it possible to transfer them via electronic forms of communication have made transactions for music, 'books' and feature films particularly popular. The nature of this subject matter may genuinely be called 'new' and 'novel', bringing new questions for the legislators and courts.

Electronic Environment Related Services

To use or access the electronic environment parties require an appropriate 'tool' for communication and a means by which to connect that tool to a network such as the Internet. The technology may come in many forms, for example, personal computers, laptops, mobile phones,⁴⁵ Personal Data Assistants (PDA's), and digital television. A Service Provider is then required to enable connection to the relevant network, for example mobile network service providers such as Vodaphone and Orange, or Internet Service Providers like AOL or Freeserve. The latter may also provide additional services including domain name registration, web hosting and storage, and e-mail accounts, often referred to as Value Added Network Services (VANS). Many electronic contracts are for the provision of these essential services.

⁴⁴ This topic is beyond the scope of this research but see; Macdonald, E & Rowland, D. *Information Technology Law*. 2nd ed. (Cavendish: London, 2000) chapter 7.

⁴⁵ WAP (Wireless Application Protocol) phones were hailed as *the way* to access the Internet on the move but were something of a failure due to lack of speed, reliability and content. See, Banan, M. "The WAP Trap: An Exposé of the Wireless Application Protocol" 2000 Free Protocols Foundation. Available at <http://www.freeprotocols.org/LEAP/Manifesto/article/TheWAPTrap/split/main.html>, last accessed 21/05/2002.

'Dematerialised Goods' and 'Data Products'

It is unnecessary at this point to consider the often unhelpful debate surrounding the definition of 'goods'.⁴⁶ It is sufficient to highlight at this point that the legal status ultimately given to this 'type' of subject matter may have far reaching implications for the contracting parties.⁴⁷ The phrase 'data product' or 'dematerialised goods' is used to identify material downloaded directly to an electronic device or 'streamed' to that device.⁴⁸ In isolation there would appear to be few problems with these items, with analogies being drawn to radio or television transmissions. However, 'intangible' items, in particularly computer software, raise a number of significant questions as to their legal 'nature'.⁴⁹

Few, if any of the items downloaded are 'new'. Music, films, literature and computer software are all commonplace consumer items. In reality the key difference is the fact that the electronic environment provides customers, or 'Information Society Service recipients',⁵⁰ with the opportunity to download the material directly without the need for a carrier medium of some kind to be provided as well. The questions raised by these 'data products', however, far outweigh this simple difference. The question for the courts, and arguably the legislature, is whether this simple difference should dictate the rights and obligations of the parties or the statutory protection available to them.

The difficulty arises when these 'new' products are considered in the light of existing definitions, such as 'goods' and 'services'. It is human nature to be comfortable with the familiar and to order 'new' things by fitting them into an existing, familiar category and at times this can be equally said of the law. This has happened previously with computer software⁵¹ and has been suggested of other 'data products'. Existing categories may have legal rights or obligations attached to them and it is therefore important to be able to establish with some certainty which category the subject matter of an electronic contract may fit in. A common example relates to the different standards implied to contracts for goods or services. Distinguishing between these two

⁴⁶ A debate which can be found below in chapter 13.2.

⁴⁷ See the discussion of implied terms in chapter 13 below.

⁴⁸ Data streaming is the technique of sending large quantities of data, as often required when distributing video, across a network in a continuous stream avoiding the download process. The stream is then accessed by the users PC for display. The streaming media is usually broadcast live, and can be from anywhere in the world.

⁴⁹ *Op cit* fn. 48.

⁵⁰ The phrase employed in European Union legislation to describe services provided in the electronic environment.

⁵¹ For example the treating of software as a 'literary work' for the purpose of copyright protection.

categories has been the cause of some debate for many years.⁵² However, deciding whether an intangible product should be classed as one of these categories or should be treated as something completely 'new', or '*sui generis*', has already caused some discomfort in the courts and been the source of much academic debate.⁵³

3.3 Conclusion

Electronic communications have created a fast, readily accessible market for electronic contracting. In turn this environment has led to the creation of the phenomenon known as electronic commerce. The most popular methods of contracting in this environment are at present, e-mail and websites. However mobile phones and other mobile technology will increasingly play role in electronic contracting as technology develops. This factor creates the first challenge for the law, to accommodate the present technology without being driven by that technology, ensuring that principles applied are flexible enough to encompass future developments.

The second challenge created by the electronic environment is the ephemeral and transient nature of electronic communications which may pose difficult questions for existing legal concepts which are based upon notions of physicality.

The entry of the consumer into the environment of cross-border contracting has highlighted concerns about levels of consumer protection and the control of personal data. A crucial consideration for the development of consumer confidence in entering electronic contracts will be whether protections available in the traditional environment will transfer to electronic contracts and provide an adequate level of consumer protection.

'Electronic agents', or computer programs capable of emulating human decision making, raise conceptual problems in relation to consent and intention in contract, and practical problems with the attribution of automated actions and liabilities flowing from those actions.

In addition to creating the need for contracts relating to activity in the electronic environment electronic communications have changed the very nature of the subject matter contracted for. Films, music albums and even books no longer require a physical

⁵² See the discussion below in chapter 13.

⁵³ See Sir Iain Glidewell in *St Albans City and District Council v. International Computers Ltd* [1997] F.S.R. 251 at 265; West, B. "Software - goods or services?" [2001] Sep, *Legal Executive* 24-25; Bullock, P "The nature of software and standard terms" [1997] 3(1) *Computer and Telecommunications Law Review* 5-7; Adams, J.N. "The snark was a boojum, you see" [1997] 1(3) *Edinburgh Law Review* 386-392; Scott, A.P. "Software as 'goods': nullum simile est idem." [1987] 3(4) *Computer Law & Practice* 133-136.

carrier medium to be transferred from a seller to the customer. This dematerialisation of traditional 'goods' questions existing legal definitions and presumptions used to establish minimum standards required as to quality or performance.

The issues raised by the nature of the electronic environment and contracting in that environment must now be considered against the background of existing legal principles in England and Wales applicable to contracts in general. In this way it should be possible to establish if there is a need for significant changes in the law or alternatively whether the existing legislative regimes and the flexibility of the common law can accommodate electronic contracts.

The first question to address however is whether the courts of England and Wales or the law of England and Wales will have a role to play in a dispute relating to any of the issues raised by electronic contracts. The rules on Jurisdiction and Applicable Law will be considered in the next section.

II

Which Court and Which Law? : Jurisdiction and Applicable Law Issues in Electronic Contracts

Introduction

The chapters in this section examine two issues of vital importance in cross-border contracts; determining which court has jurisdiction to hear a contractual dispute and identifying the correct substantive law to apply in that dispute. For the parties involved these factors may have considerable impact on their rights and obligations under the contract. It is therefore surprising to find that these issues are often relegated to brief, and arguably ineffective, contractual clauses such as,

“In case both parties were unable to settle their disputes out of court, only the courts in Brussels are competent. Only Belgian jurisdiction applies in case of a dispute.”¹

With this approach being common to many ‘well-established’ and ‘new’ electronic commerce based companies, the legal provisions relevant to these issues require consideration.

The issues are by no means new and their significance to international trade has been reflected in the co-operative efforts made by many states since the 1960’s.² The ‘new’ factor introduced by the development of electronic commerce and developments in communications technology, is that traditionally these issues have been the concern of large corporations and multinational businesses. In the past two decades small businesses, and perhaps more significantly consumers, have become increasingly involved in cross-border transactions. As Professor Ian Lloyd highlights:

“Until the emergence of the Internet, international trade was largely the province of the commercial operator. Save for the few souvenirs and bottles of duty-free which a holidaymaker might bring back into the country, almost all of the average

¹ DVD Zone 2, the European DVD specialist at <http://www.dvdzone2.com/>.

² However, as is highlighted below the key provisions which have been ratified tend to emanate from the EU, based upon its single market principles.

consumer's interactions with business would take place in the confines of a single country."³

As a consequence, concerns about whether principles originally developed to regulate international trade can, or are appropriate to, be applied to modern commercial transactions have been raised. In turn this has led to the review and amendment of some well-established and well-known Conventions.⁴

As highlighted in the introduction to this thesis, legal certainty is essential to promote confidence in entering contracts in the electronic environment. Knowing the extent of your rights and obligations is only part of the equation. Without the ability to enforce those rights and obligations effectively, the rights and obligations themselves become meaningless.

Although in many cases jurisdiction and applicable law issues are intrinsically linked, the legal question of which court has jurisdiction and which substantive law should be applied are distinct. A court with jurisdiction to hear a dispute may be compelled to apply the laws of any country in the world if the parties so desire.⁵ The issues require separate consideration in relation to electronic contracting.

The following discussion will consider the existing common law and regulatory frameworks associated with jurisdiction and choice of law issues and their application to electronic commerce and electronic contracts. Continuing the methodology of this thesis the traditional or existing provisions will be analysed to establish:

- 1) the possible outcomes of their application to electronic contracts and desirability of those outcomes;
- 2) the proposed or adopted amendments to those provisions; and
- 3) the impact of those amendments in the light of the perceived problems with the existing provisions.

³ Lloyd, I. *Legal Aspects of the Information Society* (London: Butterworths, 2000) at, p.268. The advent and proliferation of 'booze-cruising' must also be acknowledged as a significant development in cross-border trade, albeit somewhat restricted to UK citizens. (I am reliably informed that 'booze-cruising' is also popular in Finland!)

⁴ See 4.2 below.

⁵ Discussed below at 5.2. The courts do not actually apply the law, as a foreign lawyer would but rather apply the principles on the basis of evidence as a matter of fact. See McClean, D. *Morris: The Conflict of Laws*, 5th ed. (Sweet & Maxwell:London, 2000), chapter 13.

Jurisdiction

In general, parties will prefer to deal with disputes in a familiar forum adhering to the systems and procedures of their own national courts:

“Litigation is never comfortable but it seems less alarming in one’s home town, or at least one’s home country, before local judges. There is perhaps the subconscious feeling that the court is more likely to be on your side if you are the local party; the feeling may even be justified.”¹

For the consumer the prospect of pursuing an errant supplier in a foreign jurisdiction is both logistically and financially prohibitive. For the supplier the possibility of being the subject of litigation in numerous jurisdictions is equally prohibitive. In the context of electronic commerce these fears have the potential to negate many of the perceived benefits of modern communication technologies and stifle growth in an area of great economic potential.

In this chapter the rules associated with the adjudicative jurisdiction of the courts are examined to consider the effects of their application in relation to electronic contracts. In this area the common law has been largely superseded by legislative measures and international Treaty. Therefore, the majority of the discussion will focus upon the interpretation and application of the relevant instruments and the recent amendment of the Brussels Convention by the introduction of an European Community Regulation, specifically intended to take account of modern electronic forms of communication. However, as a preliminary matter a brief mention must be made about the enforcement of judgments.

¹ McClean, D. *Morris: The Conflict of Laws*, 5th ed. (Sweet & Maxwell:London, 2000) at p. 71. There are other implications of course, in particular the financial consideration of travelling to a foreign jurisdiction to resolve disputes and obtaining appropriate legal representation. As a minimum the parties will desire a level of certainty as to which courts may seize jurisdiction in the event of a dispute.

4.1 The Enforceability of Judgments

Before any discussion of the substantive law in a particular state or group of states, it is important to highlight the potential ‘void’ between the obtaining of a judgment and its enforcement. Once judgment is obtained the enforcement of that judgment is dictated by the rules of the defendant’s home-state. Whilst in the European Union and European Economic Area reciprocal arrangements exist for the recognition of judgments from other jurisdictions,² enforcement in states not party to some reciprocal arrangement may be more problematic. Courts of that state will apply their constitutional and private international law principles in deciding whether a judgment can be enforced in that state. As was recently seen in the ‘Yahoo case’³ success in a local court is considerably devalued if you cannot enforce the judgment. In many cases a judgment will only be enforceable, in any real sense, if the defendant has assets in the jurisdiction where judgment is obtained. For parties attracted by the potential benefits of ‘global’ electronic commerce this is yet another factor for consideration in their choice to enter electronic contracts with parties in other States.

4.2 Regulatory Control of Jurisdiction in the European Union and the United Kingdom

In 1968 the six original Member States of the European Community signed a convention on ‘jurisdiction and the enforcement of judgments in civil and commercial matters’, better known as the ‘Brussels Convention’. The Convention was introduced on the basis of Article 220 of the Treaty of Rome⁴

“Member States shall, so far as it is necessary, enter into negotiations with each other with a view to securing for the benefit of their nationals:

...

- the simplification of formalities governing the reciprocal recognition of enforcement judgments of courts or tribunals and of arbitration awards.”

² Such as the Brussels Convention, discussed below.

³ See *LICRA & UEJF v Yahoo! Inc and Yahoo France* (2000) Paris High Court. *Yahoo Inc v La Ligue Contre le Racisme et l'Antisemitisme* (Unreported, November 7, 2001) (ND Cal (US) The issue was a public law matter, but the principle remains true for private law matters although more reciprocity and recognition is evident in private law matters.

⁴ Now Article 293(4) of the Treaty of the European Union.

Clarification of the jurisdiction of Member State courts was considered a significant issue in achieving this objective.⁵ Due to the expansion of the European Community the original Convention was updated and amended by four Accession Conventions to incorporate new Member States and their legal traditions.⁶ Effect was given to the Treaty in the United Kingdom in 1982 by virtue of the Civil Jurisdiction and Judgments Act (CJJA).⁷ To encompass states outside the European Union (EU) a further 'parallel treaty' was signed in Lugano in 1988 by the EU Member States and the members of the European Free Trade Association (EFTA).⁸ An adaptation of the Brussels Convention can also be found in Schedule 4 of the Civil Jurisdiction and Judgments Act, for application in intra-United Kingdom jurisdiction disputes.⁹

The Brussels Convention was drafted at a time when international trade was generally the province of commercial parties, and modern forms of electronic communication could not be envisaged. The Convention suffers from ambiguity in several places in relation to contractual disputes, and these ambiguities particularly in relation to electronic contracts, have the potential to lead to uncertainty. In light of these uncertainties and the developing body of case-law from the European Court of Justice (ECJ), the Council of Ministers recommended the review and revision of the Brussels and Lugano Conventions in 1997.¹⁰ Progress was halted temporarily by the introduction of the Treaty of Amsterdam in 1999, but on March 1st 2002 the Brussels Convention was

⁵ Preamble to the 1968 Convention, as amended.

⁶ For present purposes the accession of the United Kingdom, The Republic of Ireland and Denmark, signed in Luxembourg on the 10th October 1978 is the most significant. The Convention included amendments to reflect the common law nature of the legal systems involved and significantly, made the European Court of Justice the correct forum for questions relating to interpretation of the convention.

⁷ 1982 (c 27) (as amended). This Act did not come into force until all signatories had ratified the treaty in 1987. Section 2 of the 1982 Act states, "The [Brussels Conventions] shall have the force of law in the United Kingdom, and judicial notice shall be taken of them." Section 3A contains an equivalent provision for the Lugano Convention.

⁸ Finland, Iceland, Norway and Sweden. The Lugano Treaty was closely based on the text of the Brussels Convention at the time and for the purpose of this discussion the text found in the Lugano Convention is identical to that found in the Brussels Convention. For this reason the term 'The Conventions' is used and should be treated as encompassing to the Brussels Convention (and the subsequent Accession Treaties) and the Lugano Convention unless stated otherwise. One key difference however, is that the European Court of Justice does not have authoritative rights of interpretation of the Lugano Convention, but signatories are requested to "pay due account to the principles laid down by any relevant decision delivered by courts of the other Contracting States concerning provisions of this Convention"; Article 1 of Protocol 1. Section 3A of the 1982 Act gives the Lugano Convention the force of law in the UK.

⁹ Essentially a person domiciled in a part of the United Kingdom is to be treated as a person domiciled in another contracting state. Schedule 4 of the Act has been amended by (Civil Jurisdiction and Judgments Order 2001 No. 3929) to bring the provisions in line with Regulation 44/2001 (discussed below).

¹⁰ See press release; "Commission adopts draft Regulation on Jurisdiction, Recognition and Enforcement of Judgements in Civil and Commercial Matters", Brussels, 14 July 1999, IP/99/510, at p 1.

replaced in all EU Member States except Denmark,¹¹ by Council Regulation (EC) No 44/2001 of 22 December 2000, on 'jurisdiction and the recognition and enforcement of judgments in civil and commercial matters'.¹² The new Regulation is intended to introduce uniform modern standards for jurisdiction in civil and commercial matters "taking into account new forms of commerce which did not exist when the Brussels Convention was introduced".¹³ There are clear references throughout the development of the Regulation to the concerns of companies engaging in electronic commerce, unsure of their position in jurisdictional disputes under the provisions of the Brussels Convention.¹⁴ This is seen as a disincentive to the development of electronic commerce and it was hoped that clarification, in the form of the new Regulation, would remove uncertainty.¹⁵ The key amendments to the Brussels Convention include:

- the clarification of the special jurisdiction rules in contractual law,
- new provisions to cover all consumer contracts, and
- the introduction of a common concept of the domicile of legal persons.¹⁶

The Commission was keen to ensure a smooth transition and to retain a level of legal harmony between states governed by the new Regulation and those remaining under the scope of the Brussels and Lugano Conventions:

"Continuity between the Brussels Convention and this Regulation should be ensured, and transitional provisions should be laid down to that end. The same need for continuity applies as regards the interpretation of the Brussels Convention by the Court of Justice of the European Communities and the 1971 Protocol [...] should remain applicable also to cases already pending when this Regulation enters into force."¹⁷

¹¹ The United Kingdom and Ireland did not participate in the adoption of measures introduced under Title IV of the EC Treaty (See the 'Protocol on the position of the United Kingdom and Ireland annexed to the EC Treaty.) However, they have indicated their intention to participate fully with the implementation of this proposal. See recital 20 of the final Regulation.

¹² OJ L 12/1 (16.1.2001). (Hereafter, 'the Regulation').

¹³ *Op cit* fn 10, at p.2.

¹⁴ *Ibid*.

¹⁵ *Ibid*. See also the Opinion of the Economic and Social Committee on the 'Proposal for a Council Regulation (EC) on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters'. OJ C 117/6, (26.4.2000), para 2.1.2.1.

¹⁶ *Ibid*.

¹⁷ *Op cit* fn 12, recital 19.

Hence, to a significant extent the provisions relating to jurisdiction, found in the new Regulation, remain unchanged but for the areas perceived as creating uncertainty. In Denmark the Brussels Convention will remain in place, as will the Lugano Convention in EFTA countries. The reforms contained within the Regulation, relevant to contractual obligations, will now be considered with their Brussels and Lugano Convention counterparts and associated case-law.

4.3 The Relevant Legislation

4.3.1 The Scope of the Legislative Instruments

The Conventions and the Regulation apply to civil and commercial matters, whatever the nature of the court or tribunal hearing the dispute.¹⁸ Excluded from the scope of the Convention and Regulation are disputes relating to revenue and customs or administrative matters, all of which are considered to be within the sole competence of the Member State.¹⁹ In addition, exclusive jurisdiction is given to the courts of a particular state in certain matters regardless of a party's domicile. These include, rights *in rem* in immovable property or tenancies of immovable property; proceedings which have as their object the validity of the constitution of a company or the nullity or dissolution of companies; validity of entries in public registers; and the registration or validity of patents, trade marks, designs, or other similar rights.²⁰

4.3.2 Interpretation

In order to facilitate consensus between the Member States the Conventions were couched in very general terms. Due to the broad terminology adopted, the potential for disparate interpretation and application in Member State courts threatened to undermine the harmonising objective of the measures. As a consequence, when the Accession Treaty of 1978 was signed, the ECJ was given jurisdiction to interpret the provisions contained within the Brussels Convention. The ECJ is authoritative and questions of interpretation must be referred to it, or determined in accordance with the

¹⁸ Article 1(1)

¹⁹ Article 1(2) includes; the status or legal capacity of natural persons, rights in property arising out of a matrimonial relationship, wills and succession; bankruptcy, proceedings relating to the winding-up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings; social security; and arbitration.

²⁰ Article 22 of the Regulation (Article 16 of the Convention).

principles laid down by it.²¹ In addition, Member State courts must give consideration to the explanatory reports published in the Official Journal of the European Communities.²² In relation to the Lugano convention the ECJ is not given authoritative status but nevertheless the case-law of the ECJ associated with the Brussels Convention plays an influential role in its application in Member State Courts.²³

In respect of the new Regulation the ECJ has sole jurisdiction to interpret the content of the Regulation by virtue of its powers under Article 234 (ex 177) of the Treaty on European Union.

4.3.3 Key Principles

4.3.3.1 The “Home-State” Principle

The core principle of the Convention and of the Brussels Regulation is that persons domiciled in a Contracting State shall, whatever their nationality, be sued in the courts of that State (his or her ‘home-state’).²⁴ Persons who are not nationals of that state are governed by the private international law rules on jurisdiction applicable to nationals of that State.²⁵ The concept of ‘domicile’ is central to the ‘home-state’ principle. A distinction is made between the domicile of an individual and that of a corporation or other association. In both cases it is for the courts seized to apply the ‘internal law’ of that state to determine whether a party is domiciled in that State.²⁶

4.3.3.2 The Concept of ‘Domicile’

4.3.3.2.1 Individuals

Section 41 of the Civil Jurisdiction and Judgments Act 1982 (CJJA) is the domestic provision in England and Wales that will determine the domicile of individuals for the purposes of the Brussels and Lugano Conventions. For the purposes of the

²¹ Art 1 of the 1971 Protocol as amended by the Accession Treaty of 1978, and s.3(1) of the 1982 Act. The Lugano Convention is not subject to the interpretation of the ECJ but a court must “take account of relevant decisions in the courts of another contracting state”; Article 1 of the second protocol.

²² Section 3(3) of the 1982 Act. The Jenard Report on the 1968 text [1979] O.J.C59/1; The Schlosser Report on the 1978 Accession Treaty [1979] O.J.C59/71; Reports on the 1982 and 1989 Accession Conventions [1986] O.J. C298 and [1990] C189. And the Jenard and Moller report on the Lugano Convention [1990] O.J. C189/57.

²³ See the House of Lords in *Canada Trust Co and Others v. Stolzenberg and Others (No 2)* [2002] 1 A.C. 1.

²⁴ Article 2(1) of the Convention and the Regulation. A ‘Contracting State’ is a signatory of the Convention.

²⁵ Article 2(2) of the Convention and the Regulation.

²⁶ Article 59(1) of the Regulation, Article 52 of the Convention.

Regulation, Schedule 1(9) of the Civil Jurisdiction and Judgments Order 2001 contains a provision modelled on s. 41.²⁷

The relevant provisions require that the individual is 'resident' in the United Kingdom or part thereof and that the nature and circumstances of that residence indicate that he has a 'substantial connection' with the United Kingdom or relevant part.²⁸ Three months residence raises a rebuttable presumption that there is a substantial connection.²⁹ An individual is only to be treated as domiciled in a non-Regulation/Convention State if he is resident in that state and his residence indicates a substantial connection with that state.³⁰

4.3.3.2 Corporations or Associations

Section 42 of the CJA contains the definition of domicile for the purpose of corporations or other associations. The corporation or association will only be treated as domiciled in the United Kingdom (UK) if it has its 'seat' here.³¹ A corporation or association has its 'seat' here if it was incorporated or formed under the law of part of the UK and has its registered office or official address here. Alternatively, if the central management and control of the corporation or association is exercised in the UK, then it will also be treated as having its 'seat' here.³²

During the review of the Brussels Convention it was recognised that a varied approach existed throughout the EU to the creation and seat of a legal entity and hence there had been divergence in the interpretation of 'domicile' in Member State Courts.³³ For this reason the 'domiciles' of companies and other legal persons or associations are given a new, uniform definition by the Regulation in Article 60. This new provision is intended to introduce a 'common concept of the domicile of legal persons'³⁴ and facilitate a harmonisation of approach throughout the EU.

Article 60 defines the domicile of these bodies as "the place where they have their statutory seat, central administration, or principal place of business".³⁵ There is additional guidance for the UK and Ireland in Article 60(2). 'Statutory seat' refers to the

²⁷ The provisions are identical, but for the insertion of the word 'Regulation' and will be discussed together.

²⁸ Civil Jurisdiction and Judgments Act 1982 (c 27), Section 41(2). Schedule 1, s.9(2) of the Order.

²⁹ *Ibid*, Section 41(6), Sch1 s.9(6).

³⁰ *Ibid*, Section 41(7), Sch1 s.9(7).

³¹ s.42(1).

³² Section 42(3).

³³ Particularly after the accession of the United Kingdom where the concept of a corporation's 'seat' of business was practically unknown.

³⁴ *Op cit* fn 10, at p.2.

³⁵ Article 60(1) (a,b & c).

place where the business has its registered office or, where there is no such office, the place of incorporation. If there is no 'incorporation' as such, as is the case with a common partnership, the domicile is the place where that body is legally formed.

A corporation's 'statutory seat' and 'central administration' are relatively straightforward to define and locate. The statutory seat of the body will equate to its place of legal creation and a physical location such as the address registered at Companies House. The central administration of a body will usually equate to the place from which the activities of the body are managed or controlled and this will usually be the physical place where the directors or partners are located. However, it is the interpretation of the 'new' and additional criteria of 'principal place of business' which may have significance in the context of electronic commerce. Should it be interpreted as simply an extension of one or both of the preceding criteria?³⁶ Or alternatively should it be treated as a completely independent alternate criterion in the context of the Regulation?

It may be significant that these criteria are listed as alternatives, rather than a progressive list. It would appear that a corporation or other association may be treated as domiciled in the place where it has *any* of the listed criteria. With a traditional business the three will often be found in the same place, for example Harrods' Registered office (hence statutory seat) is the same address as its central administration and principal place of business.³⁷ However, with the advent of the Internet it is quite possible that all three will be in different jurisdictions. For example, a company may be created and registered in a particular state because of a favourable regulatory or taxation environment. The parties controlling and managing the business, the directors, owners or parent company, may reside in a variety of other states exercising their control by communicating electronically. The company's business transactions may be entered into via websites stored on servers situated in a number of other states dictated by their Internet Service Provider or matters of convenience. The core business of the company may be conducted with parties in one or a number of other unrelated states with no 'physical' connection with the company's statutory seat, management or physical property. In such a case the statutory seat of the company and the location of its central administration, if it can be established at all, bear no relationship to the business activities of the company. This may be completely fortuitous or it may be a deliberate attempt to evade the

³⁶ Being intrinsically linked to the central administration of a body or annexed to the legally most important location such as the bodies' registered office.

³⁷ Harrods, 87-135 Brompton Road, Knightsbridge, London SW1X 7XL.

jurisdiction of the courts of a particular state whilst exploiting the market in the same way that a company registered and physically located there would. Arguably, the 'principal place of business' criteria provides the court with an opportunity to consider the reality of the company's presence in the state. It could be contended that if a company conducts all or the majority of its business with customers in the UK via an interactive website its principal place of business is in the UK.

There is a lack of direct authority on the meaning of Article 60 in the Regulation itself, in commentary, or in ECJ case law. It is clear that there are a number of possible interpretations of the 'principal place of business criteria'. It could be suggested that a corporation's principal place of business would be its primary, most important, main or predominant outlet or the place where it conducts the majority of its business. Alternatively it could be argued that the principal place of business criteria refers to the main physical place of the business and its activity, the place from where control is exercised and as such closely related to where the business has its 'central administration'.

In *King v Crown Energy Trading AG*³⁸ Chambers J³⁹ had to consider the meaning of 'central administration' and 'principal place of business' in the context of the Regulation. The case concerned proceedings brought by *King* for breach of a service agreement and wrongful inducement of breach of contract. *Crown Energy* sought to set aside the proceedings on the ground that *King* had not shown a good arguable case that when the action commenced *Crown Energy* had its central administration and principal place of business within England and Wales within the meaning of Council Regulation 44/2001 Art. 60(1)(b) and Art. 60(1)(c).⁴⁰ The defendants also argued that as their statutory seat, and hence 'domicile' was in Zug, Switzerland they should be sued there.⁴¹

In their defence *Crown Energy* relied heavily on an earlier Court of Appeal decision, *Owners of Cargo Lately Laden on Board the Rewia v Caribbean Liners (Caribtainer) Ltd*.⁴² In this case the court was interpreting a jurisdiction and choice of law clause in the parties' contract which stated that the country where the carrier had its 'principal place of business' had jurisdiction. The court concluded that in the context of the parties agreement 'principal place of business' was intended to mean "chief" or "most important" place, "not necessarily the place where most of the business was carried out"

³⁸ [2003] EWHC 163; [2003] I.L.Pr. 28; Times, March 14, 2003.

³⁹ Judge Chambers QC, sitting as a judge of the Queen's Bench division.

⁴⁰ This is perhaps the first point of note. The Regulation requires the 'central administration' or 'principal place of business' to be within England and Wales. *Crown Energy's* argument treats the two criteria as linked and in the judgment Chambers J appears to adopt a similar approach.

⁴¹ Under the Lugano Convention.

⁴² [1991] 2 Lloyd's Rep. 325.

but rather the “centre from which instructions were given...and ultimate control exercised.”⁴³ The case was decided in line with earlier cases based upon the Merchant Shipping Act 1894 under which the interpretation of the phrase had a significant impact on the registration of vessels.⁴⁴ In that context the principal place of business was considered to be the place from which control and management was exercised. *Crown Energy* argued that their business was entered into and controlled and managed at their offices in Zug and as such their central administration and principal place of business were located in Switzerland.

In his analysis Chambers J began by considering the location of the central administration. In doing so he ascertained the location of the most important bodies and individuals involved in the management of the company. In particular the bodies and individuals responsible for making the key business and policy decisions. He concluded that the ‘heart’ of the company was in London because the effective power and control of the organisation lay in the two management committees operating out of the London offices and hence the ‘central administration’ of the company was located in London. He then continued to determine *Crown Energy’s* ‘principal place of business’. Having emphasised that the judgment in *The Rewia* was delivered in the context of the interpretation of a contractual term and “upon the basis of cases that were themselves concerned with such a term”,⁴⁵ apparently confining the scope of the decision to cases of that nature, he stated that *The Rewia* remained an essential tool in deciding what constituted the carrying on of the principal business of a company. His Honour then proceeded to base his adjudication of ‘principal place of business’ under Article 60(1)(c) on the criteria derived from *The Rewia*⁴⁶ concluding that;

“... the application of the criteria to be derived from *The Rewia* leads me to the conclusion that there is a good arguable case to the effect that its principal place of business is and was in London.”

It has already been stated that in *The Rewia*, the Court of Appeal considered the location of the management and control of the company as decisive in interpreting the

⁴³ *Ibid* at 334 & 335.

⁴⁴ *The Polzeath* [1916] P. 241. Forfeiture in wartime of a vessel that purported to be English rather than German. It must be remembered that these cases were decided during times of war and that this *may* have influenced the approach adopted.

⁴⁵ p.493 para.10

⁴⁶ p.494.

phrase 'principal place of business' as used in the parties' contract. However, in the context of the Regulation these factors are more akin to the ones employed by the court to decide the location of the 'central administration' of a company. It would appear therefore that in *King*, Chambers J considered that the location of the central management and control of the company was the key factor upon which the criteria in Articles 60 (1)(b) & (c) were to be adjudicated.

This approach would appear to support the conclusion that the two criteria are interchangeable and effectively one and the same, rather than being potentially distinct alternatives. Indeed, in his judgment Chambers J states that despite the "disjunctive appearance" of the criteria in Article 60 there

"...could be considerable overlap between what constitutes the central administration of a company and the carrying on of its principal business,"⁴⁷

Whilst this is undeniably true (see the Harrods example above) it is not *necessarily* the case in the modern business environment, particularly the environment of electronic commerce. If the approach adopted in *King* is correct it renders Article 60(1)(c) somewhat redundant. Although it is probable that in many cases this considerable overlap between the 'central administration' and 'principal place of business' criteria will exist, this should not necessarily influence or dictate the interpretation of criteria which, it is submitted, are intended to be viewed distinctly and individually. Although there may be connections and overlap, it is important in the context of the Regulation to treat them as distinct alternatives intended to fulfil the purpose of recognising the close link created and allowing the efficient administration of justice.

Article 60 of the Regulation was intended to introduce 'a common concept of the domicile of legal persons' throughout the EU. However, the criteria included in the article, particularly the concept of a 'principal place of business' are ambiguous and as such, may require some clarification from the ECJ if divergent application is to be avoided. The court may have to consider whether business activities entered into via the Internet in a particular state represent a 'principal place of business' in that state in appropriate circumstances.

It is submitted that the principal place of business criteria provides the courts with an opportunity to recognise the fact that business activity is no longer necessarily

⁴⁷ *Ibid* p.494 at para 14.

confined to a 'physical' place of business and that business activity with bodies or citizens in a particular state may create sufficiently close link to bring within jurisdiction of courts of that state, particularly with parties from third states, if websites and other communications technologies do not qualify as secondary establishments.

If nothing more, the preceding examples would suggest that the application of the concept of 'domicile' to the electronic environment may not be particularly helpful in resolving a dispute as to whether a court has jurisdiction to hear a case concerning an electronic contract.

4.3.3.3 Derogations from the "Home-State" Principle

The home-state principle can only be departed from in accordance with the provisions set out in the Regulation or Conventions.⁴⁸ The 'exclusive jurisdiction', given to a particular State's courts in certain proceedings, is discussed above.⁴⁹ For the purpose of this discussion the provisions of interest relate to, the ability of the parties to determine which courts should hear any dispute, or 'party autonomy'; the existence of a 'branch, agency or other establishment'; the provisions concerning 'Special Jurisdiction'; and those dealing with consumers⁵⁰, insurance matters⁵¹ and employment contracts⁵², where the perceived weaker party is protected by "rules of jurisdiction more favourable to his interests".⁵³

4.3.3.3.1 Party Autonomy

The Conventions provide that the parties, one of whom is domiciled in a Contracting State, may agree that the courts of a particular Contracting State or States have exclusive jurisdiction in the event of a dispute. This option is subject to the provisions relating to Exclusive Jurisdiction and contracts with 'weaker parties' discussed below. The agreement must be in writing or evidenced in writing, in accordance with the parties' own established practice, or customary to the form of international trade or commerce, with which the parties are involved.⁵⁴ Such freedom is expected within the business community and in the eyes of some commentators is required within the

⁴⁸ Article 3(1) in all cases.

⁴⁹ Article 22 of the Regulation, 16 of the Conventions. See 4.3.1 above.

⁵⁰ Regulation Articles 15 - 17 (Articles 13 - 15 of the Conventions)

⁵¹ Regulation Articles 8 - 14 (Articles 7 - 9 of the Conventions)

⁵² Regulation Articles 18 - 21 (Article 5(1) of the Conventions)

⁵³ Recital 14 of the Regulations

⁵⁴ Article 17

electronic environment if electronic commerce is to thrive.⁵⁵ In the new Regulation the Commission were keen to recognise this, but equally keen to emphasise the protected nature of certain contracts and parties.

“The autonomy of the parties to a contract, other than an insurance, consumer or employment contract, where only limited autonomy to determine the courts having jurisdiction is allowed, must be respected subject to the exclusive grounds of jurisdiction laid down in this Regulation.”⁵⁶

The new provision found in Article 23 is identical to its predecessor, but for the inclusion of a subsection clarifying the position of electronic communications with regard to the requirement of ‘writing or evidenced in writing’.⁵⁷ Article 23(2) states that:

“Any communication by electronic means which provides a durable record of the agreement shall be equivalent to ‘writing’.”

While the clarification of requirements of form in the electronic environment is an important step in the removal of barriers to electronic commerce and the promotion of legal certainty, this measure retains an unfortunate ambiguity. The requirement of a ‘durable record’ is not further defined, leaving uncertainty as to which forms of electronic communications will be considered a ‘durable record’. For example, an e-mail message can be stored, reproduced and printed if necessary to provide evidence of the agreement. However, if the ‘agreement’ is entered into via a website, by clicking on an icon for example, it may be argued that this does not produce a ‘durable record’.⁵⁸

4.3.3.3.2 The Existence of a ‘Branch, Agency or Other Establishment’

A significant derogation from the home-state principle comes into effect where a defendant, or parent company, has a “branch, agency or other establishment” in a Member State. The parent company may find that it has to defend an action in that

⁵⁵ See, Susman, A. M. “International Electronic Trading: Some Legal Issues” [2000] *Society for Computers & Law*. Available at <http://www.scl.org/Services/default.asp?p=156&c=-999&ctID=12&cID=1140000216&prm=1>.

⁵⁶ Recital 14 of the Regulation.

⁵⁷ Article 23 (2). Requirements of form in the electronic environment are discussed in detail below in chapter 7.

⁵⁸ The majority of electronic communications can be printed out of course, and arguably this would provide a durable record of the agreement. However, if this were necessary it would remove the ‘paperless’ element of electronic contracting and an element of its appeal.

Member State rather than its home State. Although the phrase occurs in Articles discussed below, it warrants separate consideration because the interpretation adopted by the courts may have significant implications for those entering contracts electronically and for electronic commerce in general.

For the trader, seeking to expand their business by entering contracts in other Member States, this is an important issue to take into account when establishing subsidiaries or locating a branch or agency there. As was indicated in the introduction to this chapter the differences in the judicial systems of other Member States can be daunting to an overseas party. A seller or service provider, resident in the UK, may not relish the prospect of appearing before a Greek court, for example, in the event of a dispute arising in relation to a contract entered into with a party in that state. For small and medium-sized businesses this may be a determining factor in any decision to expand into overseas markets by opening a new branch or subsidiary. (For the Single Market, this has been a significant issue in the desire for harmonisation in the field of access to justice in civil and commercial disputes).

With the advent of modern communication technologies, in particular the Internet, in many cases there is no longer a need to set up a 'physical' place of business or have an agent in a particular state to take advantage of the market and enter contracts with its citizens. Indeed this is one of the primary benefits to commerce of modern electronic communications. Any measure, which has the potential to curb this possibility, will be detrimental to the development of electronic commerce. However, it may be equally detrimental for measures intended to protect weaker parties and promote confidence in electronic contracting to be ineffective where electronic communications such as the Internet are used. In many circumstances interactive websites can perform exactly the same role as a branch or agency physically present in the state. The key question at this point is whether facilities intended to create or promote the creation of electronic contracts in a particular state, or group of states, can be classed as a 'branch, agency or other establishment' bringing their proprietors within the jurisdiction of a particular court.

Justification for this derogation.

The primary justification for allowing action in a State other than the defendant's domicile in this exception is the 'special link' or 'close connection' created by the

existence of the branch, agency or establishment in that particular State. In *Etablissements Somafer SA v. Saar-Ferngas AG*⁵⁹ the ECJ explained that,

“Although Article 5 makes provision in a number of cases for a special jurisdiction, which the plaintiff may choose, this is because of the existence, in certain clearly-defined situations, of a particularly close connecting factor between a dispute and the court which may be called upon to hear it, with a view to the efficacious conduct of the proceedings.”⁶⁰

The court added that in order to ensure legal certainty the phrase ‘branch, agency or establishment’ must have an independent European interpretation common to all Member States.⁶¹ Recital 12 of the new Regulation reaffirms the necessity of an alternative ground of jurisdiction based upon this close connection between the action and the courts of a particular State:

“In addition to the defendant's domicile, there should be alternative grounds of jurisdiction based on a close link between the court and the action or in order to facilitate the sound administration of justice.”

In the new Regulation it is also made clear that in relation to insurance matters, employment contracts and consumers the derogation from the ‘home-state’ principle by reference to the existence of a branch, agency or other establishment is further justified by the desire to protect the weaker party to the dispute, as a matter of policy, in addition to the connecting factor created by the presence of the branch, agency or establishment.⁶² Additionally, where a party to the contract falls within one of the categories of ‘weaker parties’, the existence of a branch agency or other establishment in any EU Member State may have implications for parties based in non-EU States.⁶³

For the purpose of this discussion it is important to establish exactly what criteria will need to be satisfied in establishing whether a ‘branch, agency or other establishment’ exists and hence, whether the platforms and technologies employed in electronic commerce will fall within these criteria.

⁵⁹ Case 33/78, [1978] ECR 2183, [1979]1 C.M.L.R. 490.

⁶⁰ *Ibid* at 502 (para. 7).

⁶¹ *Ibid* at 503 (para. 8).

⁶² See Recital 13

⁶³ This issue is returned to below at 4.3.6.

An Electronic 'Branch, Agency or Other Establishment'?

In the 'traditional' marketplace – the physical world – the courts have looked for a presence of a physical nature, the existence of a permanent establishment where business is conducted on behalf of the parent company by employees or by an agent. If the notion of 'branch, agency or other establishment' requires some physical presence with a degree of permanency then a website, in itself, will not satisfy the requirement. If this is the approach adopted one must consider the effect that this will have on the ability of the regulatory measures to fulfil their objectives of providing 'greater protection' for weaker parties – i.e. consumers⁶⁴

If, on the other hand, an interactive website can be brought within this definition then this prospect may deter a trader, particularly a small or medium-sized enterprise (SME), from taking advantage of electronic contracts and have a significant impact on the economic potential of electronic commerce.⁶⁵

Two questions need to be addressed. Firstly, can and should an electronic presence such as an interactive website be brought within the definition of 'branch, agency or other establishment'? And secondly, can such a presence be said to be actually situated in a Member State or group of States? Some consideration of the objectives and justifications of this exception to the home-State principle, in addition to relevant authority, is necessary.

4.3.3.3 Relevant Articles

The phrase occurs, albeit with a slight variation, in the rules on 'Special Jurisdiction' and the rules in relation to 'insurance matters',⁶⁶ and 'consumer⁶⁷ and employment contracts'.⁶⁸ With the Convention terminology being retained in the new Regulation it is reasonable to assume that the body of case law relating to the earlier provisions will retain its relevance in future disputes. The provision relating to 'Special Jurisdiction' in Regulation 5(5) reads:

⁶⁴ Clearly, this is only one base for claiming jurisdiction but, as the case-law illustrates, it is not an insignificant one.

⁶⁵ This issue is discussed further below in the section on 'directing activities' at 4.3.6.

⁶⁶ Articles 8 – 14, specifically 9(2).

⁶⁷ Articles 15 – 17, specifically 15(2).

⁶⁸ Articles 18 – 21, specifically 18(2).

“A person domiciled in a Member State may, in another Member State, be sued... .. as regards a dispute arising out of the operations of a branch, agency or other establishment, in the courts for the place in which the branch, agency or other establishment is situated.”⁶⁹

This provision can only be relied upon if the defendant is domiciled in a Member State of the EU. Where a defendant is domiciled in a non-Member State the national rules of private international law will apply.

In disputes relating to insurance matters and employment or consumer contracts, more favourable rules than usual are provided to protect the interests of the weaker party to the dispute.⁷⁰ The provision relating to consumer contracts is perhaps the most significant in relation to electronic contracting at present.⁷¹ Regulation 15(2) reads:

“Where a consumer enters into a contract with a party who is not domiciled in the Member State but has a branch, agency or other establishment in one of the Member States, that party shall, in disputes arising out of the operations of the branch, agency or establishment, be deemed to be domiciled in that State.”

This provision is capable of having effect where the defendant is not domiciled in a Member State but has a branch agency or establishment in one of the Member States. The party is deemed to be domiciled in the Member State where his branch, agency or establishment exists. (This may have implications for parent bodies based in non-EU/EFTA States.)

The boundaries of phrase ‘branch, agency or other establishment’ are unclear and even with guidance from the ECJ the phrase remains open to interpretation in the Member State courts. Clearly there is uncertainty and scope for speculation as to how this phrase will be interpreted and applied in the electronic environment. Before accepting jurisdiction on the basis of the activities of a branch agency or other establishment a court must be satisfied that there is a good arguable case that a ‘branch,

⁶⁹ It is clear that this provision only applies to parties domiciled in a Member State. However, where a ‘weaker party’ is involved in the dispute a party resident in a third State will be deemed domiciled in a Member State if he has a ‘branch, agency or other establishment’ there. See the discussion below at 4.6.2.

⁷⁰ Recital 13.

⁷¹ The provision is identical to those found in relation to employment contracts and insurance matters.

agency or other establishment' exists in the Member State, and that the dispute has arisen 'out of the operations of the branch, agency or other establishment'.⁷²

4.3.3.3.4 The Relevant Case-Law

The Existence of a 'Branch, Agency or Other Establishment'

In *Etablissements A. de Bloos Sprl v. Etablissements Bouyer SA*⁷³ the ECJ responded to a request for a preliminary ruling on the phrase from the Belgian Appellate Court.⁷⁴ The European Court explained that:

“One of the essential characteristics of the concepts of branch or agency is the fact of being subject to the direction and control of the parent body.”⁷⁵

The court added that the concept of 'establishment' in the Article should be interpreted *eiusdem generis* and based on the same essential characteristics as a branch or agency.⁷⁶ In *DeBloos* the Court was not required to identify relevant factors for the determination of whether the parent body exercised direction and control over undertaking in question.⁷⁷ The issue was further addressed in *Etablissements Somafar SA v. Saar-Ferngas AG*:⁷⁸

“...the concept of branch, agency or other establishment implies a place of business which has the appearance of permanency, such as the extension of a parent body, has a management and is materially equipped to negotiate business with third parties so that the latter, although knowing that there will if necessary be a legal link with the parent body, the head office of which is abroad, do not have to deal directly with such parent body but may transact business at the place of business constituting the extension.”⁷⁹

⁷² *Canada Trust Company and other v Stolzenberg and other*. [1998] 1 WLR 547, [2000] 3 WLR 1376, supported on appeal; *Canada Trust Co v Stolzenberg (No.2)* [2002] 1 A.C. 1 [2000] 3 W.L.R. 1376 [2000] 4 All E.R. 481 [2001] C.L.C. 118.

⁷³ Case 14/76, [1976] ECR 1497, [1977] 1 C.M.L.R. 60.

⁷⁴ *The Cour d'appel de Mons*.

⁷⁵ [1977] 1 C.M.L.R. 60, at p. 82.

⁷⁶ *Ibid*.

⁷⁷ Insofar as it is under the 'direction and control' of a parent body a website would appear to satisfy this initial requirement, its actions being dictated by the website designer or proprietor.

⁷⁸ Case 33/78, [1978] ECR 2183, [1979] 1 C.M.L.R. 490.

⁷⁹ *Ibid* at 503, para. 12.

From the two rulings it would appear that to satisfy the requirement that a 'branch, agency or other establishment' exists, there has to be a good arguable case that:

1. the defendant party is an extension of the parent body and that it is under the control and direction of the parent body,
2. there is the appearance of permanency,
3. there is a management, capable of negotiating business with third parties without the third party having to deal directly with the parent body.

On this basis in *Blanckaert and Willems PVBA v. Luise Trost*⁸⁰ a commercial agent or business negotiator based in Germany, who established a sales network there on behalf of a Belgian furniture manufacturer, did not constitute a 'branch agency or other establishment' for the purpose of Article 5(5) of the Brussels Convention. The agent had the autonomy to work as and when and for whom he desired, including competitors, without being subject to the instructions of the parent body. In addition, the agent merely transmitted orders to the parent body without effectively participating in the completion and execution of transactions. An independent agency with these characteristics was not considered to have the 'character of a branch, agency or other establishment within the meaning of the Article 5(5) of the Convention'.⁸¹

There would also appear to be some tendency to expansion of the jurisdiction conferred by the phrase in the court's approach. In *Sar Schotte GmbH v. Parfums Rothschild Sarl*⁸² the court stated that even though the company in question was not technically a 'branch, agency or other establishment' it could nevertheless be equated to one because the company based in France used it as an extension of itself to pursue its activities in Germany.

However, in the case law to-date the courts have only had to consider the nature of a physical presence in a particular jurisdiction. *Somafer* was decided at a time when 'interactive websites' were not in existence and hence the terminology used by the court related to the commercial world as it existed then. With electronic commerce the presence in question will rarely be of a physical nature and the issue will depend upon the court's approach to a non-physical presence.

⁸⁰ Case 139/80 - [1981] ECR 819; [1982] 2 C.M.L.R.1.

⁸¹ *Ibid* at 15

⁸² Case 218/86 - [1987] ECR 4905; [1989] E.C.C.431.

In the electronic environment online traders often utilise one or more of the following to facilitate entering contracts with parties in a particular jurisdiction:

- 1) A website – this may be passive or interactive,
- 2) Hardware – such as servers and other technology,
- 3) An ISP to host their site,
- 4) A distribution centre or warehouse to organise the delivery of physical products.

The question to be addressed is whether these methods, individually or in combination, will bring a trader within a court's jurisdiction on the basis of this provision. In isolation it is unlikely that any of these individual factors would fall within the definition of a 'branch agency or other establishment' laid down in the case law of the ECJ. Clearly there are numerous permutations at present and there will undoubtedly be many more in the future. Each will have to be assessed on its own merit. What follows is a suggested analysis of the application of the three requirements indicated in the case law to the current climate.

Websites

Passive websites containing information or advertisements without the technology for entering contracts with customers would probably not fall within the provision because they do not 'operate' or 'act' in any way to negotiate business with third parties.⁸³ However, interactive websites may require closer examination.

An extension of the parent body?

A website is an extension of the owner's, or parent body's activity and it is obviously under its control and direction, being the result of actions taken by, or on behalf of, the parent body. However, an argument exists that electronic agents act independently of their users, and this argument may become more tenable as technology and artificial intelligence develop.⁸⁴

⁸³ In *Wolfgang Bremner and Peter Noller v. Dean Witter Reynolds Inc.* (Case C-318/93) [1994] ECR I-4275 the existence of an agency based in Germany which dealt with advertising for a US company (DWR) did not bring contracts entered into by consumers through an independent financial adviser in Germany within the scope of Articles 13 and 14 of the Brussels Convention.

⁸⁴ See Allen, T. & Widdison, R. "Can Computers Make Contracts?" (1996) 9 *Harvard Journal of Law & Technology* 25. Discussed above in chapter 3.2.

The 'appearance of permanency'.

It is important to note in relation to this factor that the requirement is for an *appearance* of permanency rather than an actual permanent presence. If an actual permanent presence were needed then websites, being transient and ephemeral in nature with no degree of permanence in a physical sense, would clearly be excluded. Equally many physical world businesses would also be excluded because their branch or agency premises are rarely 'permanent' in the true sense. In *Dinkha Latchin T/A Dinkha Latchin Associates v. General Mediterranean Holdings SA & Anr*⁸⁵ an occasional presence, in the form of a series of meetings, was sufficient to satisfy the court that a 'branch, agency or other establishment' existed in London. The appearance of permanence will be satisfied if the body gives the impression that it is permanent. This will be a question of fact in each case but it can be speculated that where a website is well-known or well-established in a particular State or has entered transactions in that State for some time, then there may be scope for the argument that the website, as a commercial entity, has an element of 'permanence' about it. The website would be no less permanent than its physical world counterparts.

A management capable of negotiating business independent of the parent body

In most cases an interactive website will be designed to enter into business transactions with third parties without the direct involvement of its owner (or parent body). Indeed this is *the* purpose of such sites. Whether there is a 'management' as such is debateable, but the site certainly has the ability to 'manage' the business electronically.⁸⁶ The court may accept the argument that the site is 'managed' by the software and programming of the site as created and controlled by the parent body.

Where is a website 'situated'?

However, even if a website can be considered a 'branch agency or other establishment', a difficulty remains in establishing that the website is actually 'situated' in a Member State or group of States. It could be argued that a website is situated on the Internet and therefore not in any State;⁸⁷ on a host computer, or server;⁸⁸ in the cache of

⁸⁵[2002] C.L.C. 330.

⁸⁶ Management - 'the process of dealing with or controlling things or people'. The New Oxford Dictionary of English. (1998) Oxford University Press.

⁸⁷ A popular argument for the proponents of an autonomous, self governing of Internet. See Lessig, L. "The Internet Under Siege" [2001] Nov/Dec *Foreign Policy Magazine*, (online) at; http://www.foreignpolicy.com/issue_novdec_2001/lessig.html.

a user's computer or in the cache of numerous servers owned by Internet Service Providers. These propositions may or may not be helpful in ascertaining the 'location' of a website, but even if they do provide an appropriate answer in a case before a court this will be purely fortuitous. The search for the location in which a website is situated is arguably an inappropriate basis for the purpose of conferring adjudicative jurisdiction. It is submitted that an interactive website should be considered situated in the State or States where its commercial activity is conducted. In this way the courts of that State will have a clear connection with any action resulting from the activities entered into via that website.⁸⁹ This would not equate to mere accessibility but rather to the participation in commercial activity in that State.

If a physical presence is required for there to be a 'branch, agency or other establishment' situated in a Member State, then the only potential argument will relate to the situations where there is something physically located in the Member State, or, in the case of consumers, one of the Member States. If the seller uses an ISP, places its own technology or uses a warehouse in a particular State, then the physical presence would appear to exist and coupled with a website, would appear to provide a 'branch, agency or other establishment' for the purpose of the Regulation. However, it has been argued that the presence of technological means to host the website or similar technologies will not satisfy the requirements for the existence of a branch or secondary establishment under the Regulation.⁹⁰ This argument is based upon the terminology employed in the Directive on Electronic Commerce⁹¹ to define an 'established service provider':

“‘established service provider’: a service provider who effectively pursues an economic activity using a fixed establishment for an indefinite period. The presence and use of the technical means and technologies required to provide the service do not, in themselves, constitute an establishment of the provider.”⁹²

⁸⁸ Which could be situated in a state completely unrelated to the parties or their activities.

⁸⁹ It is conceded that in some circumstances even this approach will have inappropriate consequences. For example, where a website is visited and a contract concluded whilst travelling through a foreign jurisdiction. In such cases the court will have to revert to the 'domiciles' of the parties to the transaction.

⁹⁰ See; Stone, P. "The Treatment of Electronic Contracts and Torts in Private International Law Under European Community Legislation" [2002]11(2) *Information & Communications Technology Law (I & CTL)* 121-139, at 122.

⁹¹ Directive 2000/31/EC of The European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market (Directive on electronic commerce) OJ L178/1. Implemented in the UK by The Electronic Commerce (EC Directive) Regulations 2002, SI 2002 No. 2013.

⁹² *Ibid* Article 2(c).

In this context it is clear that websites, servers and related technologies will not satisfy the requirement. However, the Directive also clearly states that it 'does not establish additional rules on private international law nor does it deal with the jurisdiction of Courts'.⁹³ On this basis it could be argued that the interpretation of provisions contained within instruments dealing with matters of jurisdiction should be independent and based on the purpose of the particular provision.

The phrase 'established service provider' is intended to define the service providers who are subject to the control of enforcement bodies within a particular State whose obligation it is to ensure compliance with national rules. The approach adopted to the presence of 'technical means and technologies to provide the service' is intended to prevent restriction of the free movement of services within the internal market. The existence of a 'branch, agency or other establishment' is an indication of a business entity's connection with a particular State because of the activities he pursues with citizens of that State, thus providing a court in that State with jurisdiction. It is submitted that there is no justification for adopting the approach taken to the establishment of service providers in the Electronic Commerce Directive because the purpose behind the provisions, and the terminology itself, is completely different.

If the trader is using an ISP to host the website, it may appear unlikely that this could amount to a 'branch, agency or other establishment'. In many ways the activities of the ISP are akin to those of the independent agent in *Blanckaert*, being neither under the direction or control of the proprietors of the website. However, the content and activity pursued via a website is not usually under the control of the ISP, but rather under the control and direction of the trader. If the trader or 'parent body' places its own technology in a Member State and operates an interactive website from that hardware then the physical presence exists, if indeed it is required to qualify as a 'branch agency or other establishment'.

If nothing more, this 'analysis' highlights the futility of looking for a physical presence with the appearance of permanency in the electronic environment. The two stated purposes of this exception to the home-state principle are the sound administration of justice because of the close link between the court and the action, and the protection of 'weaker parties' such as consumers. It is submitted that these purposes should be the focus when considering the issue of whether jurisdiction should be

⁹³ *Ibid* Article 1(4).

conferred rather than whether the means of conducting the activity which led to the dispute have a 'physical presence' in a State or not.

As the new 'Brussels Regulation' is intended to take account of 'new forms of commercial activity',⁹⁴ it could be expected that it should encompass new methods of having a branch agency or other establishment in a Member State. In the electronic environment bricks and mortar and a human presence are no longer necessary to obtain the benefits of having a physical place of business in that State. However, this issue is unresolved and will remain the subject of judicial interpretation.

Disputes arising 'out of the operations of the branch, agency or other establishment'

In addition to demonstrating the existence of a 'branch, agency or other establishment', it is also necessary to show that the dispute arose out of the operations of that body. In *Somafar*⁹⁵ it was stated that the concept of 'operations' comprises:

- actions relating to rights and contractual or non-contractual obligations concerning the management properly so-called of the agency, branch or other establishment itself such as those concerning the situation of the building where such entity is established or the local engagement of staff to work there.
- actions relating to undertakings which have been entered into at the above-mentioned place of business in the name of the parent body and which must be performed in the Contracting State where the place of business is established.
- actions concerning non-contractual obligations arising from the activities in which the branch, agency or other establishment within the above defined meaning has engaged at the place in which it is established on behalf of the parent body."⁹⁶

In the subsequent case of *Lloyd's Register of Shipping v Campemon Bernard*⁹⁷ it was held that, despite the wording of the *Somafar* decision, it is not a pre-condition for jurisdiction under Article 5(5) that the obligations entered into by the branch in the name of the

⁹⁴ *Op cit* fn 10.

⁹⁵ [1979]1 C.M.L.R. 490.

⁹⁶ *Ibid* at p 504.

⁹⁷ [1995] ECR 1-961.

parent body were to be performed in the contracting state in which the branch is situated. If it were so, the court highlighted the fact that article 5(5) would be somewhat redundant in the light of Article 5(1) which deals with the performance of contractual obligations.⁹⁸

The requirement that the contract be 'entered into at the place of business' could once again raise the difficult question of *where* in the electronic environment actions occur. If an interactive website is being relied upon as a 'branch, agency or other establishment', then a dispute related to a contract entered via that website may be considered arising out of the operations of a branch, agency or other establishment.

The interpretation of the phrase 'branch, agency or other establishment' may have a significant impact on parties using electronic agents and other technologies to enter electronic contracts with parties in other States. It is submitted that if these new methods of operating a secondary establishment in another state are not encompassed by the phrase 'branch, agency or other establishment', there will be an undesirable lacuna created in the Regulations and their application.

4.3.4 'Special Jurisdiction'

4.3.4.1 Contracts in General : Article 5(1)

Before Article 5(1) is discussed the approach taken by the ECJ to the definition of a contract and a contractual relationship, within the context of the Brussels Convention should be considered. With the lack of a uniform approach to the notion of 'contract' within the Member States the Court has stated that, for the purpose of the convention, the term has an independent meaning encompassing all matters having their basis in an agreement.⁹⁹ In this way the Article encompasses situations where there is a dispute as to the actual existence of a contract. However, where rights are conferred on a third party in an agreement,¹⁰⁰ they will not be treated as arising under a contract for the purpose of the Convention.¹⁰¹

Article 5 of the Convention contains a number of exceptions to the home-state principle where the subject matter of the dispute has a 'close connection' with a state

⁹⁸ Ibid at 469 (para [17]).

⁹⁹ See Case 34/82 *Peters v. South Netherlands Contractors Association* [1983] E.C.R. 987, Case 9/87 *Arcado SpA v. Haviland SA.* [1988] E.C.R. 1539 and case 38/81 *Effer SpA v. Kantner* [1982] E.C.R. 825.

¹⁰⁰ As may be the case in some legal systems including England and Wales, following the enactment of the Contracts (Rights of Third Parties) Act 1999.

¹⁰¹ See Case C-26/91 *Ste Handte et Cie GmbH v. Traitements Mecano-Chimiques des Surfaces* [1992] E.C.R. I-3967.

other than that in which the defendant is domiciled.¹⁰² The Regulation retains this provision¹⁰³ and introduces specific amendments intended to clarify uncertainty relating to the special jurisdiction rules in contractual law.¹⁰⁴ The source of the uncertainty and whether the Regulation has clarified the provision will now be considered.

The basic exception found in Article 5(1) of both instruments, states that a party domiciled in a contracting state may be sued in the courts of another contracting state;

“in matters relating to a contract, in the courts for the place of performance of the obligation in question.”¹⁰⁵

4.3.4.1.1 “Place of performance”

Whilst this phrase is, *prima facie*, a logical and justifiable criterion because of the close connection between the subject matter of the dispute and the court,¹⁰⁶ it has produced a significant body of case law relating to its interpretation and application.¹⁰⁷ If a single obligation is in question, then there are few difficulties. The place of performance of that obligation can usually be identified and if that contractual obligation is to be performed in a particular State the courts of that State have jurisdiction to hear a dispute relating to that obligation under Article 5(1).

However, the position becomes more complicated if the dispute relates to a number of obligations under the contract, some of which are central to the contract and others which could be described as subsidiary. If these obligations are to be performed in different States there could be a number of courts involved in related disputes. The ECJ has made it clear that the word ‘obligation’ in Article 5(1) refers to the contractual obligation forming the *basis* of the legal proceedings rather than the performance of any other obligation under the contract in another jurisdiction.¹⁰⁸ This is the logical conclusion when the ‘close connection’ justification for jurisdiction is considered. The uncertainty associated with this article arises when the particular obligation in dispute is

¹⁰² Article 5(5), discussed above, being one of them.

¹⁰³ And it’s numbering.

¹⁰⁴ *Op cit* fn 10 at p.2.

¹⁰⁵ Article 5(1).

¹⁰⁶ Based upon the basic rule of “special jurisdiction” or *jurisdiction ratione materiae* rather than “general jurisdiction” or *jurisdiction ratione personae*.

¹⁰⁷ See for example; *Etablissements A. de Bloos Sprl v. Etablissements Bouyer SA* Case 14/76[1976]ECR 1497, [1977]1C.M.L.R.60; *Boss Group Ltd v. Boss France SA* [1996] 4 All E.R. 970 and *Viskase Ltd v Paul Keifel GmbH* [1999] 3 All E.R.362.

¹⁰⁸ *Etablissements A. de Bloos Sprl v. Etablissements Bouyer SA* [1977]1C.M.L.R.60 at 81.

to be performed in a number of jurisdictions or, as occurs in many disputes, a number of obligations are involved, each of which may be performed in different jurisdictions.

With an electronic contract the performance of the obligations may take place in numerous jurisdictions. For example, a contract with an ISP for storage, e-mail and web-hosting may be provided in a number of jurisdictions depending on the technology in use. If the basis of the dispute is the obligation to provide these services, then the question of 'place of performance' becomes somewhat problematic. If the physical 'place of performance' can be ascertained, such as the relevant server, this may have little or no connection with the parties themselves or the contract.

Where a number of jurisdictions may be involved the first issue to consider is the risk of duplicate actions, or the inappropriate distribution of related actions.

4.3.4.1.2 Duplicate or Related Actions – *Lis Pendens*.

Where the courts in a number of States may have grounds to claim jurisdiction in a contractual dispute the potential exists for conflicting and irreconcilable judgments. This problem was envisaged at time of the drafting of the Brussels Convention and an Article was introduced to deal with the possibility of identical or related actions being brought in multiple jurisdictions. The provisions are now found, in identical form, in Articles 27 to 31 of the Regulation. Article 27 reads:

1. Where proceedings involving the same cause of action and between the same parties are brought in the courts of different Member States, any court other than the court first seised shall of its own motion stay its proceedings until such time as the jurisdiction of the court first seised is established.
2. Where the jurisdiction of the court first seised is established, any court other than the court first seised shall decline jurisdiction in favour of that court.

Hence, providing jurisdiction of the court first seised can be established, courts in other jurisdictions must decline jurisdiction in those proceedings. Where an action is closely connected to an action before another court it may be expedient to hear the issues together. In this situation any court, other than the court first seised, may stay its proceedings and may also, on the application of one of the parties, decline jurisdiction.¹⁰⁹

¹⁰⁹ Article 28

This is only a discretionary element and naturally where a court sees fit, it may still hear the dispute.

When a claim relates to a number of obligations, to be performed in different jurisdictions the question before the court becomes even more complex. In such cases the courts have applied the Latin maxim *accessorium sequitur principale*, requiring the identification of the principal obligation, to which all other obligations are deemed to be attached.¹¹⁰ However, where it is not possible to distinguish between the 'principal' obligation and those which are seen as 'accessory', the ECJ has stated that a court may only seize jurisdiction under article 5(1) in respect of obligations which are performed within its territory.¹¹¹ While this approach retains the close-connection principle as grounds for seising jurisdiction, it does have the potential to create considerable inconvenience and detract from the expressed objective of expediently dealing with disputes.

However, the difficulty remains establishing the 'place' of performance of the obligation in question. When questions of this nature arise it is for the national Courts to determine the 'place of performance' according to the rules of national law'.¹¹² Here, the potential exists for divergent interpretation of the Article, because courts in different jurisdictions may interpret contractual performance differently. In English law, the 'place of performance' will be primarily assessed on the express or implied intentions of the parties to a contract. Hence, if a contract for the sale of goods includes terms relating to delivery, then the 'place of performance' will depend on the detail of that term. If the obligation in question is the delivery of a tangible item, then that the obligation is to be performed in the place where that item was to be delivered. If the obligation is to pay money, then the debtor is usually under a general duty to pay the creditor at the creditor's place of business¹¹³ rather than the place where the customer takes steps to make that payment.¹¹⁴

The phrase 'place of performance of the obligation in question' has raised a number of questions of interpretation. When the phrase is considered in the context of the electronic environment existing uncertainties may be magnified by the problems

¹¹⁰ Case 266/85 *Shenavai v. Kreischer* [1987] E.C.R. 239. However, identifying the 'principal obligation' may still be difficult, see *Union Transport Group plc v. Continental Lines SA.* [1992] 1 W.L.R. 15 and *A.I.G. Group (U.K.0 Ltd. V. The Ethniki* [1998] 4 All E.R. 301.

¹¹¹ Case C-420/97 *Leathertex Divisione Sintetici SpA v. Bodetex B.V.B.A* (E.C.J., 1999).

¹¹² Case 12/76 *Industrie Tessili Italiana Como v. Dunlop AG* [1976] E.C.R. 1473, and Case C-440/97 *GIE Groupe Concorde v. The Subadivaxno Panjan* (ECJ, 1999).

¹¹³ *Dixal & Co. Ltd. v Gans* [1904] 2 K.B. 685

¹¹⁴ For example makes a bank deposit or posts a cheque.

associated with identifying a 'place of performance' leading to a lack of legal certainty. If the obligation forming the basis of the action is to be performed on the Internet, identifying the *place* of that performance may be difficult and even where it is possible it may be of little practical use. In the development of the Brussels Regulation the issue of clarifying this provision was addressed. The amended provision will now be considered.

4.3.4.1.3 The Regulation – An Opportunity to Clarify the 'Place of Performance'

The Regulation seeks to clarify the ambiguity in relation to the phrase 'place of performance of the obligation in question' but nevertheless retains this terminology.¹¹⁵ The assistance provided by the Regulation is the introduction of a reference to contracts for the sale of goods or the provision of services. Article 5(1) of the Regulation reads:

A person domiciled in a Member State may, in another Member State, be sued:

- (a) in matters relating to a contract, in the courts for the place of performance of the obligation in question;
- (b) for the purpose of this provision and unless otherwise agreed, the place of performance of the obligation in question shall be:
 - in the case of the sale of goods, the place in a Member State where, under the contract, the goods were delivered or should have been delivered,
 - in the case of the provision of services, the place in a Member State where, under the contract, the services were provided or should have been provided,
- (c) if subparagraph (b) does not apply then subparagraph (a) applies.

The addition of Article 5(1)(b) clarifies the place of performance in contracts for the sale of goods or provision of services, adopting an approach already applied in the courts of England and Wales.¹¹⁶ This may explain why, when dealing with the provision in the area of their sole legislative competence (the provision relating to inter-UK disputes in the CJJA), the UK government chose to retain the original wording from the Brussels Convention, indicating that the amendment adds little to the application of the

¹¹⁵ The significance of 'a close link' as an alternative ground of jurisdiction can be seen from Recital 12 of the Regulation.

¹¹⁶ See below at 4.4.

provision in the UK.¹¹⁷ However, the additions to the Article may do little to help clarify the situation with contracts not categorised as either involving a sale of goods or provision of services, in particular contracts for intangible items or 'data products' which form a large proportion of the growing electronic commerce market.¹¹⁸

The Article does envisage the situation where contracts do not fall within these categories (paragraph 1(c)) but simply refers back to the 'place of performance of the obligation in question' qualification without further direction, retaining a status quo with the existing Convention provision. The new provision does add the phrase 'unless otherwise agreed,' re-enforcing the idea of party autonomy expressed in Recital 14, allowing business parties to expressly state in their contract terms that the obligations are deemed to be performed in a particular jurisdiction.¹¹⁹

With the stated objective of clarification it is unfortunate that the Commission adopted an approach which, in the context of electronic commerce, does very little to clarify the position in relation to the intangible items which form a common subject-matter of electronic contracts. The 'place of performance of the obligation in question' remains an area of uncertainty which will ultimately require clarification by the ECJ.

Article 5 contains derogations from the home state principle of a permissive nature. However, the derogations relating to consumers, insurance matters and employment contracts carry a far more obligatory tone. The provisions relating to jurisdiction over consumer contracts will be the focus here, but the provisions relating to insurance and employment contracts are identical in form. The new Regulation contains some significant developments in this area so the position under the Convention will be considered first followed by an analysis of the changes.

4.3.5 Consumer Contracts : Articles 13-15 of the Brussels Convention

4.3.5.1 Philosophy underlying the provisions

In a consumer contract (one between a consumer and a business) the 'consumer' is usually the economically weaker party. As such, within the UK and EU, the consumer is afforded greater protection in relation to substantive and procedural matters associated with the contracts he enters. The European Commission has, as a key objective, the development of a high common level of consumer protection within the EU. By

¹¹⁷ CJJA Schedule 4 (3) (As amended by the Civil Jurisdiction and Judgments Order 2001 (SI No. 3929).

¹¹⁸ See above Chapter 3.

¹¹⁹ The ability to do this' is excluded in consumer contract, contracts of insurance or employment. See below.

creating such an environment the Commission hopes to maximise the benefits of the Single Market for the consumer and reduce the uncertainty and lack of confidence associated with entering cross-border transactions. With the economic potential of electronic commerce the perceived need for such an environment has become increased.¹²⁰

Articles 13-15 of the Brussels Convention allow the consumer to avail himself of the courts in his domicile, departing from the home-state principle, in specific circumstances. The consumer has the option of initiating proceedings against the other party in the courts of the State in which he is domiciled or in the courts of the State in which the other party is domiciled. Conversely, the consumer may only be sued in the courts of the state in which he is domiciled.¹²¹ To benefit from this provision the party must;

- 1) fall within the Convention definition of consumer; and,
- 2) enter a contract falling within one of the categories listed in the Article.

4.3.5.2 The Definition of 'Consumer'

Article 13 defines 'consumer' as a person entering a contract "for a purpose which can be regarded as being outside his trade or profession." The definition employed here is common to many European instruments.¹²² However, this definition does have the potential to exclude individuals who purchase a product, in a purely private capacity, which they may also utilise in their profession. For example the lawyer who purchases a computer to enable him to work at home, or a lecturer purchasing a computer to edit a book he has written. Arguably, both of these contracts have been entered into for a 'professional purpose'. It would appear possible, albeit on a very narrow interpretation, for such individuals to be excluded from the scope of the provision. This interpretation would appear to restrict the application of the exception for consumers. Indeed it has been suggested that any of the exceptions to the 'defendant's domicile' principle should be construed restrictively.¹²³ However, in the

¹²⁰ See the 'Communication from the Commission to the European Parliament, The Council, The Economic And Social Committee and The Committee of the Regions - Consumer Policy Strategy 2002-2006'. http://europa.eu.int/comm/consumers/policy/intro/consumer_policy_strategy_en.pdf.

¹²¹ Article 14 para.3. The provisions do not affect the right of either party to bring a counter-claim to the court in question.

¹²² For example, the Unfair Terms in Consumer Contracts Directive, discussed below in Section IV.

¹²³ See *Kleinwort Benson Ltd v Glasgow City Council (No.2)* [1999] 1 AC 153 at 163 and *Andrew Rayner v. Richard Davies* [2002] EWCA Civ 1880; [2002] WL 31676420 (CA).

Report by Professors Giuliano and Lagarde¹²⁴ on the corresponding Article in the Rome Convention, a broader interpretation is advocated:

“It [the Article] should be interpreted in the light of its purpose which is to protect the weaker party... the rule does not apply to contracts made by traders, manufacturers or persons in the exercise of a profession (doctors for example) who buy equipment or obtain services for that trade or profession. If such a person acts partly within, partly outside his trade or profession the situation only falls within the scope of [the Article] if he acts primarily outside his trade or profession.”¹²⁵

This interpretation would appear to introduce an assessment of the degree to which the party is acting within his trade or profession. In the examples of the lawyer and the lecturer above if the computers were purchased primarily for use in their profession then they would be outside of the scope of the provision. If, on the other hand, the purchases were made primarily for uses outside of their profession then arguably they would fall within the scope of the provision. If the party enters the contract with a view to pursuing a trade or profession in the future they are also excluded.¹²⁶

4.3.5.3 Type of contract

Article 13 restricts the application of the consumer protection measures to certain defined types of contract. The contract must be:

- a contract for the sale of goods on instalment credit terms; or,
- a contract for a loan repayable by instalments, or for any other form of credit, made to finance the sale of goods; or
- any other contract for the supply of goods or a contract for the supply of services, and

¹²⁴ Report by Professors Giuliano and Lagarde on: *The Convention on Law Applicable to Contractual Obligations*, OJ 1980 C282/1, 31st October. To which we are directed by Dr Schlosser in his report on the Accession Treaty to the Brussels Convention: 'Report on the Association of the Kingdom of Denmark, Ireland and the United Kingdom of Great Britain and Northern Ireland to the Convention on jurisdiction and the enforcement of judgments in civil and commercial matters and to the Protocol on its interpretation by the Court of Justice, by Professor Dr Peter Schlosser. (OJ C 59/71 5.3.79) at p. 119, para. 158.

¹²⁵ *Ibid* at p 23.

¹²⁶ Case C-269/95 *Francesco Benincasa v Dentalkit Srl.* (1997) ECR I-3767.

- (a) in the State of the consumer's domicile the conclusion of the contract was preceded by a specific invitation addressed to him or by advertising; and
- (b) the consumer took in that State the steps necessary for the conclusion of the contract.¹²⁷

Article 13 is clearly limited in the type of contracts in which the consumer is afforded added protection. In particular, to satisfy paragraphs 1 and 2 the contract must relate to the sale of goods, either on instalment credit terms or some other finance agreement associated with a sale of goods. However, it is the third paragraph of Article 13 that raises several issues relevant to its general application and more significantly, for the purpose of this discussion, its application to contracts concluded electronically.

4.3.5.1.1 'The sale of goods or supply of services'

The first element to consider is the requirement that the contract must involve the sale of goods or alternatively the supply of services. Whilst the majority of transactions can be placed in one of these categories, the subject matter of an increasing number of contracts, particularly those entered into electronically, do not fit comfortably into one category or the other.¹²⁸ The most common examples are computer software, music, video and other multimedia downloaded directly from the supplier's site to the customer's computer. Such intangible items are arguably not goods or services in the legal sense but, as has been suggested, are best treated *sui generis*.¹²⁹ If this analysis is correct, then there may be a strong argument that such subject matter is outside the scope of the provision, removing the benefits of this Article for a consumer, particularly in the field of electronic commerce. However, it is submitted that this conclusion should be avoided to prevent the consumer losing protection which he was clearly intended to benefit from by allowing the medium employed for the delivery of the material to dictate legal rights or obligations.

However, if this first requirement is satisfied, the contract must have been 'preceded by a specific invitation addressed to him or by advertising' in the State of the consumer's domicile to fall within the scope of the provision.

¹²⁷ Article 13 (1-3).

¹²⁸ See the discussion above in chapter 3.2 on the 'nature' of many products supplied electronically.

¹²⁹ In *Beta Computers (Europe) Limited v. Adobe Systems (Europe) Limited* [1996] F.S.R. 367, Lord Penrose suggested that such products such be treated *sui generis*. See also *St Albans City and District Council v. International Computers Ltd* [1997] F.S.R. 251.

4.3.5.1.2 'Preceded by a specific invitation or by advertising'

The phrase 'specific invitation' is reasonably unambiguous requiring some form of direct communication, such as a letter, 'mail-shot' or e-mail addressed to the consumer. However, it is the 'or by advertising' criteria which has caused some debate and more recently, speculative concern in relation to websites and the Internet.

Advertising can encompass a very broad range of activities and if the phrase 'preceded by advertising' were read literally it has the potential to encompass the vast majority of consumer transactions. The existence of a contract would suggest that the consumer's attention has been drawn to that supplier in some way and more often than not that 'way' is some form of advertising. The question for interpretation is whether the mere existence of an advertisement in the consumer's domicile will satisfy the requirement or whether the advertising needs to be intended for a particular jurisdiction or targeted toward it in some way? The answer to this question has particular significance to parties using a website to advertise, because in theory, the website has the potential to be seen anywhere in the world. An advertisement on the Internet by a French supplier may be seen by consumers throughout the EU. The question for a court would be whether this constitutes advertising in the consumer's domicile for the purpose of the Convention, because if it does, then the potential exists for a company engaging in electronic commerce to be faced with litigation in every Member State. This possibility gives suppliers cause for concern and arguably has the potential to stifle the growth of e-commerce within the EU.

It has been suggested that the appropriate interpretation would be that the supplier took specific steps to market his product in the consumer's State, or in some way directed his advertising to that state.¹³⁰ This approach is supported by the interpretation suggested in the background documentation to the Convention. In his Report on the Accession Convention, Professor Schlosser refers us to the report by Professors Giuliano and Lagarde, and their consideration of identical terminology found in the Rome Convention:

¹³⁰ Susman, A. M. "International Electronic Trading: Some Legal Issues" [2000] Feb/Mar *Computers and Law*. Susman argues that the trader must in some way solicit or target consumers in a particular state;

"... the trader must have directed the advertising to that state: he is not subject to its jurisdiction merely because a publication in which he advertises finds its way into that state if he is not targeting consumers in that state; and the same is thought to apply in respect of an advertisement on a Web site accessible in a state which is not directed to consumers in that state." Available at: <http://www.scl.org/Services/default.asp?p=156&c=-999&ctID=12&cID=1140000216&prn=1>.

“The first indent relates to situations where the trader has taken steps to market his goods or services in the country where the consumer resides. It is intended to cover *inter alia* mail order and door-step selling. Thus the trader must have done certain acts such as advertising in the press, or on radio or television, or in the cinema or by catalogues aimed specifically at that country, or he may have made business proposals individually, through a middle man or by canvassing.”¹³¹

Hence, some positive action on behalf of the supplier, demonstrating an intention to solicit business in that state, would be required.¹³² Recent cases in the courts of England and Wales have been decided on this line of reasoning. In *Andrew Piers Courtauld Rayner v. Richard Davies*,¹³³ Morison J stated that:

“The question is whether the defendant has been marketing his services in this country. What the Convention is looking for is the solicitation of business here.”¹³⁴

and concluded that in the immediate case,

“The consumer has not been solicited in this country by the service provider; rather the service provider's business has been solicited by the consumer.”¹³⁵

In the Court of Appeal Waller LJ concurred with the view of Morison J in the court below¹³⁶ and added that the appropriate test would seem to be the question “who invited whom to do business”.¹³⁷

Whether a website is soliciting business or directed toward consumers in a particular State will be a question of fact for the courts and will depend upon the activities of both parties. However, it would appear that the key consideration would be whether the website is deemed to be soliciting or inviting consumers in a particular State

¹³¹ Report by Professors Giuliano and Lagarde on: The Convention on Law Applicable to Contractual Obligations, OJ 1980 C282/1, 31st October at p. 23-24.

¹³² To an extent this question of interpretation has been clarified by the Regulation, see below at 4.3.6.

¹³³ [2002] 1 All E.R. (Comm) 620; [2002] WL 340242 (QBD).

¹³⁴ At para.13.

¹³⁵ *Ibid*.

¹³⁶ *Andrew Rayner v. Richard Davies* [2002] EWCA Civ 1880; [2002] WL 31676420 (CA), at para 23.

¹³⁷ *Ibid* at para 26.

to do business. In the vast majority of cases this will be the actual purpose of the website.

Interestingly, in *Rayner*, Waller LJ also made a passing comment about the claimant's attempt to introduce details of the defendants 'modest' and 'entirely ineffective' website into the proceedings.¹³⁸ He felt that its introduction would not add anything to the resolution of the issue before him, particularly as the website was not "interactive" and there was "no reliance on the website itself either being advertising or being a specific invitation".¹³⁹ It could be speculated that if his Lordship had been required to consider an "interactive website" as a "specific invitation" or "advertising", an alternative outcome may have resulted. Waller LJ also declined to comment upon the change in wording in the new Regulation and the impact (if any) it would have upon a case such as the one before him,¹⁴⁰ a point which is returned to below.

With the widely accessible nature of websites a supplier may be well advised to take clear and affirmative steps to demonstrate that he is not intending to contract with consumers in a particular State. Alternatively, he could simply decline from entering contracts with consumers in a particular State. There is clearly scope under the convention for a website to be construed as soliciting or inviting consumers to do business with the website proprietor.

4.3.5.1.3 'Steps necessary for the conclusion of the contract'

The third requirement in Article 13 is that the 'consumer took in that State the steps necessary for the conclusion of the contract'.¹⁴¹ As is discussed elsewhere¹⁴² in England and Wales, and many other jurisdictions, the contract is concluded when there is an effective acceptance of the offer. It could be argued that for this Article to apply, the acceptance, being the final step necessary for the conclusion of the contract, must take place in the consumer's State. As a general rule, the acceptance is effective when communicated to the offeror and usually at the point where he receives that communication, which for the purposes of this provision would be in the State of the supplier and not the consumer. However, from the background material to the Convention it would appear that the Article does not require the consumer to take the final steps necessary for the 'legal' conclusion of the contract but rather that he takes the

¹³⁸ *Ibid* at para 12.

¹³⁹ *Ibid*.

¹⁴⁰ *Ibid* at para 27.

¹⁴¹ Article 13(3)(b).

¹⁴² See the discussion of contract formation below in chapter 8.

necessary steps relevant to him; for example responding to the advertisement or the placing of an order.¹⁴³ In adopting an autonomous definition of 'contract' for the purpose of the convention, the ECJ has sought to avoid the divergent technicalities of offer and acceptance throughout the Member States. Indeed, this appears to have been the intended purpose of the original wording.¹⁴⁴

On the basis of this reasoning it would appear that the fact that the contract may not be technically formed under the law of a particular state, should not be significant to the application of the provision. For example, the simple action of placing an order on an interactive website should suffice. However, the provision does require that the 'necessary steps' were taken in the consumer's State. In the context of electronic contracting, and in particular contracting via an interactive website, it could be argued that the 'necessary steps' are actually taken on the computer or server upon which the supplier's website is hosted. However, this would appear an unlikely interpretation and the 'necessary steps' would probably be considered to be the consumer typing on his keyboard or clicking a mouse button in his home State.

4.3.5.4 The use of a 'branch, agency or other establishment'

The existence of a 'branch, agency or other establishment' is discussed in detail above. It is important to re-iterate at this point that parties entering contracts through a 'branch, agency or other establishment' within a Contracting State are deemed to be domiciled in that state and hence, subject to the Courts of that jurisdiction in a dispute with a consumer. This prevents circumvention of the principles by parties operating through agents within the Contracting States but being physically domiciled in a state not party to the Convention. The service provider, as a defendant, is deemed to be domiciled in the state where he has his secondary establishment, whether he is domiciled in a contracting state or not. Clearly this has potential implications for parties domiciled in third states if electronic agents and websites can be brought within this definition.¹⁴⁵

¹⁴³ The Schlosser Report once again refers us to the words of Professors Giuliano and Lagarde: "The word 'steps' includes *inter alia* writing or any action taken in consequence of an offer or an advertisement." OJ C 282/1 at 24.

¹⁴⁴ *Ibid* "the Group expressly adopted the words[...] to avoid the classic problem of determining the place where the contract was concluded."

¹⁴⁵ Of course the enforcement of any such judgment may be a different matter in states who are not party to some reciprocal recognition of judgments arrangement.

4.3.5.5 Party Autonomy : The ability to depart from the consumer provisions

The Convention measures relating to consumer contracts may only be departed from by an express agreement, entered into by the parties after a dispute has arisen.¹⁴⁶ In this way the consumer is afforded protection against contractual clauses seeking to ouster the Convention rules.¹⁴⁷ A separate agreement on jurisdiction may be entered into after a dispute has arisen, giving the consumer the opportunity to consider the consequences of that choice.¹⁴⁸

A number of issues have been highlighted in relation to the Convention provisions applicable to consumer contracts. The 'new' approach adopted in the Regulations will now be examined.

4.3.6 Consumer Contracts : Articles 15-17 of the Brussels Regulation

The provisions in the Convention had not been controversial, but had produced some difficult questions of interpretation and hence uncertainty. In order to clarify the situation and to "develop a balanced position which reconciles consumer protection measures with measures that facilitate the take-off of electronic commerce",¹⁴⁹ the European Commission proposed new provisions to cover all consumer contracts. However, the approach adopted by the Commission also extended the protection afforded to consumers in a manner which according to some commentators may actually hinder the 'take-off' of electronic commerce creating anxiety within the business community.¹⁵⁰ During the consultation period the Economic and Social Committee of the European Union expressed reservations about the approach adopted stating that the provision in the new Regulation was '...not clear enough to foster a climate of trust between the parties'¹⁵¹ emphasising that 'the prospect of being brought before foreign courts could deter small and medium-sized enterprises from using the internet to promote their services'.¹⁵² Nevertheless, the Commission rejected Parliamentary

¹⁴⁶ Article 15.

¹⁴⁷ Clauses which may in any event be susceptible to the scrutiny of UCTA and UTCCR, see below chapters 11 & 12.

¹⁴⁸ And perhaps obtain legal advice.

¹⁴⁹ *Op cit* fn.10.

¹⁵⁰ Meller, P. "Online Buyers Gain Ability to Sue." (2000) December 1st *New York Times*.

<http://www.nytimes.com/2000/12/01/technology/01NET.html>.

¹⁵¹ Opinion of the Economic and Social Committee on the 'Proposal for a Council Regulation (EC) on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters'. OJ C 117/6, 26.4.2000, para 4.2.4.

¹⁵² *ibid* at para 4.2.2.

amendments on the issue¹⁵³ and the new provisions can be found in Articles 15 to 17 of the Regulation. The following discussion will analyse the new provisions and assess the potential impact for both business and consumers.

4.3.6.1 The New Articles.

The purpose of the new articles is made clear in the preamble to the Regulation:

“In relation to insurance, consumer contracts and employment, the weaker party should be protected by rules of jurisdiction more favourable to his interests than the general rules provide for.”¹⁵⁴

The new provision, in Article 15 (1) states:

“In matters relating to a contract concluded by a person, the consumer, for a purpose which can be regarded as being outside his trade or profession, jurisdiction shall be determined by this Section, without prejudice to Article 4 and point 5 of Article 5, if:

- (a) it is a contract for the sale of goods on instalment credit terms; or
- (b) it is a contract for a loan repayable by instalments, or for any other form of credit, made to finance the sale of goods; or
- (c) in all other cases, the contract has been concluded with a person who pursues commercial or professional activities in the Member State of the consumer’s domicile or, by any means, directs such activities to that Member State or to several States including that Member State, and the contract falls within the scope of such activities.”

For the most part the provisions prescribing special rules for jurisdiction over consumer contracts are identical to those found in the Convention. Consumer is still defined as a person concluding a contract for a purpose which can be regarded as outside his trade or profession¹⁵⁵ and the options available to the consumer remain identical to

¹⁵³ Amended proposal for a Council Regulation on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. COM (2000)689 final. 1999/0154 (CNS) p. 5.

¹⁵⁴ Recital 13.

¹⁵⁵ And hence, the potential ambiguity remains. See above at 4.3.5.

those in the Brussels Convention in that he has a choice of where to bring an action, but an action may only be brought against him in the courts of his home-state.¹⁵⁶ The ability to depart from the consumer provisions of the Regulation by agreement also remains identical to the Convention. The key, and to some commentators 'burdensome', changes to the provision¹⁵⁷ are to be found in the third paragraph of Article 15.¹⁵⁸

The earlier reference to goods and services is removed, thus negating the potential for inquiries into whether 'data-products', such as software and multimedia are correctly categorised as either goods or services.¹⁵⁹ This removes a potential loophole in the provision's application to many electronic consumer contracts. The requirement that the consumer 'took the steps necessary for the conclusion of the contract' is also deleted, avoiding the technical difficulties associated with determining the place where the contract was formally concluded.¹⁶⁰ The avoidance of uncertainty was the stated purpose of the original terminology, but in the light of modern technology the phrase still had the potential to encourage unnecessary and complex technical argument. The complete removal of this requirement in the Regulation also avoids technical arguments relating to 'where' the acts or the 'necessary steps' actually took place in the electronic environment.¹⁶¹ Some commentators have suggested that the removal of this requirement will also enable a consumer to take advantage of the consumer protection provisions when entering electronic contracts whilst visiting a State other than his home-State.¹⁶² Whilst this argument is a sound one on the basis that physical location is generally meaningless in relation to electronic contracts, if a supplier uses a variation of his site for each jurisdiction¹⁶³ there may be an equally sound argument that the contract does not fall within the scope of his commercial activities in the consumer's home State.

The operative phrase "preceded by a specific invitation... or by advertising", a source of some uncertainty,¹⁶⁴ is replaced with a requirement that the supplier "pursues

¹⁵⁶ Article 16 of the Regulation, and Article 14 of the Brussels Convention.

¹⁵⁷ See, Pullen, M. "On The Proposals To Adopt The Amended Brussels Convention And The Draft Rome II Convention As EU Regulations Pursuant To Article 65 Of The Amsterdam Treaty" *EU Version - Position Paper Prepared For The Advertising Association*.

http://www.ilpf.org/events/jurisdiction/pullen_posit.htm

¹⁵⁸ Previously Article 13 (3) under the Convention.

¹⁵⁹ See the discussion in chapter 13.2.

¹⁶⁰ A potentially distracting assessment, particularly in electronic commerce. See the discussion in chapter 8 below.

¹⁶¹ Such as whether the steps were actually taken on the consumer's computer in his home state, or alternatively taken on the supplier's website, wherever that may be stored.

¹⁶² *Op cit* fn 79 at p. 125; "... if an English domiciliary placed the order from an Internet Café while on holiday in France".

¹⁶³ As many do, using the country identifier such as .co.uk.

¹⁶⁴ See the preceding discussion at 4.3.5.

commercial or professional activities in the Member State of the consumer's domicile or, by any means, directs such activities to that Member State or to several States including that Member State".¹⁶⁵ Arguably this revised provision largely follows the jurisprudence of the ECJ on the earlier terminology. However, whilst the new Article removes some of the uncertainty attributed to its predecessor, the terminology adopted does raise new questions, in particular, what qualifies as 'pursuing' commercial or professional activities or 'directing' such activities to a Member State or group of States?

4.3.6.2 'Pursuing or Directing Commercial or Professional Activities'

This terminology, and the intention behind it, has been responsible for much of the heated debate behind the Regulation's introduction. The Commission had made its intended interpretation of the phrase clear in earlier proposals for the Regulation. If a means of electronic commerce was accessible in a State, then that would constitute "an activity directed to that State". A recital was inserted to clarify this point but was later removed after pressure from business parties, other EU bodies and Member States, including the United Kingdom. The recital read:

"...Account must be taken of the growing development of the new communication technologies, particularly in relation to consumers; whereas in particular, electronic commerce in goods and services by a means accessible in another Member State constitutes an activity directed to that State. Where that State is the State of the consumer's domicile, the consumer must be able to enjoy the protection available to him when he enters into a consumer contract by electronic means from his domicile."¹⁶⁶

Arguably, the new terminology is a natural progression encompassing the existing body of case-law and official reports associated with the Convention terminology. The idea that the trader had 'done certain acts' to promote his goods or services which were 'directed' or 'aimed' at a particular country can be equated to the pursuing or directing of activities.¹⁶⁷

¹⁶⁵ Article 15(1)(c)

¹⁶⁶ Amended proposal for a Council Regulation on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. COM (2000)689 final. Ex - Recital 13. This recital did nevertheless retain a reference to 'goods and services', potentially excluding intangible items which are arguably not 'goods' or 'services'.

¹⁶⁷ See the discussion above at 4.3.5.

The response, provoked by the Commission's proposed recital, was centred on the suggestion that mere 'accessibility' would attract the application of the provision. For Internet traders the difficulty is clear. The Internet is an environment with unique attributes, one of which is the availability of its content anywhere in the world, at any time.¹⁶⁸ Hence, by simply advertising on a website the trader may be subject to the jurisdiction of the courts in any of the fifteen Member States.

The removal of the clarifying recital has left the interpretation of this contentious provision to the ECJ and Member State courts. This has the potential to create uncertainty for the service provider and the consumer as to whether a particular website or other form of electronic communication will fall within the definition. The predominant methods of electronic communication will now be considered in the light of this new terminology.

4.3.6.2.1 Direct Communication

As was the case with the Convention provision a direct communication or 'specific invitation' addressed to the consumer will clearly fall within the new criteria. This will include solicited or unsolicited e-mails and SMS messages received on an individual's computer or mobile phone. If a supplier targets consumers in one of the Member States in this way, he will be directing his commercial or professional activities there. Any contract falling within the scope of those activities entered into with a consumer in a Member State will fall within the provision.

4.3.6.2.2 Websites and Website Advertising

The uncertainty created by website activity and jurisdiction has led to the examination of websites and some discussion of whether a site is 'passive' or 'active',¹⁶⁹ the idea being that an 'active' website will fall within the provisions whereas a 'passive' site will not. Some consideration will be given to this discussion but it must be stated at the outset that, in the writer's opinion, the distinction is not a helpful or appropriate one in the context of the Regulation.

¹⁶⁸ As with all generalisations there are exceptions. The technology exists, and is in use in certain states to block sites from other jurisdictions. In China most external sites were blocked until 2001.

¹⁶⁹ This distinction is discussed above in chapter 3.

Advertising and Websites: The 'active' or 'passive' distinction.

Websites can be quite passive forms of communication designed to disseminate information to a global audience. However, the majority of commercial websites are designed to allow a customer to enter contracts on-line.¹⁷⁰ Much of the discussion surrounding the issue has focussed on the distinction between these 'interactive' websites and 'non-interactive' (passive) sites which simply advertise products or services. It has been suggested that merely 'passive' websites will not be caught by the provision found in Article 15, but 'active' websites, i.e. interactive sites designed and programmed for the purpose of entering contracts with customers, will.¹⁷¹

This approach has been compared to the adaptation in the US of the 'minimum contacts' doctrine to websites¹⁷² (i.e. whether a defendant has sufficient contacts with the forum to justify the court exercising jurisdiction over the case, and the pursuing of activities which cause a consequence in that particular state).¹⁷³ In cases heard before US courts it has been suggested that 'active' sites are sufficient to satisfy the doctrine¹⁷⁴ whereas 'passive' sites, merely providing information, are not.¹⁷⁵ However, in this context the distinction is not helpful and arguably not appropriate when considering the application of Article 15. It should also be noted that the Commission has explicitly rejected the concept stating that it "is quite foreign to the approach taken in the Regulation".¹⁷⁶

Alternatively, the courts could adopt an approach similar to that adopted under the now repealed Financial Services Act 1986 s.57 to whether an advertisement for financial services had been 'directed' toward the UK. The Financial Services Authority concluded that a variety of factors should be considered in the assessment. These included: disclaimers and warnings, links and the format and content of the site; whether the site was promoted on UK based search engines and what steps were taken to limit access (whether effective or not) i.e. filters based on address and post code and IP

¹⁷⁰ This, after all, is one of the main benefits of the Internet and the basis of electronic commerce.

¹⁷¹ See; McClean, D. *Morris: The Conflict of Laws*, 5th ed. (Sweet & Maxwell: London, 2000) at p. 112.

¹⁷² See; Reed, C. *Internet Law: Text and Materials* (Butterworths: London, 2000) chapter 7.

¹⁷³ See *Compuserve v. Patterson* 89 F 3d 1257 (6th Cir, 1996). The landmark case of *Shaffer v. Heitner* 433 U.S. 186 (1977), set the standard for future cases but the outcome must not offend the principles of fair play and substantial justice for which the standard was set in *International Shoe v. Washington*, 326 U.S. 310 (1945) and more recently *Asahi Metal Industry Co., Ltd v. Superior Court*, 480 U.S. 102 (1987).

¹⁷⁴ *Maritz Inc v Cybergold Inc* 947 F Supp 1328 (ED Mo, 1996); *Zippo Mfg Co v. Zippo Dot Com Inc* 952 F, Supp 1119.

¹⁷⁵ *Berusan Restaurant Corp v King* 937 F Supp 295 (SDNY, 1996) affirmed in 126 F 3d 25 (2nd Cir, 1997).

¹⁷⁶ Amended proposal for a Council Regulation on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. COM/2000/0689 final - CNS 99/0154 (OJ C 062 E) at p 6.

address filters.¹⁷⁷ However, the effectiveness of disclaimers has been questioned.¹⁷⁸ The language or currency used on a website has little relevance in the adjudication also. In their Joint Statement¹⁷⁹ the Council and the Commission stated the following:

“In this context, the Council and the Commission stress that the mere fact that an Internet site is accessible is not sufficient for Article 15 to be applicable, although a factor will be that this Internet site solicits the conclusion of distance contracts and that a contract has actually been concluded at a distance, by whatever means. In this respect, the language or currency which a website uses does not constitute a relevant factor.”¹⁸⁰

It is submitted that these discussions lose sight of the purpose of the Article and the correct analysis of the terminology. If the provisions in the Regulation are relied upon by a party, then clearly a dispute exists with a consumer and as the Commission points out,

“...the existence of a consumer dispute requiring court action presupposes a consumer contract. Yet the very existence of such a contract would seem to be a clear indication that the supplier of the goods or services has directed his activities toward the state where the consumer is domiciled.”¹⁸¹

It may be argued that this suggestion is tantamount to a presumption that activities have been directed to a state if a contract exists with a consumer domiciled in that state. But even if that is so, if the trader (who we must remember is in the more powerful position economically) can present a good arguable case that the consumer solicited his business, rather than visa-versa, the contract will not fall within the provision.¹⁸²

¹⁷⁷ http://www.fsa.gov.uk/pubs/guidance/gr02_1998.pdf.

¹⁷⁸ Mike Pullen “On The Proposals To Adopt The Amended Brussels Convention And The Draft Rome II Convention As EU Regulations Pursuant To Article 65 Of The Amsterdam Treaty” *EU Version - Position Paper Prepared For The Advertising Association*.

http://www.ilpf.org/events/jurisdiction/presentations/pullen_posit.htm

¹⁷⁹ Press release: Commission adopts draft Regulation on Jurisdiction, Recognition and Enforcement of Judgments in Civil and Commercial Matters. IP/99/510. (14th July 1999). Available at;

<http://www.dti.gov.uk/cacp/ca/policy/jurisdiction/eustate.htm>.

¹⁸⁰ *Ibid*.

¹⁸¹ *Op cit* fn 165.

¹⁸² As is the case under the corresponding Brussels Convention provision, see *Andrew Rayner v. Richard Davies* [2002] EWCA Civ 1880; [2002] WL 31676420 (CA).

The Article supports a strong consumer protection regime with the clear message to suppliers that if they wish to capitalise on the e-commerce consumer-market within the EU they must be prepared to go to the courts in the consumer's domicile in the event of a dispute. Support for this suggestion can be found in the Commission's refusal to yield any further ground on the possible scope of the paragraph. In rejecting the Parliament's suggestion that the Article should state that any attempt by the supplier to confine his commercial activity to a certain State should be a factor in the assessment of whether activities have been directed toward one or more Member States, the Commission stated that such an approach would "run counter to the philosophy of the provision".¹⁸³ The substantive issues in dispute remain distinct. The burden of bringing or responding to an action in another Member State is clearly disproportionate for the consumer and the prospect does deter consumers from entering electronic contracts with suppliers in other Member States.¹⁸⁴ Interpreting the provision narrowly would not sit comfortably with EU consumer protection policy and would be detrimental to the development of consumer confidence in entering electronic contracts.¹⁸⁵

There are also significant benefits to the development of e-commerce if the strict approach suggested by the Commission is adopted. The provisions could serve to:

- 1) Build consumer confidence to increase participation in e-commerce (although this is debated by those representing business).¹⁸⁶
- 2) Promote good business practice, reducing the occurrence of disputes and the need to take court action.
- 3) Encourage the development of effective and reliable alternative dispute resolution mechanisms.

Finally, it should be remembered that the accessibility of a website is not the key issue. The purpose of the provision is to afford consumers added protection where a dispute with a service provider has not been resolved amicably and the dispute resulted from a contract which was a consequence of the service providers' solicitation of business with consumers domiciled in a Member State. For service providers the

¹⁸³ *Op cit* fn 165 at p. 5.

¹⁸⁴ See the report by the National Consumers Council "E-Commerce and Consumer Protection" PD39/2000 (August 2000).

¹⁸⁵ See; 'Communication from the Commission to the European Parliament, The Council, The Economic And Social Committee and The Committee of the Regions - Consumer Policy Strategy 2002-2006'.

http://europa.eu.int/comm/consumers/policy/intro/consumer_policy_strategy_en.pdf

¹⁸⁶ See Meller. P. *op cit* fn. 139.

decision is a simple one – they can choose whether to contract with consumers in a particular State or not. If they choose to do so, then they must be prepared to appear in the courts of that state in the event of a dispute with a consumer. Only if they can show that they were actively pursued by a consumer, or deceived by a consumer as to his domicile, will they be able to avoid the Regulation provisions.

4.4 Jurisdiction and states outside the scope of the Conventions and Regulation

To be complete, some consideration must be given to contracts falling outside the scope of the Conventions and Regulation. Such contracts are covered by the rules of Private International Law.

4.4.1 The Traditional Rules in England and Wales

Historically, when the courts have been faced with a contractual dispute involving a ‘new’ method of communication, a level of pragmatism has been required to resolve the dispute equitably whilst adhering to established contractual principles and doctrine.¹⁸⁷ Commercial expediency and the allocation of risk are often found to be relevant factors in the judgments. When referring to telex communications Lord Wilberforce suggested that when disputes arise,

“... they must be resolved by reference to the intentions of the parties, by sound business practice and in some cases by a judgment where the risks should lie.”¹⁸⁸

With the progressive development of global communications technologies it is no co-incidence that many disputes before the courts have a jurisdictional issue to be resolved. In line with the judgments in the ‘classic cases’ much of the discussion surrounding electronic contracting and questions of jurisdiction has focussed on the ‘place of formation’ of the contract. This is often without acknowledgement of the fact that this issue forms only one element of a number of considerations in the court’s decision to hear a contractual dispute.

¹⁸⁷ A classic example is the development of the postal system and consequentially the ‘postal rule’. Considered below in chapter 8.4.

¹⁸⁸ Lord Wilberforce in *Brinkibon v Stahag Stahl und Handelgesellschaft Mba* [1983] 2 A.C. 34 at p. 42, referring to the multitude of possible telex communication scenarios. His sentiments were echoed by Lord Fraser at p. 43.

Under the Civil Procedure Rules¹⁸⁹ as amended by the Civil Procedure (Amendment) Rules¹⁹⁰ there are three bases of jurisdiction, presence, submission and service outside of the jurisdiction with the leave of the court.

4.4.1.1 Presence

'Presence' in this sense clearly requires some 'physical' presence within the jurisdiction to which or whom a claim form may be served.¹⁹¹ The serving of a claim form on an individual who is present in England or Wales will be subject to the *in personam* jurisdiction of the court. The duration of the defendant's presence is not relevant.¹⁹² For a company present in England and Wales a claim form is effectively served if it is delivered or posted to the company's registered office. If the company is incorporated outside of Great Britain, the form may be served on an individual, nominated by the company and authorised to accept service of process on behalf of the company.¹⁹³ The Civil Procedure Rules 1998 contain a simplified provision requiring the service of the claim form on 'a person holding a senior position' within the company or corporation.¹⁹⁴ An 'electronic presence' would not appear to be sufficient to fall within this heading; however, a claim form may be served on the agent of an overseas principle.¹⁹⁵ There may be scope, perhaps as technology develops, for an argument that a claim form could be served on an 'electronic agent' present in the jurisdiction.¹⁹⁶

4.4.1.2 Submission to jurisdiction

A submission to the jurisdiction of the court can take place in various ways. By his conduct the individual precludes himself from objecting to the jurisdiction. However, if the individual attends the court in order to dispute jurisdiction he is not taken to have submitted to the jurisdiction.¹⁹⁷

¹⁸⁹ S.I. 1998 No. 3132.

¹⁹⁰ S.I. 2000 No. 221.

¹⁹¹ Formerly known as a 'writ' under the Rules of the Supreme Court (RSC) Order 11 r1 before the introduction of the Civil Procedure Rules (S.I. 1998 No. 3132).

¹⁹² *Maharanees of Baroda v. Wildenstein* [1972] 2 Q.B. 283. However, this rule is subject to the application of the Brussels Convention (discussed above) in relation to the defendant's place of residence and 'domicile'.

¹⁹³ The person nominated to the Registrar of Companies as required by the Companies Act 1985, s.691(1)(b)(ii).

¹⁹⁴ CPR, r. 6(4).

¹⁹⁵ CPR, r. 6.16.

¹⁹⁶ See the discussion above at 4.3. However, as was argued in chapter 3, significant leaps in technology or judicial interpretation would be required if electronic agents are to be treated as 'agents' in law.

¹⁹⁷ CPR, r.11(1) and (3). *Re Dulles' Settlement* (No 2)[1951] Ch 842 and *Williams and Glyn's Bank v. Astro Dynamic Cia Naviera SA* [1984] 1 All ER 760.

4.4.1.3 Service out of the jurisdiction with leave of the court: Extended Jurisdiction under the Civil Procedure Rules

Under Rule 6.20 of the Civil Procedure Rules¹⁹⁸ the court has a discretionary power to permit service out of the jurisdiction but only in a 'proper case'. The court must take great care before it allows a claim form to be served out of the jurisdiction and any doubt or ambiguity in the application of Rule 6.20 must be resolved in favour of the respondent.¹⁹⁹ There must be full and fair disclosure of all the relevant facts by the claimant and the claim must be not only within the letter but also within the spirit of the rule.²⁰⁰ The nature of the dispute, including legal and practical issues, will also be taken into account by the court to determine whether the jurisdiction is the *forum conveniens*.²⁰¹ The claimant must convince the court that the case is a proper one for service out of the jurisdiction and that an English court is the appropriate forum. The claimant must show that a 'good arguable case' exists and there is a serious question to be tried under one of the sub-headings of the rule. For the purposes of this discussion the relevant sub-heading is CPR, r. 6.20 (5):

"A claim is made in respect of a contract where the contract -

- (a) was made within the jurisdiction;
- (b) was made by or through an agent trading or residing within the jurisdiction;
- (c) is governed by English law; or
- (d) contains a term to the effect that the court shall have jurisdiction to determine any claim in respect of the contract"

The claim has to be in respect of 'a contract', which could be construed as excluding actions relating to the contract's existence. However, the previous provision, found in Order 11 of the Rules of the Supreme Court, was very broad in its scope and it has been argued that the new provision should be no less widely interpreted.²⁰²

¹⁹⁸ Formerly, Order 11, r. 1(1) of the Rules of the Supreme Court.

¹⁹⁹ *Societe Generale de Paris v. Dreyfus Bros.* (1887) 37 Ch.D. 215, *The Hagen* [1908] P. 189 and *Re Schmitz* [1926] Ch. 710.

²⁰⁰ *Johnson v. Taylor Bros.* [1920] A.C.144 and *George Morro Ltd v. American Cynamid Corp.* [1944] K.B.432.

²⁰¹ *Seaconsfar Far East Ltd v. Bank Markhazi Jomhouri Islami Iran* [1994] 1 A.C. 438, p 452.

²⁰² McClean, D. *Morris: The Conflict of Laws*, 5th ed. (Sweet & Maxwell: London, 2000) at p.82. Therefore encompassing actions 'to enforce, rescind, dissolve, annul or otherwise affect' a contract in addition to those for breach. See *B.P. Exploration (Libya) Ltd v. Hunt* [1976] 1 W.L.R. 788 (Declaration that a contract has been frustrated).

Contracts made within the jurisdiction

For many writers this subject has been the focus of discussion in matters relating to questions of jurisdiction when considering electronic contracts.²⁰³ However, as can be seen from the previous discussion, the issue of where the contract is 'made' is secondary to the 'place of performance' in the context of the Brussels Convention and the new Regulation. Only when the Convention rules do not apply will the common law, or more accurately the Civil Procedure Rules, be relevant.

In English law there are several well-established principles in relation to the time and place at which a contract is 'made'.²⁰⁴ Primarily the point at which an acceptance is effective dictates the time and place at which the contract is formed. If this occurs within the jurisdiction the court may exercise its discretion to hear the case and permit service out of the jurisdiction. The general rule prescribes that acceptance is effective when it is communicated to (i.e. received by) the offeror. This rule is displaced where the acceptance is communicated by post and the postal rule applies. The significance of this issue can be seen in the *Entores v. Miles Far East Corp.*²⁰⁵ and *Brinkibon Ltd v. Stahlg Stahl und Stahlwarenhandels-gesellschaft mbH*,²⁰⁶ cases involving jurisdictional disputes determined on this basis. The receipt (or general) rule was preferred over the despatch (or postal) rule for acceptance with the courts expressing their reluctance to extend the dispatch rule beyond communications by post to the telex communications before them. Lord Wilberforce did however leave the potential for extending the dispatch rule open, stating that there could be 'no universal rule' to cover all situations, preferring to deal with individual cases on their facts and considering 'sound business practice' and an allocation of where the risk of loss should lie. If a party was at fault in some way in the failure of a communication, this may also indicate where the Court should allocate any subsequent loss.

The issue of contract formation in the electronic environment is discussed below in chapter 8. It is argued that only in the most unusual of situations would the courts consider the application of the postal rule to electronic contracts. However, it is also indicated that with electronic forms of communication ascertaining the time and place at which the communication of acceptance is received may be open to interpretation.

²⁰³ See for example; Murray, A. D.(2000) "Entering into Contracts Electronically: The Real W.W.W." in Edwards & Waelde (ed.) *Law and the Internet: A Framework for Electronic Commerce* (Hart Publishing: Oxford) at p.17. Davies, LJ, *A Model for Internet Regulation* [1998] *Society for Computers and Law* available at www.scl.org.

²⁰⁴ This is discussed in chapter 8.

²⁰⁵ [1955] 2 Q.B. 327.

²⁰⁶ [1983] 2 A.C. 34.

Whether the contract was 'made' within the jurisdiction may depend upon the interpretation of 'received' adopted by the courts in England and Wales. If the acceptance is "deemed to be received when the recipient is able to access it",²⁰⁷ then the 'place' of receipt could be a server located in almost any State, with the conclusion that the contract is 'made' there and not within the jurisdiction.

Contracts made by or through English agents of foreign principals.

This sub-heading only applies where the principal is the intended respondent and not where he is a claimant.²⁰⁸ It has been held that this provision encompasses not only contracts made by agents with authority to enter contracts but also those who do not have such authority but merely transmit orders to a foreign principal for his acceptance or rejection.²⁰⁹ This sub-heading has potential significance for suppliers using interactive websites or electronic agents, based on servers within the jurisdiction. The courts will have to decide whether the collection and transmission of orders electronically fall within this subheading bringing foreign principles within the jurisdiction.

Contracts governed by English law

The correct law of the contract is determined by reference to the Contracts (Applicable Law) Act 1990 discussed below.²¹⁰ Where those rules indicate that English law is the proper law of the contract the courts have the discretion to seize jurisdiction and allow service out of the jurisdiction. However, the courts have emphasised that this discretion "should be exercised with circumspection".²¹¹ The courts are reluctant to exercise jurisdiction under this subheading in a case involving a foreign corporation with no place of business in England or Wales.

Contracts containing a jurisdiction clause selecting the English Court

The courts will infer from such a term in a contract that the parties have submitted to the jurisdiction unless a party can indicate that such a clause should not be effective against him.

²⁰⁷ An interpretation adopted in relation to orders and the acknowledgement of orders under the Electronic Commerce Regulations, below in chapter 8.4.

²⁰⁸ *Union International Insurance Co. v. Jubilee Insurance Co.* [1991] 1 W.L.R. 415.

²⁰⁹ *National Mortgage and Agency Co. of New Zealand v. Gosselin* (1922) 38 T.L.R. 832.

²¹⁰ In chapter 5.

²¹¹ Lord Diplock in *Amin Rasheed Shipping Corp. v. Kuwait Insurance Co.* [1984] A.C. 50; see also *Spiliada Maritime Corp. v. Cansulex Ltd.* [1987] A.C. 460.

The Court may also seize jurisdiction in a case where a claim is made in respect of a breach of contract committed within the jurisdiction.²¹² The breach must be of a part of the contract intended to be performed within the jurisdiction.²¹³ This need not be expressly stated, but the courts must be able to infer from the true construction of the contract that this was the intention of the parties.²¹⁴ For example, if a supplier of goods is based in England, then it is reasonable to infer that the buyer's obligation to pay was intended to be performed in England. As a general rule it is the debtor's obligation to seek out the creditor.²¹⁵

The Civil Procedure Rules for deciding jurisdiction in cases involving parties based outside of the scope of the Conventions or Regulation are in many ways more reliant on a 'physical presence' or ascertaining the 'place' in which a contract was concluded or to be performed.

4.5 Conclusion

For electronic contracting, and electronic commerce in general, predictable and transparent rules on jurisdiction are necessary to promote confidence and produce legal certainty. However, from the preceding discussion, it would appear that there is a lack of a harmonised approach to the issue and a lack of clarity and legal certainty in the measures that are in place including recent developments intended to take account of the new forms of commerce.

When determining which court has jurisdiction in a dispute, the frustrating starting point is the application of a number of different legal instruments within Europe alone, depending upon which other State is involved. By virtue of the most recent EU 'harmonising' measure, for the courts of England and Wales there are now three different instruments, in addition to relevant elements of national law to consider. This study is primarily concerned with States within the European Economic Area; beyond this the situation becomes even more complex for the electronic trader. Discussions are on-going to obtain a broader consensus on this crucial issue under the auspices of The Hague Conference on Private International Law, which includes amongst others

²¹² Under CPR, r. 6.20 (6).

²¹³ *Rein v. Stein* [1892] 1 Q.B. 753.

²¹⁴ *Ibid.*

²¹⁵ *The Eider* [1893] P. 119, but *cf. Malik v. Narodni Banka Ceskoslovenska* [1946] 2 All E.R. 663.

Australia, Japan and the United States.²¹⁶ However, a finalised Convention remains some way off.

Even within Europe there is inconsistency with the terminology employed in the legal instruments in place and uncertainty in the interpretation of certain key elements. Unfortunately, many of these elements have the potential to impact upon electronic contracts. Arguably, some of the concepts fundamental to the Conventions and Regulation are inappropriate for application in the electronic environment because of their reliance on physical requirements.

For example, the concept of domicile has been the subject of some criticism, particularly in relation to electronic commerce because by definition it requires some physical presence.²¹⁷ The heavy reliance upon the physical attributes of a party and the physical location of that party will often be fruitless or produce an entirely fortuitous conclusion, in the electronic environment, which may bear little relevance to the contract in question or the dispute before the court.

The special rules on jurisdiction relating to contracts also have the potential to create uncertainty because the search for the 'place of performance of the obligation in question', particularly in contracts which are performed electronically, may lead to inappropriate or illogical results.²¹⁸ The new Regulation has introduced some clarification for contracts for the sale of goods or the provision of services but adds nothing for contracts not falling within these categories. Where a 'data product' or a license to obtain and use a copy of software is purchased, then it would appear that the courts remain undirected as to the assessment of the 'place of performance'.

The Conventions and the Regulation contain favourable provisions for 'weaker parties'. the most relevant 'weaker party' in this context is the consumer. If electronic commerce is to develop to its full potential consumers must have confidence in entering cross-border electronic contracts. The Convention provision has two elements which have been the source of some debate in traditional contracts and have the potential to create further debate in relation to electronic contracts: the requirements that the contract was 'preceded by advertising' and that the consumer took the 'steps necessary' for the conclusion of the contract in his home State. If the second element is considered in its broadest context it can be interpreted as the basic steps such as placing an order.

²¹⁶ As of October 2002 the membership was 62 States.

²¹⁷ Reed, C. *Internet Law: Text and Materials* (Butterworths: London, 2000) at p. 192.

²¹⁸ Such as the 'place of performance' being a server in a state which has no other connection with the parties or their transaction.

However, if, as is possible with electronic contracts, the consumer is 'on the move' when he places his order using a mobile piece of technology and happens not to be in his home State at the time, then the provision would arguably not apply.

Under Article 13 of the Brussels Convention, a consumer contract must be preceded by a specific invitation or advertising to qualify. What constitutes 'advertising' in a consumer's State has always been subject to some uncertainty and the advent of websites as a marketing tool has added to the uncertainty. Something more than 'passive' advertising is required – the targeting of the consumer's State in some way, but with the global availability of a websites the question of whether that site 'targets' a particular jurisdiction remains open to interpretation.

Under Article 15 of the Brussels Regulation 'specific invitation or advertising' has been replaced by a requirement that the other party pursues commercial or professional activity in the consumer's State or by any means directs such activity towards that State. In the preparation of the Brussels Regulation the changes to the provisions for consumer contracts were a source of concern for commercial parties utilising the Internet and other electronic forms of communication. The main concern related to the potential for the new provision to encompass a wide range of activities, including website advertising. The fear that the mere accessibility of a website in a particular State may lead to the courts of that State seizing jurisdiction resulted in vigorous lobbying and the removal of the clarifying recital. However, it is submitted that the concerns were misplaced and that the removal of the clarifying recital has left the potential for uncertainty which will ultimately be detrimental for business parties and consumers alike. There are a number of reasons why many of the concerns associated with the provision in the Regulation were unnecessary. First, the mere accessibility of the website is not the issue; the entering into contracts with consumers in that country is.²¹⁹ Second, the changes made by the Regulation are not quite as dramatic as perceived, particularly when the approach adopted by the ECJ is considered. Under the Convention terminology, the supplier has to direct his advertising to a particular State and essentially solicit business there. If, on the other hand, a supplier can show that *he* was pursued by the consumer and that his advertising was not directed towards the consumer's State the provision will not apply. The Regulation has essentially replaced the ambiguous phrase "or by advertising", with the terminology adopted by the courts - directing commercial activities. The activating

²¹⁹ See the Joint Council and Commission statement in Annex II of Council document 14139/00 of 14th December 2000.

factor remains the existence of a contract with a consumer, with the provision applying unless the supplier can show that he did not pursue or direct his activities in the consumer's State by soliciting business in some way, in that State. The question will remain, 'who invited whom' to do business.

However, in the context of the electronic environment the provisions in both instruments are sufficiently unclear to risk divergent interpretation in the Member States and create uncertainty for businesses and consumers entering cross-border electronic contracts. The purpose of this provision is to promote both consumer confidence and good business practice. The fears of being brought before a foreign tribunal are overstated. Most consumer contracts are of low transactional value, making court action an uneconomical and unlikely occurrence. The fact that a consumer has the legal right to take action in his home State may do nothing more than to promote the efficient handling of consumer complaints by suppliers. If a dispute does go beyond the amicable negotiation stage then the threat of legal action in a foreign court may promote the participation in Alternative Dispute Resolution (ADR) schemes by supplier. ADR, particularly by electronic means, is a far more appropriate method of resolving disputes relating to electronic commerce.²²⁰ It is also an approach promoted by both the business community and the European Commission. Consumer protection measures of the kind found in the Regulation may be just the incentive to promote the development and use of such schemes by online suppliers.²²¹

The phrase 'branch, agency or other establishment' is used in a number of contexts in the Conventions and the Regulation and it has the potential to be a significant phrase for parties using automated technologies to enter electronic contracts. The phrase is traditionally associated with a physical presence in a State. The close link between the action and the courts of that State, created by the existence of a branch agency or other establishment, means that hearing a case in that court promotes the sound administration of justice. However, the phrase is also used in relation to the protected position of weaker parties, such as consumers. With the growth in electronic commerce and associated developments in electronic communications technology there may be a need for some reconsideration of what is meant by a 'branch, agency or other establishment'. In the electronic environment a supplier can have a 'branch or agency' of his business in any State, performing all of the associated business activities including the

²²⁰ See Hornle J, 'Disputes Solved in Cyberspace and the Rule of Law', Work in Progress, [2001] (2) *The Journal of Information, Law and Technology (JILT)*. <http://elj.warwick.ac.uk/jilt/01-2/hornle.html/>.

²²¹ Such as "Which Webtrader" which had it's own code of conduct and dispute resolution mechanism.

entering of contracts, without any physical presence in that State. The consequences and effects of that activity will, in many cases, be identical to those which would result from there being a physical branch or agency in the State. It is submitted that electronic versions of branches or agencies can fall within the terminology as interpreted by the courts if a 'physical presence' in the State is not required. It is argued that as a matter of policy and for consistency, a physical presence should not be required for a supplier to operate a branch, agency or other establishment in a particular State. If a court were to decline jurisdiction on the basis of this lack of physical presence, it is submitted that the objectives of achieving the sound administration of justice and protecting consumers would be undermined.

Where an electronic contract falls outside of the scope of the Conventions or Regulation the courts will apply the Civil Procedure Rules and the associated common law principles. The rules are heavily reliant on a physical presence or 'place' in their assessment of jurisdiction. However, if the courts are faced with a new or novel situation created by an electronic contract reference may be made to the legislative provisions in place and underlying policy considerations, such as consumer protection.

If a court does have jurisdiction to hear a dispute relating to an electronic contract a further vital question must be considered before any assessment of the substantive issues of the dispute can begin. The court must establish the law applicable to the contract, or the 'proper law of the contract'.

Applicable Law

Once it is established that a court has jurisdiction to hear a dispute, the court must then determine the correct substantive law to apply, or the 'proper law' of the contract. Rules associated with contractual obligations vary considerably from one legal system to the next and the outcome of a dispute may hinge on which country's law applies. In general, a party to a dispute will want the court to apply the laws of his home State which are familiar to him. Alternatively a party may desire the application of the law of another State, which are more favourable to his commercial interests. The increase in potential for disputes as to the proper law of the contract, due to the advent and development of electronic commerce, makes this issue a prominent one for those wishing to enter contracts electronically. Legal uncertainty in this area has the potential to undermine confidence in the use of electronic commerce and consequently hinder its development within the European Union and the United Kingdom.

5.1 The Common Law Approach in England and Wales

In England and Wales for contracts entered into on or before April 1st 1991 the applicable law of the contract will be determined by the common law. The introduction of the Rome Convention¹ has meant that the common law will play a minimal role in disputes relating to electronic contracting. However, for completeness the approach adopted at common law will be discussed briefly to allow for comparison with Convention provisions.

At common law the predominant approach taken by the courts was to establish the 'proper law of the contract' by ascertaining, objectively, the intention of the parties.

¹ The Rome Convention on the Law Applicable to Contractual Obligations [1980] OJ L266.

“English law has...treated the matter as depending on the intention of the parties to be ascertained in each case on a consideration of the terms of the contract, the situation of the parties, and generally on all the surrounding facts.”²

The express selection of the proper law by the parties is persuasive in the court’s adjudication but not always decisive.³ In the absence of any express, or implied,⁴ choice by the parties the courts determined the proper law by identifying the legal system with which the contract had its closest and most real connection.⁵ The court will consider a variety of factors including the place of contracting, the place of performance, the place of residence or business of the parties and the subject matter of the contract.⁶ Many of these factors relate to a physical presence which, as was highlighted in the previous chapter, may be a difficult and arguably fruitless search in the electronic environment.

5.2 The Rome Convention

The 1980 Rome Convention on the Law Applicable to Contractual Obligations and subsequent Accession Treaties⁷ made steps towards the harmonisation of the rules relating to applicable law in contractual disputes in states within the European Economic Area.⁸ The Convention was given legal force in the United Kingdom by the Contracts (Applicable Law) Act 1990.⁹ Following the review of the Brussels Convention, the Rome Convention is due to be reviewed; however, this is unlikely to take place before 2004. Crucially the Rome Convention contains several of the phrases removed from the Regulation replacing the Brussels Convention. It is submitted that the review of the Rome Convention, when it comes, will do the same but until then the courts have the task of interpreting and applying these ambiguous phrases in the event of a dispute. Many of the difficulties, discussed in the previous chapter, associated with the interpretation of certain key provisions of the Brussels Convention are relevant to the application of the Rome Convention.

² *Mount Albert Borough Council v. Australasian Temperance and General Assurance Society* [1938] A.C. 224 per Lord Wright at p. 240.

³ Public policy issues were also relevant. See *Vita Food Products Inc. v. Unus Shipping Co.* [1939] A.C. 277 Lord Wright at p. 290.

⁴ *Jacobs v. Credit Lyonnais* (1884) 12 Q.B.D. 589

⁵ *The Assunzione* [1954] P. 150

⁶ *Re United Railways of the Havana and Regla Warehouses Ltd* [1960] Ch. 52; [1961] A.C. 1007 at 1021.

⁷ [1980] OJ L266. Accession Conventions; [1984] OJ L146, [1992] OJ L333/1 and [1997] OJ C15/10

⁸ The European Union Member States and the members of the European Free Trade Association (EFTA).

⁹ Section 2.

5.2.1 Scope of the Convention

The Convention rules apply “to contractual obligations in any situation involving a choice between the laws of different countries”.¹⁰ The phrase ‘contractual obligations’ would appear to imply that the parties be actually bound, excluding situations in which the contract is void. However, it is clear that such an interpretation is not the correct one in the context of the convention, particularly when the convention contains a provision for dealing with the consequences of nullity of the contract.¹¹

The law specified by the Convention will apply “whether or not it is the law of a Contracting State”,¹² giving parties considerable autonomy to select the most favourable contractual law.

Exclusions from the scope of the Rome Convention include questions relating to wills; succession or property rights arising out of the matrimonial relationship; rights and duties relating to the family relationship; negotiable instruments such as, bills of exchange, cheques and promissory notes; questions governed by company or agency law; trusts and rules of evidence or procedure.¹³ In addition, although not explicitly mentioned in the text of the Rome Convention, it has been suggested that intellectual property is also excluded from the provisions.¹⁴ With the high incidence of computer software as the subject matter of electronic commerce transactions, this could be seen as a significant exclusion. However, the report distinguishes contractual obligations from property rights and intellectual property, which would indicate that the intellectual property itself is subject to the exclusion rather than a contractual licence to sell or use copies of the software protected by intellectual property rights.¹⁵

5.2.2 Interpretation

By virtue of an appended declaration, it was intended that the ECJ have jurisdiction to rule on the interpretation of the Convention.¹⁶ However, the Brussels

¹⁰ Article 1 (1).

¹¹ Article 10(1)(e). McClean, D. *Morris: The Conflict of Laws*, 5th ed. (Sweet & Maxwell: London, 2000) at p. 325.

¹² Article 2.

¹³ Article 1 (a-h).

¹⁴ Official Report by Professors Giuliano and Lagarde on ‘The Convention on Law Applicable to Contractual Obligations’, OJ 1980 C282/1, 31st October (hereafter the Giuliano-Lagarde Report) at p10, interpreting Article 1.

¹⁵ See Chissick, M. and Kelman, A. *Electronic Commerce Law and Practice*, 2nd Edition (Sweet & Maxwell: London, 2000) at para 4.23.

¹⁶ Schedule 3 of the 1990 Act, The Brussels Protocol [1989] OJ L48. If ratified the implementing measure can be found in Section 3(1) of the 1990 Act.

Protocol, signed on 19th December 1988, has not yet entered into force.¹⁷ If the Protocol ever does come into force, the ECJ will have the power to give preliminary rulings on the interpretation of the Convention.¹⁸ Guidance to the interpretation of the Convention can also be found in the Official Report by Professors Mario Giuliano and Paul Lagarde published in the year of the Convention's introduction.¹⁹

5.2.3 Key Provisions

The applicable law, as determined by the Rome Convention, will govern all substantive issues relating to the contract. These include interpretation or construction of the contract, performance and discharge of the contract and the consequences of breach or nullity.²⁰

5.2.4 Party Autonomy

The core principle of the Rome Convention is freedom of choice, contained in Article 3:

“A contract shall be governed by the law chosen by the parties. The choice must be expressed or demonstrated with reasonable certainty by the terms of the contract or the circumstances of the case.”

In cases where the parties have made no express choice of law, but where the terms of the contract and the relevant circumstances connect the contract to a particular legal system, the court may assume that it was the intention of the parties that the law of that country would govern the contract.²¹ The Convention allows the parties to choose the law of a country regardless of whether that country has any connection with the parties or the subject matter of the contract. The validity of a party's consent to the choice of law will be determined in accordance with the Convention's provisions on material and formal validity, and capacity.²²

¹⁷ Belgium is yet to ratify the Protocol.

¹⁸ However, unlike Article 234 and the provision found in the Brussels Convention, there will be no *obligatory* reference from courts of last appeal. It could be argued that this has the potential to undermine the harmonising intention of the Convention.

¹⁹ *Ibid* fn 14.

²⁰ Article 10(1)(a)-(e).

²¹ *Egon Oldendorff v. Liberia Corp. (No. 2)* [1996] 1 Lloyd's Rep. 380

²² Articles 8,9 and 11 respectively as dictated in Article 3(4).

5.2.5 Mandatory Rules

The 'party autonomy' approach is tempered by the requirement that such a choice will not prejudice the "application of rules of law of [a] country which cannot be derogated from by contract, hereinafter called 'mandatory rules'".²³ Such mandatory rules will apply where "all the other elements relevant to the situation at the time of the choice are connected with one country only".²⁴ Where, for example, a party is selling property in State A and the contract is entered into in State A but the law of State B is chosen to govern the contract, the mandatory rules of State A will nevertheless apply. The question, which remains unresolved, is which factual elements are relevant to this determination? If some minor elements of the contract were not associated with State A, would the mandatory rules still apply? To extract this to an electronic example - the subject matter of a contract is to be electronically transferred from a source in Germany but the parties to the contract for supply are based in England and the product is transferred to the customer in England. However, if the chosen law is that of Germany, will the fact that the ultimate supplier is not based in the England prevent the English mandatory rules from applying?

Article 7(2) contains an additional provision for mandatory rules which are regarded by the State as applicable whatever law applies to the contract as a whole. Rules falling within this provision will be those, which have a 'policing' role in particular circumstances.²⁵ In the UK section 27(2) of the Unfair Contract Terms Act 1977 provides an example of a rule of this nature.

(2) This Act has effect notwithstanding any contract term which applies or purports to apply the law of some country outside the United Kingdom, where (either or both)

- (a) the term appears to the court, or arbitrator or arbiter to have been imposed wholly or mainly for the purpose of enabling the party imposing it to evade the operation of this Act; or
- (b) in the making of the contract one of the parties dealt as consumer, and he was then habitually resident in the United Kingdom, and the

²³ Article 3(3) and 7(2). In English law an example of this type of rule would be liability for negligently caused death, which cannot be excluded by a contractual term. Parties cannot contract-out of the provisions found within the Unfair Contract Terms Act 1977, save for 'international supply contracts' discussed in s.26.

²⁴ *Ibid.*

²⁵ The French text of the Convention head Article 7 as *lois de police*.

essential steps necessary for the making of the contract were taken there, whether by him or by others on his behalf.

The section is intended to prevent the indirect evasion of the mandatory rules contained within the Act by the choice of a foreign law. Part (b) contains a measure intended to protect the consumer, habitually resident in the UK. However, the consumer, or someone acting on his behalf, must take the “essential steps necessary for the making of the contract” in the United Kingdom. A similar phrase is contained within the Brussels Convention, a phrase omitted from the new Regulation because of the potential difficulties in establishing *where* necessary steps were taken in the electronic environment. In the context of the Brussels Convention it was submitted that the ‘steps’ referred to were not the technical legal steps of offer and acceptance, but rather the practical steps, such as filling in a form, posting a letter or typing information into a computer.²⁶ However, the phrase contained in s.27 refers to the ‘essential’ steps for the making of the contract. This could be interpreted as requiring a consideration of where the technical legal steps for agreement, offer and acceptance were taken. In this context there would appear to be an opportunity for a complex and technical argument as to where offer and acceptance actually takes place in the electronic environment.²⁷

5.2.6 Applicable Law in the Absence of Choice

Article 4 of the Convention sets out complex rules for the determination of the governing law where there is no express choice made by the parties and the court cannot infer with reasonable certainty what the parties intended. The Article reads;

“To the extent that the law applicable to the contract has not been chosen in accordance with Article 3, the contract shall be governed by the law of the country with which it is most closely connected.”²⁸

This provision is similar to the ‘closest and most real connection’ approach adopted by the English common law. Further guidance on the determinative factors is found in Article 4(2):

²⁶ Discussed above in chapter 4.3.

²⁷ This issue is addressed in chapter 8.

²⁸ Article 4(1)

“the contract is most closely connected with the country where the party who is to effect the characteristic performance of the contract has, at the time of conclusion of the contract, his habitual residence, or, in the case of a body corporate or unincorporate, its central administration. However, if the contract is entered into in the course of that party's trade or profession, that country shall be the country in which the principal place of business is situated or, where under the terms of the contract the performance is to be effected through a place of business other than the principal place of business, the country in which that other place of business is situated.”

The presumption in Article 4(2) will not apply if the characteristic performance cannot be determined and none of the presumptions will apply if it appears in the circumstances as a whole that the contract is more closely connected to another country.²⁹ In the courts of England and Wales the factors previously discussed; the place of contracting, place of performance and place of residence or business of the parties and the subject matter of the contract, will all be relevant factors in assessing whether the contract is more closely connected to another country. The consequence is that in all circumstances primacy is given to the country of closest connection.³⁰ Finally if separate elements of the contract have a closer connection with another country, then the law of that country may govern that part. There are a number of elements of Article 4 which may be difficult to apply to the electronic environment.

5.2.6.1 Characteristic Performance

The “performance, which is characteristic of the contract” is normally the performance for which payment is due, the delivery of goods or provision of a service for example.³¹ For certain subject matter the Article contains special provisions. For contracts dealing with immovable property it is presumed that the contract is most closely connected to the country where the property is situated.³² In relation to contracts for the carriage of goods it is presumed that the contract is most closely connected with the principal place of business of the carrier as long as that country is the place of loading

²⁹ Article 4(5).

³⁰ See the *obiter* comments in *Baroda v. Visa Bank* [1994] 2 Lloyds Rep 87 at 91.

³¹ The Giuliano and Lagarde Report explains this as the performance which “links the contract to the social and economic environment of which it will form part” at p 20.

³² Article 4(3).

or discharge.³³ For the majority of contracts there will be little difficulty in determining the performance characteristic of the contract. However in some contracts, be they entered into electronically or via more traditional methods, difficulty will arise when there are a number of elements of performance which could be called characteristic of the contract. If different parties resident in different states are to perform these different elements then Article 4(2) may be of little help. The occurrence of such contracts with obligations to be performed in a number of States by different parties is likely to increase with the predicted rise in electronic commerce.

When the characteristic performance of the contract can be determined, then the law applicable to the contract will be the law of:

- the habitual residence the party effecting that performance; or
- the place of central administration of the body corporate or unincorporated effecting the performance; or
- if the contract is entered into in the course of that party's trade, business or profession the principal place of business or place of business through which the performance is to be effected.

At this point an interesting contrast can be made with the 'Special Rules' on jurisdiction in matters relating to a contract whereby the defendant may be sued in the courts of the Member State where the performance is to occur.³⁴ In this context the law of the place where the party effecting performance resides is the focus rather than the place in which that performance is to occur.

5.2.6.1.1 The habitual residence or central administration of the party effecting the characteristic performance

If the party effecting the characteristic performance is not acting in the course of his trade, business or profession then the presumption is that the relevant country is the place where the individual had his habitual residence at the time the contract was made or in the case of a corporate body, its central administration.³⁵

³³ Article 4(4).

³⁴ Discussed above at 4.3.4.

³⁵ Article 5(2).

5.2.6.1.2 Contracts entered into in the course of a trade, business or profession.

If the party effecting the characteristic performance of the contract is acting in the course of his trade, business or profession then the presumption is that the country of closest connection is that in which the party has his principal place of business. However, if the performance is to be effected through some other place of business, such as a branch or agency, then the relevant country is the one in which that place of business is situated.³⁶

The latter part of this provision is an interesting one to consider in the context of electronic communications. If the characteristic performance is effected electronically via a website, is the 'website' the relevant 'place of business'? If so, in the majority of situations this could result in a conclusion that there may be no place of business as such, relevant to the transaction from where the applicable law may be applied. In such cases the courts will be left to consider the country of closest connection on the basis of a party's physical location, which, in the electronic environment may be unrelated to the transaction or the business activities of a party.

In cases where the 'characteristic performance' cannot be determined because the contract is a complex one, the presumptions found in Article 4(2-4) are disregarded and it will be for the court to decide the country of closest connection on the facts of the case. This may be a complex and arguably difficult analysis if the contract in question is made and performed in the electronic environment. The only 'place' capable of being established in this situation would be the physical place in which the party responsible for the automated performance of the contract is located.

5.2.7 Consumer Contracts

When dealing with consumers the supplier's freedom to use a contractual clause to dictate the proper law of the contract is curtailed by the protected status given to the consumer in Article 5. Article 5 reads:

1. This Article applies to a contract the object of which is the supply of goods or services to a person ('the consumer') for a purpose which can be regarded as being outside his trade or profession, or a contract for the provision of credit for that object.

³⁶ *Ibid.*

2. Notwithstanding the provisions of Article 3, a choice of law made by the parties shall not have the result of depriving the consumer of the protection afforded to him by the mandatory rules of the law of the country in which he has his habitual residence:

- if in that country the conclusion of the contract was preceded by a specific invitation addressed to him or by advertising, and he had taken in that country all the steps necessary on his part for the conclusion of the contract, or
- if the other party or his agent received the consumer's order in that country, or
- if the contract is for the sale of goods and the consumer travelled from that country to another country and there gave his order, provided that the consumer's journey was arranged by the seller for the purpose of inducing the consumer to buy.

Professors Giuliano and Lagarde emphasise that the consumer should not be deprived of the protection of mandatory provisions in the State of his habitual residence and add that “in this type of contract it is the law of the buyer (the weaker party) which should normally prevail over that of the seller.”³⁷ However, it is clear that this will rarely be the case, with business parties habitually inserting choice of law clauses into their contracts. It is only those rules deemed mandatory that will apply in the face of a contrary choice of law clause.³⁸

5.2.7.1 The ‘Consumer’

The first paragraph defines ‘the consumer’ as a party entering a contract for the supply of goods or services for a purpose, which can be regarded as being outside his trade or profession, or a contract for credit for the same. The terminology found in this definition is discussed in detail above.³⁹ At this point it is sufficient to re-iterate that the definitions of goods and services may not be appropriate to encompass modern data products, thus excluding a great many contracts entered into electronically. Professionals may also find themselves excluded from the protection contained within Article 5, if

³⁷ *Op cit* fn 14 at p. 24.

³⁸ The standing of such clauses may be affected by the Unfair Contract Terms Act 1977 and the Unfair Terms in Consumer Contracts Regulation 1999 is discussed below in section IV.

³⁹ At 4.3.5.

goods which they purchase may be used for a purpose relating to their profession even though they may have no expertise in that area or possess the funds or legal support available to a business.

The Article encompasses situations where a choice of law has been made and those where one has not.

5.2.7.2 Where a choice of law is made

Article 5 does not in itself invalidate a choice of law made by the parties, although a term doing so may attract the attention of the statutory regimes dealing with unfair terms.⁴⁰ The parties choice of law will be effective, but the consumer cannot be deprived of the protection afforded to him by the 'mandatory rules of the law of the country in which he has his habitual residence' in the circumstances prescribed by Article 5(2).

5.2.7.2.1 The Mandatory Rules

The mandatory rules would encompass statutes and statutory instruments intended to provide the consumer with a level of protection in the contracts he enters. In the UK these would include the consumer protection measures relating to distance selling, the sale of goods or services and unfair contract terms.⁴¹ Hence, the consumer is afforded greater protection but, as was the case with the Brussels Convention, certain circumstances have to exist for the provision to apply.

5.2.7.2.1 Specific Invitation or by Advertising in the Consumer's Jurisdiction

Article 5(2) proceeds to detail the specific circumstances which must exist for a consumer to benefit from the provision. The terminology employed is the same as that found in the Brussels Convention.⁴² This terminology was omitted because of the uncertainty surrounding electronic forms of communication such as websites, in the recent Regulation introduced to replace the Convention.

The contract must have been preceded, in the consumer's jurisdiction, by a specific invitation addressed to the consumer or advertising, and the consumer must have taken all the steps necessary on his part for the conclusion of the contract in that country. As is discussed above the requirement of advertising in the country in question

⁴⁰ Discussed below in chapters 11 & 12.

⁴¹ *Ibid*.

⁴² See 4.3.5 above.

has the potential to encompass a wide range of activities, particularly on the Internet. The uncertainty created by this dated terminology is also discussed at length above.⁴³ It is sufficient to note at this point that Professors Giuliano and Lagarde envisaged that the advertising would have to be aimed specifically at a particular country and the ECJ adopted the approach that the advertising must be in some way directed towards that country. In the context of the Brussels Regulation, the phrase has been replaced by a requirement of ‘directing or pursuing’ activities,⁴⁴ an approach already adopted by the courts to the terminology of the Brussels Convention. In the context of the Rome Convention the courts will continue to consider whether the supplier directed his advertising towards the consumer’s State. It will be remembered that in the *Andrew Piers Courtauld Rayner* case⁴⁵ the key question for the court was “who was inviting whom” to do business’.

5.2.7.2.2. The Steps Necessary for The Conclusion Of The Contract are taken by the Consumer in His Jurisdiction.

Although this latter part of the paragraph was inserted to avoid the classic problem of determining the place where the contract was concluded it nevertheless raises issues, particularly in relation to electronic contracts.⁴⁶ For this reason in the context of jurisdictional disputes the phrase has been replaced in the new Regulation. The guidance on this phrase from Professors Giuliano and Lagarde suggests that,

“The word ‘steps’ includes *inter alia* writing or any action taken in consequence of an offer or an advertisement.”⁴⁷

This would support the contention that only the practical steps necessary need to be taken by the consumer in his home State, rather than the technical legal steps (i.e. offer or acceptance). The phrase does leave a potential loophole however, where a consumer uses a mobile device to take the steps necessary whilst travelling in another country. In such a case the consumer has not taken the steps necessary in ‘his country’ and on a literal interpretation the contract is outside of the scope of the Article.

⁴³ At p.61.

⁴⁴ Although arguably, without a clarifying recital, the new terminology has the potential to create similar debate as to its scope. See above at p4.3.6.

⁴⁵ See 4.3.5 above.

⁴⁶ *Ibid*.

⁴⁷ *Op cit* fn 38.

5.2.7.3 Choice of law in consumer contracts in the absence of a clear choice by the parties

Where the parties to a consumer contract do not make a choice of law in their contract the contract will be governed by the law of the country in which the consumer has his habitual residence.⁴⁸ In this way the weaker party (the consumer) will benefit from the application of the substantive law of his home-state notwithstanding the fact that the contract is more closely connected to another state under Article 4. However, the consumer will still have to show that the contract was preceded by a specific invitation or advertising and that he took the steps necessary for the conclusion of the contract in the state of his habitual residence.

5.2.7.4 Exclusions from the consumer related provisions in Article 5

Article 5(4) contains a list of specific contracts excluded from the consumer measures:

“This Article shall not apply to:

- (a) a contract of carriage;
- (b) a contract for the supply of services where the services are to be supplied to the consumer exclusively in a country other than that in which he has his habitual residence.

The preferential treatment given to the consumer does not extend to contracts of carriage or to contracts for the supply of services where the services are to be supplied to the consumer exclusively in a country other than that of his habitual residence. While the first exclusion poses little difficulty, the exception relating to the provision of services has the potential to create some uncertainty for consumers and service providers who provide services electronically, such as web-hosting, data storage and mail handling services. It could be argued that a service provider who provides a data storage service via the Internet actually provides that service exclusively in the country where he, or more accurately his hardware, is based. The presence of that information on a consumer’s monitor does not necessarily mean that the service is being provided in the country in which the consumer has his habitual residence. The consumer ‘dials-up’ the

⁴⁸ Article 5(3).

service providers server and views his data from there, in much the same way as a telephone user would request information from an overseas operator or information service. It is submitted that such a narrow approach would be contrary to the intentions of the Convention. However, the approach adopted is a decision for the Member State courts.

5.3 Conclusion

The common law approaches to the proper law of the contract, although superseded by the Contracts (Applicable Law) Act and the Rome Convention, may nevertheless still play a role in the interpretation of certain key provisions. In particular the relevant factors considered when determining the country most closely connected with the contract.

The terminology in the Rome Convention is closely based on the Brussels Convention and hence contains many of the same ambiguous phrases responsible for its replacement. Unfortunately a replacement for the Rome Convention appears some way off.⁴⁹ Should a case arise, the courts would have no option but to apply the ambiguous terminology to the electronic environment.

The rules contained within the Rome Convention are rather complex and have the potential to create legal uncertainty when applied to electronic contracts. However, the dominating principle in the Convention is party autonomy and where cross border contracts are in use there will almost inevitably be a choice of law clause in the contract terms. The majority of traders entering contracts in the electronic environment have a choice of law clause in their website conditions of use which will, in the majority of situations, effectively dictate the substantive law applicable to their contract. However, there are two situations where the Convention in its present state may lead to uncertainty in its application to electronic contracts; the position where there is no effective choice of law and consumer contracts.

Where there is no effective choice of law the courts will look for the country of closest connection. The Convention contains some guidance to the assessment but it is submitted that this will often be of little help in relation to many electronic contracts entered into in the course of a party's trade or profession. The search for a 'principal

⁴⁹ On January 14, 2003 the European Commission adopted a Green Paper that launches a consultation on the revision of the Rome Convention on the law applicable to non-contractual obligations. See http://europa.eu.int/eur-lex/en/com/gpr/2002/com2002_0654en01.pdf.

place of business' or a place of business through which the characteristic performance of the contract is effected may produce unworkable or inappropriate results in the electronic environment. The only alternative in this situation will be to decide the country of closest connection on the basis of where one or other of the parties is resident.

As is the case with the Conventions and Regulation on jurisdiction, the consumer is afforded a protected position under the Rome Convention in relation to the mandatory rules applicable in his country of habitual residence and when no choice of law has been made. However, to benefit from these measures the consumer must enter the contract in specific circumstances. These circumstances equate to the criteria recently replaced in the new Regulation on jurisdiction because of the uncertainty surrounding their interpretation, particularly in relation to website activity and electronic contracts. Nevertheless, as was argued in relation to the rules on jurisdiction, the interpretation by the courts of the requirement that the contract be preceded by advertising equate to the directing or targeting of activities to the consumer's State and the enquiry of 'who invited whom to contract'. On this basis it is submitted that websites can be construed as advertising directed towards a consumer's State unless the supplier can demonstrate that he was not inviting business from consumers in that State but rather that the consumer took steps to pursue the supplier to enter the contract. It is clear that the taking of the 'necessary steps' to conclude the contract in the consumer's country can be satisfied by the taking of any action, such as the typing and order into a website. However, it is equally clear that this requirement may create a loophole whereby the consumer will lose the benefit of the mandatory rules of his habitual residence, if he takes the necessary steps whilst in a different country using a mobile piece of technology. It is submitted that this interpretation could lead to absurd results, but it is nevertheless a potential interpretation of the phrase.

The Rome Convention also contains a potentially problematic exclusion from the consumer protection measures. The exclusion of contracts for services supplied exclusively in a country other than the consumer's habitual residence has the potential to exclude services provided electronically. It could be argued that such services are actually provided in the country where the supplier has the technological means and the relevant material stored for the provision of that service to consumers, wherever they may be. If this argument is accepted the protection afforded to consumers may be significantly undermined in electronic contracts for these services.

The Rome Convention requires some amendment to enable it to accommodate electronic contracts and modern forms of communication in an effective way, particularly in the context of consumer contracts. However, it is submitted that the amendments must be carefully considered in the light of the objectives of the measure adopted to avoid creating further uncertainty for electronic contracts as has arguably occurred in relation to the rules on jurisdiction. This point will be returned to in the conclusion to this section.

Conclusion

As was stated at the beginning of this section, the two issues of jurisdiction and applicable law are of vital importance to electronic contracting.

For the business party legal clarity, certainty and consistency are needed when they are considering their business strategy, particularly when entering cross-border electronic contracts. Uncertainty as to their legal position and hence their potential liabilities may act as a deterrent to embracing electronic commerce. To benefit from the expanded market created by modern communications technologies suppliers need to be confident that they will not inadvertently find themselves the subject of legal action in a range of foreign jurisdictions because their website may be accessible there. Equally, they require a legal environment within which their customers feel confident to enter electronic contracts with them.

For the consumer, confidence fostered by the knowledge that their rights and interests will be protected when they enter an electronic contract is of paramount importance. This trust and confidence will only be developed if the legal rules on jurisdiction recognise the fact that, as a general rule, a consumer will not have either the resources or the know-how required to pursue a supplier in a different State. It is equally unlikely that a consumer will be aware of his rights under the laws of a different State and as such it is important that he is afforded the protection of the laws of his home country to which he is accustomed. Without these safeguards cross-border consumer contracts are likely to remain rare and electronic commerce within the internal market will suffer.

From the preceding discussion it is clear that although steps have been taken to harmonise the rules within the European Union and the European Economic Area, there are still significant areas of uncertainty in the application of the regulatory measures in relation to the electronic environment. It is also clear that certain key principles are inappropriate to be applied to electronic contracts because they are reliant on references to some physical presence; a presence that either does not exist, or if it does may be of little relevance to the parties and their transaction. Because of this lack of clarity and

legal certainty the needs of consumers and businesses wishing to enter electronic contracts are not being met by the relevant regulatory regimes. Unfortunately this remains the case even in the face of legislation specifically intended to recognise and accommodate new forms of communication and electronic contracts. A combination of ill-considered political lobbying and a lack of sufficiently detailed consideration of the electronic environment and electronic contracts has resulted in a Regulation which may not fulfil its declared objectives and will require interpretation by the ECJ if divergent application of its provisions is to be avoided.

If amendments to the Rome Convention follow the same course as the amendments to the rules on jurisdiction, a vital opportunity to codify and clarify the rules applicable to cross-border contracts will have been missed at a time when the creation of a clear and consistent legal framework for electronic contracts is necessary for the development of electronic commerce.

III

The Creation of Electronic Contracts

Introduction

In this section the creation of electronic contracts, fundamental to the development of electronic commerce, will be considered. A number of factors must be examined in order to assess whether their creation is permitted, facilitated or deterred by the existing legal principles.

A particular problem is created by one of the main characteristics of the electronic environment – its penchant for anonymity. Whilst the formal identification of the parties to a contract is a legal requirement in only a limited number of circumstances, the lack of a physical or even a visible presence in the electronic environment makes identification a particularly relevant issue. A lack of information about the other party in addition to uncertainty as to that party's identity can lead to a lack of confidence, making parties reluctant to contract in the electronic environment. The legislative response to this problem and the common law approach to identification in contract law will be considered.

If requirements of form create legal barriers or inconsistencies in the application of the law to electronic contracts the growth of electronic commerce will be hindered. This potential problem has been a core issue in the formulation of legislation targeting electronic commerce in the United Kingdom and the European Community. Arguably few 'barriers' are created by formal requirements in English law, but the potential barriers that do exist and the responses to those barriers must be considered.

The formation of contracts is the domain of the common law with its principles derived from centuries of considered analysis of the contractual relationship. There is an inherent flexibility in the common law which allows for the accommodation of new technology and changes in society. Unfortunately the corollary of this flexibility can be legal uncertainty, which may have a detrimental effect on electronic contracting because of the difficulty in predicting how existing principles will be applied to electronic contracts. Of particular importance in the electronic environment is the question of when and where a contract is actually formed, bringing into existence binding obligations and potential liabilities. With no personal contact between parties and the use of automated systems being common a 'new' set of circumstances will have to be

considered by the courts. To address this issue the common law rules on contractual offer and acceptance must be considered including the inevitable debate surrounding the postal rule.

Identification, Transparency, Trust and Confidence

In this chapter the increased significance of identification in the electronic environment is examined. The discussion proceeds to consider the potential responses to this need and the importance of the provision of information about contracting parties (transparency), in relation to the objective of promoting trust and confidence in entering electronic contracts.

The common law approach to mistaken identity is highlighted as a potential area of legal uncertainty which may have a significant role to play in electronic contracts because of the difficulties associated with identification in the electronic environment.

6.1 Identification in the Traditional Environment

Identification is rarely a key issue in everyday contracts. In the usual course of events the identification of the other party to a contract is only important to the extent that a seller can obtain payment.

However, the identification of the other party or parties to a contract may become crucial for a number of reasons. The first clear need arises in the event of a dispute because the obligations entered into are not performed, or performance is deficient in some way. Whether seeking payment for goods or services, or compensation for a faulty product, an action can only be taken if you can identify your contracting partner and provide sufficient evidence to show that they are the other party to the contract. A second situation whereby identification may become crucial arises when a party to the contract is under a legal obligation which necessitates the formal identification of their contracting partner. For example, where the supply of a product is restricted to individuals over a certain age, identification may be necessary to ensure that

products are not sold to people under that age.¹ Transactions for financial services also usually require strict identification procedures to comply with legislative requirements, particularly regulation relating to the prevention of money laundering.² Finally, a particular party may have been chosen as a contracting partner on the basis of his previous work or reputation, such as a well known brand name, and a level of trust and confidence in that supplier may already exist.

In modern society, with the present state of technology, one could be forgiven for imagining that, with a little precaution, establishing the identity of a contracting party should be relatively straightforward. However, with identity fraud being one of the fastest growing crimes in the UK this would not appear to be the case.³ The statistics reflect the fact that in the majority of everyday contracts the only steps necessary, and indeed taken, are those minimal elements required to ensure payment. With cash transactions there is usually no identification required at all. With credit or debit card transactions, ensuring that the card has enough credit available, has not been reported stolen, and that the individual presenting the card can reproduce a 'close enough' copy of the signature on the back of the card, will usually ensure payment.

6.2 Identification in the Electronic Environment

The situations identified in the context of traditional contracts whereby identification becomes important to the parties may equally occur where the contract is entered into electronically. However, in the electronic environment identification may be more problematic because the nature of the environment means that a contracting partner will not be physically present and even the limited benefit of seeing that individual signing a credit card receipt for example, is removed. The situation is further complicated by the fact that in the electronic environment, such as the Internet, an individual can be whatever and whoever they want to be, as Reed indicates a party can assume almost any persona he or she desires because,

“..a user’s digital identity has no necessary connection with his physical world identity.”⁴

¹ In addition, at common law a 'minor' (<18) is not bound by any contract which he makes whereas the other party will be bound, save for contracts for 'necessaries' and employment or analogous contracts. However, s.3 of the Minors Contracts Act 1987 gives the courts discretion to grant restitutionary relief.

² See the Proceeds Of Crime Act 2002 (c. 29), section 327 *et seq*.

³ The Times, 13th August 2001. See the discussion of *Shogun Finance Ltd v Hudson* below at 6.3.

⁴ Reed, C. *Internet Law: Text and Materials* (Butterworths: London, 2000) at p. 119.

The nature of the electronic environment also has the potential to increase the occurrence of identity fraud.⁵ When services are provided electronically and delivered in real-time the potential losses for a service provider are large, if he is duped by someone using another person's identity or a purely fictional one. Hence, sellers and suppliers engaged in electronic commerce generally charge the value of the goods or services, or at least authenticate the payment method, before 'despatch', be it electronic or physical.⁶ However, where two individuals enter contracts electronically or where a consumer is dealing with a supplier, they do not have this option.

Online service providers whose services include the provision of a 'virtual marketplace' for individual users are keen to highlight the difficulties associated with identification in the electronic environment to their users, as the eBay users agreement illustrates:

"3.3 Identity Verification. We use many techniques to verify the accuracy of the information our users provide us when they register on the Site. However, because user verification on the Internet is difficult, eBay cannot and does not confirm each user's purported identity. Thus, we have established a user-initiated feedback system to help you evaluate with whom you are dealing. We also encourage you to communicate directly with potential trading partners through the tools available on the Site. You may also wish to consider using a third party escrow service or services that provide additional user verification."⁷

The potential for innocently caused confusion is also increased in the electronic environment. For example, a consumer may mistakenly believe that the sender of a message or the proprietor of a website is a well known business and enter a contract under that mistaken belief. Whether this is due to some deliberate 'passing off' or is just a completely innocent case of mistaken identity this possibility has the potential to undermine confidence in electronic contracting and the development of electronic commerce.

⁵ See the comments made by the US Department of Justice at; <http://www.usdoj.gov/criminal/fraud/text/idtheft.html>.

⁶ At least on the first transaction with a new customer.

⁷ See <http://pages.ebay.com/help/policies/user-agreement.html>. With an escrow service a third party provides identity verification for users.

Where parties have an existing business relationship, or a history of transactions, there is less risk of identity fraud or confusion, but as electronic commerce develops the majority of electronic contracts are unlikely to be based upon an existing relationship. To this end, and to promote trust and confidence in the use of electronic commerce, a number of solutions have been considered. The first are practical or technological answers, such as the use of electronic signatures and biometric data. In addition to recognising the technical processes developed to address this issue legislators have also introduced a second approach intended to reduce the potential for confusion and uncertainty in the electronic environment: the introduction of statutory information requirements. It is hoped that by requiring business parties entering electronic contracts to provide detailed information about themselves and the contractual process, confidence will be increased in participation in electronic commerce activities.

6.2.1 Checking Identity in the Electronic Environment: Practical and Technical Approaches

In the physical world certain documents are deemed to be particularly authoritative for identification purposes: birth certificates, passports and driving licences for example.⁸ The elevated position that these documents command is attributable to the steps required to obtain the document and the identity checks made by the body issuing the document. Although in the traditional environment such formal means of identification are rarely necessary, in the electronic environment there may be an increased need for a greater level of identification because of the anonymous nature of that environment. Steps have been taken to create electronic forms of identification functionally equivalent to the physical world documents mentioned above. As with the physical world counterparts there are varying levels of 'reliability' associated with the methods adopted, but a common factor is the involvement of a third party. The various methods of checking identity in the electronic environment will now be considered.

6.2.1.1 Domain Name Registers and Internet Service Providers (ISP's)

When dealing with a supplier through a website the customer can make use of the domain name registry databases, such as the RIPE or NOMINET 'whois' directories,

⁸ Whether their position is justified is beyond the scope of this discussion, but it is submitted that it is difficult to sustain that any form of identification is conclusive, particularly if it does not bear an image of the individual.

to attempt to confirm the identity of the other party.⁹ However, the registry is only reliable if the registered domain name holder has given accurate information. The checks are only minimal and the information supplied limited, which makes this a form of identification of limited reliability. A party could also try to confirm an identity with the Internet Service Provider; however such service providers are subject to data protection requirements and usually have their own privacy policies which would prevent disclosure of relevant information.

6.2.1.2 Webcams and Video-Conferencing

With developments in technology it is possible to actually see the person you are contracting with using video conferencing or web-cams. At present the viability of such methods is restricted by the speed of communications, but for individually negotiated business contracts it is certainly a way forward. For years science fiction has pointed to the combination of a visual image and biometric data, such as a retina scan, to confirm identity. This approach is again reliant on a third party verifying the data collected. However, for regularly occurring electronic transactions this approach may well be considered unnecessary and in many situations would be completely impractical because suppliers will generally use automated ordering systems requiring little or no human interaction.¹⁰

6.2.1.3 Biometric Data

In this context the phrase 'biometric data' refers to "the emerging field of technology devoted to identification of individuals using biological traits, such as those based on retinal or iris scanning, fingerprints, or face recognition".¹¹ The use of biometric data to verify identification has been technologically possible for some time. However, the most reliable forms have not yet become readily available to the mass market at an affordable price.¹²

⁹ <http://www.ripe.net/perl/whois> ; <http://www.nic.uk/>.

¹⁰ This is after all one of the main benefits of electronic commerce.

¹¹ "BIOMETRICS: A Journal of the International Biometric Society." <http://stat.tamu.edu/Biometrics/>. See also <http://www.biometrics.org/>.

¹² See <http://www.biometrics.org/html/introduction.html>.

6.2.1.4 Security Certificates and Electronic Signatures

Security Certificates

'Security Certificates' are usually associated with websites and are issued by a trusted third party who will verify the information given by the website proprietor.¹³ To be issued with a certificate the website proprietor will usually be required to sign a code of practice, drafted by the certificate issuer. A member of a scheme will usually display the security certificate logo on his website and a user can 'click' on the logo to obtain details about the trader, the certification authority and any code of practice. The value to a potential customer of a security certificate as a verification of identity will depend on the trust and confidence the individual has in the certificate issuer. The well known consumer body 'Which' ran its 'Web Trader' service for a number of years and confidence in the Web Trader logo developed from the existing reputation of 'Which'. Other security certificate issuers have established a reputation in the electronic environment over a number of years, perhaps the most well known and trusted, being 'VeriSign'.¹⁴

Electronic Signatures and ID Certificates

Electronic signatures can take many forms, some of which may be very simple: the typing of one's name or initials at the end of a message; a simple scan of an individual's signature pasted into, or attached to, an electronic communication; an actual 'signature' imposed onto the document using a light pen or similar device. At the other end of the technological scale, the phrases 'digital signature' or 'advanced electronic signature' are often used to refer to electronic signatures based upon encryption and cryptographic techniques.

Electronic signatures can fulfil a number of roles, one of the main roles being to identify the party responsible for a communication. Because electronic signatures can take a number of forms their reliability as methods of identification will vary according to the method used to 'sign' a document. The most reliable forms of electronic signature are those based upon secure encryption technologies which use a third party to verify the identity of the signatory. The third party verification will usually take the form of an ID

¹³ For examples see <http://www.uk-shop-index.co.uk/security-certificates.html>.

¹⁴ <http://www.verisign.com>.

certificate which demonstrates that the third party has obtained formal identification from the certificate holder.¹⁵

In many ways electronic signatures differ from a 'traditional' signature, in that there is no clear link between the signature and the identity of the party signing. The signature may not be physically related to the object in the same way as its physical counterpart.¹⁶ However, the need to establish the identity of the party responsible for a communication in the electronic environment can be achieved successfully by the use of electronic signatures, and electronic signatures are perhaps the most reliable and readily available technology at present. However, the use of electronic signatures as a means of identification is heavily reliant on the role played by the third party, the certification authority. If electronic signatures are to be trusted as a means of identifying parties in the electronic environment those issuing certificates must maintain standards. The reliance placed upon certificates creates a need to regulate the activities of those issuing certificates and to fix them with liability, in appropriate circumstances, should the certificate be inaccurate resulting in loss. This need was recognised by the European Commission and was addressed by Directive 1999/93/EC of the European Parliament and of the Council on a Community framework for electronic signatures,¹⁷ the relevant elements of which were enacted in the Electronic Communications Act 2000.

6.2.1.5 Certification Service Providers – Regulation and Liability

Regulation of Service Providers

The registration and approval of cryptography service providers is dealt with by sections 1 to 6 of the Act. However, as a result of pressure from within the industry and bodies promoting self-regulation, this part of the Act has not come into force and will not do so until an appropriate order is agreed by Parliament. If the industry-led scheme is successful then the provision will be repealed after the expiration of five years.¹⁸ The

¹⁵ The checks made to verify identification will vary from one certification authority to another. Common requirements however, include; passports, birth certificates, driving licenses and certificates of incorporation for limited companies.

¹⁶ Angel, J. "Why use Digital Signatures for Electronic Commerce?" [1999](2) *The Journal of Information, Law and Technology (JILT)* <http://www.law.warwick.ac.uk/jilt/99-2/angel.html> at p. 6. The issue of whether electronic signatures should be treated as 'equivalent to' their more traditional counterparts is considered below.

¹⁷ OJ L13, (19.1.2000) p. 12.

¹⁸ Section 16(4).

Alliance for Electronic Business (AEB)¹⁹ is responsible for the industry-led 'tScheme'.²⁰ The scheme is intended to promote best practice and to be registered under the scheme and awarded the 'tScheme mark' service providers must be thoroughly evaluated against rigorous criteria by independent experts; agree to keep to those criteria; subscribe to the schemes Code of Conduct;²¹ and act promptly and fairly to remedy faults.

Liability of certification service providers.

The provision of information, in the form of ID certificates, intended to be relied upon by others, clearly creates potential liabilities for those issuing the certificates.

Regulation 4 of the Electronic Signatures Regulations 2002²² imposes liability on certification service providers when a person reasonably relies on a certificate, issued or guaranteed by, the service provider and suffers loss. There is no need to prove negligence on behalf of the service provider, but if the service provider can prove that he was not negligent he will not be liable.

The regulation of those providing certification services, together with the fixing of liability on service providers in appropriate circumstances, should provide a high level of reliability in relation to identifying the sender of a communication by the use of an electronic signature based on cryptographic techniques.

Even though reliable forms of identification exist in the physical world and the electronic environment, for the majority of transactions identification verification is not required and technologies such as electronic signatures are not employed. However, business parties entering high value or industrially sensitive contracts may require strong identification verification. Likewise banks and other financial service providers may be required by law to establish identity with strong verification and to this end, they generally remain in the 'paper age', requiring new customers to show themselves physically in a branch with the types of paper identification document discussed above.²³

¹⁹ An umbrella organisation encompassing the Computing Services and Software Association (CSSA); the Confederation of British Industry (CBI); the Direct Marketing Association (DMA); e-centre UK ; and the Federation of the Electronics Industry (FEI).

²⁰ www.tscheme.com. To-date the accredited and approved providers include by British Telecom 'OnSite' <http://www.btignite.com>; the Royal Bank of Scotland, 'TrustAssured' <http://www.trustassured.co.uk/>; and one by trustis, 'Certificate Factory' <http://www.trustis.com/>.

²¹ Although to call the list of good practice a code of conduct is a little generous. See <http://www.tscheme.com/codeconduct.html>.

²² Statutory Instrument 2002 No. 318.

²³ There are, of course, sound policy arguments for this approach, relating to money-laundering and organised crime. Further discussion of this issue is beyond this work, but see HM Treasury, "The UK's Anti-Money Laundering Legislation and the Data Protection Act 1998. Guidance Notes For The Financial Sector." April 2002 at http://www.hm-treasury.gov.uk/media/9A770/money_laundering.pdf.

It is in these situations that digital signatures and certification authorities may have a key role to play.

The use of electronic signatures and other technological methods of identification may not always be practical or appropriate. Even where they are, the promotion of transparency in dealings in the electronic environment may also help avoid uncertainty as to the identity of a party responsible for an electronic communication or website. The statutory information requirements embodied in a number of recent pieces of legislation may go some way to re-enforcing the identity of business parties in the electronic environment. The relevant provisions will now be considered.

6.2.2 Statutory Information Requirements

6.2.2.1 The Distance Selling Regulations

On the 31st October 2000 the Consumer Protection (Distance Selling) Regulations 2000 came into force.²⁴ The Regulations were introduced to implement Directive 97/7/EC of the European Parliament and the Council of 20 May 1997 ‘on the protection of consumers in relation to distance contracts’.²⁵ Although dealing with distance selling to consumers in general,²⁶ the Regulations clearly have implications for parties involved in electronic commerce. The Regulations apply to “any contract concerning goods or services concluded between a supplier and a consumer under an organised distance sales or service provision scheme run by the supplier who, for the purpose of the contract, makes exclusive use of one or more means of distance communication up to and including the moment at which the contract is concluded”.²⁷ “Distance communication” is defined as “any means which, without the simultaneous physical presence of the supplier and the consumer, may be used for the conclusion of a contract between those parties”.²⁸ The Regulations explicitly state that electronic mail falls within the definition,²⁹ but other means of electronic communication, such as web-

²⁴ Statutory Instrument 2000 No. 2334.

²⁵ O.J. L144,19 (4.6.97).

²⁶ “Consumers” are defined in regulation 3 as, “any natural person who, in contracts to which these Regulations apply, is acting for purposes which are outside his business”.

²⁷ Regulation 3. Certain contracts are excluded by Regulation 5. These include contracts for the sale or other disposition of an interest in land except for a rental agreement; for the construction of a building where the contract also provides for a sale or other disposition of an interest in land on which the building is constructed, except for a rental agreement; relating to financial services; concluded by means of an automated vending machine or automated commercial premises; concluded with a telecommunications operator through the use of a public pay-phone; and contracts concluded at an auction.

²⁸ *Ibid.*

²⁹ Schedule 1 para. 11.

based communications, are not mentioned. Nevertheless, it is clear that the definition of distance communication in the body of the directive is wide enough to encompass most electronic forms of communication in use at present. Support for this suggestion can also be found in the preamble to the Electronic Commerce Directive.³⁰

“... amongst others Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts and Directive 97/7EC of the European Parliament and of the Council of 20 May 1997 on the protection of consumers in respect of distance contracts form a vital element for protecting consumers in contractual matters; *those Directives apply in their entirety to Information Society Services.*”³¹

The Regulations require that in good time prior to the conclusion of the contract the supplier shall provide information to the consumer including the identity of the supplier and, where the contract requires payment in advance, the supplier’s address.³² In addition the supplier must provide this information and the geographical address of the place of business to which the consumer may address any complaints, in writing, or in another durable medium which is available and accessible to the consumer. This must be provided ‘in good time’, or at the latest at the time of delivery of goods, or during the performance of services.³³ Failure to comply with the Regulations may result in an enforcement body,³⁴ taking proceedings to obtain an injunction against a business to prevent further breaches.³⁵

The overall objective of these information requirements is to promote transparency in distance transactions and a corresponding level of trust and confidence by ensuring that the consumer is not provided with less information simply because he is using a distance means of communication. The requirements in the Regulations provide the consumer with crucial information as to the identity of the business party he is dealing with.³⁶

³⁰ Directive 2000/31/EC of The European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market (Directive on Electronic Commerce) OJ L178/1. Recital 11.

³¹ Emphasis added.

³² Regulation 7(1)(a)(i).

³³ Regulation 8.

³⁴ The Director General of Fair Trading, Trading Standards Departments in Great Britain and the Department of Enterprise, Trade and Investment in Northern Ireland.

³⁵ Regulation 27.

³⁶ The information is however, only as reliable as the party providing the information and where there is fraudulent activity the requirements will do little to help the consumer identify the other party.

6.2.2.2 The Electronic Commerce Regulations

The Electronic Commerce (EC Directive) Regulations 2002³⁷ came into force on 21st August 2002³⁸ and they provide the long awaited implementation of certain key elements of the 'Electronic Commerce Directive'.³⁹ The Regulations contain more stringent information requirements relating to the identity of a party and his place of business. A person providing an 'information society service' must make available to the recipient of the service and any relevant enforcement authority, in a form and manner which is easily, directly and permanently accessible, the following information -

- (a) the name of the service provider;
- (b) the geographic address at which the service provider is established;
- (c) the details of the service provider, including his electronic mail address, which make it possible to contact him rapidly and communicate with him in a direct and effective manner;
- (d) where the service provider is registered in a trade or similar register available to the public, details of the register in which the service provider is entered and his registration number, or equivalent means of identification in that register;
- (e) where the provision of the service is subject to an authorisation scheme, the particulars of the relevant supervisory authority.⁴⁰

Failure to provide this information can result in a 'qualified entity'⁴¹ bringing proceedings to obtain a "Stop Now Order",⁴² requiring the supplier to cease his infringing behaviour and comply with the Regulation. The Regulations promote 'good practice' and the provision of information about the identity of the service provider should give customers some confidence that they are dealing with the party they believe they are.

It is conceded, however, that although technological methods exist to prove identity and that legislation requires that certain information about a party's identity be provided to a consumer, situations will inevitably arise in the electronic environment where a party has been duped into parting with goods by fraud. Where this has occurred

³⁷ Statutory Instrument 2002 No. 2013.

³⁸ Regulation 16 however, came into force on 23rd October 2002.

³⁹ *Op cit* fn 30.

⁴⁰ Regulation 6.

⁴¹ See Regulations 2 of the The Stop Now Orders (E.C. Directive) Regulations 2001, Statutory Instrument 2001 No. 1422.

⁴² The Stop Now Orders (E.C. Directive) Regulations 2001, Statutory Instrument 2001 No. 1422, amending the Fair Trading Act 1973.

the courts will have to deal with the aftermath of the fraudulent behaviour and may have to resort to the common law approach to mistaken identity.

6.3 Mistaken Identity in Contract Law: A Common Law ‘Gordian Knot’?⁴³

A not unlikely scenario could be as follows:

An individual sees an entry on eBay of particular interest. He contacts the seller and negotiates a price for the purchase of the goods. The contract is concluded and the goods are delivered to his home. Unknown to the buyer, the seller is actually a confidence trickster who has fraudulently obtained the goods from the original owner. The confidence trickster ‘disappears’ and the original owner begins proceedings against the purchaser for the conversion of the goods.

The court’s decision will depend upon whether the confidence trickster had ‘title’ or ownership of the goods to pass on to the innocent buyer. The title would be voidable because of the fraud but nevertheless the buyer would have ownership transferred to him under the contract. Section 23 of the Sale of Goods Act 1979 states:

“When the seller of goods has a voidable title to them, but his title has not been avoided at the time of the sale, the buyer acquires a good title to the goods, provided he buys them in good faith and without notice of the seller’s defect of title.”

The original owner of the goods will argue that the confidence trickster did not have title to the goods because he made a mistake as to identity and no contract was ever formed.

Unfortunately the principles applied by the courts to disputes of this nature provide little certainty in the traditional environment and as such are unlikely to provide legal certainty when their application to the electronic environment is considered. The common law approach to mistaken identity will now be considered.

⁴³ Lord Justice Sedley in *Shogun Finance Ltd v Hudson* [2001] EWCA Civ 100; [2002] Q.B. 834, at 847.

6.3.1 The Case Law

In the courts of England and Wales there is a line of case law associated with mistaken identity or ‘identity fraud’ with which the judiciary themselves have expressed their concern and unhappiness.⁴⁴ Most recently the situation has led the Court of Appeal to declare that the law is in such a ‘sorry state’ that statutory intervention is urgently required.⁴⁵

Atiyah associates the current difficulties with principles developed in the nineteenth century and in particular two leading cases from that period “which have caused trouble ever since”:⁴⁶ *Cundy v Lindsay*⁴⁷ and *Kings Norton Metal Co. Ltd v Edridge, Merrett & Co.*⁴⁸ It is perhaps rather the later application, or misapplication, of the principles decided in those cases which has resulted in the present state of the law.

The case law relating to this issue is plagued with fine distinctions. In *Shogun Finance Ltd v Hudson*⁴⁹ Sedley LJ expressed his frustration with the current situation;

“the illogical and sometimes barely perceptible distinctions made in earlier decisions, some of them representing an unarticulated judicial policy on the incidence of loss as between innocent parties, continue to represent the law.”⁵⁰

His Lordship concludes that only Parliament or the House of Lords can remedy the present situation. However, Atiyah explains that;

“... fine distinctions do not necessarily mean that the distinctions are inherently unsound. It is the business of the law to draw distinctions and fine distinctions are often a necessary consequence.”⁵¹

Nevertheless, he continues to comment that in the cases associated with this issue the distinctions drawn by the courts are ‘elusive and theoretical’ and rather abstract, not being based upon real social or commercial distinctions.⁵²

⁴⁴ *Shogun Finance Ltd v Hudson* [2001] EWCA Civ 1000; [2002] 4 All E.R. 572; [2002] Q.B. 834 at 842, Sedley L.J.

⁴⁵ *Ibid* per Brooke L.J. at 855.

⁴⁶ Atiyah, P.S, *et al The Sale of Goods* 10th ed. (Longman: London, 2000) p. 41-42.

⁴⁷ (1878) 3 App Cas 459

⁴⁸ (1897) 14 TLR 98. The cases are both discussed below.

⁴⁹ [2001] EWCA Civ 100, (2001); [2002] Q.B. 834, at 847.

⁵⁰ *Op cit* fn 44.

⁵¹ *Op cit* fn 46 at p. 3.

6.3.2.1 The Identity/Attributes Distinction

The key distinction made by the courts is between a mistake as to the identity of a contracting party and a mistake as to that party's attributes, in particular his creditworthiness. A genuine mistake as to the identity of the other party will allow the original seller to succeed but a mistake only as to the attributes of that party, such as his creditworthiness, will not.

In *Cundy v Lindsay*⁵³ the House of Lords felt that when a firm had been duped by a rogue called Blenkarn into thinking he was in fact a firm known to the plaintiffs, Blenkiron & Co, then the contract between the plaintiff and the rogue had never existed and hence the rogue could not obtain title to the goods. This was the equivalent to a finding that the alleged contract was void due to the mistake made by the plaintiff. The sellers had never intended to accept the offer made by the rogue, but rather an offer made by a third party, Blenkiron & Co. In this way no objective agreement had been reached and hence no contract. In *Kings Norton Metal Co. Ltd v Edridge, Merrett & Co*⁵⁴ the Court of Appeal distinguished *Cundy* on the grounds that in the case before them there was no identifiable third party in existence. All that had been mistaken was the creditworthiness of the writer of a letter, the rogue. As indicated above this is a fine distinction to draw, so much so that in *Lewis v Averay*⁵⁵ Lord Denning MR described it as a "distinction without a difference".⁵⁶ The only real distinction to be made is that in *Kings Norton Metal* there was no 'other identity' with which to be mistaken.

6.3.1.2 Face-to-Face Dealings

The predominance of authority would appear to further indicate that when the two parties are in one another's presence, or 'face to face' then a claim of mistaken identity will be difficult to sustain. In *Phillips v Brooks Ltd*⁵⁷ the plaintiff's claim was based on the argument that he had never intended to contract with the rogue (North) in his shop, but rather with an existing third party (Sir George Bullough). Here there are obvious similarities with *Cundy v Lindsey*, the main difference being that the two parties in this case were in one another's presence. Horridge J felt that this was significant and that where a party is identified by 'sight and hearing', the seller contracted with the person he

⁵² Atiyah continues to suggest that the unarticulated reasons behind some of the decisions, in particular whether a party could be considered 'at fault', may have had a significant impact upon the judgments.

⁵³ (1878) 3 App Cas 459.

⁵⁴ (1897) 14 TLR 98.

⁵⁵ [1972] 1 Q.B. 198.

⁵⁶ *Ibid* at 206. Indeed, what is a persons identity but a sum of his attributes?

⁵⁷ [1919] 2 KB 243.

could 'see and hear'. The property passed even though fraud or deceit may have induced the vendor to sell.⁵⁸ However, in *Ingram v Little*⁵⁹ the Court of Appeal (Devlin LJ dissenting) felt that the true test was to identify to whom the offer was addressed, for only he could accept that offer. In *Ingram*, when the plaintiffs made their offer to sell the car in return for a cheque rather than cash, the promise was made solely to the genuine Mr Hutchinson, the owner of the cheque book. This was a fact known to the rogue who could therefore not accept the offer and thus, there could be no contract.⁶⁰ The identity of the other party had become *crucially important* to the sellers.

In a later case *Lewis v Averay*⁶¹ the Court of Appeal was faced with a situation almost identical to that before the court in *Ingram v Little*. However, the court doubted and declined to follow the decision in *Ingram v Little*. Lord Denning MR felt that the two preceding cases, *Phillips v Brooks* and *Ingram v Little*, could not be reconciled and were indistinguishable on the facts. He expressed his support for the dissenting judgment of Lord Devlin in *Ingram* and concluded that in the case before him, the plaintiff, Mr Lewis, made a contract with the person in front of him, the rogue, and therefore that the property in the goods had passed to Mr Averay. The rest of the court agreed with his decision although their criticism of *Ingram v Little* was a little less robust. The court made it clear that the judgment in *Phillips v Brooks* was an accurate statement of the law and had been so for some fifty years. It is interesting to note that the House of Lords judgment in *Cundy v Lindsay* was briefly referred to in the arguments before the court, but not mentioned in the judgment.⁶²

This vexed issue was revisited recently by the Court of Appeal in *Shogun Finance Ltd v Hudson*.⁶³ Mr Hudson had purchased a vehicle from an individual who turned out to be a 'rogue'. The rogue had entered into a hire-purchase agreement relating to the vehicle through a dealer using a stolen or unlawfully obtained driving licence and had forged the signature from the licence on the agreement. He had subsequently sold it to Mr Hudson, who had purchased it in good faith. The credit company used by the dealer, Shogun Finance, sought to recover the vehicle. They succeeded at first instance and Mr Hudson

⁵⁸ *Ibid* at p 247 referring to *Edmonds v. Merchants' Despatch Transportation Co* (1883) 135 Mass. 283.

⁵⁹ [1961] 1 QB 31.

⁶⁰ *Ibid* at p 49 per Sellers L.J. supporting the views of the judge in the court below.

⁶¹ [1972] 1 QB 198

⁶² One could be forgiven for inferring that the Court accepted counsel's argument that *Cundy v Lindsey* was a case of offer and acceptance and not one relevant to the law on 'mistake'. However, it is clear that a mistake of this nature goes to the very root of agreement i.e. the offer and acceptance. It is the effect of the mistaken identity upon the offer and acceptance which renders the contract void.

⁶³ [2001] EWCA Civ 100, (2001); [2002] Q.B. 834.

appealed. The issue before the court was whether the rogue was the “debtor” under the “hire purchase agreement” for the purposes of the Hire Purchase Act 1964 s. 27. If he was, then by virtue of section 27(2) the appellant Mr Hudson, being a “private purchaser . . . in good faith” would obtain title to the vehicle. Key to this question was whether the finance company had entered a contract with the ‘rogue’.

The appellant argued that the contract with the finance company had been entered into via an agent, the garage owner, and was therefore made face-to-face. As is discussed above, if this point were accepted by the court then on the basis of the previous decisions in *Phillips v Brooks* and *Lewis v Averay*, it would be difficult for the finance company to succeed in claiming that they had not contracted with the rogue in a face to face situation.

In contrast the respondent finance company argued that the garage owner was not their agent and that the transaction was not face to face, but rather at a distance and therefore the principle relating to face to face dealings should not apply. The case was of the nature decided in the cases of *Cundy v Lindsay* and *Kings Norton Metal* and therefore, the judgments in those cases should apply. In addition the respondents argued that the Court of Appeal decision in *Hector v Lyons*⁶⁴ decided that the principles applicable to ‘unilateral mistake’, where the parties were in the presence of each other (i.e. face-to-face dealings *inter praesentes*), should not apply to ‘written contracts’.⁶⁵

It is this latter argument which found favour with the majority in the Court (Dyson LJ and Brooke LJ) in *Shogun Finance Ltd v Hudson*. The Court felt bound by the decision in *Hector v Lyons* and therefore, as the ‘rogue’ did not feature in the hire-purchase agreement he was never party to it, and hence not ‘the debtor’ for the purpose of section 27. Brooke LJ stated that

“. . . the hire-purchase agreement, if it was made between anyone, was made between the claimants and Durlabh Patel of 45 Mayflower Road, Leicester. The claimants did not make this agreement with anyone else. Durlabh Patel is a real person who lives at 45 Mayflower Road, Leicester”⁶⁶

On this basis he distinguished the present case from *Kings Norton Metal*. Dyson LJ went on to consider the position if the principle in *Hector v Lyons* did not apply, concluding that

⁶⁴ [1988] 58 P. & C.R. 156, The Times, December 19, 1988.

⁶⁵ *Ibid.*

⁶⁶ [2002] Q.B. 834 at p 855.

there was insufficient evidence to give rise to any relationship of agency between the finance company and the car dealer and therefore that the case was akin to *Cindy v Lindsay*. In this situation His Lordship was satisfied that the identity of the customer, a Mr Patel who did exist, was of fundamental importance to the respondents and therefore the 'contract' between themselves and the rogue was void.⁶⁷

Sedley LJ delivered a strong dissenting judgment. He felt that if the decision in *Hector v Lyons* was not to conflict with judgments in *Cindy v Lindsay* and *Kings Norton Metal* it had to be read in the context of its own facts, a case concerning an individual who had not been named in a written contract, seeking to enforce that contract.⁶⁸ However, in the case before him he felt that *Hector v Lyons* was distinguishable on its facts and proceeded to consider the law relating to unilateral mistake. His Lordship acknowledged that he was bound by precedent, in particular *Cindy v Lindsay*, but continued that he could distinguish *Cindy* on the grounds that the car dealer was acting as an agent of the finance company albeit in the very limited capacity envisaged by Lord Morris of Borth-y-Gest in *Brarwhite v Worcester Works Finance Ltd* when he pointed out that a "dealer may for some ad hoc purpose be the agent of a finance company".⁶⁹ To this extent although the facts did not support the argument that the car dealer was the finance company's agent for the purpose of making the hire purchase agreement, he was their agent for certain specific purposes connected with that agreement. His Lordship proceeded to explain:

"One such purpose was to ascertain the identity of the hirer; another was to convey by fax the proffered proof of his identity, the driving licence; a third was to submit by fax the draft agreement signed by the hirer. These were the very elements which, had they been carried out in the claimants' offices, would have amounted to face to face dealing with the rogue."⁷⁰

This analysis led him to consider the principles applicable to unilateral mistake in face to face dealings and on this basis he concluded:

⁶⁷ However, the rationale behind this conclusion is, at the very least, open to criticism. Dyson LJ felt that as the identification and location of the hirer was essential for the finance company to be able to serve a notice of default under the Consumer Credit Act 1974, the identity of the hirer was to be *regarded* as being of fundamental importance to the respondent. This should not of itself, be sufficient to support an argument that the identity rather than the creditworthiness of the other party was crucial to the respondent. Surely this adjudication should be made on the facts of the particular case, as indicated in the earlier caselaw.

⁶⁸ *Op cit* fn 44.

⁶⁹ [1969] 1 AC 552, at 573.

⁷⁰ *Op cit* fn 44 at p. 844.

“I would hold that the claimant finance company, using the dealer as its agent, had in law contracted face to face with a fraudsman in circumstances insufficient to rebut the presumption that it was with him, and not with the person he claimed to be, that they were contracting.”⁷¹

All members of the court voiced their disquiet with the state of the law applicable to cases of this kind commenting that it was ‘remarkable’ that the law governing the consequences of a common fraud of this nature was ‘still in doubt’.⁷²

6.3.2 Alternative approaches?

In light of this criticism it is important to consider the comments of the Law Reform Committee in their 12th Report: *Transfer of Title to Chattels* in 1966.⁷³ It is also necessary to consider whether any of the alternative options discussed in that report could form the basis of a way forward for the House of Lords or Parliament. The options suggested were, to allow for the apportionment of loss by the courts on the basis of culpability, or, the treating of contracts as voidable rather than void in situations of mistaken identity, to provide some protection for innocent third parties.

The suggestion that the courts should be given the power to apportion the loss between the two innocent parties has, not surprisingly, received support from the judiciary. In *Ingram v Little*, Lord Devlin proffered the apportionment of loss between the parties on the basis of culpability:

“... the loss should be divided between [the parties] in such proportion as is just in all the circumstances. If it be pure misfortune, the loss should be borne equally; if the fault or imprudence of either party has caused or contributed to the loss, it should be borne by that party in the whole or in the greater part.”⁷⁴

In adopting this solution his Lordship indicated that he was suggesting nothing novel and merely satisfying the “true spirit of the common law” by “doing practical justice”.⁷⁵

⁷¹ *Ibid.*

⁷² *Ibid* at p 836

⁷³ Law Reform Committee, 12th Report: *Transfer of Title to Chattels* (Cmnd. 2958, 1966).

⁷⁴ [1961] 1 QB 31, 73-74.

⁷⁵ *Ibid.* He referred to the Law Reform Acts of 1935, 1943 and 1945 as examples of “a modern inclination towards a decision based on a just apportionment rather than one given in black or in white according to the logic of the law.” At p. 842.

There is a distinct practical logic in suggesting that sellers or finance companies take reasonable steps to confirm the identity of the buyer in the modern world with the technology available. To have the steps actually taken figure in any assessment of where the loss should lie would *prima facie* appear to be just. This approach would also have the advantage of being a question of fact in each case, an adjudication which is transparent based upon a distinction between sound commercial practice and less responsible behaviour.⁷⁶ As Dr Brian Jack states:

“Ultimately the question of the blameworthiness of each party, in allowing themselves to be drawn into a contract with the rogue, will be a question of fact in each case. It would therefore appear more satisfactory for courts to be given statutory powers to assess the facts and to apportion loss between the parties in accordance with their culpability in causing the loss.”⁷⁷

At the very least it is inequitable to allow a party to succeed in avoiding a contract on the basis of mistaken identity if that party has not taken what would appear to be reasonable steps in the circumstances to confirm the other party's identity.

However, in 1966 the Law Reform Committee rejected the idea of equitably distributing the loss because “judicial power to apportion loss in this way would introduce too much uncertainty into the law.”⁷⁸ Even without considering the present level of uncertainty in the law it is submitted that any uncertainty created by the power to apportion loss would at least be transparent, being based upon questions of fact and would certainly be more palatable than the present position with its inherent potential for injustice.

After their dismissal of the idea of empowering the judiciary to apportion loss the Law Reform Committee concluded that the best way forward would be to treat cases of mistaken identity as *voidable* so far as third parties are concerned, rather than *void*.⁷⁹ In this way title could pass to the third party at a point prior to the original owner taking steps to avoid the contract. However, it has been commented that his approach would

⁷⁶ It could be suggested that this is why the finance company in *Hudson* accepted a faxed copy of a driving licence and a signature on a credit agreement to confirm that Mr Patel was indeed entering the agreement. As a method of confirming identity these steps are of minimal reliability, but as the finance company felt assured that they could recover the vehicle in the event of fraud that this approach was adequate. With identity fraud on the increase this approach must be considered as socially irresponsible.

⁷⁷ Jack, B. “Mistaken identity in contract law: a re-examination.” [2001] *Nott. L.J.* 10(2), 57-63 at p 63.

⁷⁸ *Op cit* fn 73, at para 9.

⁷⁹ *Ibid* at para 15.

nevertheless be rather arbitrary, because the position of the innocent third party would depend upon the speed at which the original seller took steps to avoid the contract.⁸⁰ This may well be one of the factors why the report was not acted upon.

6.3.3 Mistaken Identity and Electronic Contracts

Regardless of criticisms and suggested alternative approaches, if courts are faced with disputes of the nature identified in the scenario above, the principles discussed will bind until the House of Lords or Parliament decide otherwise.

Electronic contracts are generally concluded at a distance and without the parties to the contract being simultaneously present. It follows that in the majority of situations a contracting party is not identified by 'sight and hearing' but by the information he provides in his message or in an online form. This analysis highlights two points relevant to a claim of mistaken identity. First, that the contracts are not usually concluded face to face and second that the contracts are usually reduced to writing.⁸¹ In light of the case law discussed above both of these factors would indicate that the principle applied in *Candy v Lindsey* to non-face-to-face situations would apply. Therefore, if a party could show that he was duped into thinking that he was contracting with a third party, who existed at the time, he could succeed in a claim to recover the goods he parted with. This approach could have significant implications for those entering electronic contracts because, for the purchaser, there is a risk that an unknown third party (the original seller) could make a successful claim against goods purchased in good faith for value. At present the law places a significant burden on the buyer to ensure that the person selling the goods is the bona fide owner of the goods and can pass title to him.⁸²

With the scale of identity fraud at present this situation is cause for concern and on a wider perspective it does little to persuade vendors to take steps, in identifying the buyer, that would contribute to reducing fraud and the associated losses. Statistics show that the fear of fraud is one of the factors cited as deterring the use of electronic commerce. Any policy intended to promote legal certainty and confidence in electronic contracting must surely take this problematic doctrine into account.

⁸⁰ Atiyah, P.S, *et al The Sale of Goods* 10th ed. (Longman: London, 2000) p.44; *Op cit* fn 77, Jack at 62.

⁸¹ Or at least an electronic form of writing. See chapter 7 for a discussion of electronic communications and 'writing'.

⁸² However, the significance of the issue may be reduced in the electronic environment where 'intangible' products – which are probably not capable of being classified as goods, are an increasingly common subject matter for electronic contracts. See chapter 3 above and 13 below for a discussion of this issue.

6.4 Conclusion

In situations where formal identification is a contractual requirement, in the physical world the combination of particular documentation and a physical presence of a party can provide a high level of reliability in identification. In the electronic environment technology has provided electronic signatures and related certificates and in the future may provide accessible biometric identification to fulfil this role. These methods can be considered functionally equivalent to their real world counterparts. Unfortunately, having to take such steps to identify the other party with a degree of certainty does require additional steps in the contracting process, making it more cumbersome, time consuming and therefore expensive for the supplier and the customer.

In the electronic environment, distance, anonymity, automation and a lack of face to face contact create the potential for increased fraudulent activity. Steps have been taken to protect consumers and most credit card companies emphasise that they 'protect' their customers against online fraud. By virtue of regulation 21 of the Distance Selling Regulations card issuers must, where a consumer's payment card⁸³ is used fraudulently in connection with a distance contract, allow the consumer to cancel the payment and where the payment has already been made, provide a re-credit or refund all sums paid. The card issuer will no doubt pass on any potential losses to the supplier and it is submitted that this may promote an increased desire to confirm identification in electronic contracts.

It is clear that two issues need to be addressed: the fraudulent activity and the fear of fraud expressed by consumers and businesses alike. To an extent the fraudulent activity can be addressed by the use of technology and the promotion of good practice by suppliers. The majority of 'responsible' suppliers have taken steps to 'get to know' their customers, particularly first time customers, by confirming details and checking delivery address details with payment card issuers details.⁸⁴ To address the fears associated with fraud and the electronic environment it is important to provide information about the technology available. It is equally important for contracting parties to provide information about themselves to promote the development of trust and confidence.

For vendors and service providers the primary concern is the obtaining of sufficient information to obtain payment. While this approach is not morally

⁸³ Which includes debit, credit or store cards.

⁸⁴ See Thorntons < <http://www.thorntons.co.uk/>>, Interflora < <http://www.interflora.co.uk/>> and Amazon < <http://www.amazon.co.uk/>> sites.

reprehensible (it does of course reduce costs because it is quick and convenient), cases like *Shogun Finance Ltd v Hudson* do indicate that there is a serious question to be addressed in relation to which party should bear the responsibility for losses due to identity fraud.

Where the identification of a party or authentication of particular information is considered important, or the contract is of particular significance, the law has previously imposed 'formal requirements' or 'requirements of form' to be fulfilled before the contract or communication to be valid. In the next chapter, those 'requirements of form' will be considered. The discussion will also consider whether the role of formal requirements may be of increasing importance in the electronic environment.

Formal Requirements

In the previous chapter the increased significance of identification in contractual relationships created in the electronic environment was highlighted and the practical and technological solutions to the issue were considered. The importance of detailed information about the identity of the contracting parties, particularly in contracts between businesses and consumers, was illustrated by reference to legislative developments applicable to electronic contracts. The unsatisfactory state of the law in relation to identity fraud was demonstrated by an examination of the common law approach to mistaken identity in contracts.

In this chapter formal requirements in the contractual process and their implications for electronic contracting will be considered. The issue has led to academic comment¹ and even a report containing advice for government from the Law Commission, entitled “Electronic Commerce: Formal Requirements in Commercial Transactions”.² Existing formal requirements, found in numerous legislative provisions and those applicable to certain ‘types’ of contract, have been considered as potential legal barriers to the use of electronic contracts. Their removal is seen as a key requirement in order to facilitate the use of electronic contracts and to promote the development of electronic commerce. The issues surrounding formal requirements and their perception as ‘barriers to electronic commerce’ will be examined with the relevant legislative provisions introduced to address the issue.

The discussion of ‘traditional’ formal requirements is followed by a consideration of formal requirements transferred to, or created expressly for, the electronic environment. Certain formal requirements are justifiable due to strong policy considerations and functionally equivalent requirements may be necessary for contracts entered into in the electronic environment. There may equally be justification for the introduction of formal requirements specifically intended for application to electronic

¹ See for example; Davies, LJ, *A Model for Internet Regulation*, 1998, available at <http://www.scl.org>.

² Law Commission, “Electronic Commerce: Formal Requirements in Commercial Transactions” 3rd December 2001, available at <http://www.lawcom.gov.uk>.

contracts because of the nature of the electronic environment. The problems associated with identification, discussed in the previous chapter, may be seen as one such justification.

The inappropriate introduction of new formal requirements applicable to electronic contracts is also considered. The regulation of electronic contracts may in some situations inadvertently create new electronic requirements of form, where no formal requirement exists for their non-electronic counterparts. As a consequence requirements imposed upon electronic contracts may be seen as more extensive, creating further barriers to their use. These 'e-formalities' and their potential effects on electronic contracting are examined.

7.1 The Role of Formal Requirements

As a general rule, in English law, contracts do not have to be in writing, signed, or follow a particular form to be effective. However, with certain contracts relating to particular subject matter the law, for a variety of reasons, prescribes certain requirements of form such as writing, signature, original documentation and so on. For example, section 2(1) of the Law of Property (Miscellaneous Provisions) Act 1989 provides that contracts for the sale or other disposition of an interest in land can only be made in writing.

Fuller³ suggests a number of reasons for the certain formal requirements in relation to contractual obligations:

1. to promote certainty by requiring clear evidence of the terms;
2. to encourage the parties to give full consideration to the legal obligations being undertaken; and
3. to provide protection to the person in the weaker bargaining position.⁴

In addition to providing certainty, encouraging consideration and providing protection for weaker parties, requirements of form appear in what could be considered 'gateways' to certain legal rights or protection. For example section 3 of the Unfair Contract Terms

³ Fuller "Consideration and Form," (1941) *Col LR* 799.

⁴ *Ibid.*

Act 1977 provides that a party will be afforded a level of protection against exemption clauses if he 'deals as consumer' or on the other party's '*written* standard terms'.⁵

7.2 Electronic Communications and Formal Requirements: The problem

Existing formal requirements, such as writing and signature, pose *prima facie* difficulties when using electronic forms of communication with their ephemeral nature and predominantly intangible form. Many of the accepted definitions of formal requirements infer a physical, permanent or visible form.⁶ If electronic communications cannot satisfy formal requirements there exists a potential restriction on the ability of electronic commerce to fulfil its economic potential because certain transactions will be excluded from the environment. International bodies,⁷ the European Union and the United Kingdom government have all recognised the potentially detrimental effect formal requirements may have on the growth of electronic commerce.

During the introduction of the Electronic Commerce Directive the European Commission stated that

“Electronic commerce will not fully develop if concluding on-line contracts is hampered by certain form and other requirements which are not adapted to the on-line environment.”⁸

To this end the approaches adopted to regulating electronic commerce have a common goal of removing formal requirements which may act as 'barriers' to electronic contracting. However, before legislative attempts to address the perceived problem are considered it is prudent to examine whether, by their own virtues, electronic forms of

⁵ Emphasis added. For a more detailed analysis of this particular problem see, Macdonald, E & Poyton, D. "A particular problem for e-commerce: Section 3 of the Unfair Contract Terms Act 1977" (2000) 3 *Web JCLI* available at <http://webjcli.ncl.ac.uk/2000/issue3/macdonlad3.html>.

⁶ See the discussion of 'writing' below at 7.2.

⁷ See the Guide to Enactment of the UNCITRAL Model Law on electronic Commerce (1996) at para 46 *et seq.* General Assembly Resolution 51/162 of 16 December 1996, UNCITRAL Model Law on Electronic Commerce. Available at, <http://www.uncitral.org/english/texts/electcom/ml-ecomm.htm>.
UNCITRAL.

⁸ "Proposal for a European Parliament and Council Directive on certain legal aspects of electronic commerce in the internal market" COM(1998) 586 final. OJ C 030 (05/02/1999) at p.4. This sentiment was echoed by the British government in the DTI 'Consultation Document on Implementation of the E-Commerce Directive' at p 15. 10th August 2001. Available at http://www.dti.gov.uk/cii/ecommerce/europeanpolicy/arch_condoc.shtml.

communication are capable of actually satisfying the most problematic and common requirements of form – writing and signature.

There are two pertinent issues to consider at this point:

- whether electronic communications can satisfy the formal requirements; and,
- if they can, whether that proposition can be stated with sufficient certainty to promote confidence in the use of electronic contracts where formal requirements exist.

7.2.1 Will electronic communications satisfy existing requirements of form?

7.2.1.1 The Literal and Purposive Approaches.

The analysis of a requirement of form may be approached by the courts in two ways. The first is a straightforward literal approach, requiring an examination of whether an electronic form will satisfy the existing definition of a requirement. If electronic forms can fall within existing definitions, such as ‘signature’, ‘writing’ or a ‘document’, then there is no problem. However, even if the ‘new’ forms of communication can be accommodated by the existing definitions, the failure to take the opportunity to evolve the definition may be questioned.⁹

The second approach would require a more imaginative and purposive interpretation to be adopted by the courts. This approach would take into consideration the function and purpose behind the requirement of form and examine whether the electronic form of communication can fulfil that function. If it can, then arguably it should be treated as equivalent to the more traditional forms and accommodated within the existing definition as ‘recognition of technological change’.¹⁰ This was the approach adopted by Mann LJ, in *Lockheed-Arabia v. Owen*. In his consideration of whether a photocopy could be classed as ‘writing’ for the purpose of the Criminal Procedure Act 1865, citing *Bennion, Statutory Interpretation*¹¹, his Lordship reiterated the opinion that

“an ongoing Statute ought to be read so as to accommodate technological change.”¹²

⁹ The argument being that *at some point* technology is likely to out-grow a dated definition and it is better, for commercial certainty, to be proactive rather than reactive.

¹⁰ However, it must be remembered that this approach can only be adopted where there is sufficient scope in the definition in question.

¹¹ Bennion, F. A. R. *Statutory Interpretation: A Code* 2nd ed (Butterworth: London, 1992) at p. 627.

¹² *Lockheed-Arabia v. Owen* [1993] Q.B. 806 at p 814.

A further illustration of this approach can be found in *Victor Chandler International v. Commissioners of HM Customs & Excise*.¹³ In the Court of Appeal Sir Richard Scott VC stated that

“..it is now a well known rule of statutory construction that an “ongoing” statutory provision should be treated as “always speaking”.”¹⁴

By applying this purposive approach His Lordship concluded that the distribution of a teletext page could be considered to be the distribution of a ‘document’ for the purposes of the Betting and Gaming Act 1981 because the activity clearly fell within the range of activities Parliament intended to address in the section.

When considering whether an electronic form of communication satisfies a requirement of form in an existing statute this approach may be adopted to deduce whether the form in question fulfils the purpose for which the original requirement was introduced. This ‘purposive’ approach requires the courts to discover Parliaments intention in introducing the measure and to implement that intention:

“It must be very clear that the new situation falls within the Parliamentary intention.”¹⁵

This accommodating approach will be restricted if it would require the distorting of a meaning to an absurd level or if the purposes of the provision would be undermined by the accommodation of this technological change. However, if an electronic communication fulfils the intended purpose of the statutory requirement there appears little reason why it should not be treated as equivalent to their traditional counterparts and accommodated within existing and “ongoing” statutes.

Nevertheless there remains a difficulty with this approach where a requirement of form serves a number of functions. The courts may have to consider whether the electronic communication must satisfy *all* or just *some* of the functions in question. This may require an investigation beyond that with which the courts may feel comfortable. The greatest limitation on this approach, however, is the situation where the court feels that it cannot adequately discern the intention of Parliament from the material available

¹³ [2000] 2 All E.R. 315.

¹⁴ At para 27, also citing Bennion *op cit* fn 11.

¹⁵ *Op cit* fn 13 at para. 32.

and as a consequence is unable to extend the boundaries of the definition of a particular requirement to accommodate electronic form.

It is necessary at this point to analyse these two approaches in the context of the two most commonly occurring formal requirements – ‘writing’ and ‘signature’. It must be noted before this analysis is undertaken that in the opinion of the Law Commission

“statutory requirements for ‘writing’ and a ‘signature’ are generally capable of being satisfied by e-mails and by website trading (but not by EDI).”¹⁶

However, the Commission conceded that there was a lack of consensus on these issues. It is respectfully submitted that any ‘generalisation’ of these issues in relation to the rapidly changing electronic environment is inherently dangerous and unlikely to promote the legal certainty required to increase and maintain confidence in electronic contracting.

7.2.2 ‘Writing’

7.2.2.1 The Literal Approach

In a normal sense the words ‘writing’ or ‘written’ connote a visible mark on some physical medium. However, even the New Oxford Dictionary of English recognises that writing may differ in the computing context and defines it as “to enter (data) into a specified storage medium or location in store.”¹⁷ Electronic communications can take a variety of forms. When printed out a data message is indistinguishable from other forms of writing and when displayed on screen it is clearly visible as writing. However, in other forms data messages or electronic communications have no visible or real physical form:¹⁸ for example when a message is transmitted digitally from a mobile phone or Personal Digital Assistant (PDA), sent via copper telephone lines or optical fibre, or stored on a medium such as a hard disk drive, CD ROM or other form of digital storage. In this form the messages assume their intangible, ephemeral and invisible form. In electronic communications such as EDI the communications rarely, if ever, assume their tangible or visible form. It must be considered which if any of these forms of electronic communications will satisfy a requirement of ‘writing’.

¹⁶ *Op cit* fn 2 at p. 40.

¹⁷ New Oxford Dictionary of English 1998.

¹⁸ It is accepted that there is a physical form, as in a change to the carrier or storage medium – but not a physical form recognisable as writing.

If legislation requires that a particular type of contract or contractual communication be 'written', then the courts will have a number of aids to the interpretation of that requirement. The first may be an autonomous definition in the particular Act. For example, in the Copyright Designs and Patents Act 1988, the requirement of 'writing' is satisfied by,

“any form of notation or code, whether by hand or otherwise and regardless of the method by which, or medium in or on which it is recorded.”¹⁹

The definition is couched in very general terms, clearly capable of encompassing 'electronic writing'. An undoubtedly 'medium neutral' definition is adopted which does not discriminate against forms of electronic writing or a data messaging.

However, if, as occurs in the majority of situations, there is no autonomous definition in the Act in question, then the courts may turn to the definition found in the Interpretation Act 1978. This Act provides default definitions for use in statutory interpretation for certain words and phrases, which will apply unless the precise wording or context of the section indicates to the contrary.²⁰ Schedule 1 of the Act defines 'writing' as including

“... typing, printing, lithography, photography and other modes of representing or reproducing words in visible form and expressions referring to writing are construed accordingly.”

The definition and the forms expressly included in the definition demonstrate the need for the representation or reproduction of words 'in visible form'. As is indicated above, with electronic forms of communication this will depend upon the 'phase' of the communication in question. If it is in its normal storage or transmission phase then, unless put under an electron microscope, there is nothing visible to the human eye and hence no 'visible' representation of 'words'.²¹ In this state the communication would appear not to satisfy the Interpretation Act requirement, being

¹⁹ Section 178.

²⁰ Section 5.

²¹ Even what is visible when viewed under an electron microscope can not really be classed as 'words'.

“on/off states of switches in a processing chip or as magnetic or optical variations on the surface of some recording medium.”²²

However, when an electronic message is received and displayed in some way, it clearly becomes a representation of words in visible form and correspondingly should satisfy the definition. EDI communications, which invariably do not move out of their transmission or storage phase, would appear not to satisfy the requirement.²³

“Because the parties are not able to view the EDI message, the Interpretation Act requirement of visibility will not be satisfied and such a message will not, in our view, be capable of satisfying a statutory writing requirement.”²⁴

However, it is submitted that examining the medium to this extreme is perhaps not necessary, and some support can be found by drawing an analogy with another medium explicitly mentioned in the Interpretation Act.

For all practical purposes the contents of an electronic communication or data message are only active when they are viewed on screen or printed out, and again for all practical purposes it is impossible to prove their existence until they are.²⁵ Here, an analogy can be drawn with photography and photographic film, the former being specifically mentioned in the statute.²⁶ When a picture is taken it is stored on the film, whatever the subject matter of the picture; be it a portrait, a landscape or a picture of a written document, it is nothing more than a variation in the composition of a variety of chemicals. This image will be ‘stored’²⁷ until the film is developed and a print, negative or slide is produced. There is no way of viewing any recognisable representation of the image or the writing in a photographed document whilst the film is in its primary form. In a similar way by looking at the surface of a floppy disc or other form of storage, even with the aid of an electron microscope, you cannot discern anything more than the magnetic or optical variations on its surface. Nevertheless, for the purposes of the Interpretation Act the developed photograph of the document can constitute ‘writing’.

²² Reed, C. *Digital Information Law Electronic Documents and the Requirements of Form*. (London : Centre for Commercial Law Studies, Queen Mary and Westfield College, 1996).

²³ In some circumstances the communications can be displayed by one of the parties if required, which would then appear to satisfy the requirement.

²⁴ *Op cit* fn 2 at p. 11 para. 3.20.

²⁵ Except via an electron microscope.

²⁶ Macdonald, E & Poyton, D. “A particular problem for e-commerce: Section 3 of the Unfair Contract Terms Act 1977” (2000) 3 *Web JCLI* available at <http://webjcli.ncl.ac.uk/2000/issue3/macdonlad3.html>.

²⁷ Barring deterioration over long period of time or poor storage.

By analogy there is no reason why digital information or electronic communications, displayed on screen or printed out should not be classed as 'writing' for the purpose of the Act.

However, transactions which take place directly between computers, such as EDI and electronic agents, are rarely reduced to a visible form or anything resembling a visible representation of words. Such communications would probably not, even with a broad interpretation, fall within the definition.

7.2.2.2 The purposive approach – the 'function' of writing

Reed suggests that requirements for writing are imposed because they are a "historical hangover from the Statute of Frauds" or "the transactions are somehow more 'formal' or 'serious' than other contracts, and require writing to emphasise their unusual nature."²⁸ In the UNCITRAL Model Law on Electronic Commerce the functions served by the formal requirement of writing are stated as including providing tangible evidence of the party's agreement; to make the parties aware of the obligations they were undertaking; to provide an unaltered and permanent record of the agreement for subsequent reference; and to allow for the easy reproduction of the data. When considering the purposive interpretation of a requirement of writing in a statute the courts will consider which of these functions the requirement was intended to fulfil and assess whether the electronic form of communication will equally fulfil that function. This is referred to in a legislative sense in the Model Law as a 'functionally equivalent' approach.²⁹ Section 3 of the Unfair Contract Terms Act 1977 provides a useful illustration. The protection provided by section 3 will only apply if a party to the contract 'deals as consumer' or on the other party's 'written standard terms'. The Act is discussed in detail in chapter 11 but for the purpose of this discussion it can be summarised that the legislative intention behind this requirement was to protect weaker parties to a contract against 'standard form' agreements, over the content of which they have no control. The 'written' part of the requirement is there to indicate that the terms of the agreement are pre-formulated. On a purposive construction a set of pre-formulated terms recorded or transmitted electronically would clearly be within the 'mischief' targeted by Parliament's introduction of the section.

²⁸ Reed, C. *Digital Information Law: Electronic Documents and the Requirements of Form*. (London : Centre for Commercial Law Studies, Queen Mary and Westfield College, 1996) at p. 88.

²⁹ *Op cit* fn 7, at para. 15 *et seq.*

However, even if this analysis is correct, the problem remains that it is, at present, purely speculative and there is at least a level of uncertainty as to how the courts will approach the question. The uncertainty created, even if wrongly perceived, is capable of acting as a deterrent to commercial parties looking to enter electronic contracts, hindering the development of electronic commerce.³⁰

7.2.3 'Signature'

Where a statute requires a 'signature' or that a document be 'signed' the courts have only occasional and limited guidance what is required and very little guidance as to a definition of 'signature'.³¹ Hence, a body of case law has developed and in England and Wales which has given the formal requirement of a 'signature' a generous interpretation, accepting everything from a cross on a page to a rubber stamp or facsimile of the signature.³² Signatures also retain great significance as indicators of a party's commitment to an agreement.³³

In the electronic environment a signature can also take a variety of forms. At the most basic a typed name or initials at the bottom of a message and at the other end of the scale cryptographic and biometric techniques can provide a technologically advanced method of 'signing' a document. As Reed indicates,³⁴ at common law the 'benchmark' has been the 'manuscript signature' with a variety of other forms of signature being considered by analogy to it:

"Variations on this theme have been considered by the English courts from time to time, ranging from simple modifications such as crosses³⁵ or initials³⁶, through pseudonyms³⁷ and identifying phrases³⁸, to printed names³⁹ and rubber stamps.⁴⁰

³⁰ See, Smith, G. J. H. *Internet Law and Regulation*. (Sweet and Maxwell: London) at p. 471.

³¹ For example, there is no definition of 'signature' in the Interpretation Act. See Reed *op cit* fn 28 at p. 262.

³² See *Bennett v. Brnoffitt* (1867) L.R. 3 C.P. 28 and *Jenkins v. Gaisford and Thring* (1863) 3 Sw. & T. 93.

³³ See chapter 9 below, and the discussion of incorporation.

³⁴ Reed C, 'What is a Signature?', 2000 (3) *The Journal of Information, Law and Technology (JILT)*. <http://elj.warwick.ac.uk/jilt/00-3/reed.html/> at p 2.

³⁵ *Baker v. Dering* (1838) 8 A&E 94.

³⁶ *Hill v. Hill* [1947] Ch 231.

³⁷ *Redding, in re* (1850) 14 Jur 1052, 2 Rob. Ecc. 339.

³⁸ *Cook, In the Estate of (Deceased). Murison v. Cook and Another* [1960] 1 All ER 689 (holograph will signed 'your loving mother').

³⁹ *Brydges v. Dix* (1891) 7 TLR 215; *France v. Dutton*, [1891] 2 Q.B. 208. Typewriting has also been considered in *Newborne v. Sensolid (Great Britain), Ltd.* [1954] 1 QB 45.

⁴⁰ *Lazarus Estates, Ltd. v. Beasley* [1956] 1 QB 702; *London County Council v. Vitamins, Ltd., London County Council v. Agricultural Food Products, Ltd.* [1955] 2 QB 218.

In all these cases the courts have been able to resolve the question whether a valid signature was made by drawing an analogy with a manuscript signature.”

However, as Reed explains the developments in communication technologies may mean that “analogies with manuscript signatures may no longer be appropriate or even possible.”⁴¹

It can be seen that the courts have tended to adopt a flexible and purposive approach in the past and such an approach would continue to fit well with the philosophy behind regulating electronic commerce. This ‘functional’ approach has been recognised by the Law Commission in their advice on formal requirements in e-commerce transactions:

“The common characteristic of the cases is that the courts looked to whether the method of signature used fulfilled the function of a signature [...] rather than whether the form of signature used was one which was commonly recognised.”⁴²

The functions of a signature are various but the generally accepted functions include authenticating a message; ensuring the integrity of a message; and demonstrating intent to participate or accede to the contents of a message.⁴³ The approach adopted by the court would depend upon the purpose of the requirement in a specific statute but with the generous approach adopted by the courts it would appear that electronic signatures, whatever their form, would probably be capable of satisfying formal ‘signature’ requirements. This conclusion is supported by the Law Commission:

“Digital signatures, scanned manuscript signatures, typing one’s name (or initials) and clicking on a website button are all methods of signature which are capable of satisfying a signature requirement.”

However, the problem remains that this proposition has not been tested in the courts and the reliance on analogy or previous approaches adopted may not be sufficient to promote confidence in their use and the legal certainty required. For this reason, the

⁴¹ *Ibid*

⁴² *Op cit* fn 2, at p. 13, para. 3.26.

⁴³ See, Angel, J. “Why use Digital Signatures for Electronic Commerce?”[1999] (2) *The Journal of Information, Law and Technology (JILT)*. <http://elj.warwick.ac.uk/jilt/99-2/angel.html>.

need to regulate to clarify the position of electronic communications in relation to requirements of form has been a predominant issue in the regulation of electronic commerce.

7.3 Regulatory Solutions to the Potential Barriers Created by Formal Requirements

Whether or not the existing legal definitions could encompass electronic communications, governments and supranational bodies have recognised that the uncertainty created has the potential to undermine commercial confidence. The general consensus in recommendations and legislation appears to be that formal requirements which may discriminate against electronic forms of communication and contracting should be removed unless doing so would undermine the purpose of the requirement. The approaches of the United Nations, the European Union and the United Kingdom will now be considered.

7.3.1 The United Nations Commission on International Trade Law (UNCITRAL) 'Model Law on Electronic Commerce'⁴⁴

The UNCITRAL Model Law was one of the earliest examinations of the needs of the developing commercial activity known as 'electronic commerce'. The Model Law was developed to

“..assist all States significantly in enhancing their legislation governing the use of alternatives to paper-based methods of communication and storage of information and in formulating such legislation where none currently exists.”⁴⁵

The Model Law has been the template upon which many pieces of national electronic commerce related legislation have been developed⁴⁶ and the European Commission has referred to the work of UNCITRAL and the Model Law in a number of its framework Directives.⁴⁷

⁴⁴ *Op cit* fn 7.

⁴⁵ General Assembly 85th plenary meeting 16 December 1996.

⁴⁶ For example see the background material to Australia's Electronic Transactions Bill 1999, available at, <http://www.law.gov.au/publications/ecommerce/etaem.html>.

⁴⁷ See, the Opinion of the Economic and Social Committee on the Communication from the Commission to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions: "A European Initiative in Electronic Commerce" (COM(97) 157 final) Brussels, 29 October 1997; and the Common position adopted by the Council with a view to the

The approach adopted in the Model Law to formal requirements is one of 'functional equivalence' which is described as

“based on an analysis of the purposes and functions of the traditional paper-based requirement with a view to determining how those purposes or functions could be fulfilled through electronic-commerce techniques.”⁴⁸

The approach is applied whether the formal requirements amount to an “obligation to comply” with the requirement or simply the provision of “consequences in the absence of a particular formal requirement”.⁴⁹ The objective of this approach is to

“enable such data messages to enjoy the same level of legal recognition as corresponding paper documents performing the same function.”⁵⁰

The Model Law gives legal recognition to electronic communications (data messages)⁵¹ and decrees that they will meet formal requirements of 'writing' providing they are accessible and available for subsequent reference.⁵² With signatures the 'functional equivalence' approach takes into account the reliability and appropriateness of the method adopted in the circumstances.⁵³

The functional equivalence approach suggested in the Model Law provides for a non-discriminatory approach to electronic forms of communication where they can fulfil the function of their paper-based counterparts.

adoption of Directive of the European Parliament and of the Council on certain legal aspects of Information Society services, in particular electronic commerce, in the Internal Market (“Directive on electronic commerce”)98/0325 (COD) 14263/99.

⁴⁸ *Op cit* fn 7 at para. 15.

⁴⁹ *Ibid*

⁵⁰ *Ibid* at para 18.

⁵¹ Article 5 Legal recognition of data messages

Information shall not be denied legal effect, validity or enforceability solely on the grounds that it is in the form of a data message.

⁵² Article 6(1) Writing

Where the law requires information to be in writing, that requirement is met by a data message if the information contained therein is accessible so as to be usable for subsequent reference.

⁵³ Article 7 Signature

(1) Where the law requires a signature of a person, that requirement is met in relation to a data message if:

(a) a method is used to identify that person and to indicate that person's approval of the information contained in the data message; and
(b) that method is as reliable as was appropriate for the purpose for which the data message was generated or communicated, in the light of all the circumstances, including any relevant agreement.

7.3.2 The European Union

7.3.2.1 The General Approach

The European Community recognised the need to remove formal requirements which could create barriers to electronic contracting or uncertainty as to the validity of electronic contracts in the early preparatory work to producing a 'legal framework' for electronic commerce:

“For electronic commerce to develop its full potential, it must be possible for contracts to be concluded on-line unrestricted by inappropriate rules (such as a requirement that contracts be drawn up on paper).”⁵⁴

However, the Commission was also concerned that disparate approaches being adopted in the Member States may in themselves create problems for those wishing to enter cross-border electronic contracts within the internal market:

“Moves in certain Member States to enact new legislation are apparent and there are already differences in approach which entail a real risk in the short term of fragmenting the internal market.”⁵⁵

Consequently a measure was included in the Electronic Commerce Directive to address formal requirements and create a harmonised approach throughout the European Union.⁵⁶ The provision is found in Article 9 of the Electronic Commerce Directive and it requires Member States to ensure that

“... their legal system allows contracts to be concluded by electronic means. Member States shall in particular ensure that the legal requirements to the contractual process neither create obstacles for the use of electronic contracts nor result in such contracts being deprived of legal effectiveness and validity on account of having been made by electronic means.”⁵⁷

⁵⁴ “See press release; “Commission adopts draft Regulation on Jurisdiction, Recognition and Enforcement of Judgements in Civil and Commercial Matters”, Brussels, 14 July 1999, IP/99/510, at p. 2.

⁵⁵ “Proposal for a European Parliament and Council Directive on certain legal aspects of electronic commerce in the internal market” COM(1998) 586 final. OJ C 030 (05/02/1999) at p. 8.

⁵⁶ *Ibid.*

⁵⁷ Article 9.

Two distinct approaches to the implementation of this provision and the removal of legal barriers to electronic commerce and electronic contracting can be identified.

The first would be to adopt a 'medium neutral' approach declaring that electronic communications will satisfy formal requirements such as writing unless legislation expressly provides otherwise.⁵⁸ The second approach would be to amend the legislation containing formal requirements, which may act as barriers to the use of electronic communications, on a piecemeal basis. While the former provides for the rapid adoption of electronic communications, the latter, slower approach allows for the analysis of the purpose and function behind a requirement to ensure that the electronic form is 'functionally equivalent' to its 'real-world' counterpart. The language included in the Article is wide enough to encompass either approach which, arguably, has weakened its harmonising effect. From the material published in the development of the Directive it can be suggested that the desired approach was the more rapid of the two requiring a medium neutral approach with exceptions for certain specific types of contract:⁵⁹

"...the Member States have an obligation to succeed, carry out a systematic review of those rules which might prevent, limit or deter the use of electronic contracts and to carry out this review in a qualitative way, i.e. not seek simply to amend the key words in the rules (e.g. "paper") but to identify everything which might in practice prevent the "effective" use of electronic contracts."⁶⁰

7.3.2.2 The EU Approach to 'Signatures'

An electronic communication can be 'signed' in a number of ways including the simple typing of a name or initials at the bottom of an e-mail or the use of encryption technology to create an 'electronic signature'. The European Commission recognised the potential importance of electronic signatures to electronic commerce at an early stage:

"In order to make good use of the commercial opportunities offered by electronic communication via open networks, a secure and trustworthy

⁵⁸ This approach was first adopted in Singapore in the The Electronic Transactions Act 1998.

⁵⁹ See Recital 34

'Each Member State is to amend its legislation containing requirements, and in particular requirements as to form, which are likely to curb the use of contracts by electronic means; the examination of the legislation requiring such adjustment should be systematic and should cover all the necessary stages and acts of the contractual process, including the filing of the contract; the result of this amendment should be to make contracts concluded electronically workable;'

⁶⁰ *Op cit* fn 55 at p. 25.

environment is therefore necessary. Cryptographic technologies are nowadays widely recognised as the essential tool for security and trust in electronic communication. Two important applications of cryptography are digital signatures and encryption.”⁶¹

The Electronic Signatures Directive⁶² was introduced in 1999 and one of its objectives was to give electronic signatures legal validity:

“In order to contribute to the general acceptance of electronic authentication methods it has to be ensured that electronic signatures can be used as evidence in legal proceedings in all Member States”⁶³

The Directive envisages a distinction being made between the various forms which an electronic signature may take. The most secure and reliable forms of electronic signature are classed as ‘advanced electronic signatures’. An ‘advanced electronic signature’ is one which:

- (a) is uniquely linked to the signatory;
- (b) is capable of identifying the signatory;
- (c) is created using means that the signatory can maintain under his sole control;
- and
- (d) is linked to the data to which it relates in such a manner that any subsequent change of the data is detectable;⁶⁴

When an electronic signature satisfies these requirements and is based on a ‘qualified certificate’ and created by a ‘secure-signature-creation device’, it is afforded equivalent status to a traditional signature:

⁶¹ European Commission document “Towards A European Framework for Digital Signatures and Encryption” COM (97) 503 final (8.10.1997).

⁶² Directive 1999/93/EC of the European Parliament and of the Council of 13 December 1999 on a Community framework for electronic signatures OJ L 13/12 (19/01/2000).

⁶³ Recital 21.

⁶⁴ Article 2(2).

“Member States shall ensure that advanced electronic signatures which are based on a qualified certificate and which are created by a secure-signature-creation device:

- (a) satisfy the legal requirements of a signature in relation to data in electronic form in the same manner as a handwritten signature satisfies those requirements in relation to paper-based data; and
- (b) are admissible as evidence in legal proceedings.”⁶⁵

In this way the most reliable and secure forms of electronic signature would automatically fulfil any formal legal requirement of signature.

The Directive also provides that other electronic signatures, whatever form they may take, shall not be denied legal effectiveness or admissibility as evidence solely on the grounds that they are in electronic form or do not fulfil the criteria for advanced electronic signatures.

If implemented correctly the Directive removes legal uncertainty as to whether advanced electronic signatures can fulfil formal legal requirements.

7.3.3 United Kingdom

In the United Kingdom Article 9 of the Electronic Commerce Directive was implemented by Section 8 of the Electronic Communications Act 2000. The approach adopted in the legislation is a piecemeal approach whereby an ‘appropriate’ minister may introduce an amending statutory instrument where existing legislation is found to contain a potential barrier to electronic commerce.

“(1) Subject to subsection (3), the appropriate Minister may by order made by statutory instrument modify the provisions of

- (a) any enactment or subordinate legislation, or
- (b) any scheme, licence, authorisation or approval issued, granted or given by or under any enactment or subordinate legislation,

in such manner as he may think fit for the purpose of authorising or facilitating the use of electronic communications or electronic storage (instead of other

⁶⁵ Article 5(1).

forms of communication or storage) for any purpose mentioned in subsection (2).

(2)

(a) the doing of anything which under any such provisions is required to be or may be done or evidenced in writing or otherwise using a document, notice or instrument;

...

(c) the doing of anything which under any such provisions is required to be or may be authorised by a person's signature or seal, or is required to be delivered as a deed or witnessed.

A number of amendments have been made removing or amending formal requirements to date, but while it is clear that this method of implementation is within the terms of the article it is potentially a piecemeal and slow method of creating a level playing field for electronic communications.⁶⁶ This over-cautious approach may ultimately lead to uncertainty and arguably has not made the UK the 'best place to do e-commerce by 2002'.⁶⁷

7.3.3.1 The UK Approach to Signatures.

As indicated above, electronic signatures are likely to be accepted as capable of satisfying formal requirements of signature because of the broad interpretation of a 'signature' adopted by the courts. However, to provide legal certainty it is desirable to have this speculative analysis declared by statute in some way. From the preceding discussion of the European Electronic Signatures Directive it could be assumed that with the implementation of that provision would come a degree of legal certainty as to the ability of the most reliable form of electronic signatures to satisfy formal requirements. However, this is not the case because the UK government felt that it would be more appropriate to allow the courts to adjudicate on whether such a formal requirement has been satisfied. In the Electronic Communications Act 2000 the requirements of the Directive are allegedly satisfied by section 7 which declares that electronic signatures are

⁶⁶ To 31st August 2002 12 orders had been made. See [http://www.e-envoy.gov.uk/oeo/oeo.nsf/sections/index/\\$file/index.htm](http://www.e-envoy.gov.uk/oeo/oeo.nsf/sections/index/$file/index.htm).

⁶⁷ Despite the obvious contradiction in this goal it was nevertheless undermined by this piecemeal and tentative approach to medium neutral legislation.

admissible in legal proceedings. It is submitted that this approach undermines the legal clarification intended by the introduction of the Directive.⁶⁸

7.4 Formalities for the Electronic Environment

The removal of 'barriers' to electronic contracting and the need for clarity and legal certainty are seen as essential pre-requisites to the development of electronic commerce. However, in taking steps to achieve these objectives legislators must avoid the creation of new 'obstacles' to the use of current or future technology.⁶⁹ Inappropriate or unnecessary legislative requirements, prescribing minimum standards for legally acceptable electronic communications may result in unintended and undesirable consequences. Requirements of form, adopted specifically for the electronic environment, may have the effect of excluding some forms of electronic communication and not others. This can lead to further uncertainty and potential disputes as to whether particular forms of electronic communication comply with the requirements. Such disputes are both unnecessary and costly, and have the potential to undermine confidence rather than to promote it. Smith explains that, ideally,

“... electronic commerce legislation should create, so far as possible, a single medium-neutral legal environment governing paper and non-paper transactions, rather than to create separate parallel regimes for paper and electronic form.”⁷⁰

There are a number of justifications for the introduction of new regimes for the electronic environment. First, the new and novel nature of the technology may mean that no parallel can be drawn with existing forms of communication creating a need for new regulation.⁷¹ Second, there may be a need to remove legal uncertainty regarding the status of electronic communications to promote commercial confidence.⁷² Third, there may be a desire at State level to ensure that citizens are afforded the levels of protection

⁶⁸ “Advanced electronic signatures” do not feature in the Electronic Communications Act 2000 but they are referred to in the Electronic Signatures Regulations 2002 (Statutory Instrument 2002 No. 318). However, this provision only deals with the supervision of certification-service-providers, their liability in certain circumstances and data protection requirements concerning them.

⁶⁹ The requirements will usually be based upon present technology but even with expert advice legislators are ill equipped to predict future developments in such a rapidly changing technological environment. Prescriptive rules introduced on this basis are inevitably going to create problems for future technologies.

⁷⁰ Smith, G. J. H. *Internet Law and Regulation*. (Sweet and Maxwell: London) at p. 471.

⁷¹ This possibility is uncommon even with modern advancements in technology. However, electronic signatures, cryptographic and biometric techniques may serve as examples in this context.

⁷² For example, the validity of electronic contracts and requirements of form under discussion here.

to which they are accustomed, in particular consumers. Finally, and arguably most importantly for the use of electronic contracts and development of electronic commerce, the promotion of trust and confidence in the use of electronic communications. Uncertainty or a fear of the unknown creates a lack of trust and confidence in the use of electronic contracts, particularly for small businesses and consumers. All of the preceding factors may be cited to justify regulation which introduces formal requirements, unique to the electronic environment, or 'e-formalities'. A number of e-formalities and their implications for those entering electronic contracts will now be considered.

7.4.1 'E-Formalities'

Formal requirements have been introduced into electronic contracts in two main ways: first, where a requirement of form is retained from the traditional environment because of the function it performs; and secondly, where requirements are introduced for electronic contracts where previously there were none in the traditional environment. By introducing new e-formalities legislators are often seeking to facilitate electronic commerce by promoting confidence in the use of new forms of communication and create legal certainty for electronic contracts.

7.4.1.1 Requirements retained from the traditional environment

A formal requirement may be as important in the electronic environment as it is in the traditional environment because of the function it performs and the policy behind that function. In such a case an equivalent method of fulfilling that function must be found for electronic contracts. Where a requirement of form, such as 'signature' or 'writing', is retained for the electronic environment because of the function or purpose it serves it is important to examine the standards set for electronic communications to ascertain if they are truly equivalent to their traditional counterparts or if the standards set are higher. If they are, then this will create a discriminatory approach and a dual set of standards for parties entering contracts dependant upon the communication medium used. A discriminatory approach of this nature may deter parties from using electronic communications to enter contracts and as a result act as a barrier to the development of electronic commerce. Smith⁷³ uses the example of a pencilled cross on a paper document which will satisfy the formal requirement of 'signature' at common law,

⁷³ *Op cit* fn 70.

despite its lack of permanence and inherent unreliability. The standard set for an electronic signature to be acceptable is arguably higher, creating a dual level and non-equivalent requirement of form.⁷⁴ The risk of adopting over-burdensome requirements has been recognised by legislators, as illustrated in the advice given to the Australian Attorney General by the Electronic Commerce Expert Group in 1998 prior to their adoption of electronic commerce related legislation:

“There is always the temptation, in dealing with the law as it relates to unfamiliar and new technologies, to set the standards required of a new technology higher than those which currently apply to paper and to overlook the weaknesses that we know to inhere in the familiar. Many proponents of government action in the area of electronic commerce, particularly digital signatures and certification authorities, seek legislation in order to clarify rights and responsibilities, as well as to adapt the law to the perceived needs of new technology. In some instances, the legislation which has been enacted seeks to pick technology winners, apportion liability among private parties to electronic transactions, grant special liability limitations for certain parties, and generally introduce regulatory controls beyond that currently required under other bodies of law, such as consumer law, contract law and commercial law.”⁷⁵

7.4.1.2 Requirements Where Previously There Were None – New E-Formalities

It was indicated above that there may be justifications for the introduction of formal requirements into electronic contracts where in traditional contracts none existed. One specific justification was discussed in the previous chapter, the anonymity of the electronic environment and the difficulties with identification. However, even where the introduction of formalities is *prima facie* justified the requirements introduced must be appropriate for the electronic environment, sufficiently clear to avoid legal uncertainty and the consequences of failing to comply with the requirements must be proportionate to their function. Two particular pitfalls, which appear to have been overlooked by the legislature, are the introduction of unqualified and undefined standards which require

⁷⁴ Without providing a higher level of legal recognition.

⁷⁵ “Electronic Commerce: Building the Legal Framework”. Report of the Electronic Commerce Expert Group to the Attorney General, 31 March 1998. Chapter 4, 2.11 (Emphasis added). Available at <<http://152.91.15.15/ahome/advisory/eceg/ecegreport.html>>. Laddie J. adopts a complementary approach in *Re a debtor (No 2022 of 1995)*, *ex parte Inland Revenue Commissioners v The debtor* [1996] 2 All ER 345.

further interpretation by the courts and the introduction of standards which may require an analysis of the technology involved to decide whether the standard has been complied with. This submission can be illustrated by examining certain requirements found in the Consumer Protection (Distance Selling) Regulations 2000 and the Electronic Commerce (EC Directive) Regulations 2002.⁷⁶

The Consumer Protection (Distance Selling) Regulations 2000

These regulations require a wide range of information be provided to the consumer 'in writing or in another *durable medium* which is available and accessible to him'.⁷⁷ The same requirement is contained within the regulation detailing how a consumer may exercise his right to cancel the contract.⁷⁸ However, neither the Regulations nor the original Directive, give guidance as to the meaning of this phrase, in particular which technologies and electronic forms of storage and communication will be considered a 'durable medium'.

Uncertainty as to which forms of communication will satisfy the 'durable medium' requirement may encourage (or require the court to undertake) a technical analysis of the form of communication employed. With a wide range of communication mediums in existence (and undoubtedly more in the future) this kind of analysis may be unhelpful and confusing. The preferable and more likely approach would be a pragmatic and purposive (or teleological) one. If a communication medium serves the intended purpose of the requirement that should be sufficient, whatever form the communication medium takes.⁷⁹

In its guidance on the Regulations the Department of Trade and Industry has indicated that fax and electronic mail are likely to meet the requirement of a durable medium but no further guidance is given.⁸⁰ This clearly leaves scope for uncertainty.

Although the Distance Selling Directive, upon which the Regulations are based, contains no definition of 'durable medium', in later directives some attempt was made to define the phrase.⁸¹ It could be argued that reference should be made to these later

⁷⁶ Statutory Instrument 2000 No. 2334. and Statutory Instrument 2002 No. 2013 respectively.

⁷⁷ Regulations 8, 10 and 17.

⁷⁸ Regulation 10.

⁷⁹ In this way debates about individual forms of communication such as 'voicemail' and text message will be avoided. This approach would have the added advantage of being sufficiently flexible to encompass new developments in technology as they arise.

⁸⁰ DTI Guidance on The Consumer Protection (Distance Selling) Regulations 2000
<http://www.dti.gov.uk/ccp/topics1/guide/distsell.htm>

⁸¹ Directive 2002/92/EC of the European Parliament and of the Council of 9 December 2002 on insurance mediation. Official Journal L 009, 15/01/2003 P. 0003 – 0010. 2003 OJ L 9. Directive

definitions when considering the term in the context of legislation based upon earlier directives where no definition was given. However, it would appear that cross referencing in this manner must be approached with some caution. The European Court of Justice (ECJ) has indicated that this may not be a suitable approach to the interpretation of European legislation, favouring interpretation based upon the context and purpose of the particular instrument rather than a unified standard interpretation for a particular word or phrase.⁸²

However, in this particular situation the phrase in question, 'durable medium', has been introduced to accommodate or acknowledge the wide variety of modern communication technologies in use and as such the phrase is employed for the same purpose in each of the instruments. Arguably this could provide support for a uniform interpretation of the phrase. With only minor changes the definition found in the Distance Selling of Financial Services Directive⁸³ is reproduced in later directives containing the phrase. Article 2(f) of the directive reads:

“ ‘durable medium’ means any instrument which enables the consumer to store information addressed personally to him in a way accessible for future reference for a period of time adequate for the purposes of the information and which allows the unchanged reproduction of the information stored”

Arguably, since the potential uncertainty in the meaning of the phrase 'durable medium' has been recognised a 'uniform' definition has been adopted in later directives. Further, indicative lists of appropriate media have also been included for guidance. Recital 20 of the Distance Selling of Financial Services Directive reads:

2002/65/EC of the European Parliament and of the Council of 23 September 2002 concerning the distance marketing of consumer financial services and amending Council Directive 90/619/EEC and Directives 97/7/EC and 98/27/EC. Official Journal L 271, 09/10/2002 P. 0016 – 0024. 2002 OJ L 271 (the amendments to Directive 97/7 do not include the definition of durable medium). Proposal for a Directive of the European Parliament and of the Council on the harmonisation of the laws, regulations and administrative provisions of the Member States concerning credit for consumers /* COM/2002/0443 final - COD 2002/0222 */. Official Journal C 331 E, 31/12/2002 P. 0200 – 0248. 2002 OJ C 331. In this proposal reference is made to the definition found in 2002/65, indicating that a uniform approach is being adopted?

⁸² See Case C-168/00 *Simone Leitner v TUI Deutschland GmbH & Co. KG*, [2002] ECR I-2631. The opinion of the Advocate General in this case favoured a more methodological approach whereby an abstract term could be interpreted in the light of the whole *aquis communautaire*. The Commission has also expressed the opinion that the approach adopted by the court in the *Leitner* case could lead to fragmentation of EC law at national level. See Communication from the EC Commission to Parliament and Council on 'A More Coherent European Contract Law: An Action Plan', Brussels, 12.2.2003. COM(2003) 68 final, at para.21.

⁸³ OJ L 271/16. A 'partner' to directive 97/7 which concerns distance selling generally but does not apply to financial services.

“Durable mediums include in particular floppy discs, CD-ROMs, DVDs and the hard drive of the consumer’s computer on which the electronic mail is stored, but they do not include Internet websites unless they fulfil the criteria contained in the definition of a durable medium.

The initial exclusion of an Internet website may appear significant for electronic commerce, however, if steps are taken to allow the customer to store and reproduce the relevant information through the site then the criteria will be satisfied. The methods commonly used would include the provision of a reference area or specific data storage area on the site accessible to the customer.

The phrase is defined in terms of its function or purpose, retaining an element of flexibility in relation to the period of time for which the information must be accessible. What is an ‘adequate’ period of time must be decided by reference to the purposes of the information. Whilst this flexibility is understandable because of the wide range of information involved, it does leave some room for a divergent approach in national courts.

It can be concluded that the essential characteristics of a ‘durable medium’ would appear to be a storage medium which allows the customer to access and reproduce the information, unchanged, at a later date. The information must be available in this way for an appropriate period of time taking into consideration the nature and purpose of the information.

Failure to satisfy the formal information requirements in the Regulations may have a significant impact upon the rights of the service provider and the consumer. For example, a service provider’s failure to provide the appropriate information can extend the consumer’s right to cancel the contract, without penalty, to up to three months and seven working days after the delivery of goods or the signing of a contract for services.⁸⁴ The failure may also lead to a ‘qualified entity’ bringing proceedings under section 35 of the Fair Trading Act 1973⁸⁵ to obtain an injunction to prevent further infringement (‘Community infringement’) or alternatively to ensure compliance. Such a declaration would require the trader to stop the infringement or not to engage in the conduct which would constitute an infringement. The may also lead to further damage to the suppliers

⁸⁴ Regulations 11& 12.

⁸⁵ As amended by the Stop Now Orders (E.C. Directive) Regulations 2001.

reputation due to the publication of the infringement in reports by the Office of Fair Trading. Further failure by a supplier may even lead to contempt of court proceedings.

While the formal information requirement can be justified on the grounds of promoting consumer trust and confidence in entering distance contracts, in particular electronic contracts, the lack of a clear definition creates the potential for uncertainty and a lack of clarity which may act as a deterrent to sellers and suppliers to entering electronic contracts.

The Electronic Commerce (EC Directive) Regulations 2002

The Electronic Commerce Regulations also contain provisions requiring certain information to be provided to customers in a particular form. In regulation 6 general information about the service provider must be given “in a form and manner which is easily, directly and permanently accessible”. The requirement is without further qualification and raises several questions including what methods of providing information in the electronic environment will be considered ‘permanently accessible’. The DTI has suggested that temporary ‘down time’ will not prevent information from being considered ‘permanently accessible’, but little further guidance is added. However, in relation to electronic contracts, key information to be provided prior to the placing of the order need only be provided “in a clear, comprehensible and unambiguous manner”⁸⁶ with no requirement that it be in a permanent form. Clearly a distinction is made between the two sets of information to be provided, the former being available to the consumer for review and reference whereas the latter need only be readable and understandable without necessarily being available for review. However, the provision contains far too much scope for interpretation to promote certainty. It could be argued that information on website would be ‘permanently accessible’ if the user chose to copy and save the page to his hard drive, or alternatively printed the page out. The provision has alternatively been interpreted as requiring, for example, a ‘hard copy’ of the information required to be sent with goods delivered.

Regulation 9(3) states that “where the service provider provides terms and conditions applicable to the contract to the recipient, the service provider shall make them available to him in a way that allows him to store and reproduce them.” This regulation raises two points. The first is the fact that it imposes a requirement not applied to non-electronic contracts – the provision of terms in a manner which allows

⁸⁶ Regulation 9.

for storage and reproduction. This 'e-formality' can arguably be justified on the grounds of promoting trust and confidence by ensuring transparency in electronic contracts. Secondly, the provision requires the information to be provided in a manner which allows the recipient to store and reproduce it. This would appear to infer that all that is required is that the information may be copied in some way which arguably can be satisfied by the provision of the information by almost any electronic means. It is submitted that the multiple standards of delivery and accessibility required of different sets of information the Regulations do not assist the creation of clarity and legal certainty for parties entering electronic contracts.

7.4.3 The Consequences of Failing to Comply with the E-Formalities

The failure to comply with a requirement of form must also be considered in the light of the consequences of that failure. The outcome must balance the objective of the requirement with the potential for injustice created by the denial of a person's rights because of a failure to comply. This is particularly so when technical knowledge may be required in order to determine what complies with the electronic requirement of form. The deprivation of rights and defeating of expectations, caused by the invalidating of a contract for a failure to comply with requirements of form, may be seen as wholly disproportionate to the original purpose of the requirement. The potential for injustice will inevitably deter use rather than promote good practice.

This potential problem was highlighted during the implementation of the Electronic Commerce Directive. In the draft implementing regulations if a service provider failed to comply with three specific requirements that went to the 'substance' of the contracts (the availability of the terms and conditions, the acknowledgement of the order and the provision of means allowing input errors to be identified and corrected) the consumer was entitled to cancel the contract 'at any time'. During the consultation period interested bodies emphasised that such an approach had the potential to create injustice and impose disproportionate penalties on service providers.⁸⁷ The Government recognised the validity of this argument and the right to rescind, at the court's discretion, is now limited to situations where the service provider has not made available means of allowing the consumer to identify and correct input errors.⁸⁸ Failure to comply with the other information requirements is now limited to the more proportionate penalty of

⁸⁷ Electronic Commerce (EC Directive) Regulations 2002: Public Consultation – Government Response. July 31, 2002. Available at <http://www.dti.gov.uk/cii/docs/ecommerce/govtresponse.pdf>.

⁸⁸ As is required by regulation 11(1)(b).

damages for breach of statutory duty and where appropriate a court order for compliance.

7.5 Conclusion

Formal requirements often have sound policies behind their application, but they may equally be indicative of a particular state of affairs at the time of their introduction. The ability, or inability, of electronic contracts and electronic methods of communication to fulfil these requirements has resulted in the introduction of legislation to deal with the issue. In this chapter the necessity of such regulation and the ability of electronic communications to fulfil formal requirements were considered. It was concluded that although in many cases electronic communications could probably fulfil existing formal requirements this proposition could not be asserted with sufficient certainty or consistency. Therefore the legislative removal or amendment of formal requirements appears justified for the promotion of legal certainty and confidence in the use of electronic contracts.

Two legislative approaches to this issue can be identified. The first would be a 'blanket' approach declaring electronic communications as equivalent to their paper-based counterparts unless indicated otherwise; and the second would be to examine each formal requirement individually and amend it as appropriate. The former approach provides for the rapid adoption of and use of electronic communications with the possibility of excluding certain types of contract if, for policy reasons, the use of electronic communications was deemed inappropriate. The latter allows for a more conservative approach to the adoption of electronic forms of communication and the detailed consideration of whether electronic communications can provide a functionally equivalent means of fulfilling the formal requirement. In the United Kingdom the second approach was preferred and section 8 of the Electronic Communications Act provides for the piecemeal amendment of formal requirements which may act as barriers to the use of electronic communications.

Formal requirements may be transferred to, or specifically developed for, the electronic environment. However, they may also be introduced inadvertently by the use of terminology in regulatory requirements which is ambiguous or undefined, as illustrated by the Distance Selling and Electronic Commerce Regulations. Formal requirements of this nature have the potential to create uncertainty and as a consequence undermine the use of electronic contracts. A provision which may require a technical or expert analysis

of the technology used to establish whether a requirement has been complied with may create an additional 'barrier' to the use of electronic contracts.

From the preceding discussion it can be concluded that although the ideal solution for electronic contracting is the creation of a medium neutral and non-discriminatory legal environment, any regulatory changes must also ensure that appropriate safeguards remain in place to protect parties entering certain specific contracts or those in a weaker bargaining position. The approach adopted by the UK government to the removal of formal requirements demonstrates a policy-driven approach to the issue. However, the inevitably slow speed at which this approach produces the required legislative changes combined with the sustainable, but nevertheless speculative, belief that certain electronic communications will, probably, generally fulfil formal requirements may ultimately prove to have been detrimental to the use of electronic contracts.

The Formation of Electronic Contracts

In this chapter the legal issues relating to contract formation will be discussed in the light of modern electronic forms of communication. The 'nature' of electronic contracting is discussed above in chapter 3. At this point it is sufficient to note that whichever method of electronic communication is employed, the basic principles governing the formation of that contract should remain the same.

The focus of discussion will be the traditional breakdown of contract formation into the search for an offer and corresponding acceptance. The discussion will proceed to consider proposed and recently enacted regulatory measures having a direct impact on the formation process or intended to permit and facilitate electronic contracting.

Whilst the offer and acceptance analysis may appear rudimentary it is nevertheless the predominant approach adopted by the courts and establishing the existence of a contractual relationship is crucial to subsequent analysis of parties' rights and obligations. For the parties concerned, establishing the precise time and place of contract formation not only allows them to know with some certainty exactly when they are contractually bound but will also dictate which contractual terms form part of their agreement.¹ The DTI and the Law Commission have made it clear they believe that the common law in England and Wales is more than capable of accommodating the new forms of communication and that there is no need to change any of the existing principles or introduce specific legislation to deal with contract formation.²

In relation to applicable law and jurisdictional matters the significance of the place of contract formation has been significantly reduced with the introduction of harmonising Conventions and Regulation; nevertheless, it still has a role to play as part of

¹ See below chapter 9.

² See the Department of Trade and Industry (March 2002) "Interim Guidance to the Electronic Commerce (EC Directive) Regulations 2002" at p. 22; and The Law Commission guidance, "Electronic Commerce: Formal Requirements in Commercial Transactions" 3rd December 2001, available at www.lawcom.gov.uk.

the private international law of England and Wales in disputes falling outside of the relevant Conventions and Regulations.³

8.1 Agreement: Objectivity and Intention

Before embarking upon analysis of contract formation the courts' approach to assessing agreement must be considered. The courts are looking for an 'intention to be bound' and the predominant approach is to make an objective assessment of the parties' behaviour; subjective intention is rarely a consideration.⁴ Whatever medium of communication is used, it is the objective assessment of the party's words and conduct that is important. In the words of Blackburn J in *Smith v Hughes*:⁵

"If, whatever a man's real intention may be, he so conducts himself that a reasonable man would believe that he was assenting to the terms proposed by the other party, and that other party upon that belief enters into the contract with him, the man thus conducting himself would be equally bound as if he had intended to agree to the other party's terms..."⁶

and more concisely, Lord Denning in *Storer v Manchester City Council*:⁷

"In contracts you do not look into the actual intent in a man's mind. You look at what he said and did. A contract is formed when there is, to all outward appearances, a contract."⁸

The courts are interested in outward appearances of the communication's content rather than its form; hence websites, e-mail, SMS messaging and other forms of electronic communication will be considered individually on their own particular merits. It is important to note that the offer and acceptance analysis will need to be considered in the light of the fact that the vendor's 'responses' may be automated. More often than not, particularly with interactive websites, the person responsible for the site's presence,

³ See chapters 4 & 5 above.

⁴ The subjective assessment may be important where, for example, one party is aware or should reasonably be aware of a mistake by the other party. See *Hartog v Colin & Shields* [1939] 3 All ER 566 and *Centrovincial Estates plc v Merchant Investors Assurance Co Ltd* [1983] Com LR 158.

⁵ (1871) LR 6 QB 597.

⁶ *Ibid* at p 607.

⁷ [1974] 3 All ER 824.

⁸ *ibid*, at p 828.

the web site proprietor, will have no knowledge of each individual transaction as it is made. This raises the question of whether the requisite intention to be bound can be ascribed to him in this situation. Specifically, can the words or conduct of the automated electronic system be attributed to the website proprietor as his own acts, signifying his 'intention to be bound'?

8.2 Intention and Automated Systems

The use of electronic agents was considered in chapter 3 and it was highlighted that the use of automation to effect contracts is not a new occurrence. For many years automatic vending machines have been in use, from ticket machines to the office drinks dispenser. In the past decade fully automated stock ordering systems using Electronic Data Interchange (EDI) have become the norm for many commercial enterprises. However, with EDI transactions, the requisite intention to be bound is usually expressly stated in the parties' Interchange Agreement.⁹ In the context of the present discussion it is the actions of interactive websites and other automated electronic systems such as 'electronic agents', where no prior agreement exists between the parties, that are the focus. These systems are designed and programmed by, or on behalf of, the supplier to fully automate the contractual process. As Gringras has commented, such web sites "fuse the advertising and the shop".¹⁰ They act as the advertisement and when so programmed carry out the transaction, sometimes delivering the product or beginning the service automatically with no human intervention. The benefits of such systems to the electronic trader are clear: they provide the ability to enter transactions at any time with as many customers as the system will allow with minimal implications for human or physical resources (such as employees, office space and equipment).

Previously the courts have found little difficulty in attributing the actions of automatic machines to their owner and thus providing evidence of the requisite intent. In the words of Lord Denning in *Thornton v Shoe Lane Parking*¹¹, a transaction facilitated by an automated ticket machine

⁹ See chapter 2.

¹⁰ Gringras, C. *The Laws of the Internet*. (Butterworths: London, 1997) at p 14.

¹¹ [1971] 2 QB 163.

“... can be translated into offer and acceptance in this way: the offer is made when the proprietor of the machine holds it out as being ready to receive the money... .”¹²

By implication, the placing of the machine there to perform a task (in *Thomton* to enter a contract with the customer for the use of the car park), indicates that the proprietor intends to be bound by transactions entered into by that machine. If this analysis were to be applied to automated websites then the actions of that website could be attributed to the supplier. By designing a website in this way the proprietor holds the site out as ready to contract on his behalf.¹³

International developments in this area would appear to support this analysis. The Guide to Enactment of the UNCITRAL¹⁴ Model Law on Electronic Commerce¹⁵ states that, “data messages that are generated automatically by computers without human intervention should be regarded as ‘originating’ from the legal entity on behalf of which the computer is operated.”¹⁶ However, it has been suggested that there are some significant differences between the system considered in *Thomton* and interactive web sites.¹⁷

In *Thomton* the machine in question was a stand-alone offer for a unilateral contract; a customer could either accept or decline the offer. There was no room for negotiation or further discussion, the conduct of placing the coin in the machine concluded the contract, and all that remained was the performance of the contract vis-à-vis the parking of the car in the facilities provided. Many modern automatic vending machines do not work in this way and interactive websites and electronic agents can go beyond merely communicating an offer of a unilateral contract to the extent that they can create the illusion that they are actually making ‘decisions’.¹⁸ Hence, it could be argued

¹² *Ibid* at 169.

¹³ See Glatt, C, “Comparative Issues in the Formation of Electronic Contracts” (1996) 6 *Int JLIT* 34.

¹⁴ United Nations Commission on International Trade Law.

¹⁵ General Assembly Resolution 51/162 of 16 December 1996, UNCITRAL Model Law on Electronic Commerce. Available at, <http://www.uncitral.org/english/texts/electcom/ml-ecomm.htm>.

¹⁶ Paragraph 35. Article 2 of the Model Law states;

(c) “Originator” of a data message means a person by whom, or on whose behalf, the data message purports to have been sent or generated prior to storage...

¹⁷ In that they go beyond ‘mere communication’ of contractually significant messages by emulating actual human decision making. See Nicoll, C.C. “Can Computers Make Contracts?” [1998] (January) *Journal of Business Law (JBL)* 35; and the discussion in chapter 3.2.

¹⁸ For example - a standard soft drink vending machine. The items are displayed and priced ‘offering’ the soft drink of choice should adequate remuneration be placed in the slot. However if there is no stock left in the machine no drink can be dispensed. Is this a conditional offer (on there being sufficient stock)? An analysis more congruent with existing case law is that the offer is made when the drink of choice is

that the computer has taken the decision to make an offer or acceptance. The human proprietor has no knowledge of these decisions at the time. How then can the requisite intention to be bound be attributed to the human proprietor? In fact, the answer would seem to be a simple one. The computer is only emulating human decision making to the extent permitted by the programming. The programming was introduced by, or on behalf of, the proprietor for that very purpose. Thus, by creating the website in that manner it must be presumed that the proprietor intends to be bound by the activities of that site. As Glatt states,

“Even the most sophisticated software does not make autonomous decisions, but operates according to previous programming. The responsibility therefore, remains with the principal, who decides to use such software with the intention of being bound by its declarations”¹⁹

More importantly, to the objective observer the computer is demonstrating an intention to be bound. The prior instructions given to the computer by or on behalf of the proprietor are responsible for this. It can only be concluded that *objectively* he intends to be bound by the activities of that website or electronic agent, for the duration that the website or agent remains active. To hold otherwise, would require a step away from the objective view of agreement and require an apportioning of the risk of errors or failures in such automated systems on a party who has no control over the system. In a variety of contexts the common law has developed an approach to mistakes as to the subject matter of a contract, be it the price, quantity or some other quality. It is submitted that there is no reason why, in situations whereby an electronic agent or website makes a mistake, or acts erroneously, the existing principles should not apply. As a general rule, the user of an electronic agent or a website proprietor will only be able to escape his apparent consent to a contract in situations where the other party knew or reasonably ought to have known of the mistake or error.²⁰

selected. The machine is automated and performs pre-programmed tasks, but there are still variables in the system. If there is no stock left, or inadequate remuneration is inserted the machine will ‘reject’ the offer and suggest an alternative selection or return the money. The contract is only concluded when the machine accepts the offer by dispensing the drink. Interactive web sites will often work on the same basis.

¹⁹ *Op cit* fn 13, at p.46.

²⁰ This issue is returned to below at 8.3.1.3.

8.3 Traditional concepts: Offer and Acceptance

The traditional categories of offer and acceptance are by no means definitive and the courts themselves have emphasised the fluidity in the contract formation process. Sometimes even identifying an offer or an acceptance is problematic.²¹ Nevertheless the courts have re-iterated the value of the traditional approach and are of the view that cases incompatible with the offer and acceptance analysis will be unusual:

“... there may be certain types of contract, though I think they are exceptional, which do not fit easily into the normal analysis of a contract as being constituted by offer and acceptance”²²

Hence the traditional offer and acceptance analysis will form the basis of the following discussion. It is first necessary to distinguish offers from invitations to treat.

8.3.1 Offers and Invitations to Treat

In the search for agreement the law distinguishes offers from invitations to treat. The former can be accepted to form a contract whereas the latter is seen as merely part of the negotiating process or alternatively an invitation to others to make an offer. The basis for the distinction is an objective assessment of the intention of the parties. The courts will consider whether the words or conduct of a party indicate a willingness to be bound should the other party unequivocally accept the terms of the offer. Such willingness distinguishes an offer from an invitation to treat.

A body of case law has developed placing many regularly occurring transactions into a particular category. For example, advertisements, trade circulars, shop windows or displays and auctions are not generally treated as offers but merely as invitations to treat, inviting offers from the public.²³ It is often argued that this approach reflects commercial reality in as much as it relates to the intention of the parties. Illustrating this

²¹ In *Clarke v Dunraven (The Sarania)* [1897] AC 59 an offer and acceptance between the two parties is difficult to find, but nevertheless a binding agreement was found. In the electronic world, E-bay (and other virtual ‘auction’ sites), and group buying sites would appear to require the same analysis with the parties creating a binding agreement between themselves on the common terms of the service provider. See also *Trentham Ltd v Archital Luxfer* [1993] 1 Lloyd’s Rep 25 per Steyn LJ at p 30.

²² *Gibson v Manchester City Council* [1979] 1 WLR 294, per Lord Diplock at 298.

²³ See *Partridge v Crittenden* [1968] 2 All ER 421, *Pharmaceutical Society of Great Britain v Boots Cash Chemists* [1953] 1 QB 401 and *Payne v Cave* (1789) 3 Term Rep 148, respectively.

point, Lord Herschell, when referring to a trade circular in *Grainger & Son v. Gough (Surveyor of Taxes)*²⁴ stated:

“The transmission of such a price list does not amount to an offer to supply an unlimited quantity of the wine described at the price named, so that as soon as an order is given there is a binding contract to supply that quantity. If it were so, the merchant might find himself involved in any number of contractual obligations to supply wine of a particular description which he would be quite unable to carry out, his stock of wine of that description being necessarily limited.”²⁵

To hold that such a circular or advertisement was an offer would leave the seller with no flexibility if, for example, he ran out of stock or received a response from a customer to whom he did not intend to supply his product.²⁶ However, this analysis becomes less convincing once the alternatives available are considered.²⁷ Nevertheless, general classifications of advertisements, circulars and shop displays have become established.

It is important to remember that it is the objective assessment of the words and conduct of the parties in the particular case which will be decisive. Hence, auctions promoted as being ‘without reserve’²⁸ and certain advertisements²⁹ have been construed as offers. With unilateral contracts, the classic case *Carlill v. Carbolic Smoke Ball Co*³⁰ serves as an illustration. The wording of the advertisement combined with the advertiser’s conduct, the depositing of £1000 in its bank to show its ‘sincerity in the matter’, satisfied the court that it should be construed as an offer. In a more recent case, *Boweman v. Association of British Travel Agents Ltd*³¹ Hobhouse LJ re-iterated the point in his analysis of an ABTA notice:

“In my judgement this document is intended to be read and would reasonably be read by a member of the public as containing an offer of a promise which the customer is entitled to accept . . . it satisfies the criteria for a unilateral contract

²⁴ [1856] AC 325.

²⁵ *ibid* at p 334.

²⁶ For example, due to some regulatory or licensing requirement.

²⁷ For example the ‘offer’ could be treated as conditional on there being stock available etc. However, this has not been the approach taken by the courts. See Gatt, *op cit* fn 13 above, and Macdonald, E and Rowland, D. *Information Technology Law* (Cavendish: London, 2000) at p297.

²⁸ *Warlow v. Harrison* (1859) 1 E&E 309. *Barry v. Davies* [2000] 1 WLR 1962.

²⁹ In particular the ‘reward’ or ‘unilateral contract’ cases. See the discussion below of *Carlill v. Carbolic Smoke Ball Co* [1893] 1 QB 256.

³⁰ [1893] 1 QB 256.

³¹ [1996] CLC 456.

and contains promises which are sufficiently clear to be capable of legal enforcement. The principles established in the *Carbolic Smoke Ball* case apply."³²

In the light of these points the most common forms of electronic communication will now be considered.

8.3.1.1 E-Mail and Text Messaging (SMS)³³

As with all forms of communication the courts will deduce from the language used (in addition to relevant conduct)³⁴ whether a party had the requisite intention to be bound in determining whether an offer has been made.

An interesting issue raised by these particular forms of electronic communication relates to the use of 'spam' or unsolicited commercial communications to an e-mail address or mobile phone. In general such communications take the form of advertisements promoting a (usually completely unwanted) product or service. With some of the new generation of mobile phone systems subscribers receive messages relating to promotions in their geographical area or area they are visiting from automated systems. Even though they may be mass promotional communications, such messages will be analysed on the basis of their content to ascertain if an intention to be bound exists. If they are phrased unequivocally, in the form of a promise in return for certain acts, i.e. "The first fifty customers to register on 'anon DVDs dot com' web site will receive the new 'Harry Potter' movie absolutely free",³⁵ the courts may well construe them as offers, binding on the seller once the requested conduct is performed. The senders of the message may argue that such e-mails are merely promotional material or 'mere puffs of advertising' but nevertheless if the words used indicate an intention to be bound they will be construed as unilateral offers, or offers to the whole world. Anyone fulfilling the requirements contained within the e-mail may bind the sender (which in the case of e-mail could be a lot of potential customers).

³² *ibid* at p 463.

³³ 'Short Message Service' (SMS) affords the user the ability to send and receive short (160 characters) text messages to and from GSM (Global System for Telecommunications) mobile phones almost anywhere in the world. Most modern mobile phones accommodate this service.

³⁴ Such as the depositing of £1000 in the bank to settle claims in the *Carlill* case.

³⁵ Based upon an actual e-mail received by the author.

8.3.1.2 Websites

For legitimate commercial entities the most effective form of promotion via electronic media is a collection of pages on a website on the Internet or World Wide Web. Websites can vary in complexity from a basic text format with perhaps a few images, to a framed and fully interactive multimedia site. They are primarily used to promote products and services to a potentially vast audience at relatively low cost but increasingly, with developments in technology, they are also used to facilitate contract formation and actually deliver products or services.³⁶ In the context of the Internet this possibility represents perhaps the most valuable asset inherent in the system. Because websites can be divided into distinct 'types', for the analysis of contract formation it is important to consider whether such sites will generally be construed as offers or invitations to treat.

'Passive Sites'

A website may be used solely for marketing purposes, taking the format of a catalogue or price list with illustrations or descriptions of products or services. If the site does nothing more and is not couched in terms which might suggest a unilateral offer, it will probably be looked upon as an invitation to treat. There is no intention to be bound, just a desire to disseminate information about services or products.³⁷ The courts' analysis of such a site would probably reflect the approach taken by Herschell LJ in *Grainger and Son v. Gough*.³⁸ The courts recognise the need to permit sellers to freely disseminate information about their products or services without the risk of being obliged to supply everyone who sees their promotional material. The seller is not indicating an intention to be bound by advertising his products or services, simply inviting members of the public to consider making an offer.

However, it must also be remembered that, where appropriately worded, the courts will classify promotional materials as offers, capable of being accepted to form binding agreements. A website, which promises something in return for a customer's conduct, will probably be construed as an offer.³⁹ For example, websites offering free

³⁶ The most common service contract entered into by electronic means is for Value Added Network Services (VANS) such as file-storage and electronic mail. The direct download of computer software and the procurement of electronic media products such as music or video are the most popular products delivered electronically. See <http://www.yahoo.com>.

³⁷ The contents of the site may be significant in relation to any representations made therein which may be relevant to the terms of the contract or a subsequent claim for misrepresentation.

³⁸ [1856] AC 325, see above at 8.3.1.

³⁹ See the *Carbolic Smoke Ball* and *Boweman* cases above.

downloads or services in return for the customer filling details in an on-line form leave little room for further negotiation and the supplier would appear to intend to be bound should a customer perform the requested conduct. A popular trend in electronic advertising is the 'Click here for FREE trial' on a page promoting a service or product. On the wording of the advert there would appear to be a clear offer, the free trial in return for the conduct requested - the clicking on the icon.⁴⁰

'Interactive Sites'

Many websites go beyond the basic promotion of products or services and provide the customer with a 'virtual shopping experience', reproducing some of the familiar elements of the self-service store.⁴¹ After perusing the products on offer, the customer selects the items he desires and symbolically places them in his 'virtual basket'. When his selection is complete, he is instructed to click on an icon taking him to the 'checkout'. Once again the analogy can be drawn with the site's real-world counterpart. As stated above, a shop display will usually be treated as an invitation to treat with the customer making the offer by handing the selected goods to the cashier. Somervell LJ illustrates this analysis in *Pharmaceutical Society of Great Britain v. Boots Cash Chemists*:

"I can see no reason for implying from this self-service arrangement any implication other than that, [...] it is a convenient method of enabling customers to see what there is and choose, and possibly put back and substitute, articles which they wish to have and then to go up to the cashier and offer to buy what they have so far chosen"⁴²

The clicking on the 'checkout' or 'purchase' icon is the equivalent of taking the selected items to the cashier or shopkeeper and offering to make a purchase. The

⁴⁰ It may be argued that with such 'free' offers the customer provides no consideration. However, the information provided, usually e-mail address and personal profile, is of considerable commercial value, clearly capable of satisfying consideration requirements. In addition to the 'click' the site will often request credit card details in addition to personal information and e-mail addresses.

⁴¹ In the US this approach has been commonplace for some time. From this approach has developed the 'virtual mall' bringing websites from various well known suppliers 'under one roof' to create a familiar environment for shoppers to have confidence in. For an example of this approach see 'ShopSmart' at <<http://www.barclaysquare.co.uk>> or UK online virtual shopping mall at <<http://www.codehot.co.uk/shopping.htm>>.

⁴² [1953] 1 Q.B. 401 at p 405.

customer makes the offer at that point and the web site owner can then chose whether or not to accept the offer.⁴³

However, an alternative analysis of the website situation is possible. With an interactive shopping website the 'actions' of the website are controlled by the pre-programmed software, programmed by the proprietor or on his behalf, to emulate human decision making. The conclusion of the contract and often the despatching of the goods or provision of the service is performed without the intervention or immediate knowledge of the proprietor. When considered in this way the website demonstrates characteristics similar to the ticket machine in *Thornton v Shoe Lane Parking*.⁴⁴ Although the customer can browse the site and select items he is interested in, choose delivery dates and even add gift wrapping and personal messages, he cannot negotiate the contract, in any real sense, with the software. In this way an argument can be constructed that the website is making a unilateral offer to sell the goods to the customer. If the customer performs the acts requested by the website proprietor – select goods, input delivery and payment details and click on a 'confirm' icon, he can do no more and the automated system does the rest. There is little difference between this situation and Mr Thornton's, when he chose to use the Shoe Lane Car Park. For website proprietors this conclusion would be very unwelcome because it would mean that they would be bound to any mistakes made on the website or by their software. With this in mind many websites, in their website 'terms of use', state that no contract is formed until the proprietor's software has confirmed the despatch of the goods requested.⁴⁵ In this way they are expressly negating any intention to be bound until a specific point, preventing the activities of the site being treated as an offer. In two of the recent erroneous pricing incidents, namely the Amazon mis-priced iPaq Pocket PC and the Kodak £100 digital camera,⁴⁶ the legal advice given turned on the nature of the communications between the parties and in particular the Amazon.com conditions of website use which clearly state that,

⁴³ As is discussed in chapter 3, this may be an automated response rather than a conscious act by the website owner.

⁴⁴ *Op cit* fn 11.

⁴⁵ See the 'Terms of Use' at the bottom of the Amazon.com website. <http://www.amazon.co.uk/>.

⁴⁶ Reported at <http://news.zdnet.co.uk/> 19/03/2003 and 31/01/2002 respectively.

“No contract will subsist between you and Amazon.co.uk for the sale by it to you of any product unless and until Amazon.co.uk accepts your order by e-mail confirming that it has dispatched your product.”⁴⁷

A dispute of this nature has not reached a court yet but as a caveat, it must be noted that the effectiveness of such a clause will depend upon how clearly such terms of use were brought to the user’s attention. The issue of mistakes in the agreement process is considered further below.

In *Thornton* Lord Denning placed emphasis on the fact that Mr Thornton had become irrevocably bound at the moment he inserted his coin, giving him no opportunity to object or get his money back:

“He is committed beyond recall. He was committed at the very moment when he put his money into the machine. The contract was concluded at that time.”⁴⁸

Sir Gordon Willmer also referred to the absence of an opportunity for Mr Thornton to change his mind or withdraw:

“[.]in the case of a ticket which is proffered by an automatic machine there is something quite irrevocable about the process. There can be no locus poenitentiae.”⁴⁹

This factor was clearly influential in their Lordships’ decision. In the majority of website transactions there *will* be an opportunity, or for a consumer a number of opportunities to withdraw from the transaction. This may also be a factor for consideration in the analysis of any electronic contractual process.⁵⁰

However, with automated websites further analysis of the transaction may be necessary to consider whether a ‘counter offer’ is made when the system responds to the customer’s order. Following the submission of his order a customer will usually receive a response from the vendor’s website, containing details of his order and terms and

⁴⁷ *Op cit* fn 45.

⁴⁸ [1971] 2 QB 163, at 169.

⁴⁹ *Ibid* at p 174.

⁵⁰ To an extent the Electronic Commerce and Distance Selling Directives (and implementing regulations) provide opportunities for a consumer to withdraw from an electronic contract in certain circumstances. Discussed above at 7.4.

conditions relating to the transaction.⁵¹ If the response does no more than clarify terms of the original offer in a manner anticipated, then the customer's offer will stand.⁵² However, if new terms are introduced or existing terms are amended then the customer's offer will be extinguished and the response he receives will be an offer from the vendor (or his automated system) which is then open to being accepted or rejected by the customer.⁵³

8.3.1.3 Mistakes and Errors in Contract Formation⁵⁴

If a contractually significant communication contains an error, or is sent or made available by mistake then the question may arise as to whether a party will be bound. Clearly the party will not have the relevant intention on a subjective analysis, but from the objective point of view the courts may consider him bound due to the objective appearance of his intent.

The potential for disputes in this area was highlighted recently when a catalogue of 'errors' on the web-sites of high profile retailers, including Argos, Amazon and Kodak were brought to light in the media.⁵⁵ In all of the incidents an item was illustrated on a website at the wrong price.⁵⁶ In the 'Argos free TV debacle', as it was dubbed,⁵⁷ a television was advertised for two pounds ninety-nine rather than two hundred and ninety-nine pounds. A small computer error, according to the company, but one with considerable impact. The error did not become the subject of court action, but nevertheless led to some academic comment and consideration of the relevant contractual principles. On the basis of the common law principles discussed above there is persuasive argument that in such situations the web pages would be considered no more than invitations to treat. On this basis the retailer was quite entitled to 'reject' the

⁵¹ The most common being terms relating to delivery and product returns, but often more significant terms relating to liability, applicable law and jurisdiction will often be included.

⁵² Being equivalent to further enquiries or simple clarification of the existing terms and conditions. *Stevenson v McLean* (1880) 5 QB 346.

⁵³ Such a response would be considered a counter-offer by the courts. *Jones v Daniel* [1894] 2 Ch 332. This will not only have implications for the timing of the conclusion of the contract but may also affect issues such as jurisdiction (above at 4.4) and incorporation of terms (below at 9).

⁵⁴ Mistakes are also considered in the section on mistaken identity in contract law at 6.3. Here, the focus is a more detailed analysis of errors in pricing and the activities of electronic agents, such as interactive websites.

⁵⁵ See Azim-Kahn, R. & MacQueen, H. L. "The Argos Free TV Debacle: Two Legal Opinions" (1999)1(9) *Electronic Business Law* 9-10; ZDNet News (news.zdnet.co.uk) on 19/03/2003 and 31/01/2002 respectively.

⁵⁶ A regular occurrence in the 'real' world and one which is met with disbelief when the customer is informed that, on the strict letter of the law, the store owner is not obliged to sell the item to them at the marked price.

⁵⁷ See Azim-Kahn, R. & MacQueen, H. L. *op cit* fn.55.

offers made by customers responding to the erroneous advert.⁵⁸ However, the potential exists, particularly with the development of interactive websites, for the 'offer' to be made by the vendor rather than the customer, which the customer may then accept. Alternatively the customer's offer could be accepted by the vendor's automated website.⁵⁹ In these situations the question of whether the seller is bound to sell at the erroneous price will be raised.

It has been indicated that the law takes an objective approach to agreement. Whether the offer was made due to human or computer error the vendor will be bound by his 'apparent' agreement. In *Centrovincial Estates plc v Merchant Investors Assurance Co. Ltd*⁶⁰ the court decided that

"In our opinion... it is contrary to the well established principles of contract law to suggest that the offeror under a bilateral contract can withdraw an unambiguous offer, after it has been accepted in the manner contemplated by the offer, merely because he has made a mistake which the offeree neither knew or could reasonably have known at the time when he accepted it."⁶¹

By implication this judgment suggests a different conclusion where the offeree knows or, as a reasonable person, should have known of the mistake. Hence, in *Hartog v Colin and Shields*⁶² Singleton J concluded that,

"The plaintiff could not reasonably have supposed that the offer contained the offeror's real intention"⁶³

and on this basis could not enforce the agreement against the offeror. If a 'reasonable man' in the position of the offeree ought to have known of the error then he will not be permitted to 'snap up' that erroneous offer.⁶⁴ Clearly there is potential here for arguing that in the Argos case, the erroneous error on the website could not be 'accepted' to

⁵⁸ It must also be remembered that advertisements and other promotional devices are subject to regulation and controlled on public policy grounds. Of particular relevance is the Consumer Protection Act 1987, s.20 (misleading price indications).

⁵⁹ This was the position in the Kodak incident *op cit* fn 55 above.

⁶⁰ [1993] Com. L.R. 158.

⁶¹ *Ibid* per Slade LJ.

⁶² [1939] 3 All E.R. 566.

⁶³ See also *Watkin v Watson-Smith* *The Times*, July 3, 1986.

⁶⁴ See also *Scriven Bros & Co v Hindley & Co* [1913] 3 KB 504.

form a binding contract on the basis that a 'reasonable person' ought to have realised that there was a mistake.⁶⁵

However, there is some debate as to the correct outcome in a situation where the offeree does not know that the 'offer' does not contain the offeror's real intention but does not necessarily believe, or has not formed an opinion on, whether the offeror has the requisite intention. One view is that the offeror is bound because the objective test is satisfied as long as the offeree does not know that the offer does not contain the offeror's intention.⁶⁶ Whilst this approach would appear in line with the dicta in *Centrovincial Estates* there is some criticism of this reasoning and its potentially harsh consequences for the offeror. Professor Atiyah⁶⁷ has criticised the approach taken in the *Centrovincial* case and suggested that the decision in *The Hannah Blumenthal*⁶⁸ casts doubt on *Centrovincial* and similarly decided cases.⁶⁹ In *The Hannah Blumenthal* Brightman L states that "The test in my opinion is not wholly objective"⁷⁰ and he proceeded to emphasise the importance of the offeree's subjective state of mind.

Atiyah argues that the outcome of such cases should not be based on whether a communication can be classified as an offer which has been accepted or not, but rather on a party's reliance on the communication. It is the altering of the offeree's position in reliance on the apparent offer which should give rise to obligations.⁷¹

"Why should an offeree be entitled to create legal rights for himself by the bare act of acceptance when he has in no way relied upon the offer before being informed that it was made as a result of a mistake and did not in reality reflect the intention of the offeror?"⁷²

It can be concluded therefore, that even where there is an objective appearance of an intention to be bound, the subjective state of mind of the offeree may be decisive.

⁶⁵ However, in the modern commercial market this argument may not always be available, particularly where websites are using very low prices or 'loss-leaders', to attract custom. The travel industry is a particularly good example with airlines and holiday firms offering ridiculously cheap deals to the first few customers (a classic example being the 'Hoover free flights' offer in the 1990's).

⁶⁶ *Tankreederei Ahrenkeil GmbH v Frahuil SA (The Multitank Holsatia)* [1988] 2 Lloyds Rep. 486 at 492; *Furness Withy (Australia) Ltd v Metal Distributors (UK) Ltd (The Amazonia)* [1990] 1 Lloyds Rep. 236 at 242.

⁶⁷ Atiyah, P.S. "The Hannah Blumenthal and classical contract law" (1986) 102 (Jul) *Law Quarterly Review (LQR)* 363 - 369 at 368.

⁶⁸ *Paal Wilson & Co. A/S v Partenreederei Hannah Blumenthal* [1983] 1 All ER 34 (HL); [1983] 1 A.C. 854.

⁶⁹ For example *The Leonidas D* [1985] 2 All E.R. 796.

⁷⁰ *Op cit* fn 68 at p 924.

⁷¹ See also Treitel, G.H. *The Law of Contract* 11th ed (2003) p.9.

⁷² *Op cit* fn 66.

It may also be relevant whether his state of mind puts him in a position to suffer some prejudice from reliance on that objective appearance.⁷³

One additional consideration in the electronic environment is the ease with which an error may be made and the speed at which that erroneous communication may reach the other party. Even if a party is aware of the mistake he has made, the nature of electronic communications means that before he has any chance to retrieve the message an automated system may have confirmed the order and concluded the contract. This particular type of mistake has, to an extent, been considered by legislators and as a consequence provisions have been introduced to minimise the risk, particularly in relation to consumers.

The potential for customers to input errors by, for example, hitting the wrong keys or striking the enter key too soon and accidentally concluding a contract, was recognised during the development of the Electronic Commerce Directive.⁷⁴ In the final Directive the following provision can be found in Article 11;

“Member States shall ensure that, except when otherwise agreed by parties who are not consumers, the service provider makes available to the recipient of the service appropriate, effective and accessible technical means allowing him to identify and correct input errors, prior to the placing of the order.”⁷⁵

The opportunity to identify and correct errors, including those which the consumer may not have been aware of when initially inputting his information, was seen as an important factor in the development of trust and confidence in electronic commerce and new technology. The provision does not apply to contracts concluded exclusively by means of electronic mail or equivalent individual communications, which, although the preamble to the Directive states that it should not, has the potential to create a loophole.⁷⁶ It is assumed that with an e-mail you will always have an opportunity to amend it before sending it whereas with an interactive website a customer may not

⁷³ *Ibid.*

⁷⁴ See “Proposal for a European Parliament and Council Directive on certain legal aspects of electronic commerce in the internal market” COM(1998) 586 final. OJ C 030 (05/02/1999) at p. 12.

⁷⁵ Article 11(2). Implemented by the Electronic Commerce (EC Directive) Regulations 2002 (SI 2002 No. 2013). See below at paras. 8.4.3 & 8.4.5.

⁷⁶ Recital (39) “The exceptions to the provisions concerning the contracts concluded exclusively by electronic mail or by equivalent individual communications provided for by this directive, in relation to information to be provided and the placing of orders, should not enable as a result, the by-passing of those provisions by providers of information society services.”

always have the opportunity to check what he has typed.⁷⁷ Nevertheless with e-mail communication mistakes may be made or the message may have been corrupted in transmission.

If the analysis indicates that an offer has been made, a corresponding acceptance is required to form a contract.

8.4 Acceptance

As a general rule the time and place at which acceptance is effective indicates the conclusion of the contract. This 'point' in time is of great significance to the parties indicating the moment at which they become bound and further, the point after which no more terms or conditions may be introduced into the contract.⁷⁸ Although in relation to jurisdictional and applicable law issues, the 'place' acceptance occurred has become less influential, it nevertheless retains a residual role, particularly when one of the parties is domiciled in a non EU or EFTA (EEA) State.⁷⁹

In the electronic environment 'when' and 'where' a contract has been concluded may be difficult to ascertain. This uncertainty has led to much debate as to which rules should apply and also whether legislation should be introduced to clarify the position. Much of the impetus behind attempts to clarify the situation has resulted from the desire to provide a harmonised approach, particularly within the EU, to facilitate and aid the development of electronic commerce. On the need to provide a legal framework for electronic commerce in the internal market the European Commission stated that:

“Moves in certain Member States to enact new legislation are apparent and there are already differences in approach which entail a real risk in the short term of fragmenting the internal market.”⁸⁰

Nevertheless, the starting point for a discussion of the issues remains the common law principles in England and Wales.

Acceptance is the final and unequivocal assent to the terms of the offer. An acceptance should not contain any new terms or variations of the terms of the offer. If it does so, the courts will treat it as a counter-offer and the original offer will be brought to

⁷⁷ In practice the supplier's site will usually send an e-mail to the customer clarifying the order and giving the customer opportunity to check and amend the order where necessary.

⁷⁸ Unless the contract allows for such introduction either expressly or impliedly.

⁷⁹ See chapters 4 & 5 above.

⁸⁰ *Op cit* fn 70 at p.8.

an end.⁸¹ However, if the communication merely seeks to clarify or confirm the detail of the offer it will not be treated as a counter-offer but rather a 'mere inquiry' and the original offer will stand.⁸²

At this point the approach adopted by some interactive websites must be considered. Often the customer's order, which will usually equate to a contractual offer, will be followed by a message (either on screen or via e-mail) from the supplier, or his electronic agent, confirming that the order has been received. However, in addition to this confirmation it is common for the message to include additional terms relating to delivery, choice of forum and applicable law. If this was not clearly provided for in the original offer then this communication will be a counter-offer requiring an acceptance by the customer before the contract is concluded.⁸³

8.4.1 Acceptance: The General Rule

As a general rule acceptance must be communicated to the offeror. Silence may be seen as equivocal and there would have to be compelling evidence to satisfy the court that a contract had been concluded.⁸⁴ However, there are at least two situations where although the offeree is silent an acceptance may still be found.

In a unilateral contract the performance of the conduct stipulated in the offer constitutes acceptance.⁸⁵ Hence, if an e-mail or SMS message offers a 'free gift' in return for your presence at a particular venue, then fulfilling that request will constitute acceptance. Communicating your intent to accept the offer to the offeror is not necessary.

In a bilateral contract, if the offeree is silent but his conduct is unequivocal then the courts may find that the conduct itself provides the objective manifestation of intent required. In *Brogden v Metropolitan Railway Co*⁸⁶ the court upheld the existence of a bilateral contract on the basis of the party's conduct. The railway company did not communicate its acceptance to Brogden but their conduct clearly indicated their intention to accept and Brogden was aware of this conduct. Lord Cairns felt that

⁸¹ *Hyde v Wrench* (1840) 3 Beav 334 and *Jones v Daniel* [1894] 2 Ch 332.

⁸² See Lush LJ in *Stevenson v McLean* (1880) 5 Q.B.D. 346.

⁸³ Even if the original offer was made 'on the suppliers terms and conditions' which provided for this occurrence, questions would still remain as to the effectiveness of such clauses, particularly against a consumer. See below chapters 10 & 11.

⁸⁴ See *Felthouse v Bindley* (1862) 11 C.B. (N.S.) 869, where the facts would appear to support a compelling argument that the nephew had accepted the offer. *c.f. The Hannah Blumenthal* [1983] AC 854.

⁸⁵ See *Carlill v. Carbolic Smoke Ball Co* [1893] 1 QB 256 and *Boweman v. Association of British Travel Agents Ltd* [1996] CLC 456.

⁸⁶ *Brogden v Metropolitan Railway Co* (1877) 2 App Cas 666.

“... approbation was clearly given when the company commenced a course of dealing which is referable... only to the contract, and when that course of dealing was accepted and acted upon by [Brogden] in the supply of coals.”⁸⁷

The conduct was in itself unequivocal and could not be attributed to anything other than acceptance of the offer.⁸⁸ In later cases the courts have emphasised that the conduct must *only* be referable to the contractual document in question, otherwise the courts will not infer that the parties had agreed to that document.⁸⁹ It is also clearly important that the offeror is aware of the conduct.

In addition to establishing what will constitute an acceptance it is also necessary to consider the point at which that acceptance is effective. There must be some “external manifestation of assent” which “the law can regard as communication of the acceptance to the offeror”.⁹⁰ This may take a variety of forms depending upon the nature of the case but in general, communication of acceptance is effective when it is ‘received’ by the offeror or brought to his attention. At what point an electronic communication is actually ‘received’ may be the subject of some uncertainty.⁹¹ However, before this point is considered it is necessary to examine whether a well-established exception to the general rule on acceptance - the postal rule - has a role to play in the electronic environment.⁹²

8.4.2 Acceptance: The Postal Rule

The most significant⁹³ exception to the rule that acceptance is only effective when communicated to the offeror, is the ‘postal rule’. In *Entores Ltd v Miles Far East Corporation*⁹⁴ Lord Denning expressed the rule thus:

⁸⁷ *Ibid* at p 680.

⁸⁸ See also *Trentham Ltd v Archital Luxfer* [1993] 1 Lloyd's Rep 437.

⁸⁹ See Rix J. in *Jayaar Impex Ltd v Toaken Group Ltd* [1996] 2 Lloyd's Rep 437 at p 446.

⁹⁰ *Powell v Lee* (1908) 99 LT 284.

⁹¹ See below at 8.4.3.

⁹² See Murray, A.D. “Entering Into Contracts Electronically: The Real W.W.W.” in Edwards, L. & Waelde, C. (eds) *Law and the Internet: A Framework for Electronic Commerce* 2nd ed. (Hart: Portland, Oregon, 2000) at p. 17 and Downing, S. & Harrington, J. “The Postal Rule in Electronic Commerce: A Reconsideration” (2000) 5(2) *Communications Law* 43.

⁹³ And undeniably the most academically debated. See Houghton, K. & Vaughan-Neil, K. “E-mail and the postal rule” (2001) 12(5) *Computers & Law*, 31-35; Werner, J. “E-commerce.co.uk - local rules in a global net: online business transactions and the applicability of traditional English contract law rules.” (2001) 6 *International Journal of Communications Law and Policy (IJCLP)*; Irish Law Times. “Old commercial law rules: traps for the unwary?” (1995) 13(2) *Irish Law Times (ILT)* 25; Stone, R. “The postal rule in the electronic age.” (1992) 5(Spr) *Student Law Review* 15-16,18; Gardner, S. “Trashing with Trollope:

“When a contract is made by post it is clear law throughout the common law countries that the acceptance is complete as soon as the letter is put into the post box, and that is the place where the contract is made.”⁹⁵

In effect the rule, or more correctly the exception to the general rule, brings the point of contract formation forward. In order to assess the merit of any suggestion that the postal rule should apply to any form of electronic communication, the origin and purpose of the postal rule must first be considered.

The case usually attributed with the ‘creation’ of the rule is *Adams v. Lindsell*⁹⁶. In this case the courts were faced with adjudicating which of the parties should bear the risk of a lost or delayed communication of acceptance. On the facts it would appear that the court placed the risk with the party in error (in this case the offeror), however, that was not the stated reasoning in the case. Lord Ellenborough C.J. felt that the rule was necessary because without it no contract entered into at a distance could be concluded:

“... no contract could ever be completed by the post. For if the defendants were not bound by their offer when accepted by the plaintiffs till the answer were received, then the plaintiffs ought not to be bound till after they had received the notification that the defendants had viewed their answer and assented to it. And so it might go on *ad infinitum*.”⁹⁷

However, as Professor Treitel explains, the potential for infinite communications is avoided with *any* rule whether that rule dictates that the letter becomes effective on posting or delivery; the existence of *a* rule will suffice.⁹⁸ (Although this obvious point did not prevent the debate surfacing in early drafts of the Electronic Commerce Directive in the Commission’s attempts to clarify the point of contract formation).⁹⁹ Gardner

a deconstruction of the postal rules in contract.” (1992) 12(2) *Oxford Journal of Legal Studies* 170-194; Morrison, P. “E-Commerce In The Construction Industry” (2002) 7.1 *Con & Eng Law* 7; Glatt, C. “Comparative Issues In The Formation Of Electronic Contracts” (1998) 6 *IJL & IT* 34.

⁹⁴ [1955] 2 All E.R. 493

⁹⁵ Lord Denning in *Entores Ltd v Miles Far East Corporation* [1955] 2 All E.R. 493; [1955] 2 Q.B. 327 at p. 331.

⁹⁶ (1818) 1 B & Ald 681. However, this case was in fact decided before any general rule that acceptance must be communicated existed, see Simpson, “Innovation in Nineteenth Century Contract Law” (1975) 91 *Law Quarterly Rev* 247.

⁹⁷ *Ibid*.

⁹⁸ Treitel, G.H. *The Law of Contract* 10th ed. (Sweet & Maxwell: London, 1999) at p. 24. See also Gardner S, “Trashing with Trollope: A Deconstruction of the Postal Rules in Contract” (1992) 12 *OJLS* 170.

⁹⁹ A debate which bore a striking resemblance to Lord Ellenborough’s statement in *Adams v. Lindsell*.

suggests that the court's reasoning in *Adams v. Lindsell* was rather more focussed on an older subjective notion of contract than practicality:

“Perhaps the best explanation for the court's choice of posting is that on the facts of the case this view involved the lesser departure from the *consensus* model. At posting, the parties happen simultaneously to contemplate contracting together...; whereas by the time of the letter's delivery the defendants no longer intended contracting with the plaintiffs.”¹⁰⁰

Here what must be emphasised is that, for whatever reason, in *Adams v Lindsell* the court decided that a letter of acceptance would be effective on posting.

In later cases, further justifications for the postal rule were put forward. In *Household Fire and Carriage Accident Insurance Co v. Grant*¹⁰¹ Thesiger LJ suggested agency as a basis for the rule. In attempting to reconcile the need for communication of acceptance to the offeror with the postal rule and the principle of *consensus ad idem* he continues:

“How then are these elements of law to be harmonised in the case of contracts formed by correspondence through the post? I see no better mode than that of treating the post office as the agent of both parties.”¹⁰²

Faced with such irreconcilable principles the concept of agency was a convenient distraction, but as was stated at the time¹⁰³ and has been stated many times since, the idea that the post office is an agent of both parties for such communications is but a fiction.¹⁰⁴ It must be said that a consistent and sustainable justification for the postal rule is difficult to ascertain:

“The decisions which established these rules offered various justifications for them, but it has for some time been accepted that these justifications are not

¹⁰⁰ Gardner, *op cit* fn 94, at p. 171.

¹⁰¹ (1879) 4 Ex D 216, 223-4.

¹⁰² *Ibid* at 221.

¹⁰³ See the dissenting judgment of Bramwell L.J. at p 238.

¹⁰⁴ See Atiyah *Introduction to the Law of Contract* 5th ed. (Oxford: Clarendon Press, 1995) at p. 71; Macdonald, E & Rowland, D. *Information Technology Law*. 2nd ed. (Cavendish: London, 2000) at p305; Downing and Harrington (2000) 5(2) *CommL* 43; Gardner “*Trashing with Trollope: A deconstruction of the Postal Rules in Contract*” [1992] 12 *OJLS* 170, 173.

wholly successful. It has proved harder, however, to find satisfactory alternative explanations.”¹⁰⁵

Presented with the task of apportioning a loss due to a failure in the communication of acceptance by post, the courts chose to favour the offeree. The risk of loss or delay in the post through neither party’s fault had to be placed on one party or the other. The apparent injustice created by such allocation has been tempered by the acknowledgement that the offeror may readily exclude the effect of the rule.¹⁰⁶ In addition the rule should not apply where the offeree is at fault through, for example, failing to correctly stamp and address the communication or where the rule’s application would result in ‘manifest inconvenience or absurdity’.¹⁰⁷

However, further consideration has been given to the scope of application of the postal rule in relation to more modern forms of communication. In particular, the question of its application to telex or fax has been addressed and can provide some guidance to the likelihood of its use in the context of e-mail or web-based contracting.

In *Entores Ltd v Miles Far East Corporation*¹⁰⁸ the Court of Appeal was invited to consider the extension of the postal rule to telex communications. In rejecting this possibility Denning LJ emphasised the ‘instantaneous’ nature of telex communication as a decisive factor in the decision:

“My conclusion is that the rule about instantaneous communications is different from the rule about the post. The contract is only complete when the acceptance is received by the offeror; and the contract is made at the place where the acceptance is received.”¹⁰⁹

However, in his judgment Lord Denning did not discuss the underlying principles or purpose of the postal rule; rather he concentrated on the relative knowledge of the parties in relation to a failed or delayed communication. In his assessment, the party at fault or who should reasonably have known of an error or problem will be ascribed the risk of any subsequent loss. Where this assessment does not indicate that one party was in a better position to know of the error, Lord Denning felt that there was no need to

¹⁰⁵ *Ibid* Gardner, referring to the decision of the Court of Appeal in *Henthorn v. Fraser* [1892] 2 CH 27.

¹⁰⁶ *Hokwell Securities v Hughes* [1974] 1 All E.R. 161.

¹⁰⁷ *ibid per* Lawton LJ at p. 168.

¹⁰⁸ [1955] 1 Lloyd's Rep. 511; [1955] 2 Q.B. 327.

¹⁰⁹ *Ibid* at p 515.

depart from the general rule on communication of acceptances when dealing with 'instantaneous' forms of communication.¹¹⁰

In the more recent case of *Brinkibon v Stahag Stahl und Stahlwarenhandelsgesellschaft mbH*¹¹¹ the House of Lords was faced with a situation similar to that in the *Entores* case. Once again the possibility of extending the postal rule principles to telex communication was rejected. However, the court was more forthcoming with a discussion of underlying principles and reasoning. Referring to *Harris's Case*¹¹² and *Household Fire and Carriage Accident Insurance Co v. Grant*¹¹³ Lord Wilberforce stated his view of the rationale behind the postal rule. In his judgment he acknowledged that the rule's development could, in part, be attributed to the potential for fraud and other unscrupulous behaviour should the general rule on acceptance be applied to the post.¹¹⁴ He also emphasised that the exception relating to postal acceptances had its "foundation in convenience".¹¹⁵ Arriving at the same conclusion Lord Fraser explained the practical convenience of the postal rule in the light of the inevitable delay associated with the delivery of a letter. However, he continued to express his disquiet regarding the 'instantaneous communication' distinction:

"There is very little, if any, difference in the mechanics of transmission between a private telex from one business office to another and a telegram sent through the Post Office, especially one sent from one large city to another. Even the element of delay will not be greatly different in the typical case."¹¹⁶

However, he continued that a telex sent directly between acceptor's and offeror's offices should be treated 'as if it were an instantaneous communication'.¹¹⁷ His reasoning was thus:

"One reason is that the decision to that effect in *Entores Ltd v Miles Far East Corp* [...] seems to have worked without leading to serious difficulty or complaint

¹¹⁰ For some time the focus of debate has been the issue of whether communication is 'instantaneous' or not. However, even Denning conceded that communications such as telex were, at best, 'virtually instantaneous' indicating that perhaps this issue was not the focus of his reasoning?

¹¹¹ [1983] 2 A.C. 34.

¹¹² (1872) LR 7 Ch App 587.

¹¹³ (1879) 4 Ex D 216.

¹¹⁴ For example the offeree denying the existence of a contract should the deal turn sour in the time between posting and delivery.

¹¹⁵ Reiterating the words of Lord Thesiger *op cit* fn 98 at p224.

¹¹⁶ *Op cit* fn 107 at p 43.

¹¹⁷ *Ibid* emphasis added.

from the business community. Secondly, once the message has been received on the offeror's telex machine, it is not unreasonable to treat it as delivered to the principal offeror, because it is his responsibility to arrange for prompt handling of messages within his own office. Thirdly, a party (the acceptor) who tries to send a message by telex can generally tell if his message has not been received on the other party's (the offeror's) machine, whereas the offeror, of course, will not know if an unsuccessful attempt has been made to send an acceptance to him. It is therefore convenient that the acceptor, being in the better position, should have the responsibility of ensuring that his message is received."¹¹⁸

To deal with these reasons individually, the first is an observation relating to the practicality of the rule. While the validity of this statement could be debated either way, it does not really indicate a principle of law. The second of Lord Fraser's observations does not relate to the application of the postal rule at all, but rather to the general rule and the point at which acceptance is deemed to be received by the offeror.¹¹⁹ The third point, and arguably the basis of the decision, relates to the allocation of risk of a failure in communication to the party in the best position to be aware of such failure. This will inevitably be the offeree because, in the usual course of events, only he will be aware that an acceptance has been sent.

It is debatable whether in this or the *Entores* case the court's adjudication was based on whether the method of communication was instantaneous or not. Rather the underlying rationale was whether in the normal course of events errors or failures in delivery of the communication would be apparent to either party. With a letter sent by post, the sender cannot reasonably be expected to know that the letter has been delayed or lost. With telex and other forms of communication a considerable delay is not 'inevitable' and there is a persuasive argument that one or other party may reasonably be expected to be aware of a problem within a short period of time. In addition, in both of the cases the court emphasised that if there was an element of fault in relation to the delivery of the communication, then the culpable party would bare the risk of any subsequent loss.

In spite of the reluctance to extend the postal rule to telex the courts appear to have left some discretion for further exceptions to the general rule:

¹¹⁸ *Ibid.*

¹¹⁹ This issue is returned to below at 8.4.3.

“No universal rule can cover all such cases; they must be resolved by reference to the intentions of the parties, by sound business practice and in some cases by a judgment where the risks should lie.”¹²⁰

Although in his judgment Lord Wilberforce is referring to telex communication this passage does reinforce the suggestion that the courts will take a pragmatic approach when confronted with a similar problem. The introduction and increased use of the postal system resulted in particular problems for the courts to solve. The solution was the ‘postal rule’ and that is exactly what it is - a rule for the post. As Professor Atiyah states:

“... the rule must now be accepted for what it is, no better and no worse than any other solution of a practical problem.”¹²¹

With the dramatic increase in the use of modern electronic forms of communication the courts may once again be required to find a solution to a difficult problem. Faced with parties in dispute as to if, when, or where a contract has been formed, when messages have been sent via e-mail or some other form of electronic communication, the courts may be required to decide between the ‘receipt’ and ‘despatch’ rule in their adjudication. This does not necessarily mean that the solution applied to an earlier problem can be transferred to the new situation. However, without legislative intervention the courts will be bound to interpret the rather unsatisfactory case law in order to resolve the dispute.

Some commentators have suggested that the postal rule may be applied to e-mail communication but not to online transactions, such as interactive websites.¹²² E-mail demonstrates many features similar to the postal system. After the point of despatch the sender of the communication has very little control over what happens to it and he has done ‘all he can do’ in handing control over to a third party. There is inevitably some

¹²⁰ Lord Wilberforce in *Brinkibon v Stahag Stahl und Stahlwarenhandels-gesellschaft mbH* [1983] 2 A.C. 34 at p 42, referring to the multitude of possible telex communication scenarios. His sentiments were echoed by Lord Fraser at p 43.

¹²¹ Atiyah, *op cit* fn 100.

¹²² See; Murray, A.D. “Entering Into Contracts Electronically: The Real W.W.W.” in Edwards, L. & Waelde, C. (eds) *Law and the Internet: A Framework for Electronic Commerce* 2nd ed. (Hart: Portland, Oregon, 2000) at p. 26 and Downing, S. & Harrington, J. “The Postal Rule in Electronic Commerce: A Reconsideration” (2000) 5(2) *Communications Law* 43.

form of delay with the use of e-mail because more often than not the two parties are not communicating simultaneously. It has been suggested that the postal rule should be reformulated in the 'twenty-first century', focussing on the nature of the communication itself.

“Where an offer contemplates acceptance by a non-immediate form of communication, that acceptance is effective from the time it leaves the acceptor’s control.”¹²³

However, as Murray observes, such a definition is heavily reliant on the distinction between immediate and non-immediate forms of communication; a volatile and difficult distinction at present and one which may become increasingly blurred in the future. More importantly however, it is a distinction based on the references to ‘instantaneous communication’, which, it is argued above, detract from the substantive reasoning of the courts in the *Entores* and *Brinkibon* cases.

The treating of a contractually significant communication in different ways, solely on the basis of the means of communication adopted is difficult to justify. The difficulty is highlighted by the attempts to identify the rationale behind the introduction of the postal rule in order to ascertain whether it is applicable to other forms of communication. New forms of electronic communication raise new legal questions and it is important that a sound rationale forms the basis of their treatment by the law. Without a sound rationale for different treatment or alternatively a uniform approach to the treatment of all forms of communication there will be uncertainty in the law.

In the more recent cases addressing the issue, the courts have placed the emphasis on the allocation of risk and a consideration of which party is in the better position to know of, and take action on, a failure in communication. Within this rationale the courts have re-enforced the application of the general rule on the communication of acceptance. With telex communication a delay is quite possible and at times inevitable. Although the same can be said of e-mail and other forms of electronic communication, in relation to telex, the courts have not found it necessary or desirable to make an exception to the general rule on acceptance on the grounds of commercial or judicial convenience. It is submitted that the case will be the same for e-mail and other forms of electronic communication.

¹²³ See Murray *ibid*

One of the few clear points to arise out of this analysis is that if the offeror is at fault in some way in not receiving an acceptance or delaying its receipt, the court will rule in favour of the offeree. In the electronic environment, if a party fails to download or read e-mail or data from a website, or fails to ensure that an interactive website is dealing effectively with communications of acceptance, a court may rule that in law he has 'received' that communication and is thereby bound.

8.4.3 When is an Electronic Communication of Acceptance 'Received'?

If the courts decide that the general rule on acceptance applies to an electronic communication, so that it must be received to be effective, then the crucial issue becomes the time and place of *receipt* of that communication. In the electronic environment there are numerous identifiable points along the communications network at which a communication may be considered 'received' by the addressee.¹²⁴

In the assessment of whether a communication has been 'received' the objective approach to agreement adopted by the courts of England and Wales must be considered. It would appear that 'actual' communication to the offeror or to an agent is not necessary. Statements supporting this suggestion can be seen, in the context of telex communication, in the speeches of Lord Denning in *Entores* and Lord Fraser in *Brinkibon*. Lord Fraser stated that:

"... once the message has been received on the offeror's telex machine, it is not unreasonable to treat it as delivered to the principal offeror, because it is his responsibility to arrange for prompt handling of messages within his own office."¹²⁵

As a *caveat*, however, it must be accepted that if a communication arrives at a time when it would not be reasonable to expect the offeror to receive communication of acceptance then this principle will not apply. For example, if a communication were to arrive outside of office hours, then the offeror cannot reasonably be said to have 'received' it until the beginning of the next working day.¹²⁶

¹²⁴ For example, the point at which an e-mail arrives at his service provider's server or the point at which the e-mail is downloaded to the recipient's computer.

¹²⁵ *Op cit* fn 107, per Lord Fraser at p. 43.

¹²⁶ See Gatehouse J in *Mondial Shipping and Chartering BV v Astarte Shipping Ltd* [1995] CLC 1011. His comments were in the context of contractual notice rather than acceptance of an offer, but the principle is consistent. See also *Schelde Delta Shipping B.V. v Astarte Shipping Ltd (The Pamela)* [1995] 2 Lloyd's Rep 249.

If a business party is using e-mail, a website or other form of electronic communication then Lord Fraser's treatment of telex can readily be applied, placing the responsibility to efficiently handle communications on the offeror. However, the nature of the electronic environment raises yet another important question; what are the 'office hours' of the on-line environment? The lack of geographical and temporal constraints on the Internet means that it is conceivable, or arguably *usual* for interactive websites to operate twenty-four hours a day. This is after all one of the main advantages of electronic commerce. For the purpose of this present discussion it could be argued that the 'office hours' are all-day every-day. This would suggest that as soon as a message of acceptance is received on the service provider's site it is effective. The service provider may attempt to limit the virtual office hours of the site to specific period, within which he or his staff are able to monitor the communications. Naturally the site owner will have to state which time-zone he is referring to (GMT for example) if wishing to restrict his 'office hours'. The problem with adopting this approach would be the risk that such restrictions may deter custom from individuals in different time zones, removing one of the key benefits of the electronic environment.¹²⁷

In *Entores* Lord Denning emphasised the point that if the offeror is at fault in some way he may be "estopped from denying the receipt of the acceptance where it would be reasonable to expect him to ensure that the message is received."¹²⁸ Hence, the collection or 'prompt handling' of communications will clearly be the responsibility of the party using the technology, as will be the maintenance of that technology (this is analogous to ensuring that a telex machine does not run out of paper). Lord Wilberforce's declaration that no universal rule can cover all cases and that reference must be made to not only the parties' intentions but also "sound business practice"¹²⁹ and risk allocation must also be remembered. This pragmatic approach is particularly relevant when the wide range of business practice in the electronic environment is considered. The key question for the purpose of this discussion is; how may this objective view of receipt be applied to electronic forms of communication?¹³⁰

With web-based and e-mail communications there are various points at which the communication could be considered received - when downloaded to the offeror's

¹²⁷ This may explain why many commercial websites do not restrict their 'business hours' and have 24hr helplines.

¹²⁸ *Op cit* 104 per Lord Denning at p. 515.

¹²⁹ *Op cit* fn 107.

¹³⁰ For an interesting comparison with the German civil system on this point see; Niemann, Jan-Malte. "Cyber Contracts - A Comparative View On The Actual Time of Formation." (2000) 5,2 *CommL* at p48.

computer or when it arrives on the server from where he is able to access the communication. By analogy with Lord Fraser's statement in *Brinkibon*, it has been suggested that as the offeror is responsible for the 'prompt handling of messages', the arrival in the offeror's electronic mailbox on the server is the appropriate point.¹³¹ However, the distinction has also been made between an offeror operating his own server and one utilising an Internet Service Provider's facilities.¹³² The communication in the former being 'received' when it arrives on the server and in the latter only being 'received' when it is downloaded from the server. In any event, with an objective approach the point at which the communication is considered received will vary depending on the factual scenario. However, this approach does create an unfortunate amount of uncertainty, particularly for parties looking to commercially exploit the electronic environment. This has led to a perceived need amongst service providers to explicitly state the intended legal consequences of every communication. Whilst this does give the illusion of creating certainty it makes websites cumbersome, containing extensive terms and conditions which, in any event, may be ineffective in the face of local rules and legislation in different jurisdictions.¹³³

8.4.3 Regulatory Clarification of the Point of Acceptance?

The 'receipt' of electronic communications has been addressed in both the UNCITRAL Model Law and the Electronic Commerce Directive. While the question of whether that communication is an acceptance and whether acceptance is effective on despatch or receipt will remain to be decided by the courts on the basis of common law principles, the provisions in these instruments, the Electronic Commerce Directive in particular, may influence the court's assessment of when that communication is received.

8.4.3.1 The UNCITRAL Model Law on Electronic Commerce.¹³⁴

The UNCITRAL Model Law on Electronic Commerce contains the following provision which deals with the time and place of despatch as well as receipt:

¹³¹ The equivalent to the arrival on the telex machine. See Rowland and Macdonald, *op cit* fn 27 at p. 306.

¹³² See Chissick, M. and Kelman, A. *Electronic Commerce: Law and Practice*, 2nd ed. 2000, (Sweet and Maxwell: London, 2000) at para. 3.45.

¹³³ See chapter 4 above.

¹³⁴ General Assembly Resolution 51/162 of 16 December 1996, UNCITRAL Model Law on Electronic Commerce. Available at, <http://www.uncitral.org/english/texts/electcom/ml-ecomm.htm>.

Article 15

(1) Unless otherwise agreed between the originator and the addressee, the dispatch of a data message occurs when it enters an information system outside the control of the originator or of the person who sent the data message on behalf of the originator.

(2) Unless otherwise agreed between the originator and the addressee, the time of receipt of a data message is determined as follows:

(a) if the addressee has designated an information system for the purpose of receiving data messages, receipt occurs:

(i) at the time when the data message enters the designated information system; or

(ii) if the data message is sent to an information system of the addressee that is not the designated information system, at the time when the data message is retrieved by the addressee;

(b) if the addressee has not designated an information system, receipt occurs when the data message enters an information system of the addressee.

(3) Paragraph (2) applies notwithstanding that the place where the information system is located may be different from the place where the data message is deemed to be received under paragraph (4).

(4) Unless otherwise agreed between the originator and the addressee, a data message is deemed to be dispatched at the place where the originator has its place of business, and is deemed to be received at the place where the addressee has its place of business. For the purposes of this paragraph:

(a) if the originator or the addressee has more than one place of business, the place of business is that which has the closest relationship to the underlying transaction or, where there is no underlying transaction, the principal place of business;

(b) if the originator or the addressee does not have a place of business, reference is to be made to its habitual residence.

An 'information system' is defined as 'a system for generating, sending, receiving, storing or otherwise processing data messages'.¹³⁵ A data message 'enters' an information

¹³⁵ Article 2(f)

system at the time when it becomes available for processing within that information system.¹³⁶

The message is considered despatched when it “enters an information system outside the control of the originator, which may be the information system of an intermediary or an information system of the addressee.”¹³⁷ So for example, if an e-mail is being sent from an individual’s PC, the moment that the message leaves the sender’s outbox it enters the Internet Service Provider’s system from where it will proceed to the senders mail-host.¹³⁸ From the moment of clicking ‘send’ the data message moves to a system beyond the sender’s control. When using an interactive website the information input by the customer (the data message) enters the service provider’s system when the ‘submit’ icon is clicked.

The time of receipt is defined with reference to whether the recipient has ‘designated an information system for the purpose of receiving data messages’ or not. A ‘designated information system’ is intended to include the situation where a party has specified an address for the receipt of a data message, for example a communication of acceptance, but not the situation where an address is simply included on a website or other documentation without any specific indication that it should be used for such purposes.¹³⁹

To summarise the provision – if a system is specified or designated by the addressee the message is deemed received when it is available for processing on that system. So, for example, as soon as an e-mail is available for downloading on the web-host’s server it is deemed received. As soon as information is submitted on a supplier’s interactive website it is available for processing and hence, deemed received. Consequently, if the data message in question were to be a legal acceptance then it would be effective at that point. If the message is sent to a system other than the one specified then it is only received when the addressee actually retrieves the message from the system. In this case the e-mail would only be deemed received when the recipient has actually downloaded the message or information to his machine or accessed the information remotely from his server. If the addressee does not specify a system then the message will be deemed received when it is available for processing on *an* information system of the addressee. This once again places the onus on the recipient to

¹³⁶ Guide to Enactment of the UNCITRAL Model Law on electronic Commerce (1996) at para. 103.

¹³⁷ *Ibid* para.101.

¹³⁸ In many cases these will be one and the same.

¹³⁹ *Op cit* fn 133 at para.102.

specify the address for significant communications or to maintain a continuous check on all of his addresses or sites. While this approach may be suitable for business parties, putting the onus on them to handle their communications efficiently, it is arguably not a suitable system for the individual or consumer.

If it is not 'otherwise agreed by the parties', then the message of acceptance may be deemed received and therefore effective at a point before the offeror has read or may even be aware that the message exists. This places the onus very firmly with the party making the offer. If you are aware that you have an 'offer' 'out there' and you have indicated an address and mode of communication it is reasonable to make you responsible for dealing with those messages efficiently.

The Model Law does not explicitly deal with the issue of whether the message is intelligible or useable by the addressee or take into account system down-time or faults. This may be seen as a potential flaw. In relation to the attribution of data messages the Model Law does however incorporate an approach similar to the common law position to the 'snapping up' of erroneous offers (discussed above 8.3). Article 13 is intended to prevent the originator of a message from denying that the message, as received, was the one sent by him or on his behalf. If a data message is received with errors and the recipient "...knew or should have known,[..], that the transmission resulted in any error in the data message as received" he will not be entitled to assume that the message is as the originator intended to send, or act upon that assumption.¹⁴⁰

8.4.3.2 The Electronic Commerce Directive

The Directive does not explicitly deal with contractual acceptance but it does indicate the point at which a communication is deemed to be received. If the communications referred to happen to be the contractual acceptance, then the relevant provision may be of influence in the court's adjudication. Article 11 of the Electronic Commerce Directive deals with 'receipt' of a data message in the context of the placing of an order with a service provider and the service providers' obligation to acknowledge the receipt of that order.¹⁴¹

¹⁴⁰ Article 13(5) and para 90. In the preliminary materials to the proposed UNCITRAL Convention on Electronic Contracting (A/CN.9/WG.IV/WP.95 available at <http://www.uncitral.org>) the issues of input mistakes and transmission errors are discussed and it is suggested that in certain situations natural persons may not be bound by such errors when contracting with automated systems. See chapter 3.2, above.

¹⁴¹ Communications which may, or may not amount to an offer and acceptance on the application of the principles discussed above.

“- The order and acknowledgement of receipt are deemed to be received when the parties to whom they are addressed are able to access them.”¹⁴²

The phrase ‘able to access them’ leaves some scope for interpretation. The Regulation implementing the Directive in the UK¹⁴³ imports the phrase verbatim in regulation 11(2)(a) and the Guidance for Business suggests that when the message is ‘capable of being accessed’ by the recipient it will be deemed received, which adds little.¹⁴⁴ The meaning of ‘access’ is not further clarified and it is stated that its meaning ‘may vary according to the circumstances’.¹⁴⁵ During system downtime, there would be scope for an argument that the message is not capable of being accessed by the intended recipient. However, if the system downtime is controlled by the recipient or is due to his poor maintenance this may be a factor, particularly if the courts are faced with an allocation of risk for losses incurred. Even if the message is ‘capable of being accessed’ it would appear necessary to consider whether it is reasonable to expect the recipient to access it at that time. A message sent in the middle of the night is ‘capable of being accessed’ but if the recipient is a consumer or even a small business with restricted business hours then it is surely not reasonable to deem a contractually significant message as ‘received’. The Article does not explicitly deal with contract formation and hence, it is open to the courts to adopt whichever approach they deem appropriate. To this end the uncertainty as to the time of ‘receipt’ of a message and hence, the point at which a contract is concluded, remains.

8.4.5 Contract Formation and the Electronic Commerce Directive: A Missed Opportunity?

One of the five key issues to be addressed by the Electronic Commerce Directive¹⁴⁶ was the on-line conclusion of contracts. Disparities in the legal approach adopted in different Member States to the formation of electronic contracts, could have a detrimental effect on the economic benefit to be gained from the development of

¹⁴² Article 11.

¹⁴³ The Electronic Commerce (EC Directive) Regulations 2002, S. I. 2002 No. 2013.

¹⁴⁴ Guidance for business on the Regulations 5.29 (a) available at <http://www.dti.gov.uk/cii/docs/ecommerce/businessguidance.pdf>

¹⁴⁵ *Ibid.*

¹⁴⁶ Directive 2000/31/EC of The European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market (Directive on electronic commerce) OJ L178/1.

electronic commerce.¹⁴⁷ The European Parliament¹⁴⁸ in its report on electronic commerce in May 1998 observed that,

“The conclusion of contracts electronically in a transfrontier and networked environment brings about a number of important questions which will have to be addressed in order to facilitate electronic commerce transactions across borders. For instance, the determination of where and when an electronic contract is concluded and which country’s law is applicable, could be addressed differently by the Member States. These questions... should be clarified in order to facilitate electronic contracting within the EU.”¹⁴⁹

In addition to facilitating their use, it was hoped that the Directive would remove “legal insecurity by clarifying in certain cases the moment of conclusion of the contract...”.¹⁵⁰ Unfortunately the final Directive fell short of this stated goal. In fact, it may well be that the goal itself was responsible for its downfall.

The provision introduced to “determine clearly the time at which the contract is concluded”¹⁵¹ could be found in the original draft of Article 11. The Article was entitled ‘Moment at which the contract is concluded’ and read;

“Member States shall lay down in their legislation that, save where otherwise agreed by professional persons, in cases where a recipient, in accepting a service provider’s offer, is required to give his consent through technological means, such as clicking on an icon, the following principles apply:

- (a) the contract is concluded when the recipient of the service:
 - has received from the service provider, electronically, an acknowledgment of receipt of the recipient's acceptance, and

¹⁴⁷ Particularly the different approach in systems based in the common law to those developed on the basis of Roman Law in the civil system.

¹⁴⁸ Committee on Economic and Monetary Affairs and Industrial Policy.

¹⁴⁹ “Report on the communication from the Commission to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions on a European Initiative in Electronic Commerce” (COM(97)0157 - C4-0297/97). (A4-0173/98) at p 21. This opinion was echoed by other Community bodies in the subsequent ‘Proposal for a European Parliament and Council Directive’ COM(98) 586 final; Official Journal C30, 05/02/99. Available at; <http://www.ispo.cec.be/ecommerce/legal/documents/legalframew/legalen.pdf>.

¹⁵⁰ Proposal for a European Parliament and Council Directive on certain legal aspects of electronic commerce in the internal market” COM(1998) 586 final. OJ C 030 (05/02/1999). Executive Summary at p.4.

¹⁵¹ *Op cit* 146, at p 27.

- has confirmed receipt of the acknowledgment of receipt;”¹⁵²

The Article respected party autonomy by excluding ‘professional persons’ from its application where they had express provision in their agreement.¹⁵³

The fact that the proposed Article only covered situations where the recipient responded to a service provider’s offer appeared to immediately restrict its application.¹⁵⁴ Whilst it could be argued that it is unlikely that the phrase was intended to mean ‘contractual offer’ in the sense discussed above, some of the background material would suggest otherwise. The Commission clearly stated that the Article only addressed the situation whereby

“- a concrete offer made by a service provider (the situation in which the service provider only issues an invitation to offer is not covered).”¹⁵⁵

The provision also appeared to add complexity to the process of forming electronic contracts by requiring an additional communication from both parties before a contract was concluded. This requirement led some authors to dub the Article the ‘ping-pong’ provision.¹⁵⁶ In England and Wales, if the service provider has made an ‘offer’ in the legal sense and the customer has communicated his ‘acceptance’ of that offer, then the contract is complete. *Prima facie*, the wording of this early provision appeared to require the abandonment of the traditional analysis by requiring two further communications before the contract is concluded. The draft Article was also criticised by the European Parliament in their draft report on the proposed Directive:

“On the surface this procedure appears rather cumbersome: while it is quite normal for the recipient to receive confirmation from the service provider so as to be certain that his or her order has been recorded, it appears rather strange to require the recipient to restate his or her desire to conclude the contract.”¹⁵⁷

¹⁵² *Ibid* at p 45.

¹⁵³ A phrase intended to allow businessmen the freedom to conduct business as they desired, later rephrased to ‘parties who are not consumer’.

¹⁵⁴ Primarily because in the most common commercial scenarios it is the customer who makes the offer.

¹⁵⁵ *Op cit* fn.146 at p 26.

¹⁵⁶ See, Lodder, A “Legal Aspects of Electronic Commerce” (2000) *European Network For Legal Information, Study and Training (ENLIST)*. <http://itlaw.law.strath.ac.uk/ENLIST/subjects/ec/commentary/>.

¹⁵⁷ European Parliament Committee on Legal Affairs and Citizens’ Rights “Draft Report on the proposal for a European Parliament and Council Directive on certain legal aspects of electronic commerce in the internal market.” 10th February 1999 A4-0000/99, DOC_EN\PR\370\370547 at p 31.

Although the stated purpose of the Article was to clarify the point of contract formation, it is clear that the focus of the Commission was the protection of individuals against becoming bound inadvertently or accidentally. In doing this they isolated one particular form or method of electronic contracting.

“The Article addresses a specific situation:

- a contractual process in which the recipient of the service only has the choice of clicking “yes” or “no” (or the use of another technology) to accept or refuse an offer.”¹⁵⁸

Rather than being a provision to deal with difficult contractual issues in general, it became absorbed in one particular cause for concern with electronic contracting. In the drafting, the proposal added complexity and lacked clarity, leaving the potential for disparate implementation in the Member States. The final removal of any attempts to harmonise national laws in relation to the conclusion of contracts came when the Council adopted its Common Position:

“The Council considered that it was not appropriate to harmonise national law regarding the moment at which a contract is concluded. For this reason Article 11 has been renamed and now limits itself to certain requirements regarding the placing and receipt of orders on-line.”¹⁵⁹

The Commission was clearly frustrated at the lack of willingness in Council and Parliament to accept its attempt to harmonise the law relating to electronic contract formation. This was expressed in their communication to the European Parliament:

“In order to facilitate rapid adoption of the Directive, which is a matter of urgency, the Commission has accepted these changes to its amended proposal.”¹⁶⁰

¹⁵⁸ *Op cit* fn 146 at p.26.

¹⁵⁹ Common Position (EC)No 22/2000 adopted by the Council on 28 February 2000 “with a view to adopting a Directive 2000/.../EC of the European Parliament and of the Council of ...on certain legal aspects of information society services, in particular electronic commerce, in the internal market” (‘Directive on electronic commerce’). OJ C128/32 (8.5.2000) at 49.

¹⁶⁰ SEC(2000) 386 final 1998/0325 (COD).

In the final Directive the Commission's desire to protect against parties being bound accidentally or in error is fulfilled with the insertion of the requirement that service providers

“make available to the recipient of the service appropriate, effective and accessible technical means allowing him to identify and correct input errors, prior to the placing of the order.”¹⁶¹

It is unfortunate that the Commission did not focus on clarifying uncertainties in the formation of electronic contracts in general, rather than this particular problem. However, it is conceded that whatever the terminology used, in such a measure significant resistance would probably have still been encountered in the Council.

Nevertheless, the opportunity remained for some consideration of this important issue in the implementing Regulations of the Directive.

8.4.5.1 The Electronic Commerce (EC Directive) Regulations [2002]¹⁶²

The Article adopted in the final Directive is solely concerned with the placing of the order and associated obligations of the service provider. Nevertheless, the UK Government had an opportunity to clarify the point of contract formation in its transposition of the Directive into domestic law. However, as is the case with the majority of the Directive, the implementing Regulations import the terminology wholesale from the relevant Articles with only certain definitions and sanctions added to the text where required.¹⁶³ In the Government's opinion issues of contract formation, as with other substantive contract law issues, could be left to the courts and the common law.¹⁶⁴

Regulation 9 contains the requirements relating to the provision of information when contracts are concluded electronically and regulation 11 contains the service provider's obligations in relation to the placing of the order.¹⁶⁵ The Regulations apply when any order is placed through technological means where one party is a consumer or where neither party is a consumer but the parties have not agreed otherwise.

¹⁶¹ Article 11(2).

¹⁶² SI 2013.

¹⁶³ The Electronic Commerce (EC Directive) Regulations 2002, Statutory Instrument 2002 No. 2013.

¹⁶⁴ DTI Interim Guidance March 2002 p18 para 5.27.

¹⁶⁵ Found in Article 11 of the Directive.

Although the Regulations contain no direction on technical contract formation issues, Regulation 12 does make reference to ‘contractual offers’ declaring that in relation to Regulation 9(1)(c)¹⁶⁶ and Regulation 11(1)(b)¹⁶⁷ the order “shall be the contractual offer”.

This provision raises two questions; firstly, is the regulation referring to a ‘contractual offer’, as understood at common law and discussed above? And second, if it is, what are the implications for the contracting parties?

As to the first question, the language used makes it quite clear that the ‘offer’ referred to is a contractual offer as understood at common law. The regulation contains the expression of parliament’s approach that questions of whether an ‘order’ is a ‘contractual offer’ are left to the common law and the courts, except in the two situations clearly identified. This interpretation is also consistent with one of the main purposes of the provision which is to ensure that before committing to a contractually significant communication, after which they may be irrevocably bound by the service provider’s acceptance, the customer is afforded the opportunity to examine their order and correct or delete any errors.¹⁶⁸

The consequences of this provision would appear to be that where an ‘order’ is a contractual offer at common law, prior to a customer placing that order;

- he must be provided with, in a clear, comprehensible and unambiguous manner, the information regarding the technical means of identifying and correcting input errors; and,
- provided with appropriate, effective and accessible technical means allowing him to identify and correct input errors.

Failure to provide the relevant information will allow a customer, or ‘service recipient’, to bring an action against the service provider for damages for breach of statutory duty.¹⁶⁹ Failure to provide the means to identify and correct input errors will allow the customer to rescind the contract, at the discretion of the court.

¹⁶⁶ The requirement to provide information “in a clear, comprehensible and unambiguous manner... the technical means for identifying and correcting input errors prior to the placing of the order”.

¹⁶⁷ The obligation to “make available to the recipient of the service appropriate, effective and accessible technical means allowing him to identify and correct input errors prior to the placing of the order”.

¹⁶⁸ It could be argued that this is regulatory overkill and repetition, particularly with respect to consumers with the Distance Selling Regulations in place. However, as is discussed above in 7.4.1. there are some significant exceptions to the Distance Selling Regulations which may be caught by this provision.

¹⁶⁹ Regulation 13.

The 'order' or contractual offer must be acknowledged without undue delay by technological means. Whether this acknowledgement is considered an acceptance of an order which constitutes a 'contractual offer' will depend upon the application of the common law principles discussed above. Regulation 11(2)(b) states that 'the acknowledgement of receipt may take the form of the provision of the service paid for where that service is an information society service'. Where this is the case, if the order was a contractual offer, the provision of the service would equate to acceptance by conduct.¹⁷⁰ However, if the service is provided and additional terms, not introduced before the original offer, are included this will equate to a counter offer and hence be open to acceptance or rejection by the customer. Naturally, if the service has begun this creates a dilemma.

In practice, the provision of information and the means to correct errors is usually achieved on interactive websites by the display of a confirmation screen after the customer has input his or her requirements. This gives the opportunity to correct errors before the final submission of the order and the making of the contractual offer.

If the interpretation discussed above is correct, it is submitted that there are a number of potential anomalies with its application.

Whether a 'contractual offer' is made is undoubtedly a question for the courts, who will apply the common law principles discussed earlier in this chapter to the facts of the particular case. With the penalties for failing to comply with regulation 9(1)(c) and 11(1)(b) being dependent upon the customer making the 'contractual offer', this would appear to require the pre-judging of whether the customer is making an offer in the legal sense by the supplier in his decision when to provide the information and the opportunity to correct errors. This is arguably a rather unfair burden, particularly when the means of electronic communication used may dictate how much information can be provided and at what point in the contractual process.¹⁷¹ The government has indicated that technical limitations associated with the means of electronic communication in use and temporary interruptions in service will not be treated as a failure to satisfy the information requirements in the Regulations. However, it will be for the service provider to demonstrate that he has fulfilled the requirements, and whether attempts have been made to resolve technical problems will clearly have an impact upon whether

¹⁷⁰ See *Brogden v Metropolitan Railway*, *op cit* fn 82.

¹⁷¹ For example, the limit of 160 characters which may be included in an SMS message to a mobile phone.

appropriate, effective and accessible technical means of identifying and correcting input errors have been provided.¹⁷²

Another anomaly in this provision is created by the situation whereby the customer is not technically making the offer but rather ultimately 'accepting' an offer made by the service provider. By implication it would appear that this provision does not cover the situation where the service provider makes the offer and not the customer, which would appear strange if the justification for this approach is to avoid parties, particularly consumers, being erroneously or un-intentionally bound to electronic contracts. Surely there is at least a significant possibility that a consumer may unwittingly 'accept' an offer, and it could be argued that this possibility is even more likely to occur, with actions such as the 'clicking' of an icon requiring less conscious thought and conduct. Users will not give thought to such technical legal analysis of their actions and it cannot have been intended, but the provision as it stands remains open to interpretation.

The reason for the exclusion of 'contracts concluded exclusively by exchange of electronic mail or by equivalent individual communications' from the information requirements in regulation 9(1) & (2) and the correction of input errors in regulation 11, is not immediately clear. It is nevertheless a direct transposition of the relevant Articles in the Directive. From the preparatory material and the Directive's preamble, it would appear that the purpose of this exclusion was to clarify the definition of 'Information Society Service' and hence the applicability of the Directive's provisions. Hence, Recital 18 reads:

"... television broadcasting within the meaning of Directive EEC/89/552 and radio broadcasting are not information society services because they are not provided at individual request; by contrast, services which are transmitted point to point, such as video-on-demand or the provision of commercial communications by electronic mail are information society services; the use of electronic mail or equivalent individual communications for instance by natural persons acting outside their trade, business or profession including their use for the conclusion of contracts between such persons is not an information society service."

¹⁷² See the Department of Trade and Industry "Interim Guidance for Business on the Electronic Commerce (EC Directive) Regulations 2002." March 2002 p 18 para 5.3.

The reference to “natural persons acting outside their trade, business or profession” clearly indicates that the exclusion is intended to encompass communications between individuals, including contracts entered into by electronic communications in a purely private capacity. The exclusion is clearly not intended to cover business parties or service providers even if their contracts are entered into via e-mail or equivalent with an individual. This position is supported by recital 39 in the context of electronic contracts:

“The exceptions to the provisions concerning the contracts concluded exclusively by electronic mail or by equivalent individual communications provided for by this Directive, in relation to information to be provided and the placing of orders, should not enable, as a result, the by-passing of those provisions by providers of information society services.”

However, without the benefit of the preamble the regulation is open to interpretation and on a literal reading of the provision, its application would appear to depend upon the interpretation of the phrase ‘concluded exclusively’. If interpreted as referring to the technical ‘conclusion’ of a contract, this would include only the acceptance of the offer – the point at which, in law, the contract is concluded. This would mean that as long as the contract was technically concluded by e-mail or equivalent individual communication it would fall within the exclusion whether one of the parties was a consumer and the other a business. However, such a technical definition is unlikely to have been intended in this context. At the other extreme this phrase could be interpreted as requiring the complete contractual process, including initial contact and negotiation, to be concluded exclusively by e-mail or equivalent individual communications. This interpretation could result in a contract between two individuals, which began on an open forum or website but was concluded via e-mail or equivalent, falling outside of the exception and being subject to the information and contractual requirements of the Regulations.

Either one of these interpretations, would have the potential to create a significant loophole in the protection provided by the Directive. An interpretation somewhere between these two extremes may be proposed, but when the almost infinite variables and possible permutations are considered, any intermediate interpretation

would result in considerable uncertainty and arguably defeat one of the main objectives of the Directive.

It is submitted that the exception should be interpreted as excluding individual communications, by e-mail or equivalent forms of communication, between parties acting outside their trade, business or profession. In this way the integrity of the protection afforded by the Directive, particularly to consumers, and the promotion of trust and confidence in electronic contracting, will be maintained.

8.5 Conclusion

The formation of electronic contracts is an essential element of electronic commerce. In all commercial activity legal certainty is important to enable parties to establish their obligations and liabilities and assess the potential risk involved with any venture. In the developing world of electronic commerce a lack of legal certainty has been identified as a potential barrier to its use and to the promotion of trust and confidence in the electronic environment.

In the absence of any new regulatory instrument and a change in position by the UK government, the common law rules relating to offer and acceptance will be applied to disputes relating to the formation of electronic contracts for the foreseeable future.¹⁷³

From the preceding discussion it would appear that the common law principles of contract formation can be applied to electronic communications with little difficulty. For example, the distinction between an offer and an invitation to treat, based upon the objective assessment of the words and conduct of the parties requires an essentially factual investigation. One point to note however, is that by virtue of the wide variety of electronic forms of communication available and in particular the unique attributes of interactive websites, what may be considered 'just advertising' by a supplier could be construed as an offer because of the 'automation' of the contractual process. This would require the courts to adopt an approach similar to that of Lord Denning in *Thornton*, which may be distinguished in cases where the customer is not "committed beyond recall" by his initial actions. Nevertheless it remains a potential risk for those using interactive websites, a risk which has been met in some cases by the introduction of 'terms of use' on websites expressly stating that no contract exists until confirmation of the order by the supplier.

¹⁷³ Where the law of England and Wales is the applicable law of the contract. See chapter 5 above.

In the past the common law has adapted to new forms of communication as they have been introduced. The history of the common law is punctuated by litigation testing existing principles in the context of the new methods of communication. The postal rule is a notable example of an adaptation to a new communication development and the later examination of the rule adopted for the post in the context telex and fax illustrates the need to test existing principles as technology develops. No doubt the existing principles will be tested in the context of the new methods of electronic communication at some point. However, the example of the postal rule also serves to illustrate a fundamental problem with the common law approach. If the rationale behind a particular principle is not articulated clearly by the courts then the ability to predict the later application of that principle to new situations becomes problematic.

With electronic contract formation considerable debate has surrounded the rules on acceptance with comparisons being made between the postal system and electronic forms of communication, in particular e-mail. It is submitted that for electronic contract formation the focus of discussion should be the issue of when the acceptance is deemed received. The postal rule is just that, a rule for the post. However, the assessment of when an electronic communication should be considered received can be identified as a further potential source of some uncertainty because of the range of possibilities created by the nature of electronic communications. A clarifying regulatory measure would not only prevent costly litigation but would also create legal certainty and confidence in the use of electronic contracts.

At a regulatory level attempts have been made to address the issue of contract formation. In the European Union the Commission sought to clarify the point of contract formation in the early drafts of the Electronic Commerce Directive. The Commission's attempt did not come to fruition for two reasons; first, the measure introduced was ill-conceived and confusingly drafted because of a lack of focus on the general issue of contract formation rather than one potential problem, and second, there is resistance to European approaches to the harmonisation of contract law principles in general from a number of States (particularly the United Kingdom).¹⁷⁴ Hence, this issue of vital importance to electronic contracts and more generally electronic commerce is left to the uncertainties of litigation. The common law is more than capable of adapting to

¹⁷⁴ This is illustrated by the lack of interest in the ratification of the European Contract Law principles by Member States. A new bout of discussions on the issue of the harmonisation of contract law principles has recently begun. See the 'Communication from the Commission to the European Parliament and the Council - A more coherent European contract law - An action plan' COM/2003/0068 final. OJ C 063 (15/03/2003).

the new forms of communication and accommodating electronic contracts, but for the growth of electronic commerce legal certainty is needed sooner rather than later. The common law does, as a general rule, have a predisposition for 'later' rather than sooner.

The common law has encountered automation in the contractual process in the past and the approaches adopted then remain appropriate today. However, the nature of automation in the electronic environment and developments in artificial intelligence may challenge more than just the principles and presumptions of the common law in the future. Nevertheless, the attribution of the actions of automated 'machines' to the party responsible for putting the machine into use should not be affected by what is essentially a question of liability for the failure or malfunctioning of the machine. The objective approach to the formation of contracts ensures that a party is able to rely on the apparent intention of another party, however that intention is communicated.

It can be concluded that whilst the common law principles of contract formation are flexible enough to accommodate electronic contracts, uncertainty exists in relation to the potential application of a number of crucial issues in the electronic environment. This uncertainty has the potential to undermine confidence in the use of electronic contracts until such time as the issues find their way to the courts for clarification. As a consequence, there is a temptation at this point to lament the demise of the original version of Article 11 of the Draft Directive on Electronic Commerce, a measure intended to clarify the point of contract formation. However, even the most favourable reading of that provision would do little to aid clarity or create certainty in the contract formation process. It is regrettable that the Commission did not find more support for their attempt and were not able to develop the Article into a more functional solution to a problem which will inevitably find its way into the courts of England and Wales at a point in the future.

Conclusion

In this section a number of potential problems relating to the creation of electronic contracts have been identified.

The anonymity of the Internet and other forms of electronic communication has the potential to undermine confidence in parties seeking to enter electronic contracts. In response to this problem, methods of facilitating identification in the electronic environment, in particular electronic signatures have been given legal recognition in statutory provisions. Measures, in the form of statutory information requirements, have also been introduced to alleviate the problem with identification by making the activities of suppliers contracting in the electronic environment transparent. These measures may go some way to developing trust and confidence in electronic contracting, particularly with consumers.

Formal requirements have been demonised as potential barriers to electronic commerce; however, in reality in England and Wales their potential impact upon electronic contracting would probably be minimal. It is the confusion and uncertainty created in relation to the ability of electronic communications to satisfy formal requirements which has the potential to damage confidence in electronic commerce. In response to this issue the European Community introduced a pro-active measure in the Electronic Commerce Directive requiring Member State governments to remove legal requirements which may pose potential barriers to the use of electronic communications. It was argued that the approach adopted by the UK government in section 8 of the Electronic Communications Act is too conservative to achieve the desired objective with sufficient speed to facilitate the use of electronic communications.

Finally, and arguably most importantly the common law principle of contract formation were considered. Here, because of the generic rules developed by the common law and the objective approach to agreement few fundamental difficulties in application can be identified. The potential problems created by the rules on contract formation are created because of the uncertainty in predicting how those principles will be applied in the electronic environment. The slow speed at which the common law is

developed means that the issues may not be resolved for some time. Legal uncertainty in this crucial area may have detrimental consequences for electronic commerce and it is submitted that regulatory intervention on this issue is required to create a clear and consistent legal environment for the creation of electronic contracts.

IV

The Contents of Electronic Contracts:

Terms and Overriding Legislation

Introduction

The chapters in this section examine the contents of a contract or more specifically the terms of the contract, which dictate the rights and obligations of the parties. Terms can be expressed by the parties or implied in a number of ways.¹ The incorporation of express terms and relevant legislative control of those terms form the basis of the discussion in chapters 9 and 10. The discussion of implied terms in electronic contracts in chapter 11 provides the opportunity to examine the debate surrounding computer software and other intangible goods which form the subject matter of an increasing number of electronic contracts.

In the previous section the formation of electronic contracts was considered. The discussion highlighted a number of critical issues relating to the time and place of contract formation in the electronic environment as indicated by the existing common law principles. The lack of regulatory guidance on the issue of electronic contract formation, despite the concerted efforts of the European Commission, means that the common law principles will continue to apply where the law of England and Wales is the proper law of the contract. It was concluded that the common law is capable of accommodating contract formation by electronic means however, but until there is judicial pronouncement in relation to issues such as contractual acceptance by electronic means, there will be scope for speculation and legal uncertainty.

A particular problem created by uncertainty as to the time and place of electronic contract formation relates to the effective introduction and incorporation of contractual terms and conditions. It is a basic tenet of the common law that new contract terms cannot be introduced after the point at which the contract is formed. If the point of contract formation is uncertain, ensuring the effective incorporation of terms may become problematic.

Parties entering electronic contracts must consider the common law rules relating to the manner in which the terms may be effectively introduced. Practical constraints may affect the approach adopted to incorporating terms and conditions in the electronic environment. For example the 160 character limit on text messages to many mobile

¹ See below on implied terms.

phones and the difficult balance between the effective introduction of terms and conditions on a website without detracting from, or completely undermining, the promotional effect of that website and its ease of use. The application of the legal principles of incorporation of terms must not have the effect of removing the advantages associated with modern forms of electronic communication.

Once the parties to electronic contracts have taken steps to incorporate their terms they must also consider the potential effects of regulatory measures upon those terms. Such regulatory measures, intended to 'police' the content of contractual terms, may be considered 'mandatory rules' within that jurisdiction and apply regardless of any choice of applicable law made by the parties.² In the United Kingdom the two key measures are the Unfair Contract Terms Act 1977 (UCTA) and the Unfair Terms in Consumer Contracts Regulations 1999 (UTCCR). The application of such measures may render contractual clauses ineffective on the basis that a particular term is 'blacklisted'³ or that it falls foul of the requirement of reasonableness applied by UCTA or the fairness test found in UTCCR. The consumer is afforded a significant degree of protection against 'unfair terms' and terms attempting to exclude or limit a seller or supplier's liability. In appropriate circumstances the use of terms deemed unfair in consumer contracts will result in a supplier facing legal proceedings instigated by the Director General of Fair Trading (DGFT) or other body charged with the elimination of unfair terms in consumer contracts. The seller or supplier will usually be unable to exclude the application of the consumer protection regulation effective in the consumer's domicile.

The parties to electronic contracts will also need to consider terms implied into certain types of contract by legislation, in particular the Sale of Goods Act 1979 and the Supply of Goods and Services Act 1982. These terms have recently been the subject of judicial consideration in the context of computer software, a popular subject matter for electronic contracts. The obligations contained in these implied terms may have important consequences for parties entering electronic contracts in relation to standards of contractual performance.

As the terms of a contract dictate the rights and obligations flowing from the agreement they are crucial to all parties concerned. Contract terms allow commercial parties to adjust their price and service in the light of a risk analysis of their obligations. So for example, a photographic developer may offer a cheap service which has a strict

² The approach taken to 'mandatory rules' is considered above at chapter 4.3.

³ For example, in a consumer contract terms purporting to exempt liability for the implied terms of the Sale of Goods Act 1979 are automatically ineffective by virtue of s. 6 of UCTA.

limitation of his liability should something go wrong, but may accept higher risk and greater liability if the customer pays a premium rate.⁴ In the electronic environment the desire to control the risks and liabilities associated with a business venture is no less than it is in the physical environment. The potential impact of existing common law principles and regulatory measures upon the content of electronic contracts will now be considered.

The discussion will begin with the rules on incorporation and their application in the electronic environment.

⁴ The usual compensation would be restricted to the price of a film and free processing. The premium rate allows the trader to either obtain insurance against those risks or alternatively put additional systems in place to negate the risk.

The Incorporation of Contractual Terms in Electronic Contracts.

The first hurdle for parties entering into electronic contracts is to ensure that they adopt appropriate methods to ensure incorporation of their terms. In an ideal world all parties to an agreement would have complete knowledge of all of the terms prior to giving their consent and hence be fully aware of their rights and obligations. However the reality of commercial practice is very different. Parties will rarely read all of the terms of a contract prior to agreeing, particularly where the contract is based upon a standard form agreement rather than being individually negotiated between the parties. The terms are usually simply referred to in some way and it is for the other party to decide whether to consult the terms or not. The majority of business is conducted on this basis to save time, reduce costs and increase efficiency. The courts recognise the commercial necessity of this practice and the objective approach to incorporation of terms adopted by the courts does not require actual knowledge of the terms but rather a reasonable opportunity to become acquainted with the terms.

In the electronic environment the need to refer to contractual terms contained elsewhere is often a necessity because of practical constraints created by the technology. With mobile phones the length of text message sent is often restricted to 160 characters. Clearly if a supplier had to include terms and conditions in the message there would be little room for the information he was attempting to convey. With websites, if a service provider had to include all of his terms and conditions on his main webpage, navigation would become cumbersome and there would be little room left for promotional information about his products or services. Hence, the terms and conditions are often only referred to in the main document or communication and are accessible via a hypertext link, sent via a separate e-mail or alternatively available in a scroll box. This

not only avoids cluttering the front page or main contract page, it also saves the customer from having to trudge through a long list of terms.

The rules developed by the courts are commonly referred to as incorporation by signature, notice and a consistent course of dealing. These methods will now be considered in the context of electronic contracting.

9.1 Incorporation by Signature

In the UK the simplest and most common method of demonstrating acquiescence to the contents of the contract is by a signature. Although it has been criticised for its ‘artificiality’,¹ the approach adopted to incorporation by signature, as illustrated by *L’Estrange v Graucob*, remains prevalent.² If a party signs a document, in the absence of a claim of fraud, misrepresentation³ or *non est factum*, then the court will conclude that “the party signing it is bound, and it is wholly immaterial whether he has read the document or not”.⁴ In the context of the incorporation of terms into electronic contracts it must be considered whether an electronic form of ‘signing’ a message containing terms and conditions will be treated in the same way as a more traditional form of signature.

Electronic signatures have been considered already in the context of formal requirements and their fulfilment by electronic means of communication.⁵ The courts’ flexible approach to the concept of ‘signature’ at common law would appear to indicate that electronic methods of signing will be treated as equivalent to their traditional counterparts.

In *Re a debtor (No 2021 of 1995), ex parte Inland Revenue Commissioners v The debtor; Re⁶ Laddie J* made reference to the ability of modern technology to apply a ‘signature’ on behalf of its user;

“For example, it is possible to instruct a printing machine to print a signature by electronic signal sent over a network or via a modem. Similarly, it is now possible with standard personal computer equipment and readily available popular word processing software to compose, say, a letter on a computer screen, incorporate

¹ See Lord Devlin in *McCutcheon v David MacBrayne Ltd* [1964] 1 WLR 125 at 133.

² [1934] 2 K.B. 394.

³ *Curtis v Chemical Cleaning and Dyeing Co* [1951] 1 KB 805.

⁴ [1934] 2 K.B. 394 per Scrutton L.J. at 403.

⁵ See chapter 7.2 above.

⁶ Also known as *Inland Revenue Commissioners v Conbeer* [1996] 2 All E.R. 345, at 353.

within it the author's signature which has been scanned into the computer and is stored in electronic form, and to send the whole document including the signature by fax modem to a remote fax. The fax received at the remote station may well be the only hard copy of the document. It seems to me that such a document has been 'signed' by the author."⁷

By analogy it could be argued that if a party electronically signs an electronic document in any way the approach in *L'Estrange* should be adopted and, in the absence of fraud, misrepresentation or a claim of *non est factum*, the signatory should be bound to the contents of the agreement he has signed.

However, it is submitted that there are a number of reasons why the courts may not accept such a direct application of the principle embodied in *L'Estrange* to electronic signatures.

First there are a wide range of actions which could be categorised as 'signing' in the electronic environment and it would be inappropriate to give them all the same evidential weight as the manifestation of a party's intent to be bound to contractual terms. For example the use of a 'digital' or electronic signature created by cryptographic software is one of the more advanced methods and the process required to use the signature would indicate a strong intention to assent or authenticate the contents of a message on behalf the signatory. However, the typing of one's name or initials at the bottom of an e-mail or into a data field on a website and the clicking of the 'send' or 'I accept' icon represents a less reliable indication of an intention to assent to the contents of a message or webpage. Although it is argued above that all of these methods would be capable of satisfying a formal requirement of a signature, they should perhaps not be given equal weight as evidence of a party's intent to assent to contractual terms. The suggestion that different forms of electronic signature should be given different evidential weight is supported by the approach adopted in the Electronic Signatures Directive.⁸ In Article 5 of the Directive a distinction is made between 'advanced electronic signatures' based on a qualified certificate and other forms of electronic signature, with the former being afforded a superior legal status to the latter. In the United Kingdom, the implementation of this provision in section 7 of the Electronic

⁷ *Ibid* at 353.

⁸ Directive 1999/93/EC of the European Parliament and of the Council of 13 December 1999 on a Community framework for electronic signatures. OJ L 13/12 (19. 1. 2000).

Communications Act 2000 leaves the matter of evidential weight to the courts declaring only that electronic signatures are admissible in evidence.

Secondly, the approach adopted in *L'Estrange* has the benefit of creating legal certainty, but as indicated at the beginning of this section it has been criticised for its artificial approach to the incorporation of contractual terms, both in the courts of England and Wales⁹ and other common law jurisdictions. It has been suggested that where clauses are particularly unusual or unreasonable then a signature on the document should not be conclusive unless reasonable notice of the terms has been given to the person signing.¹⁰ There may be scope for an argument that with the advent of new technology and modern methods of contracting this less restrictive approach should be adopted. However, the potential success of such an argument must be doubted in the light of the regulatory measures now in place to enable the courts to deal with unfair or unreasonable contract clauses.

Finally, another factor which may exclude the application of the strict *L'Estrange* approach to electronic signatures may be the manner in which the purported 'signature' is made in relation to the electronic document or message containing the terms. The electronic signature may not be 'attached' to the document containing the terms but rather made on an order confirmation page which refers to terms and conditions found elsewhere. If this is the case then the question will be whether there has been reasonable sufficient notice of the terms.

The real issue is not whether the actions equate to a 'signature' in the traditional sense, but rather what emphasis should be placed on that action in so far as it indicates intent to be bound.

9.2 Incorporation by Notice

If there is no 'signature' indicating assent to the terms of a contract, and it is submitted that this will be the case in the majority of e-commerce transactions, the question before the courts will be whether the party has been given 'reasonably sufficient

⁹ See Lord Devlin in *McCutcheon v David MacBrayne Ltd* [1964] 1 WLR 125 at 133, [1964] 1 Lloyd's Rep. 16 at 25; *Levison v Patent Steam Cleaning Co* [1978] 1 QB 69 (per Lord Denning MR at p 78); *Jones v Northampton Borough Council and another* (1990) Court of Appeal (Civil Division), The Times 21 May 1990, The Independent 25 May 1990; and *Ocean Chemical Transport Inc And Another V Exnor Craggs Ltd* [2000] 1 Lloyd's Rep 446, (per Evans LJ at paras 48&49).

¹⁰ In *Tilden Rent-A-Car v Clendenning* (1978) 83 DLR (3d) 400 the Ontario Court of Appeal held that unusual and onerous terms were not incorporated into the contract by a signature. A signature could "... only be relied on as manifesting assent to a document when it is reasonable for the party relying on the signed document to believe that the signer really did assent to its contents."

notice' of the terms of the contract.¹¹ Where there may be no actual knowledge of the terms (either because the customer ignored them, only read part of them, or was not aware of them) the person seeking to rely upon the terms has to take reasonable steps to bring the terms to the attention of the other party, either before or at the time of contracting.

9.2.1 Timing

The conclusion of the contract is the defining moment in relation to the parties' rights and obligations. To be effective terms must be introduced or brought to the other party's attention before or at the latest at the time of contract formation. Terms introduced after this point cannot form part of the parties' agreement.¹² It has been indicated that in many electronic contracts the point of contract formation may be unclear and as a consequence many service providers and online retailers attempt to prescribe the point of contract formation in their terms of website use.¹³

9.2.3 Notice

The test for whether a party has been given 'reasonably sufficient notice' of terms displayed on a sign or contained within an unsigned document is a question of fact based upon all of the circumstances of a particular case.¹⁴ The objective approach adopted means that notice of the existence of the terms is necessary rather than notice of their contents:

"the customer is bound by the [...] condition if he knows that the ticket is issued subject to it; or, if the company did what was reasonably sufficient to give him notice of it."¹⁵

If the 'document' containing the contractual terms is not of a type which a reasonable person would expect to contain contractual terms then the court may

¹¹ *Parker v South Eastern Railway Co Ltd* [1877] 2 CPD 416.

¹² *Olley v Marlborough Court Hotel* [1949] 1 KB 532; and the discussion of Lord Denning in *Thomton v Shoe Lane Parking* [1971] 2 QB 163. In the electronic environment the point of conclusion of the contract has been a contentious issue. See chapter 8 above.

¹³ For example Amazon.com state that;

"No contract will subsist between you and Amazon.co.uk* for the sale by it to you of any product unless and until Amazon.co.uk accepts your order by e-mail confirming that it has dispatched your product."

The validity of this approach will of course depend upon whether these terms are effective.

¹⁴ *Parker v South Eastern Railway Co Ltd* [1877] 2 CPD 416.

¹⁵ *Thomton v Shoe Lane Parking* [1971] 2 QB 163, per Lord Denning at 170.

conclude that reasonable notice has not been given.¹⁶ Equally, if a document is part of a transaction which is well known to have standard terms and conditions associated with it, then it may be easier to show that reasonably sufficient notice has been given.¹⁷ If the inclusion of contract terms in a particular document is customary or common within a trade this may also provide evidence that reasonably sufficient notice has been given.¹⁸ The test is objective but if the party seeking to rely on the terms knows or reasonably ought to know that the individual or group individuals he is dealing with may have difficulty acquiring the information about the terms this may affect the amount of notice he must give.¹⁹

An important practical effect of this approach is that terms and conditions may be incorporated into a contract by reference to another document. It was indicated above that in the electronic environment there may be practical and technological limitations upon the amount of information which may be displayed on a screen or sent in a particular message format. If using a mobile phone or Personal Digital Assistant (PDA) reference to another document may be the only way to introduce terms and conditions. This makes incorporation by reference particularly important to electronic contracting.

The practical solutions adopted to the incorporation of terms by those entering electronic contracts have been varied and are, as of yet, untested by the courts. It can be speculated that simple references such as 'this agreement is subject to the supplier's terms and conditions' may be ineffective because they do not provide the customer with any opportunity to acquaint himself with the terms. However, the use of references with a hypertext-link to another webpage may be reasonably sufficient notice provided that the link features prominently at some point before the contract is concluded. Likewise the popular use of dialogue boxes requiring the customer to at least scroll through the terms and conditions before proceeding to contract will provide strong evidence that the supplier has given reasonably sufficient notice of his terms. In the mobile phone environment reference is often made to a website where the terms and conditions may be found or a telephone number linked to a recorded message of the terms and conditions.

¹⁶ *Parker v South Eastern Railway Co Ltd* [1877] 2 CPD 416, per Mellish LJ at p 422; *Chapleton v Barry UDC* [1940] 1 KB 532.

¹⁷ *Alexander v Railway Executive* [1951] 2 KB 882.

¹⁸ *British Crane Hire Corporation v Ipswich Plant Hire* [1975] QB 303.

¹⁹ *Thompson v LM & S Railway* [1930] 1 KB 41; *Richardson, Spence & Co v Rountree* [1894] AC 217 and *Geier v Kujawa Weston and Warne Bros (Transport)* [1970] 1 Lloyd's Rep 364.

At common law one further factor must be considered in relation to incorporation of terms by notice and that is the approach adopted to clauses which could be considered unusual or unreasonable. Prior to the introduction of legislative control of contractual terms the courts developed common law rules which could be used to control the incorporation and use of unreasonable and unusual contract terms. One method employed was the more restrictive approach to whether reasonably sufficient notice had been given of particularly onerous contractual terms, or those considered 'unusual or unreasonable'. Lord Denning's 'Red Hand Rule'²⁰ remains the most well known declaration of this principle and even with the introduction of legislation the 'rule' retains a role in the incorporation of contractual terms.²¹ Dillon LJ expressed the rule thus:

"if one condition in a set of printed conditions is particularly onerous or unusual, the party seeking to enforce it must show that that particular condition was fairly brought to the attention of the other party."²²

Whilst the use of such terms is by no means excluded by this principle the notice given of such terms would need to be explicit, drawing the other contracting party's attention to the term or terms.

9.3 Incorporation by a Consistent Course of Dealing

Where parties have contracted on a number of occasions previously the court may infer that, in the absence of contrary indication, the parties intend to contract on the terms used consistently in their previous dealings, even if the terms have not been introduced in the instant case.²³ The argument that a consistent course of dealing has incorporated terms will usually arise in a situation where there has been a breakdown in communication between the parties and the document containing the terms and conditions has arrived after the contract has been concluded. This occurrence is by no means unlikely in the electronic environment whereby e-mails can on occasion mysteriously vanish for hours, if not days. However, the courts appear to be less willing

²⁰ *Spurling v Bradshaw* [1956] 1 WLR 461; *Thomton v Shoe Lane Parking* [1971] 2 QB 163.

²¹ *Interfoto Picture Library v Stiletto Visual Programmes* [1988] 1 All ER 348; [1989] Q.B. 433; *Montgomery Litho Ltd v Maxwell* [2000] S.C. 56; [1999] S.L.T. 1431; *O'Brien v MGN Ltd* [2001] EWCA Civ 1279; [2002] C.L.C. 33; Times, August 8, 2001 (CA).

²² *Interfoto Picture Library v Stiletto Visual Programmes* [1988] 1 All ER 348; [1989] Q.B. 433 at 439 per Dillon L.J.

²³ *Herry Kendall & Sons v William Lillico & Sons Ltd* [1966] 1 Lloyd's Rep. 197 per Diplock L.J.

to incorporate terms by a consistent course of dealings where one of the parties is a consumer.²⁴ If this approach is adopted in the electronic environment it may have implications for suppliers who only introduce their terms and conditions explicitly on the first visit of a particular consumer.

Attempts have been made to harmonise the approach to the incorporation of terms in the electronic environment in the UNCITRAL Model Law on Electronic Commerce and the early drafts of the Electronic Commerce Directive. These attempts will now be examined.

9.4 Attempts to Regulate the Incorporation of Terms

9.4.1 UNCITRAL Model Law on Electronic Commerce²⁵

An addition was made to the Model Law in 1998 introducing Article 5bis to accommodate incorporation of terms by reference.

“Information shall not be denied legal effect, validity or enforceability solely on the grounds that it is not contained in the data message purporting to give rise to such legal effect, but is merely referred to in that data message.”²⁶

The new Article was introduced to recognise that “in an electronic environment, incorporation by reference is often regarded as essential”.²⁷ However, the Article simply indicates that a permissive approach should be taken to incorporation by reference and arguably reflects the existing approach at common law.

The approach adopted in the European Commission in the development of the Electronic Commerce Directive however, had the potential to significantly alter the approach adopted to the incorporation of terms.

²⁴ *Hollier v Rambler Motors* [1972] 2 QB 71.

²⁵ UNCITRAL Model Law on Electronic Commerce (1996). General Assembly Resolution 51/162 of 16 December 1996, UNCITRAL Model Law on Electronic Commerce. Available at: <http://www.uncitral.org/english/texts/electcom/ml-ecomm.htm>.

²⁶ *Article 5 bis. Incorporation by reference* as adopted by the Commission at its thirty-first session, in June 1998.

²⁷ Guide to Enactment of the UNCITRAL Model Law on electronic Commerce (1996) at para 46-2.

9.4.2 The Draft Electronic Commerce Directive and incorporation by reference in electronic contracts.²⁸

The provision in the draft Directive was introduced to develop consumer confidence in electronic contracts by promoting transparency in the contractual process and fair dealing. The draft Article 10(2) read:

“Member States shall provide in their legislation that the different steps to be followed for concluding a contract electronically shall be set out in such a way as to ensure that parties can give their full and informed consent.”²⁹

Although clearly intended to deal with the contract formation process the requirement of ‘full and informed consent’ had implications for the incorporation of terms by reference. How can a party be said to have given his full and informed consent to a contract when he may not have read or even seen the terms and conditions? The Article had the potential to create uncertainty in the contractual process rather than promote confidence.

The terminology was removed from the final Directive and the only reference to contractual terms is the requirement that where the service provider makes terms and conditions available to the recipient of a service, they are made available in a way that allows him to ‘store and reproduce them’.³⁰ The Article is reproduced verbatim in Regulation 9(3) of the Electronic Commerce (EC Directive) Regulations and failure to comply can result in a court order requiring compliance. However, in the light of the preceding discussion the object of the requirement must be questioned. The provision refers to situations ‘where the service provider provides terms’, yet, if the service provider does not provide terms to the recipient of a service, whether by reference or otherwise, it must be questioned whether they will form part of the contract at all. The early versions of this requirement simply stated that contract terms and general conditions provided to the consumer must be made available in a way that allows him to store and to reproduce them.³¹ With no further comment from the Commission on the Article it can only be concluded that the addition of ‘where the service provider provides terms...’ has little effect, with the clear object of the Article being the accessibility of the

²⁸ Amended Proposal for a European Parliament and Council Directive on certain legal aspects of electronic commerce in the internal market COM(1999)427 final.

²⁹ Emphasis added.

³⁰ Article 10(3).

³¹ *Op cit* fn 28 at p 25.

terms and conditions of the transactions to the recipient of the service for future reference. The Department of Trade and Industry guidance on the Regulations simply explains that the provision does not require that the making available of the terms take the same form as in the original transaction.³² It is submitted that where the service provider does not provide the terms and conditions of the contract to the recipient, they will only be incorporated into the contract where there has been reasonably sufficient notice by reference to the terms or a previous consistent course of dealing between the parties.

9.5 Conclusion

The common law principles of incorporation can readily be applied to electronic contracts but there are a number of potential difficulties which may result in uncertainty. It is unclear what approach the courts will take to particular acts performed in the electronic environment, which are often referred to as 'signing' the terms so as to acquiesce to their content. There are a number of sustainable arguments why the strict common law approach to incorporation by signature, illustrated by *L'Estrange v Graucob*, should not be applied to even the most 'reliable' forms of electronic signature. It is submitted that the act of using an encryption based method of authenticating a communication will provide strong evidence of a party's intent, although it may still be argued that the signatory has not actually 'signed' the document containing the terms.

In the majority of electronic contracts the question will ultimately be one of whether reasonable sufficient notice has been given of the terms. Here a potential problem is created by the lack of certainty as to the precise point of contract formation in the electronic environment highlighted in chapter 8. The terms must be introduced before the contract is concluded and uncertainty as to that point poses a *prima facie* problem for the incorporation of terms. There are numerous methods of introducing contractual terms in the electronic environment and as of yet none have been tested as to whether they provide reasonably sufficient notice of the terms. It is uncertain whether simple references will be sufficient to incorporate terms and the general approach adopted by the courts indicates that this assessment may depend upon the status of the

³² Department of Trade and Industry "A Guide for Business to the Electronic Commerce (EC Directive) Regulations 2002 (SI 2002/2013) 31 July 2002. The example given is the sending of a copy of the terms along with the goods. Naturally such terms would have to have been introduced prior to the conclusion of the contract in any event.

parties to the contract and whether the terms are unusual or unreasonable.³³ While this provides the courts with flexibility in their adjudication it does little to enhance the predictability of the legal environment within which electronic contracts will have to operate.

Incorporation by a consistent course of dealings will have a role to play in electronic contracts because parties using websites often do not require returning customers to scroll through or visit their terms pages. However, it may be difficult to successfully argue there has been a consistent course of dealing where one of the parties is a consumer or where there have only been limited previous dealings.

Regulatory measures have not substantially addressed the issue of incorporation of terms. The UNCITRAL Model Law simply recognises the importance of incorporation by notice in the electronic environment. The provision with the potential to have a co-incidental impact on the incorporation of terms, found in early versions of the Electronic Commerce Directive was removed in the final Directive. It is submitted that a requirement of 'full and informed consent' would be impractical in the electronic, or any other contractual environment.

For the creation of a predictable and consistent legal environment for electronic contracts guidance is needed in relation to the incorporation of terms. For the promotion of electronic commerce this guidance is required sooner than is likely to occur if it is left to the unpredictability of a judicial pronouncement on the issue. For this reason regulatory guidance is required, indicating in particular what steps are necessary to provide reasonably sufficient notice of terms to customers on a website or other electronic medium whilst at the same time complying with technical constraints and attempting to offer a suitably attractive format to encourage custom.

³³ For recent examples of this approach see *Villella v MFI Furniture Centres Ltd*, [1999] I.R.L.R. 468 and *O'Brien v MGN Ltd*, [2001] EWCA Civ 1279; [2002] C.L.C. 33; Times, August 8, 2001.

Legislative Measures Relevant to the Terms in Electronic Contracts

Legislative intervention, policing contractual terms, has become commonplace in the modern commercial environment. The intervention is often justified on the grounds of social policy, protecting weaker or vulnerable parties and reducing economically wasteful practices. The approach taken may vary and the regulation may be based on the particular type of contract, the legal status of the contracting parties or the particular type of clause in use.

In the United Kingdom the Unfair Contract Terms Act 1977 was introduced, to an extent, reflecting the approach adopted by courts and the prevailing judicial attitude towards exemption clauses.¹ The intervention of Parliament in this matter served the dual purpose of satisfying the need for clarification of the legal position at a pace appropriate to the needs of commerce and equally placating the constitutional argument that the legislature is the correct forum for a control based on social policy.

The European Community has had a considerable impact on the approach to contractual terms, specifically in relation to consumer protection. The desire to maximise the potential of the internal market by promoting confidence in cross-border transactions and the free movement of goods and services has led to a number of Community based provisions, in particular the Council Directive on unfair terms in consumer contracts.² A significant development introduced by the Directive was the involvement of certain organisations to take action against undesirable contractual clauses and practices rather than restricting the right to those individually affected and relying on their desire and financial ability to litigate.

Electronic Commerce raises identical concerns to those associated with more traditional commerce, in particular the need to control the use of unfair contractual terms by the party in a dominant position. To an extent these concerns are magnified by the cross-border nature of the electronic medium. The extent to which regulatory measures already in existence apply to the world of electronic contracting is as important an issue

¹ The development of the 'Red Hand Rule' for example. See above at 9.2.

² 93/13/EEC. (1993) OJ L95/29 (21.4.93).

as ensuring that new or proposed regulation accounts for the needs of the electronic environment.

However, it is accepted that legislative regimes alone cannot guarantee the development of the desired confidence in cross border transactions. Many sellers exploit the lack of knowledge of many of their customers regarding their legal rights³ and the same lack of knowledge means that confidence is not increased. Information about the rights and protection available empowers the customer and removes the ability of a supplier to utilise unfair terms and conditions to influence the customer's behaviour and perception of his position. The need to ensure the availability of information, about consumer rights in particular is recognised in the European legislation as can be seen in the Distance Selling Directive:⁴

“Member States shall take appropriate measures to inform the consumer of the national law transposing this Directive and shall encourage, where appropriate, professional organizations to inform consumers of their codes of practice.”⁵

Nevertheless legislative controls have the ability to considerably influence the development and exploitation of the electronic marketplace. Indeed, the existing legislation may mould the development of electronic contracting with suppliers wishing to enter and exploit markets where the regulation may be high but the customer confidence is correspondingly high. Equally, overbearing regulation may have the negative effect of stifling commercial expansion with service providers establishing and marketing in jurisdictions with less stringent control.

If electronic contracts fall within the jurisdiction of particular legislation, then that legislation will be applied to them in the same way that it applies to more traditionally formed contracts. The application and potential effects of UCTA and UTCCR to electronic contracts will now be considered. To assess the impact of the legislation effectively its background and purpose must also be considered.

³ See; Macdonald, E. “The emperor's old clauses: unincorporated clauses, misleading terms and the Unfair Terms in Consumer Contracts Regulations.” [1999] 58(2), *C.L.J.* 413-436.

⁴ Directive 97/7/EC of the European Parliament and the Council on the protection of consumers in relation to distance contracts, (1997) OJ L144/19 (4.6.97).

⁵ Article 16 ‘Consumer information’.

The Unfair Contract Terms Act 1977.

The Unfair Contract Terms Act 1977 (“The Act”) is a complex piece of legislation with a variety of distinct elements. Many commentators¹ have expressed the opinion that the short title to this Act is somewhat misleading.² The Act does not deal explicitly with the “fairness” of contract terms, nor does it deal solely with “contractual” terms. Essentially the Act tackles the use of exemption clauses, the generic phrase for terms that aim to exclude, restrict, or limit particular liabilities.

The application of the Act follows a logical formula and it is the application of the key provisions of the Act, and the elements most relevant to electronic contracting that will form the basis of the following discussion.

The core questions raised by this thesis will be addressed:

- Are the background and objectives of the Act compatible with contracting in the electronic environment?
- Does the scope of the Act encompass electronic contracting?
- Does the application of the Act to electronic contracting produce logical, appropriate or desirable results?, and if not
- What amendments or changes are necessary or appropriate?

At the time of writing, these questions are particularly relevant because the Law Commission is embarking on a major consultation on the amendment of the legislative regimes on unfair terms.³

¹ See for example, Macdonald, E. “Mapping the Unfair Contract Terms Act 1977 and the Directive on Unfair Terms in Consumer Contracts” [1994] Sep *J.B.L.* 441-462; and Rogers, W.V.H. and Clarke M.G. *Unfair Contract Terms Act 1977* (Sweet and Maxwell: London, 1978).

² The original long title of the Act does to some extent clarify its scope;

“An Act to impose further limits on the extent to which under the law of England and Wales and Northern Ireland civil liability for breach of contract, or for negligence or other breach of duty, can be avoided by means of contract terms and otherwise, and under the law of Scotland civil liability can be avoided by means of contract terms.”

³ The Law Commissions Consultation Paper No 166 3RD July 2002. <http://www.lawcom.gov.uk>.

11.1 Background to the Act

The text of the Act broadly follows the recommendations found in the Law Commission's 'Second Report on Exemption Clauses'.⁴ The Commission recommended legislative provision to curtail the use of exemption clauses. Such control was considered necessary and in the public interest, to protect parties against potential injustice arising from the abuse of exemption clauses by business parties in a dominant bargaining position. In the words of the Law Commission:

"It is clear that exemption clauses are much used both in dealings with private individuals and in purely commercial transactions. We are in no doubt that in many cases they operate against the public interest and that the prevailing judicial attitude of suspicion, or indeed of hostility, to such clauses is well founded."⁵

It can be seen from this short passage that in formulating their proposals the Commission acknowledged the pragmatic approach taken by the courts to instances of injustice created by the use of exemption clauses.⁶ Perhaps the best example of the 'prevailing judicial attitude of suspicion and hostility' referred to in the report is the often cited judgment of Lord Reid in *Suisse Atlantique*.⁷ Of exemption clauses, Lord Reid said:

"Probably the most objectionable are found in the complex standard conditions which are now so common. In the ordinary way the customer has no time to read them, and if he did read them he probably would not understand them. And if he did understand and object to any of them, he would generally be told he could take it or leave it. And if he then went to another supplier the result would be the same. Freedom to contract must surely imply some choice or room for bargaining."⁸

In some respects, the reference made by Lord Reid to 'freedom to contract' with no 'room for bargaining' epitomised the decline in favour of the traditional doctrine of freedom

⁴ Law Comm. No. 69 (1975).

⁵ *Ibid.* at p4. Paragraph 11.

⁶ There are many examples of the approach taken by the courts to exemption clauses they feel are 'objectionable'. A full discussion is beyond the scope of this chapter, but examples the 'tools' created by the courts to deal with exemption clauses, such as the rules of incorporation, in particular the 'Red Hand Rule' are discussed in the preceding chapter (10).

⁷ *Suisse Atlantique Societe d'Armerent Maritime SA v. NV Rotterdamsche Kolen Centrale* [1966] 2 All ER 61. [1967] 1 AC 361.

⁸ *Ibid.* at p. 409.

of contract. References can be found within the extract to some of the key issues often associated with the decline of the doctrine and also to the emergence of legislation such as the Unfair Contract Terms Act. For example, the increased use of standard form contracts in business practice; the often obscure methods of presentation and incomprehensible terminology employed by suppliers in their contractual documents; and the dominance of business parties in the contractual process due to the increasingly monopolistic market and the entrance of the 'consumer' into that market.⁹

Hence, the lack of influence over the contents of the contract by the weaker party and the corresponding lack of real freedom to contract exemplified by Lord Reid added credence to the Commissions argument for legislative control. Nevertheless, although persuasive argument existed for controlling the use of exemption clauses, questions remained regarding the correct application of that control. The principal fear was that in order to fulfil its objectives the Act would interfere with the parties' contract to such an extent that the outcome would

“..be tantamount to remaking the parties' contract for them”.¹⁰

The need to strike an appropriate balance between the competing interests of the parties whose contracting practices would be affected by the legislation is clear. The argument for the control of exemption clauses focussed on the desire to protect 'weaker' parties against the unfair and unreasonable use of such clauses and the potential for injustice. In contrast, the need to allow commercial entities to contract freely and exercise an element of control over their liabilities was accepted as essential in modern commerce. It was recognised that in many cases exemption clauses operate in a beneficial manner and satisfy commercial realities and the undeniable need for parties to establish boundaries to their liabilities.¹¹ The corollary effect being, in theory, lower prices based on commercially efficient allocation of risk.

To an extent the final version of the Act takes account of these competing interests. This is achieved by the 'layering' of the level of control exerted by the 'active sections' of the Act, in their application to exemption clauses. The greater the public interest in the subject

⁹ Further analysis of the doctrine of freedom of contract is beyond the scope of this thesis but see, Atiyah, P.S. *Introduction to the Law of Contract* 5th ed. (Oxford: Clarendon Press, 1995) p.15. *et seq.* Atiyah isolates three influential factors in the decline of the doctrine, 1) The increase in use of standard form contracts, 2) The decline in the importance of free choice and intention as grounds for legal obligation and 3) The emergence of the consumer as a contracting party and a litigant.

¹⁰ *Op cit* fn.4 at p.53 n.138.

¹¹ *Ibid.*

matter of the exemption clause the more absolute the protection afforded. For example, clauses purporting to exclude or limit liability for negligently caused death or personal injury face an absolute ban.¹² Where a party to the transaction 'deals as consumer' they are afforded greater protection by the Act due to the inherent inequality of bargaining power.¹³ Finally, where the Act dictates, the assessment of the exemption clause is made on the basis of the test or requirement of reasonableness. Here the courts are charged with the task of balancing the interests of the parties in the light of various guiding factors to assess how reasonable the use of the exemption clause was.¹⁴

11.2 Background in Relation to Electronic Commerce.

In relation to electronic methods of contract formation the relevant background issues on the Act's inception remain constant. The same potential exists for the use and abuse of exemption clauses in electronic contracts and the same desire to limit potential business liabilities drives commercial interests. In fact, due to the international nature of electronic commerce the need for a supplier to control potential liability increases and hence curbs on his ability to influence that potential liability may become a relevant factor in his entrance into a particular market. However, even if the background objectives of the Act make it appropriate to apply to electronically formed contracts, the question of whether the scope of the Act can encompass electronic contracts remains.

11.3 The Scope of the Unfair Contract Terms Act.

As indicated above the short title of the Act does not do justice to its broad scope of application and its potential impact on the use of exemption clauses. *Prima facie*, the scope of the Act would appear broad enough to encompass contracts made via an electronic medium. However, the Act does contain specific limitations on its applicability and it is important to consider the implications of these restrictions in the light of electronic contracts.

A common concern in relation to the facilitation of electronic commerce is the inclusion of particular formal requirements in legislative provisions.¹⁵ However, the use of a formal requirement which cannot be fulfilled by electronic contracts not only has the potential to affect the proliferation of electronic contracting but may exclude a contracting

¹² Section 2(1).

¹³ Section 6, for example.

¹⁴ See the discussion of section 11 below at 11.6.

¹⁵ See the discussion in chapter 7 above.

party from valuable protection by virtue of their chosen medium of communication. In general, the Unfair Contract Terms Act contains no specific requirements of form. Hence contracts and notices, facilitated via e-mail, EDI, the Internet and other electronic media are all potentially subject to the Acts provisions.¹⁶ However, there is one reference to a particular 'form' in section 3 which has the potential to inhibit the application of the Act. This will be returned to in the discussion of that section.

The Act is not restricted to a particular class of customer or a particular contractual relationship, although a significant element of the Act does relate to the protection of parties who 'deal as consumer'. In contrast to the Regulations on Unfair Terms in Consumer Contracts,¹⁷ which are restricted to 'natural persons', commercial entities may benefit from the provisions of the Unfair Contract Terms Act even if they have taken corporate form.¹⁸ With one of the key barriers to the participation in cross border electronic contracting being a lack of customer confidence, this added protection may be seen as an important factor to small or medium sized enterprises looking to procure goods and services online.

A business can benefit from the Act's mandatory provisions prohibiting the use of clauses that relate to

- negligently caused death or personal injury;¹⁹ and
- the obligations as to title implied into contracts for the sale of goods or hire purchase²⁰.

In addition any party may challenge the validity of an exemption clause in a contract on the grounds that it is unreasonable if

- the clause excludes liability for negligently caused loss or damage (other than death or personal injury)²¹; or
- the clause limits or excludes liability arising in contract and is contained in the other parties "written standard terms of business"²²; or

¹⁶ Providing always that they fall within the Acts geographical jurisdiction. See chapter 4.

¹⁷ S.I.1999/2083. Discussed in chapter 12 below.

¹⁸ Although the form of any replacement legislation is still unclear, there is strong support for the protection afforded business parties being retained, or even expanded. See the Law Commission consultation paper *op cit* fn 3.

¹⁹ s.2(1).

²⁰ s.6(1).

²¹ s.2(2).

²² s.3. (Discussed below at 11.5.2).

- the clause excludes or limits liability for breach of the implied terms in contracts for the sale of goods or hire-purchase²³.

Finally, a business party may also benefit from the provisions of the Act when they deal outside their regular field of business and satisfy the definition of “dealing as consumer” for the purpose of the Act.²⁴

As with any regulatory measure emanating from the UK the Act is, of course, confined in its application to the jurisdiction of the United Kingdom, save for specific situations.²⁵ However, the key restrictions contained within the Act relate to the type of clauses within its remit, the basis of liability and specific express exclusions from the scope of the Act. The influence of these restrictions, in the light of electronic contracting, will now be considered.

11.3.1 Exemption Clauses: Terms Which ‘Exclude or Restrict’.

The Act is restricted in application to exemption clauses relating to certain categories of business liability. The term ‘exemption clause’ is seldom used in the Act itself, instead the Act refers to terms which ‘exclude or restrict’ the particular liability. However, to limit the scope of the Act to clauses which explicitly ‘exclude or restrict’ liability, would leave the Act susceptible to evasion by employing terms which whilst not explicitly excluding or restricting liability, nevertheless have an equivalent effect. The response of the Law Commission was to extend the scope of the Act to clauses, which have equivalent effect to excluding or limiting liability,²⁶ and clauses often described as exemption clauses “in disguise”.²⁷ The main provision can be found in section 13 and by virtue of this section, terms which are drafted in the form of an obligation, or impose onerous criteria for the enforcement of a liability, are treated as if they had directly limited or excluded that liability.²⁸

13. Varieties of exemption clause.

- (1) To the extent that this Part of the Act prevents the exclusion or restriction of any liability it also prevents-

²³ s.6(3).

²⁴ s.12. See the discussion below at 11.5.2.

²⁵ Section 27 provides specifically for situations where parties “opt in” to the provisions of the Act and situations where a deliberate attempt is made to oust the jurisdiction of the Act, when dealing with a consumer.

²⁶ Section 13.

²⁷ Section 3(2)(b). See, Macdonald, E. *Exemption Clauses and Unfair Terms* (Butterworths: London, 1999) at p. 3; Yates, D. *Exclusion Clauses in Contracts* 2ed, (Sweet and Maxwell: London, 1982), pp88-94.

²⁸ *Stewart Gill Ltd v Horatio Myer & Co Ltd* [1992] 2 All ER 257.

- (a) making the liability or its enforcement subject to restrictive or onerous conditions;
- (b) excluding or restricting any right or remedy in respect of the liability, or subjecting a person to any prejudice in consequence of his pursuing any such right or remedy;
- (c) excluding or restricting rules of evidence or procedure;

and to that (extent) sections 2 and 5 to 7 also prevent excluding or restricting liability by reference to terms and notices which exclude or restrict the relevant obligation or duty.

(2) But an agreement in writing to submit present or future differences to arbitration is not to be treated under this Part of this Act as excluding or restricting any liability.

Subsection 1(a) deals with clauses which make the liability or its enforcement subject to restrictive or onerous conditions. These would include time limits on the making of claims which in reality do not allow sufficient time to discover the problem giving rise to a claim,²⁹ or alternatively clauses, which require the party making the claim to pay for the return of a faulty product before a claim can be made. This additional cost has the potential to deter the pursuit of a legitimate claim, particularly with relatively small ticket items.

The use of terms requiring the customer to pay for returns may be a particular problem in electronic contracts because of the increased opportunities for cross-border transactions. The additional costs associated with returned items may be a deterrent to businesses wishing to take advantage of the electronic commerce market and contract terms passing this cost on to the customer may be popular. However, these potential costs may also act to deter customers from entering cross border electronic contracts because they will usually be less able to accommodate the additional cost.³⁰ In the electronic environment the items purchased are often relatively inexpensive consumables and the risk of additional delivery costs may completely remove the financial benefits associated with e-commerce. Subsection 13(1)(b) addresses clauses which exclude or restrict a right or remedy in respect of the liability, or subject a person to any prejudice in consequence of his pursuing any such right or remedy. This would include clauses which allow a claim for damages but purport to exclude the right to terminate a contract on breach. Clauses promising free repairs or

²⁹ Law Commission *op cit* fn 4 at paras. 162 *et seq.*

³⁰ Consumers are specifically afforded protection against such terms, but for the small business UCTA may be a very important source of protection. See below at 11.5.2.

replacement but precluding the right to reject the goods would also fall within this category.³¹

Finally, clauses that attempt to exclude or restrict rules of evidence or procedure are brought within the scope of the Act by subsection 13(1)(c). This would include a clause proclaiming that a signature on a delivery note unequivocally demonstrates that the goods supplied satisfy the specifications or description in the contract.

The clauses described in section 13 will, where the Act indicates, be subject to the requirement of reasonableness and the facts surrounding their use will become relevant.³² Section 13 merely brings the clauses within the scope of the Act, to be tested in the courts. The final part of section 13(1) applies to sections 2 and 5 to 7 and is designed to capture clauses which define the parties' obligations under a contract in a manner which has the equivalent effect of removing or limiting a liability which would otherwise arise, i.e. preventing the liability from arising *ab initio*. The intention behind this subsection is to prevent the evasion of the Act by articulate drafting.³³

The courts have adopted the "but for" test when applying this section to determine whether a term falls within the scope of the Act.³⁴ Hence, if the obligation would have arisen "but for" the term, then the term will become subject to the Act. An example of such a clause would be the obligation in an employment contract for a junior doctor to work exceptionally long hours, potentially leading to injury. The clause had the effect of trying to exempt the employer from his duty of care which would exist "but for" the clause.³⁵ Another example would be a term indicating that goods are 'sold as seen' in an attempt to evade the obligation arising under the Sale of Goods Act that the goods comply with their description.³⁶

The interpretation adopted by the courts to this section of the Act has been criticised as too wide and lacking discrimination, bringing some clauses inappropriately within the scope of the Act. It has been argued that an "expectations test" would be more appropriate being less mechanical and enabling the courts to "make an appropriate 'form and substance' distinction for the purposes of section 13(1)".³⁷ In extending the

³¹ On a literal interpretation this subsection also has the potential to encompass clauses compelling the use of arbitration, which is returned to below.

³² Discussed below at 11.6.

³³ To a large extent it mirrors the provision found in section 3(2)(b).

³⁴ *Smith v Eric S Bush (a firm)* [1989] 2 All ER 514 and *Philips Products Ltd v Hyland* [1987] 2 All ER 620.

³⁵ *Johnstone v Bloomsbury Health Authority* [1991] 2 All ER 293.

³⁶ This implied obligation may only be excluded against a party not dealing as consumer and the term satisfies the requirement of reasonableness – section 6(2).

³⁷ Macdonald, E. "Exclusion clauses: the ambit of s 13(1) of the Unfair Contract Terms Act 1977" (1992)12(3) *LS* 277. An extensive analysis of this issue is not within the scope of this thesis, but it is

scope of the Act to clauses with equivalent effect the Law Commission sought to limit the potential for evasion. However they also appreciated that in doing so they gave rise to the possibility of bringing certain contractual terms inappropriately within the Acts control. One such type of clause, particularly relevant to the electronic environment, is the arbitration clause³⁸ which could be construed as attempting to restrict a right or remedy in respect of a liability.³⁹ However, arbitration clauses are not contrary to public policy and do not oust the jurisdiction of the courts.⁴⁰ When used appropriately they can reduce costs and save the parties and the courts time and inconvenience. In addition, arbitration is subject to specific legislation⁴¹ as recognised by the Law Commission.

“we consider that the possibility that an arbitration clause may operate to the detriment of a party to a contract is a matter which should be regulated by the law relating to arbitration.”⁴²

Hence, section 13(2) attempts to place such clauses beyond the scope of the Unfair Contract Terms Act.⁴³ One point which must be highlighted, however, is the requirement that the agreement to arbitrate be ‘in writing’. The application of requirements of form of this nature to electronic contracts is discussed above in chapter 7. However, it must be re-iterated at this point that without an amendment to the Act by the ‘appropriate minister’,⁴⁴ there will be scope for speculation and legal uncertainty as to whether electronic forms of ‘writing’ will satisfy the requirement in section 13(2). However, in the context of section 13(2), a consideration of the purpose, or function, of the requirement of writing may help remove some of the uncertainty.

undeniable that the issue raises the same criticisms whatever the form of the contract, be it electronic or more traditional. See also *op cit* fn 27.

³⁸ Arbitration and other methods of Alternative Dispute Resolution (ADR) are particularly important for electronic commerce because of their speed, reduced costs and ability to operate effectively in the electronic environment, when compared to the judicial system. A discussion of the importance of arbitration and other forms of ADR is beyond the scope of this research. For a more detailed discussion of the issues see Hornle J, “Disputes Solved in Cyberspace and the Rule of Law”, Work in Progress, [2001](2) *The Journal of Information, Law and Technology (JILT)*. <http://elj.warwick.ac.uk/jilt/01-2/hornle.html/>.

³⁹ The right to go to court to obtain a remedy.

⁴⁰ *Scott v Avery* (1885) 5 H.L.C. 811

⁴¹ For example the Arbitration Act 1996. Arbitration has been the subject of legislation since the 1950’s.

⁴² *Op cit* fn 4 at para. 163.

⁴³ “But an agreement in writing to submit present or future differences to arbitration is not to be treated under this Part of this Act as excluding or restricting any liability.”

⁴⁴ Section 8 of the Electronic Communications Act 2000, see chapter 7.3.

It is submitted that the requirement of a 'written agreement' in section 13(2) relates directly to the desire only to exclude those agreements regulated by the Arbitration Acts from the provisions in the Act. This proposition is supported by references in the Law Commission Report and the scope of the Arbitration Act 1996, the application of which is generally limited to 'agreements in writing':⁴⁵

"The provisions of this Part apply only where the arbitration agreement is in writing, and any other agreement between the parties as to any matter is effective for the purposes of this Part only if in writing."⁴⁶

However, in contrast to UCTA the Arbitration Act does include guidance on the requirement of writing in section 5(6):

"References in this Part to anything being written or in writing include its being recorded by any means."⁴⁷

This definition could therefore be satisfied by an agreement to arbitrate being recorded in electronic form. However, the agreement must be 'recorded', indicating that a permanent copy must be held somewhere which may mean that if the 'agreement' is entered into on a website or by two 'electronic agents' and therefore transient in nature, it may not satisfy the requirement.

11.3.2 Business Liability.

With the exception of section 6(4) the control exerted by the Act is restricted to clauses relating to "business liability", that is liability for breach of obligations or duties arising from things done, or to be done, by a person in the course of a business (whether his own business or another's).⁴⁸ 'Business' includes a profession and the activities of any government department or local authority.⁴⁹ This definition was adopted to encompass a

⁴⁵ The reference to writing relates to Part 1 of the Act. This Part contains the key provisions of the Act including; stay of legal proceedings, arbitral proceedings and tribunal formation and conduct, jurisdiction, awards, costs and powers of the courts in relation to the award.

⁴⁶ Section 5(1) of the Arbitration Act 1996 (1996 c.23).

⁴⁷ Emphasis added.

⁴⁸ Section 1(3)(a).

⁴⁹ Section 14.

broad spectrum of activities, including business to consumer and business to business activities and not restrict the scope of the Act.

“We refer to a transaction where one party is, and the other is not, acting in the course of a business as a “consumer transaction”, and to a transaction in which each party is acting in the course of a business as a “commercial transaction”, using the word commercial in its widest sense as covering commercial, industrial, official and professional activities.”⁵⁰

Contracts formed between individuals, via e-mail, auction sites and private web pages will be beyond the scope of the Act. Regulation of transactions between individuals was felt unnecessary by the Law Commission;

“No one has suggested to us that the use of exemption clauses in connection with services supplied in a purely private capacity is widespread or gives rise to concern;... we have confined our attention to situations in which the use of exemption clauses appears to be the source of a social problem.”⁵¹

A key phrase in the assessment of whether activities are within the scope of the Act is “in the course of a business.” This phrase can be found in a number of sections of the Act and there remains some debate as to its correct interpretation.⁵² The predominant definition in the context of the Act was established in *R&B Customs Brokers v United Dominions Trust*⁵³ in relation to section 12 of the Act which defines “dealing as consumer”.⁵⁴ The court decided that to be “in the course of a business” the activity had to be “integral” to that business or, if incidental to that business, occurring with “sufficient regularity”.⁵⁵ However, it has been argued that this interpretation is inappropriate for application to the definition of “business liability” in section 1(3)⁵⁶ because it would have the effect of restricting the scope of the bulk of the Act considerably.⁵⁷ Sections 2 to 7 of the Act would

⁵⁰ *Op cit* fn 4 para. 4, n 18. Emphasis added.

⁵¹ *Ibid* para. 9.

⁵² See, Macdonald, E. “In the course of a business – a fresh examination” (1999) 3 *Web JCLI* available at; <http://spade3.ncl.ac.uk/1999/issue3/macdonald3.html>.

⁵³ *R&B Customs Brokers v United Dominions Trust* [1988] 1 All ER 847.

⁵⁴ Discussed below at 11.5.

⁵⁵ *Op cit* fn 53.

⁵⁶ *Op cit* fn 52.

⁵⁷ Specifically sections 2 to 7.

only apply to activities, which are “integral” to the business of the seller or “incidental but occurring with sufficient regularity”.

One possible alternative to this definition was adopted by the Court of Appeal in *Stevenson v Rogers*,⁵⁸ a case concerning the phrase “in the course of a business” in the Sale of Goods Act. The court preferred a distinction based upon whether the contract was made in a “purely private capacity” outside the confines of a business. This test would provide a less restrictive approach to the definition of ‘business liability’ in section 1(3) more in keeping with the underlying purpose of the Act, but restrict the scope of the definition of “dealing as consumer”. However, the definition of a purely private sale is open to wide interpretation, potentially creating further uncertainty.

11.3.3(a) Exemptions from the Scope of the Act: Section 26 ‘International Supply Contracts’

The limits and controls on the use of exemption clauses, imposed by the Act are not applicable to international supply contracts. This exclusion could have significant consequences for parties engaging in cross-border electronic commerce. The excluded contracts are defined in section 26:

s 26 International supply contracts.

(1) The limits imposed by this Act on the extent to which a person may exclude or restrict liability by reference to a contract term do not apply to liability arising under such a contract as is described in subsection (3) below.

(2) The terms of such a contract are not subject to any requirement of reasonableness under section 3 or 4 and nothing in Part II of this Act shall require the incorporation of the terms of such a contract to be fair and reasonable for them to have effect.

(3) Subject to subsection (4), that description of contract is one whose characteristics are the following—

(a) either it is a contract of sale of goods or it is one under or in pursuance of which the possession or ownership of goods passes; and

(b) it is made by parties whose places of business (or, if they have none, habitual residences) are in the territories of different States (the Channel

⁵⁸ *Stevenson v Rogers* [1999] 1 All ER 613. A judgment based on the Sale of Goods Act 1979, but dealing with the same phrase. Discussed below at 11.6.

Islands and the Isle of Man being treated for this purpose as different States from the United Kingdom).

- (4) A contract falls within subsection (3) above only if either—
- (a) the goods in question are, at the time of the conclusion of the contract, in the course of carriage, or will be carried, from the territory of one State to the territory of another; or
 - (b) the acts constituting the offer and acceptance have been done in the territories of different States; or
 - (c) the contract provides for the goods to be delivered to the territory of a State other than that within whose territory those acts were done.”

The exclusions only apply to contracts for the sale of goods or those under or in pursuance of which the possession or ownership of goods passes. The definition of ‘goods’ in relation to the subject matter of many electronic contracts is considered above in chapter 3 and discussed in detail below in chapter 13. It is sufficient to note at this point that although many electronic contracts are for ‘traditional’ goods and will potentially fall within the scope of the exclusion in section 26, an increasing number will not, being for services or intangible products. As a consequence, the provisions controlling exemption clauses considered in this chapter will remain relevant to many electronic contracts in spite of their ‘international’ nature.

In addition to being a contract concerning goods, the contract in question must involve the carriage of the goods between States, offer and acceptance across State borders or delivery in a different State to that where the contract was made.

In situations where an electronic contract falls within the scope of section 26 there are some significant consequences to consider, particularly if a consumer is party to the contract in question. Perhaps the most significant consequence would be the removal of the protection afforded by section 6 of the 1977 Act relating to terms implied by section 12 and sections 13 – 15 of the Sale of Goods Act 1979.⁵⁹ Under the Act terms seeking to exclude or limit liability for breach of obligations arising from section 12 (implied undertaking as to title) are automatically ineffective. Attempts to exclude or limit liability for obligations arising under sections 13 – 15 of the 1979 Act (implied undertakings as to conformity with sample, or as to the quality of goods or fitness for a

⁵⁹ The section also applies to corresponding provisions in the Supply of Goods (Implied Terms) Act 1973.

particular purpose) are automatically ineffective against a consumer and only effective insofar as they satisfy the requirement of reasonableness against a non-consumer.

To an extent the Unfair Terms in Consumer Contract Regulations can fill this potential loophole however their effect would only be to subject the term in question to the fairness test rather than providing a prohibition on the use of such terms.⁶⁰

An examination of the background and purpose of this provision may provide a basis for a consideration of whether the exclusion remains an appropriate one for application to electronic contracts.

According to the Law Commission of the time there were a number of justifications for the exemption introduced in section 26.⁶¹ They felt that a country of destination approach should be adopted in relation to goods that were exported from the United Kingdom, with the laws of the country to which the goods were exported regulating contractual freedoms in relation to consumers and other purchasers. The Commission believed that in this way UK exporters would not be placed at a disadvantage in relation to some of their foreign competitors. A second relevant issue was the fact that international supply contracts 'ordinarily involved transactions of some size between parties who were engaged in commerce' and as such the terms of such contracts should be left to the discretion of the business parties dealing at arms length.

Since the 1975 report was produced there have been a number of significant changes in the character of international trade. In particular increased harmonisation of the European Union including an extensive consumer protection policy and the promotion of cross border commerce. With the increased accessibility of foreign markets due to modern communication technologies and the increasing involvement of consumers in contracts whereby goods may be provided or delivered in states other than the consumer's habitual residence, the justifications for the exemption found in section 26 may need reconsidering.

In their recent consultation document on unfair terms in contracts⁶² the Law Commission considered the exclusion found in section 26 in the light of current commercial activity and the developments in consumer protection at the European level. The Law Commission identified the potential gap in the protection afforded by the Unfair Contract Terms Act and highlighted the failure to draw a distinction between

⁶⁰ The Director General of Fair Trading may use his powers under the Regulations to suggest to sellers and suppliers that the terms in question should be removed. See below at p 257.

⁶¹ Law Commission Second Report on Exemption Clauses (Law Com. No. 69. August 1975)

⁶² Law Com No. 166 (Joint Consultation document, November 2002)

consumer and non-consumer contracts in section 26. The Commission concluded that in the light of European Legislation relating to unfair terms in consumer contracts⁶³ and consumer guarantees⁶⁴ the exemption found in s.26 may be contrary to European Law and policy in relation to consumers. The Commission also noted a potential discrepancy in relation to the Rome Convention on the law applicable to contractual obligations (enacted in the UK in the Contracts (Applicable Law) Act 1990) in that the consumer retains the protection of the mandatory rules of his or her home state, regardless of whether the applicable law as dictated by the Acts provisions is the law of his or her home state.

The Commission makes a preliminary proposition that in any new regulations on unfair terms the exclusion found in section 26 is not reproduced in relation to consumer contracts. In this way the consumer does not lose any of the protection afforded by the laws of his habitual residence.

In addition it is suggested that the implied undertakings as to title are so fundamental that the prohibition on excluding or limiting liabilities arising out of s.12 of the Sale of Goods Act should be affirmed in relation to consumer or non-consumer purchasers of goods, whether or not those goods are delivered to the UK.

11.3.3(b) Exemptions From the Scope of the Act: Schedule 1

The contracts contained in Schedule 1 of the Act are either wholly or partly excluded from its application. In general they reflect the need or existence of specific provisions with appropriate safeguards and controls for the particular subject matter.⁶⁵ Sections 2-4 of the Act do not extend to contracts of insurance; contracts or parts of a contract relating to the creation or transfer of an interest in land or intellectual property rights; any contract relating to the formation or dissolution of a company or its constitution; or the transfer of securities;⁶⁶ charterparties and carriage of goods by ship or hovercraft.⁶⁷ Contracts of employment are excluded from the scope of Section 2 of the Act, except insofar as they favour the employee.⁶⁸

⁶³ Council Directive 93/13/EEC on unfair terms in consumer contracts (O.J. No. L95, 21.4.93, p. 29) implemented in the UK by the Unfair Terms in Consumer Contracts Regulations 1999 (previously 1994).

⁶⁴ Directive 1999/44/EC "on certain aspects of the sale of consumer goods and associated guarantees" implemented in the UK by The Sale and Supply of Goods to Consumers Regulations 2002.

⁶⁵ In a similar vein to the discussion of arbitration clauses above.

⁶⁶ (Sch 1, 1(a-e)).

⁶⁷ (Sch 1, paragraph 2 & 3).

⁶⁸ (Sch 1, ss4).

A number of the contracts excluded by Schedule 1 are increasingly being formed electronically. However, the most common of these excluded contracts being formed electronically are those involving material protected by copyright and other intellectual property rights. Computer software and a wide range of entertainment media can be 'dematerialised' and transferred easily, quickly and conveniently by electronic forms of communication, particularly the Internet. The majority of these items will be protected by copyright and if the exclusion in Schedule 1(1)(c) were to encompass such contracts a significant number of electronic contracts would be beyond the scope of UCTA. However, the vast majority of transactions only involve the transfer of a licence to use, which is arguably not the creation, transfer or termination of a right or interest in the intellectual property.

If a particular contract does involve the transfer or creation of a right or interest in intellectual property there may be a further limit on the effects of Schedule 1(1) if the Schedule is interpreted correctly. By virtue of section 1(a) it is clear that any contract of insurance is beyond the scope of sections 2-4 of the Act. However, the ousters contained in subsections (b) to (e) contain a subtly different terminology and appear to be of a more limited effect than subsection 1(a). In subsections (b)-(e) contracts are only excluded from the scope of sections 2-4 of the Act in so far as the contract relates to the particular subject matter contained within those subsections. For example, if a customer were to enter a contract for a piece of software and the contract contained the transfer of a right or interest in the intellectual property, then only the aspects relating to that intellectual property would be excluded from the scope of sections 2-4 of the Act. Support for this interpretation can be found in the judgment of Thayne Forbes, J. in *The Salvage Association v CAP Financial Services Ltd*⁶⁹ that a restrictive approach will be taken in the application of the paragraph.

"The use of the words "... any contract so far as it relates to..." in subparagraph (c) shows clearly that the subparagraph is strictly limited in its application and that it does not necessarily extend to all the terms of a relevant contract."⁷⁰

And

"If a term is one which is concerned with aspects of the contract between the parties other than the creation or transfer of rights in the intellectual property attaching to the product, then paragraph 1(c) does not apply."⁷¹

⁶⁹ [1995] F.S.R. 654.

⁷⁰ *Ibid* at p. 663.

Hence, only the terms which directly relate to the creation, transfer or termination of intellectual property rights will be excluded. This approach is consistent with the terminology used in the Schedule, particularly when the omission of the words “so far as it relates to” in the subparagraph excluding contracts of insurance is considered.⁷²

11.3.4 Evasion of the Act by the use of a ‘choice of law’ clause

It has already been noted above that under the Rome convention a consumer cannot be deprived of the protection of the mandatory rules of his habitual residence, examples of which would include the provisions in the UCTA. However, to benefit from this protection the consumer must enter the contract in specific circumstances; the contract must be preceded by a specific invitation addressed to him or by advertising and the consumer must take the steps necessary for the conclusion of the contract in his habitual residence.⁷³

The Unfair Contract Terms Act also contains a provision in s.27(2)(b) to attempt to deal with evasion of its protection by choice of law. The provisions of the Act apply notwithstanding a contract term which applies or purports to apply the law of some country outside the United Kingdom where a consumer, who is habitually resident in the United Kingdom, has taken the steps necessary for the conclusion of the contract here.⁷⁴ In tandem, these provisions provide the consumer with significant protection when entering electronic contracts, particularly with overseas vendors who may seek to exclude the protection afforded by UCTA by using a choice of law clause.

In relation to non-consumers, party autonomy is retained with parties free to choose the law of any country to apply to their contract. However, s.27(2)(a) does allow the court to retain some discretion to apply the provisions of the Act in the face of a conflicting choice of law clause where it appears to the court or arbiter that the clause has been included ‘wholly or mainly’ to evade the operation of the Act

11.4 Structure of the Act.

The Act can be divided into ‘active’ sections and ‘definition’ sections. The ‘active sections’ determine the application of the Act. These sections dictate the type of notice or

⁷¹ *Ibid.*

⁷² There has been some debate regarding the correct interpretation of the clause, see *Micklefield v SAC Technology* [1991] ALL ER 275 and *Electricity Supplies Nominees Ltd v IAF Group plc* [1993] All ER 372.

⁷³ See Chapter 5 para 5.2.7 above.

⁷⁴ This requirement is discussed in detail above in chapter 4 (4.3.5).

contractual clause subject to control and the form of that control, in particular whether the clause is subject to total prohibition or to the test of reasonableness. Key definition sections supplement the active sections. The definition sections explain the terminology used within the Act, to aid application.

11.5 Substantive Elements of the Act and their potential impact on electronic contracting.

11.5.1 Negligence Liability.⁷⁵

10.5.1.1 Definition of “negligence”: Section 1(1).

The word ‘negligence’ has a specific definition in the context of the Unfair Contract Terms Act. The definition encompasses a breach of any obligation, arising from the express or implied terms of a contract, to take reasonable care or exercise reasonable skill in the performance of the contract; of any common law duty to take reasonable care or exercise reasonable skill (but not any stricter duty); and, of the common duty of care imposed by the Occupiers Liability Act 1957 or the Occupiers Liability Act (Northern Ireland) 1957.

This is a deliberately broad definition of negligence, expressly including reasonable care and skill in the performance of a contract in addition to the common law duty to take reasonable care. The need to bring as many clauses as possible within the scope of the Act, beyond the technical meaning of negligence in English Courts, reflected a growing concern regarding clauses or notices restricting or excluding liability for negligence. In the words of the Law Commission:

“... clauses or notices exempting from liability for negligence are in many cases a serious social evil and our review of the powers at present at the disposal of the court for dealing with such clauses shows that they are far from adequate.”⁷⁶

⁷⁵ Negligence liability

(1) A person cannot by reference to any contract term or to a notice given to persons generally or to particular persons exclude or restrict his liability for death or personal injury resulting from negligence.

(2) In the case of other loss or damage, a person cannot so exclude or restrict his liability for negligence except in so far as the term or notice satisfies the requirement of reasonableness.

(3) Where a contract term or notice purports to exclude or restrict liability for negligence a person’s agreement to or awareness of it is not in itself to be taken as indicating his voluntary acceptance of any risk.

⁷⁶ *Op cit* fn 4 above at page 19 para. 44.

Section 2 of the Act places a total prohibition on the exclusion or limitation of liability for death or personal injury⁷⁷ and permits the exclusion or limitation of liability for other damage only insofar as the term or notice satisfies the requirement of reasonableness.⁷⁸ The section is not limited to contractual terms but extends to non-contractual notices purporting to restrict or exclude liability for negligence.⁷⁹ 'Notice', for the purposes of the Act includes: an announcement, whether or not in writing, and any other communication or pretended communication.⁸⁰ A classic example of this type of notice would be a notice declaring that the use of a car park, building or other facility is at the 'owner's risk'. Notices delivered in electronic form clearly fall within this definition with the express exclusion of a need for 'writing' and the inclusion of 'any other form of communication'.

The inclusion of notices in this section extends its application to a growing practice in the online environment. On the Internet in particular, many Internet Service Providers and other web sites utilise notices purporting to exempt them from liability for negligently caused loss. These notices are usually introduced at the point of entrance to the site as 'terms and conditions of website use', before the downloading of material or in e-mail disclaimers. With no contractual nexus being required by the section these notices are within the scope of the provision and subject to the corresponding controls on their use. Clauses seeking to exempt liability for negligence will often be found with downloads of software or other media. Such downloads have the potential to transfer viruses and the service provider will seek to exclude or restrict his liability against a claim that he negligently allowed a virus to be downloaded with his media causing damage to the recipient's machine. By virtue of this section, such a clause will have to satisfy the 'requirement of reasonableness' to be effective.

The section does not discriminate between those who deal as consumer for the purpose of the Act and those who do not. This approach gives the section a broad scope for application, in line with the approach taken to the definition of negligence discussed above. Small and medium sized enterprises can benefit from this provision, which may in turn increase confidence in the use of the Internet and other electronic media.

⁷⁷ Section 2(1).

⁷⁸ Section 2(2).

⁷⁹ *Davies v Parry* [1988] 1 EGLR 147 and *McCullagh v Lane Fox & Partners Ltd* [1996] 1 EGLR 35.

⁸⁰ Section 14.

The injured party's apparent agreement to, or awareness of, the term should not, in itself indicate voluntary acceptance of any risk.⁸¹ The Law Commission stated that, "awareness of the content of the term or notice is a matter to take into account, but cannot of itself be regarded as conclusive: the courts must still have regard to all the relevant facts of the case".⁸² Hence, an apparent consent to the risk of loss or damage will not automatically provide a defence for a service provider in an action for loss due to negligence.⁸³ The clause or notice will still be either subject to the complete prohibition in section 1(1), or subject to the requirement of reasonableness in section 1(2).

Internet Service Providers (ISP), those wishing to sell products on-line and even businesses providing free or trial period offers or services will have to consider the possibility that their exemption clauses may be tested under section 2 of UCTA.⁸⁴ One of the most significant potential risks for an ISP is liability for loss or damage occurring due to a breach in security on his server. Most service providers employ security safeguards for their own protection and to promote confidence in the minds of their customers or users. For the majority such protection involves the use of a secure server and some form of encryption. However, even with the implementation of security measures there remains a tangible risk that a customer's personal or financial information may be 'stolen' or that a virus may be transmitted to a customer directly, or within a downloaded piece of software or information. With this possibility in mind, service providers see exemption clauses or disclaimers as a necessary safeguard against the possibility of a flood of actions should their security be breached. By virtue of Section 2 of UCTA such clauses will be subject to the test of reasonableness.⁸⁵

A potentially important benefit of the application of section 2 of the Act to electronic contracting is the ability to control, to some extent, the use of exemption clauses and notices by service providers to transfer the risk of using the electronic medium to the customer or user.

⁸¹ Section 2(3).

⁸² *Op cit* fn 4 above, page 51 para 134.

⁸³ The defence of *volenti non fit injuria*.

⁸⁴ Naturally the fact that the service is 'free' may go some way to demonstrating the reasonableness of the clause.

⁸⁵ Discussed below at 11.6.

11.5.2 Contractual Liability⁸⁶

Section 3 of the Unfair Contract Terms Act is a broadly applicable provision concerning contractual liability. The wide scope of the section creates the potential for overlap with other parts of the Act, in particular sections 2 and 6. Contractual terms excluding or restricting liability for breach of contract are the main targets of the section, although terms that stipulate that a party may render a contractual performance substantially different from that reasonably expected, or render no performance at all, are included by virtue of section 3(b).⁸⁷

The application of the section to any breach of contract, rather than to a specific category of breach, contributes to the overall breadth of applicability of the Act.⁸⁸ This is complemented by the fact that the section offers protection to parties who deal as consumer and to those who do not, but who deal on the other parties 'written standard terms of business'. A contractual term falling within the scope of section 3 is subject to the requirement of reasonableness in any adjudication of whether the term is effective. The section has three discernible elements:

- a) the applicable forms of contractual relationship, or 'gateways'⁸⁹ to the section;
- b) the nature of the contract terms which will attract the application of the section; and
- c) the application of the requirement of reasonableness to the term in question.

11.5.2.1 The "Gateways".

Section 3 is only applicable where one party either 'deals as consumer' or on the other party's 'written standard terms of business'. Although these 'gateways' are

⁸⁶ Liability arising in contract.

This section applies as between contracting parties where one of them deals as consumer or on the other's written standard terms of business

As against that party, the other cannot by reference to any contract term- when he himself is in breach of contract, exclude or restrict any liability of his in respect of the breach; or claim to be entitled-

(i) to render a contractual performance substantially different from that which was reasonably expected of him, or

(ii) in respect of the whole or in any part of his contractual obligation, to render no performance at all,

except in so far as (in any of the cases mentioned above in this subsection) the contract term satisfies the test of reasonableness.

⁸⁷ This subsection is, in many ways, analogous to the provision found in section 13(c) of the Act.

⁸⁸ Section 6 for example is limited to breaches of the statutory implied terms in contracts of sale or hire purchase.

⁸⁹ This label is used by Jacobs, E. *Effective Exclusion Clauses* (Fourmat: London, 1990). ch.5.

essentially distinct, there is some scope for overlap between them. By their very nature consumer contracts will almost invariably contain the seller's 'written standard terms'. At this point two factors require consideration; the definition of the phrase 'deals as consumer' and the definition of 'written standard terms of business'.

*'Dealing as consumer'*⁹⁰

This definition is of considerable importance within the Act because those who 'deal as consumer' are afforded greater protection against exemption clauses. To 'deal as consumer' a party must neither make the contract in the course of a business or hold himself out as doing so, and the other party must enter the contract in the course of a business. The Act does not define 'in the course of a business' and interpretation has been left to the courts. The approach adopted by the courts has been the subject of criticism from academic commentators⁹¹ and the courts themselves have departed from the interpretation adopted in the context of UCTA when considering the meaning identical terminology in different consumer protection oriented Acts.⁹² Nevertheless, the approach adopted in *R & B Customs Brokers v United Dominions Trust* remains the leading authority on the matter.⁹³

'In the course of a business'

To 'deal as consumer' the buyer must not make, or hold himself out as making the contract 'in the course of a business'. Equally, the seller must make the contract 'in the course of a business'. The inclusion of this second requirement reflects the desire

⁹⁰ Section 12 "Dealing as consumer".

- (1) A party to a contract "deals as consumer" in relation to another party if-
 - (a) he neither makes the contract in the course of a business nor holds himself out as doing so; and
 - (b) the other party does make the contract in the course of a business; and
 - (c) in the case of a contract governed by the law of sale of goods or hire-purchase, or by section 7 of this Act, the goods passing under or in pursuance of the contract are of a type ordinarily supplied for private use or consumption.
- (2) But on a sale by auction or by competitive tender the buyer is not in any circumstances to be regarded as dealing as consumer.
- (3) Subject to this, it is for those claiming that a party does not deal as consumer to show that he does not.

⁹¹ Macdonald, *op ci* fn 52.

⁹² See *Stevenson v Rogers* [1999] 1 All ER 613. The most recent attempt to alter the situation arose out of the government's beleaguered attempts to implement the EC Directive on consumer guarantees.

Unfortunately due to the rather rushed (poor) drafting the phrase remains. It is hoped that the issue will be redressed in the forthcoming Law Commission overhaul and amalgamation of UCTA and UTOCR.

⁹³ [1988] 1 All ER 847.

expressed by the Law Commission not to interfere with individuals entering contracts in a private capacity.⁹⁴ The contracts targeted were those between businesses and individuals acting in their private capacity. However, when interpreting the provision, rather than attaching importance to the Law Commission's distinction of those agreements entered into in a 'purely private capacity' from those entered in a 'business capacity' the courts adopted a definition applied previously to cases concerning a similarly worded provision in section 1 of the Trade Descriptions Act 1968 (TDA).⁹⁵

In the context of the TDA, in *Davies v Sumner*⁹⁶ Lord Keith considered tasks which were 'integral' to a business clearly 'in the course of a business', but that if the contract was for a purpose not 'integral' to the business then a certain degree of regularity was required before the activity could be considered 'in the course of a trade or business'.

"The expression 'in the course of a trade or business' in the context of an Act having consumer protection as its primary purpose conveys the concept of some degree of regularity..."⁹⁷

This definition was discussed in detail by the Court of Appeal and applied to the Unfair Contract Terms Act in *R&B Customs Brokers v United Dominions Trust*.⁹⁸ Dillon LJ explained the definition of 'in the course of a business' thus:

"There are some transactions which are clearly integral parts of the business concerned, and these should be held to have been carried out in the course of those businesses; this would include, apart from much else, the instance of a one-off adventure in the nature of trade where the transaction itself would constitute a trade or business. There are other transactions, however, such as the purchase of the car in the present case, which are at the highest only incidental to the carrying on of the relevant business; here a degree of regularity is required before

⁹⁴ *Op cit* fn 4 at para. 9.

⁹⁵ 1(1) Any person who, *in the course of a trade or business*, - (emphasis added). The purpose of the two Acts is however, somewhat incompatible.

⁹⁶ *Davies v Sumner* [1984] 3 All ER 831, [1984] 1 WLR 1301 (HL)

⁹⁷ *Ibid* at 835. See also *Haverling London Borough v Stevenson* [1970] 3 All ER 609.

⁹⁸ [1988] 1 All ER 847.

it can be said that they are an integral part of the business carried on and so entered into in the course of that business.”⁹⁹

His Lordship explained that the primary purpose of both the TDA and UCTA was consumer protection and that it would be ‘unreal and unsatisfactory’ to conclude that the phrase ‘in the course of a business’ had a significantly different meaning in the two Acts. In particular he felt that the phrase should not be given a wider meaning in the context of section 12.

Hence, three forms of transaction can be identified as ‘in the course of a business’ for the purpose of section 12:

- 1) transactions being integral to the business concerned,
- 2) transactions not integral to, but occurring with ‘sufficient regularity’ and,
- 3) one-off adventures in the nature of trade.

The advantage of this approach is the expansion of the protection afforded by the Act to business entities entering transactions not integral to the business and not occurring with a sufficient degree of regularity. In *R&B Customs Brokers* this gave the company valuable protection against a clause which would have resulted in an extensive and unexpected loss for them. However, the approach taken in *R&B Customs* has been criticised and at times overlooked.¹⁰⁰

The first criticism relates to the function of the statute from which the definition was taken. The Trade Descriptions Act, although concerned with consumer protection, is a criminal statute and the definition relates to the boundaries of a criminal offence. It is arguable that in this context a narrow approach should be adopted in defining who may be liable for a criminal act. The Unfair Contract Terms Act deals with civil liability; the approach and reasoning adopted in the context of criminal liability is not necessarily apposite when dealing with civil liability and the purpose of the 1977 Act. Arguably a wider definition *should* be adopted in the context of section 12.

⁹⁹ *Ibid* per Dillon L.J. at p 854.

¹⁰⁰ As indicated above. See also *St Albans City & District Council v International Computers Ltd* [1996] 4 All ER 491; [1997] F.S.R. 251. The court did not make any reference to the judgment in *R&B Customs Brokers*.

The second argument relates to the scope and applicability of the Act. Section 12(1)(b) requires that the seller or supplier does act 'in the course of a business' for any party to qualify as dealing as consumer.¹⁰¹ The consequence of the approach adopted in *R&B Customs Brokers* is that the protection afforded by the Act may be restricted. For example, any subsequent sale by *R&B* would deny the other party the protection of dealing as consumer because *R&B* would not be dealing in the course of a business as required by s12(1)(b).

Finally, as has already been indicated, the phrase 'in the course of a business' is also used in Section 1(3) defining 'business liability' and correspondingly the scope of the majority of the Act. If the definition accepted in *R&B Customs* were applied here it could severely restrict the scope of the Act. Sections 2 to 7 of the Act would only apply to sales, which are 'integral' to the business of the seller or 'incidental but occurring with sufficient regularity'. This would appear to be over restrictive and not in the spirit of the legislative purpose of the Act.

The differing degrees of protection against unfair contract terms, afforded by UCTA are intended to reflect the need to protect the consumer as a 'weaker party'. The basis for differentiating under *R&B Customs* is the nature of the business carried on by the seller rather than anything to do with strength of bargaining power. If *R&B* is applied consistently it will restrict the application of the Act.

An alternative approach to avoid the risk of unduly restricting the scope of the Act, would be to use a different definition of 'in the course of a business', in the context of different sections of the Act. However, as pointed out by Kidner, to give the same phrase different meanings in the same statute would lead to confusion and be something of an absurdity.¹⁰² There would appear to be some justification for a reconsideration of the definition of 'in the course of a business' in the context of UCTA.

In the most recent judicial discussion of the phrase 'in the course of a business', *Stevenson v Rogers*,¹⁰³ the Court of Appeal decided that the definition adopted in *R&B Customs Brokers* and *Davies v Sumner* was inappropriate to apply in the context of the Sale of Goods Act. When dealing with the implied terms of the Sale of Goods Act the Court felt that a wider definition should be adopted to broaden the application of the implied

¹⁰¹ The purpose behind this requirement being the exclusion of 'purely private sales' between individuals from the scope of the Act.

¹⁰² Kidner, R. "The Unfair Contract Terms Act 1977 - who deals as consumer?" (1987) 38 *NILQ* 46.

¹⁰³ [1999] 1 All ER 613.

term. The Court felt that the phrase 'in the course of a business' should be given its natural meaning which Potter L.J. explained would help the courts to

“distinguish between a sale made in the course of a seller’s business and a purely private sale of goods outside the confines of the business (if any) carried on by the seller.”¹⁰⁴

The emphasis in this definition would be whether the sale was a 'purely private' one or not. This definition would appear to extend the term 'in the course of a business' to a wider range of activities. However, if this definition were adopted uncertainty would remain – how should the phrase 'purely private sale' be defined? Nevertheless it would encompass the more 'natural' meaning of 'in the course of a business' vis-à-vis 'anything done by and for a business'.¹⁰⁵ There are also a number of references to contracts made in a 'purely private' capacity in the Law Commission Report. Finally, there is certainly scope for an argument that the definition adopted for UCTA should be the same as the one adopted in for the SGA and not the one applied to the TDA. UCTA and SGA provide consumer protection in relation to civil liability whereas the TDA deals with criminal liability.

At present a business entering contracts outside of their normal field of business is afforded an added level of protection by the definition adopted in *R & B Customs*. For business parties, particularly small businesses, this additional protection will be welcomed when contemplating entering contracts with larger and more powerful corporations. However, the broader effect of the provision may be undermined by this interpretation.

'Holding out'

To 'deal as consumer' a party must not enter the contract 'in the course of a business' or 'hold himself out' as doing so. By 'holding out' the customer is giving the impression that he is entering the contract as a business party, usually to obtain a trade discount, extended credit or to buy products not usually sold retail. By holding out the customer assumes the potentially higher liability risk associated with a non-consumer transaction. Due to the lack of any physical meeting of the parties in the electronic and

¹⁰⁴ *Ibid* per Potter LJ at 623.

¹⁰⁵ Macdonald, *op cit* fn 52.

in particular on-line environment the question of whether a party is 'holding out' may become more important because of difficulties in identifying the contracting parties.

The burden of proof is on the party claiming that the other has held himself out as acting in the course of a business and hence did not deal as consumer. In *R & B Customs* this burden was apparently not satisfied by showing that the contract and finance application were made out in the company's corporate name and the business details were entered on to the finance form. The issue of holding out was not discussed further in that case and the issue has received little attention in the courts. A difficulty exists in assessing where the courts will draw the line on holding out.

Many businesses using websites provide a different set of terms for consumer or business customers, reflecting the statutory regime of the jurisdiction involved. This system usually operates by asking whether the customer is a trade customer or an individual. While this does not necessarily dictate the legal standing of a customer it may be the only realistic way that a supplier can distinguish between his customers for the purpose of trade discounts. By declaring that they are 'trade' the customer would obtain the discount, but may enter the contract on less favourable terms than the normal consumer. It would appear clear in this situation that the customer is 'holding himself out' as making the contract 'in the course of a business'. However, if the *R & B Customs* definition of 'in the course of a business' were applied consistently, this would require that the buyer gives the impression, or 'holds out', that the transaction is integral to his business or occurring with sufficient regularity. This would be a rather artificial and difficult approach for the courts to apply. The more realistic approach would be to investigate whether the customer indicated that he was acting in a business rather than private capacity. Unfortunately this approach would create a rather bizarre and unacceptable dichotomy whereby a customer may be holding itself out as acting 'in the course of a business', but under the test in *R & B Customs*, not actually acting in the course of a business because the transaction itself is not integral to his business or occurring with sufficient regularity. Once again the definition in *R & B Customs* appears incompatible with the rest of the Act

It is submitted that what should be required here is that the seller reasonably believed that he was dealing with a business party, in the broadest sense. This would include the taking of appropriate steps if there is uncertainty. At this point the definition of "in the course of a business" adopted in *Stevenson* would appear more appropriate, if the party is assessed on the basis of whether or not he is holding out as entering the

contract in the capacity of a purely private individual or not? This would be a more logical and arguably fairer approach.

A practical approach for a supplier in this situation may be to attempt to create some form of collateral contract with the customer, by requesting that the customer electronically 'signs' a document declaring that he is entering the contract in the course of his business and indemnifying the seller for any additional liability incurred due to the purchaser transacting on "trade" terms. Nevertheless, such an agreement may be open to challenge under other sections of the Unfair Contract Terms Act and potentially UTCCR.

Goods 'ordinarily supplied for private use or consumption'

Section 12(1)(c) requires that goods purchased must be of a 'type ordinarily supplied for private use or consumption' for a party to qualify as dealing as consumer. The phrase is clearly intended to exclude purchases of goods not usually sold in the consumer market. However, the phrase is rather ambiguous in what is meant by a 'type' of goods. Many 'types' of goods are not ordinarily supplied for private use because of their cost. Does this mean that because an individual can afford the goods he does not qualify as a consumer? With more competitive markets and advancements in technology the cost of products not ordinarily associated with private use has been reduced. Electronic commerce means that these products are also readily available. Computer software is a case in point. Computer software, if it can be categorised as goods,¹⁰⁶ can have many applications. Some of these could be seen as 'ordinarily supplied for private use' such as home office products, but what if someone purchases the professional version of a package or state of the art video capture devices, mixing and editing deck? Some individuals hobbies may also mean that they purchase items not ordinarily supplied for private use.

An item may ordinarily be supplied for private use or consumption in small quantities, but if an individual buys a very large quantity of that item does that take him outside the definition of 'deals as consumer'? In the context of 'one-off adventures in the nature of trade'¹⁰⁷ an analogy has been drawn with revenue law cases whereby the large quantities of an item purchased led the court to determine that the items were not

¹⁰⁶ See the discussion in chapter 13.2.

¹⁰⁷ Such ventures will also be classed as 'in the course of a business' because they have the 'flavour of trading'. See Dillon LJ in *R & B Customs Brokers v United Dominions Trust* [1988] 1 All ER 847 at p 854.

meant for private use.¹⁰⁸ It is submitted that even before the advent of electronic commerce the 'quantity' of an item purchased is not a good criteria upon which to define activities as 'in the course of a business'. Advances in cross channel transport have resulted in hundreds of people purchasing goods in quantities which would suggest that they are not for private use or consumption. However, the cheap prices mean that individuals will buy 'unusual' quantities to save money. With the advantages of the internet the likelihood of purchases of 'unusual' quantities of certain items may increase with individuals taking advantage of better value and a one time transportation cost. The nature of a market may dictate what is purchased and in what quantity.

A decision on whether a party may or may not be classed as a consumer and afforded the additional protection provided by the Act based upon the nature of the goods purchased would appear to leave room for considerable uncertainty. This is particularly undesirable in the electronic environment where the 'type' and the 'quantity' of goods may not be 'ordinary'.¹⁰⁹

The issues discussed above in relation to the definition of "in the course of a business" result in uncertainty in the definition of consumer and have the potential to create an undesirable dichotomy within the Act.¹¹⁰

It is important for parties entering a potentially large number of cross border or international contracts to ascertain and control their foreseeable liabilities. Whilst this concern remains constant regardless of the medium used for entering such contracts, the borderless nature of the Internet and other electronic media makes the issue particularly relevant for electronic contracts.

¹⁰⁸ See Koffman, L. and Macdonald, E. *The Law of Contract* 4th ed. (Tolley, 2001) at p. 197. *Rutledge v Inland Revenue Commissioners* (1929) 14 TC 490 and *Martin v Lowry* [1927] AC 312.

¹⁰⁹ The position has recently been amended by the Sale and Supply of Goods to Consumers Regulations 2002 (Statutory Instrument 2002 No. 3045), Regulation 14. From March 1st 2003, where the first party 'not dealing in the course of a business' is an individual this subsection will not apply. In section 12, after subsection (1) the following subsection is inserted; "(1A) But if the first party mentioned in subsection (1) is an individual, paragraph (c) of that subsection must be ignored." This position acknowledges that a business or corporate entity may 'deal as consumer', but retains the perceived limitations associated with subsection (c) in place. The uncertainties discussed in the preceding section remain in place.

¹¹⁰ This contention relates to the use of the phrase "in the course of a business" in section 1 in the context of "business liability" and the approach adopted in relation to section 12 under *R & B Customs Brokers*. To avoid restricting the scope of the Act the two identical phrases would appear to require different definitions.

'On the Others Written Standard Terms'

The second 'gateway' to the section requires a party to contract on the others "written standard terms of business". This phrase raises a number of questions of interpretation, particularly in the electronic environment.

The first point to note is that the standard terms must be in 'written' form. Traditional requirements of form such as writing and signature have the potential to create uncertainty in the context of electronic communications.¹¹¹ If electronic forms of communication do not satisfy this requirement then many electronic contracts will be excluded from the scope of section 3 and parties, particularly small businesses, may lose valuable protection.¹¹² The issue is discussed in chapter 7 where it is concluded that electronic communications which take visible form will probably satisfy a formal requirement of writing, whereas communications which remain solely in their 'electronic phase' (such as EDI or contracts concluded by electronic agents) probably will not. If this interpretation were adopted by the courts then there would be scope for the argument that where contract terms remain in 'electronic form' they are not 'written' and will not fall within this part of section 3.¹¹³

The remainder of the terminology used in the second 'gateway' to the application of section 3 also requires some consideration. There are three important questions:

- Whose standard terms?
- How 'standard' do the terms have to be?
- Which terms are subject to the Act?

Whose standard terms?

A party may contend that the standard terms are not 'his', but rather standard terms drafted by his supplier or a particular trade body and therefore beyond the scrutiny of section 3. For example a party may supply goods on a standard form common to a

¹¹¹ See above in chapter 7.

¹¹² Macdonald, E. & Poyton, D. "A particular problem for e-commerce: Section 3 of the Unfair Contract Terms Act 1977." [2002] 3 *WebJCLI*. Available at <http://webjcli.ncl.ac.uk/2000/issue3/macdonald3.html>.

¹¹³ However, the clear objective of the section is to deal with standard form contracts (particularly when the section applicable to Scotland is considered. Section 17 uses the phrase 'standard form contract' rather than 'written standard terms'). The court may consider that the 'written' requirement should not be an obstacle capable of defeating the purpose of the section.

particular trade or industry, which may have been drafted by a regulatory body. Certain goods, computer software for example, may be supplied with standard terms in a license agreement from the producer of the software. In neither of the preceding scenarios can the 'standard terms' be properly called the supplier's standard terms. However, a court may reject such a proposition on the basis that in joining a particular trade body, or using an agent, or supplying particular goods, the supplier has adopted the terms or conditions 'as his own'. What is important is that the terms are the basis on which his business is conducted rather than the origin of the terms.

How 'standard' do the terms have to be?

Clearly if the parties have negotiated the individual contract to their specific needs the terms will not be 'standard'. In *The Flamar Pride*¹¹⁴ Potter LJ felt that the fact that the contract was

“negotiated between the parties, in that the standard form of [...] agreement which the defendants possessed at the time [...] was subject to a number of alterations to fit the circumstances of the plaintiffs' case before its terms were finalized between the parties.”¹¹⁵

precluded it from falling within s.3 (1) of the Act. However, the 'negotiations' must actually have an effect on the substance of the standard terms otherwise section 3 will still apply. In *St Albans City & District Council v International Computers Ltd*¹¹⁶ Nourse LJ agreed with the words of Mr Justice Scott Baker in the court below, that the

“...defendant's general conditions remained effectively untouched in the negotiations... the plaintiffs accordingly dealt on the defendant's written standard terms for the purposes of section 3(1)”¹¹⁷

¹¹⁴ *Flamar Interocean v Dermac (The Flamar Pride and The Flamar Progress)* [1990] 1 Lloyd's Rep. 434.

¹¹⁵ *Ibid* at (p.438).

¹¹⁶ *St Albans City & District Council v International Computers Ltd* [1996] 4 All ER 491; [1997] F.S.R. 251.

¹¹⁷ *Ibid* at p. 263. See also *Salvage Association v CAP Financial Services Ltd* [1995] F.S.R. 654 and *Watford Electronics Ltd v Sanderson CFL Ltd* [2000] 2 All E.R. (Comm) 984.

There has been some judicial indication that where there has been no negotiation of the relevant exempting terms in a contract, then the contract will be treated as on 'written standard terms'.¹¹⁸ In *Pegler Limited v. Wang (UK) Limited*¹¹⁹ the court did not consider it necessary for the entire contract to be in standard form; just standard in relation to the 'material clauses'. The exemption clauses inserted by the seller were non-negotiable and therefore the contract had been concluded on the seller's 'written standard terms of business'. It could be argued that this is a rather generous interpretation of the phrase but it is certainly in line with the purpose of the Act.

The predominant approach to whether a contract has been entered into on the other party's 'written standard terms' would appear to require that the seller's pre-formulated terms and conditions had not been significantly altered or departed from as a result of negotiations. It has also been suggested that the relevant case law suggests that the exemption clause in question must not have been the subject of negotiations.¹²⁰ However, it is submitted that this factor should not be decisive in the question of whether the contract is made on written standard terms but rather a relevant factor in the assessment of the reasonableness of that clause. The 'gateways' to section 3 are indicative of contractual relationships where one party has a dominant or controlling level of bargaining power.¹²¹ The important question in relation 'standard terms of business' should be the existence of pre-formulated terms and the extent to which they are varied by the parties negotiations.

For many electronic contracts, particularly those entered into via interactive websites or by other electronic agents, the terms and conditions will be pre-formulated and fixed with no room for negotiation. There may be a 'choice' as to the terms relating to payment method and delivery, but such choices cannot truly be called negotiations and would not preclude the contract from being on standard terms for the purpose of section 3.

Which terms are subject to the Act?

A final question which must be considered is whether the offending clause itself has to be one of the 'written standard terms' of the contract. It will often be the case

¹¹⁸ *St Albans City & District Council v International Computers Ltd* [1996] 4 All ER 491; [1997] F.S.R. 251 per Nourse L.J. at 253.

¹¹⁹ [2000] B.L.R. 218.

¹²⁰ Poole, J. *Contract Law* 6th ed. (Blackstone Press: London, 2001) at p. 203.

¹²¹ Or in more popular terms, where one party is 'weaker'.

that the exclusion or limitation clause will be part of the standard terms used by a party, but it is possible that situations will arise where the clause in question cannot be considered part of the standard terms. For example an exclusion clause may only be added by a party when he has a dominant position in the transaction whereby he can impose a term usually unacceptable to his more 'equal' business partners.

Comments made in the *St Albans* and *Pegler* cases would appear to indicate that the exemption clauses are the 'material clauses' for the purpose of assessing whether the contract was entered on standard terms and would therefore have to form part of the standard terms. However, as was indicated above this approach would arguably be contrary to the terminology employed in section 3(2).

Section 3(2) contains the phrase "by reference to any contractual term" which, on a literal reading, would appear to include all terms whether they are express or implied, written or standard.¹²² This interpretation would also appear to correspond with the objectives of the Act. Once a contract falls within the scope of section 3 (i.e. the contracting parties pass through one of the 'gateways'), then any term, of the nature mentioned in subsection 2,¹²³ will be subject to the test of reasonableness, which is discussed below.

11.5.3 Implied Terms in Contracts of Sale and Hire-Purchase

Sections 6 and 7 of the Act contain specific provisions relating to terms purporting to exclude or limit liability for breaches of the statutory implied terms in contracts for the sale or supply of goods.¹²⁴ Liability for breaches of the implied condition relating to the seller's title to the goods he is selling¹²⁵ may not be excluded or restricted by reference to any contractual term.¹²⁶

¹²² There is little case law relating to this issue but the case law which does exist, would suggest a different interpretation. See *McCrone v. Boots Farm Sales Ltd.* [1981] S.L.T. 103, which considers the application of the equivalent., but slightly differently worded, Scottish section of the Act.

¹²³ Terms excluding or restricting liability for breach of contract and terms that stipulate that a party may render a contractual performance substantially different from that reasonably expected, or render no performance at all.

¹²⁴ Implied terms are discussed below in chapter 13..

¹²⁵ Sale of Goods Act 1979 s. 12. The corresponding term in relation to hire-purchase is s. 8 of the Supply of Goods (Implied Terms) Act 1973.

¹²⁶ s 6(1)(a).

The ability to exclude or restrict liability for breaches of the implied terms as to conformity with sample, satisfactory quality and fitness for purpose,¹²⁷ is dependent upon the status of the other contracting party. If the contract is with a party who 'deals as consumer' then the liability cannot be excluded or restricted by reference to any contract term.¹²⁸ If the contract is with a party acting otherwise than as consumer, then the liability may be excluded or restricted, but only in so far as the term satisfies the requirement of reasonableness.¹²⁹

The control of the use of terms purporting to restrict liability for breach of the implied terms is particularly important to maintain standards of performance in contracts for the Sale of Goods. The implied terms of the Sale of Goods Act are discussed further in the next chapter but it is important to note at this point that the protection in UCTA only explicitly applies to the terms implied under the Sale of Goods Act and not equivalent terms implied at common law. This point may be relevant when the legal categorisation of 'dematerialised goods' is being considered.

11.6 The "Requirement of Reasonableness"

The requirement of reasonableness is defined in Section 11 of the Act with additional guidance to be found in Schedule 2.¹³⁰ The requirement is applied to exemption clauses under a number of sections of the Act. Some commentators have suggested that the "judicial discretion" provided by the requirement creates uncertainty and has the potential to inhibit efficient business liability management and contract planning.¹³¹ The potential risk of inconsistent application due to the broad nature of the discretion has also been highlighted.¹³² This argument may be re-enforced by the fact that application of the requirement is a very factual process unlikely to be considered on appeal.¹³³ Nevertheless, there is considerable guidance as to the application of the test within the Act itself and this has been complemented by a number of prominent cases.

¹²⁷ s 13 – 15 Sale of Goods Act 1979 and 9 – 11 Supply of Goods (Implied Terms) Act 1973.

¹²⁸ s 6(2).

¹²⁹ s 6(3).

¹³⁰ Schedule 2 specifically refers to the application of section 6 and 7 of the Act, but the courts have indicated that the factors listed within Schedule 2 are relevant to any application of the requirement of reasonableness. *Stewart Gill Ltd v Horatio Myer & Co Ltd* [1992] 1 QB 600, per Smith LJ at p.608.

¹³¹ Adams, J. and Brownsword, R. "The Unfair Contract Terms Act: a decade of discretion." [1988] 104 *L.Q.R.* 94-119.

¹³² Collins, H. *Regulating Contracts* (Oxford University Press, 1999).

¹³³ See *St Albans v City and District Council v International Computers Ltd* [1995] FSR 686; [1996] 4 All ER 481. cf. *Watford Electronics Ltd v Sanderson CFL Ltd* [2000] 2 All E.R. (Comm) 984.

11.6.1 The Test.

The clause must have been a “fair and reasonable one to be included having regard to the circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made”.¹³⁴ It is for the party seeking to rely on the clause to prove that it is a fair and reasonable one.¹³⁵ A variety of factors will be considered in this assessment and the courts will ‘weigh up’ all of these factors in a particular case to come to their decision.¹³⁶ Certain factors are referred to in relation to particular sections of the Act or types of clause,¹³⁷ however, the courts have given these factors a wider and more general application.¹³⁸

In relation to clauses seeking to restrict or limit liability rather than exclude it altogether two specific factors are highlighted by section 11(4); the resources available to a party for the purpose of meeting the liability should it arise; and the cost and availability of insurance cover.

Schedule 2 of the Act lists among the “matters to which regard is to be had”; the relative bargaining strength of the parties; whether an inducement (such as a lower price) was given in exchange for agreeing to the term; whether through trade custom or previous dealings between the parties the customer ought to have known of the existence and extent of the term; whether any condition placed upon the enforcement of liability was realistic or practicable (such as a time limit); and whether the goods to be supplied had been personalised for the customer.

Although each case will turn on its own facts, the relative strength of bargaining power of the parties appears to be a leading factor in the court’s assessment. Where consumers are involved the courts have adopted a predictably protectionist approach when considering the reasonableness of a clause.¹³⁹ In contrast, where two business parties are involved the courts have indicated that the parties themselves are the best judges of the commercial fairness of their transaction and in particular the

¹³⁴ Section 11(1).

¹³⁵ Section 11(5).

¹³⁶ *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd* [1983] 2 AC 803.

¹³⁷ For example s 11(2) refers to Schedule 2 in relation to the application of section 6 or 7 and s 11(4) factors relevant in the assessment of limitation clauses.

¹³⁸ *Stewart Gill Ltd v Horatio Myer & Co Ltd* [1992] 1 QB 600, per Smith LJ at p.608 and *Photo Production v Securicor Transport Ltd* [1980] AC 827.

¹³⁹ *Smith v Eric S Bush* [1990] 1 AC 831.

reasonableness of the terms of their agreement. In *Watford Electronics Ltd v Sanderson CFL Ltd*¹⁴⁰ Chadwick LJ stated that

“... the court should be very cautious before reaching the conclusion that the agreement which [the parties] have reached is not a fair and reasonable one.”¹⁴¹

Nevertheless, where a party does not ‘deal as consumer’ but there is a clear inequality of bargaining power the courts may still adopt a protectionist approach in the assessment of the reasonableness of an exemption clause.¹⁴²

11.7 Conclusion

The Unfair Contract Terms Act has played an important role in policing exemption clauses since its commencement. It continues to do so and in recent years the Act has played a prominent role in a number of disputes relating to computer software,¹⁴³ which has been identified as a popular subject matter for electronic contracts. At the beginning of this chapter the stated objectives were to consider whether; the background and objectives of the Act were compatible with contracting in the electronic environment; the scope of the Act could encompass electronic contracting; the application of the Act to electronic contracting would produce logical, appropriate or desirable results and whether amendments to the act were necessary. These questions will now be considered.

The reason for the introduction of the Act, the control of the use of exemption clauses, remains an important consideration in the modern business environment. There is evidence of the use of potentially unreasonable exemption clauses in electronic contracts from the work of the Office of Fair Trading under the Regulations discussed in the next chapter. The balance achieved by the Act, between legitimate business needs and the protection of parties in weaker bargaining positions, is particularly relevant to the electronic

¹⁴⁰ [2001] EWCA Civ 317 [2001] 1 All ER (Comm) 696.

¹⁴¹ *Ibid* at para 54.

¹⁴² See *St Albans v City and District Council v International Computers Ltd* [1995] FSR 686; [1996] 4 All ER 481.

¹⁴³ *Watford Electronics Ltd v Sanderson CFL Ltd* [2000] 2 All E.R. (Comm) 984; *SAM Business Systems Ltd v Hedley & Co* [2002] EWHC 2733 [2003] 1 All E.R. (Comm) 465; *Horace Hobman Group Ltd v Sherwood International Group Ltd* [2000] unrep (WL 491372); and *Pegler Ltd v Wang (UK) Ltd (No. 1)* [2000] B.L.R. 218 70 Con. L.R. 68 [2000] I.T.C.L.R. 617.

environment. Small 'start-up' businesses, able to prosper and benefit from the opportunities created by modern electronic forms of communication, must be able to control their potential risks and liabilities in order to remain viable. Customers, in particular consumers, must be confident that they will not be subject to excessively harsh, or unreasonable, contractual clauses in order to promote involvement in electronic commerce.

The Act is generally 'medium neutral' and will therefore encompass electronic contracts; however, it does contain two references to the requirement that an agreement must be 'written', which may be seen as having the potential to exclude, at least some, electronic forms of communication. Section 3 is a very important part of the Act providing protection against the exemption of liability for breach of contract in general. The requirement that a non-consumer party enters the contract on the other's 'written standard terms of business', has the potential to exclude electronic contracts, if they are not considered in 'written' form. However, this potential problem may be overcome by the courts declaring that an electronic communication containing standard terms will be considered 'writing' for the purpose of the Act.¹⁴⁴ This interpretation could be further supported by reference to the purpose of the section which is clearly to address 'standard form contracts' containing exemption clauses. The reference to an 'agreement in writing' in relation to arbitration agreements can be attributed to the regulatory measures applicable to arbitration in general, wherein it clearly states that agreements may take any form. Electronic agreements would therefore satisfy the requirement as long as they are 'recorded' in some way. Ideally, in any revision of the legislation the references to writing should be either qualified with a definition including electronic forms of communication or removed.

The application of the Act to electronic contracts will cause few undesirable results. However, the definition of 'in the course of a business' as adopted in *R & B Customs Brokers*, has been the source of some general criticism. When considering the amendment of the legislation on unfair terms this issue will probably be addressed by the adoption of a uniform definition of consumer akin to the definition found in UTCCR. However, although this may bring consistency it will remove a level of protection afforded business parties at present when they deal outside of their usual business activity. This protection may be particularly important in promoting confidence in the entering electronic contracts with more powerful trading partners, facilitated by the development of electronic communications. It would therefore be beneficial to ensure that some provision is introduced to protect business parties entering occasional contracts outside of their usual business activities.

¹⁴⁴ See the discussion in chapter 7.

The Unfair Terms in Consumer Contracts Regulations¹

In tandem with the Unfair Contract Terms Act the Unfair Terms in Consumer Contracts Regulations ('the Regulations') should provide a formidable *caveat* for sellers and suppliers when formulating their standard terms for use in their daily business with consumers. The Regulations contain several unique elements, capable of influencing consumer contracts in general; however certain elements may have particular implications for electronic contracting.

A dual approach to the control of unfair terms in consumer contracts is adopted in the Regulations. First, in a dispute between a seller or supplier and a consumer the consumer may use the Regulations to argue that a term is 'unfair' and hence ineffective against him.² Secondly, the Regulations provide the Director General of Fair Trading (DGFT) and other "Qualifying Bodies"³ with the power to take action and to seek injunctions to prevent suppliers continuing to use "unfair terms". This second approach provides a level of regulatory control, previously unseen in England and Wales, capable of having an effect on the continued use of unfair terms in general, rather than being restricted in impact to the confines of a specific case.⁴

The role of the DGFT and other qualifying bodies is a significant one in the promotion of consumer trust and confidence in general and will be particularly important for the development of consumer confidence in the electronic environment.

¹ S.I.1999/2083.

² Regulation 8.

³ Listed in Schedule 1 Parts 1 and 2.

⁴ For example, a term declared ineffective in a case brought under the Unfair Contract Terms Act only prevents reliance on the term in that specific case. The term in question may remain in use as a dissuasive device utilised by an unscrupulous supplier to deter claims and it will only cease to do so when another case is taken to court. Under the Regulations the use of an unfair term may of itself attract the attention of the DGFT and result in the threat of action.

If the DGFT or other qualifying body (after notifying the DGFT) believes that a party is using, or recommending the use of, an unfair term drawn up for general use in contracts concluded with consumers, then he or they can apply for an injunction (or interim injunction) to prevent the continued use of that term.⁵ In practice, these 'powers' have been little used, with the DGFT preferring a more conciliatory approach employing a combination of negotiation and persuasion to obtain a consensus with the seller or supplier. This approach will usually involve the issuing of a warning with advice on the action required, followed by a request for an informal undertaking that the seller or supplier will take the agreed action to delete or amend the offending term. There is considerable activity, as a glance at any of the OFT's Bulletins on Unfair Terms will indicate.⁶

By initiating a decline in the practice of employing unfair terms this broader regulatory control may become an influential factor in the facilitation of electronic contracting. In turn, this should provide an environment of greater confidence for consumers entering contracts in the electronic market. However, the existence of regulation does not of itself create confidence; a lack of knowledge of the rights and protection available is capable of rendering even the most extensive consumer protection provision impotent. This factor is recognised as particularly important in cross border transactions and was identified in the preamble to the Directive responsible for the initial introduction of the Regulations.⁷

"Whereas, generally speaking, consumers do not know the rules of law which, in Member States other than their own, govern contracts for the sale of goods or services; whereas this lack of awareness may deter them from direct transactions for the purchase of goods or services in another Member State..."⁸

The need and desire to disseminate information to consumers is reflected in the Regulations in the hope of creating greater public awareness of the existence of the provisions and of the work being done by the Office of Fair Trading.⁹ The publication of case studies and descriptions of terms considered 'unfair' provides sellers and suppliers with guidance in relation to contract terms and good business practice. This

⁵ Regulation 12.

⁶ <http://www.offt.gov.uk>

⁷ Directive on Unfair Terms in Consumer Contracts 93/13/EEC. O.J. L95/29 (21.4.93).

⁸ *Ibid* Recitals 5 and 6.

⁹ Regulation 15.

not only encourages suppliers to comply with the Regulations to avoid adverse publicity but it also empowers consumers with information about their rights and increases consumer confidence by demonstrating that there are bodies actively protecting their interests. This may go some way to addressing consumer issues identified by the National Consumer Council in their report "E-Commerce and Consumer Protection":

"When pressed, consumers expressed doubts about using sites in other European States mostly because of an anticipated language barrier. Awareness of EU consumer protection and harmonisation was low, which is hardly surprising given the paucity of knowledge about consumer protection and enforcement generally."¹⁰

The scope of the Regulations, or more specifically the scope of the Directive on which the Regulations are based, fulfils another important factor in the promotion of electronic contracting. The Directive, as a Community measure, required implementation by all of the Member States of the European Community. This factor gives the substantive elements of the Regulations an intrinsic cross border dimension. The objective and effect of the Directive should, ideally, provide a level of uniformity across the European Union which in turn should provide increased consumer confidence in cross-border transactions.¹¹ Confidence in contracting outside the home jurisdiction is one of the key areas identified as restricting the development of electronic consumer commerce.¹²

The following discussion will consider whether the Regulations can be readily applied to electronic contracts and whether their application will fulfil the objectives of providing legal certainty and promoting trust and confidence in electronic contracting. The literature produced by the Office of Fair Trading also provides an opportunity to exam the Regulations 'in action' as it were and in particular the effects the Regulations are having in the electronic environment.

¹⁰ "E-commerce and consumer protection." A report by the National Consumer Council. Ref. PD39/2000, August 2000. p. 2 para. 6.

¹¹ The implementation of the Directive is left to the Member States in relation to resultant effect. However this is always subject to the principle that any National Regulation should be interpreted in the light of the Directive.

¹² *Op cit* fn 9. However, as is discussed below their findings were not promising; "Few of the people in the focus groups had bought online from abroad, and few had felt the need or desire to do so. In the omnibus survey one in five of those with Internet access said they would never buy online from abroad." (at page 2 para. 3).

12.1 Background

The Regulations are based on the European Council Directive on Unfair Terms in Consumer Contracts.¹³ The Directive was introduced under the legislative provisions of Article 100a of the EC Treaty, an article concerned primarily with the establishment of the internal market.¹⁴ The purpose of the Directive is clearly stated in Article 1:

“The purpose of this Directive is to approximate the laws, regulations and administrative provisions of the Member States relating to unfair terms in contracts concluded between a seller or supplier and a consumer.”

By ensuring that unfair terms were not enforceable against individual consumers and preventing the continued use of unfair terms the Directive would create a Community wide minimum basic level of consumer protection and increase consumer confidence in cross border transactions.¹⁵

The Regulations on Unfair Terms in Consumer Contracts 1994 were the first attempt to implement the Directive in England and Wales.¹⁶ On their introduction the Regulations attracted a degree of criticism. In fact the criticism was such that the Consumers Association applied for a judicial review of the interpretation of the Directive in the Regulations.

The initial criticisms arose because of the delay in introducing the Regulations: they were introduced on the 1st July 1995, 5 months after the implementation date specified in the Directive.¹⁷

In addition to being overdue, the implementing Regulations were inappropriately worded and introduced an added layer of confusion to the control of unfair terms instead of taking the opportunity to clarify the overall control of unfair terms in England and Wales.¹⁸ The Regulations were essentially a transposition of the English version of the Directive; however, in certain key places the text of the Regulations differed from that in the Directive. For example, in implementing Article 7 of the Directive, the

¹³ 93/13/EEC. O.J. No. L95, 21.4.93, p.29.

¹⁴ Now found in Article 95 of the Consolidated Version of the Treaty on European Union (OJ C340, (10.11.1997), pp. 173-308.

¹⁵ Recital 6.

¹⁶ S.I. 1994/3159.

¹⁷ 31st December 1994 Article 10(1). In itself not an unknown occurrence in relation to Community measures.

¹⁸ It was argued at the time that the opportunity should be taken to review UCTA and combine it with the new Regulations. See Reynolds, F.M.B. “Unfair Contract Terms” (1994) 110 *LQR* 1. As was indicated above, the suggestion has finally reached the Law Commission.

Regulations restricted the ability to take action against the continued use of unfair terms to the Director General of Fair Trading,¹⁹ whereas the Directive extended the power to those with a “legitimate interest under national law in protecting consumers”.²⁰ The Regulations also restricted the definition of seller and supplier, to parties who “sell goods” or “supply goods or services”.²¹ As a consequence, the 1994 Regulations were revoked and replaced by the Unfair Terms in Consumer Contracts Regulations 1999²² which were intended to “reflect more closely the wording of the Directive”.²³

The key changes to the Regulations include the expansion of the power enjoyed by the Director General of Fair Trading, to take action against suppliers using “unfair terms”, to certain “qualifying bodies”.²⁴ The new Regulations also introduce the power to require traders to produce copies of their standard contracts and information about their use. This provision will hopefully facilitate investigations into the practices of sellers and suppliers and the terms they employ in their standard contracts. The definitions of “seller” and “supplier” are also amended to clarify their scope.²⁵

12.2 Definitions and Scope.

The Regulations apply a test of fairness to terms, which have not been “individually negotiated”,²⁶ in contracts concluded between a “consumer” and a “seller or supplier”.²⁷ The Director General of Fair Trading or any qualifying body may apply for an injunction against any person appearing to be using or recommending the use of an unfair term drawn up for general use in contracts concluded with consumers.²⁸

The Regulations only apply to contracts with “consumers”, as defined in regulation 3.

¹⁹ Regulation 8.

²⁰ Article 7(2). This led to the Consumer Associations application for a judicial review of their exclusion from the general regulatory powers of the Regulations

²¹ Regulation 2. This restriction could have excluded certain consumer transactions to which the Regulations were clearly intended to apply. In particular the sale and transfer of computer software an increasingly common subject matter in electronic contracting.

²² S.I.1999/2083.

²³ Explanatory Note at para.2. S.I. 1999/2083.

²⁴ Listed in the new Schedule 1.

²⁵ The removal of the reference to a ‘seller of goods’ and a ‘supplier of services’, see 13.2. below.

²⁶ Regulation 5.

²⁷ Regulation 4(1).

²⁸ Regulation 12.

12.2.1 The Definition of “Consumer”

A “consumer” is defined, for the purpose of the Regulations, as

“any natural person who, in contracts covered by these Regulations, is acting for purposes which are outside his trade, business or profession;²⁹

The use of the words, “natural person” in the definition of consumer automatically excludes corporate or governmental bodies from the scope of the Regulations.³⁰ This can be contrasted with the Unfair Contract Terms Act, which, by virtue of the definition of “in the course of a business” adopted in *R & B Customs Brokers*, retains the possibility of corporate bodies “dealing as consumer”.³¹ Partnerships however, do not enjoy a legal personality in England and Wales and could technically qualify for protection if they satisfy the second part of the definition.³²

In addition to being a “natural person” the party must also enter the transaction for “purposes which are outside his trade, business or profession”. What constitutes a purpose ‘outside’ of a trade, business or profession is open to interpretation. A restrictive interpretation would require the activity to be completely unrelated to the individual’s trade, business or profession. The difficulty with this interpretation is that it could include transactions entered into by an individual, in a private capacity, but which may have characteristics related to his trade, business or profession.³³ Alternatively, the phrase could be interpreted as ‘outside’ the ‘normal activities’ of his trade, business or profession.³⁴ The DTI in its guidance notes to the Regulations refer to “business-related purposes” as falling outside the protection of the Directive,³⁵ which would suggest that a more restrictive approach is preferred. This approach is supported by the Court of Justice which has expressed the opinion that it will not take into account the fact that the activities of a trader are unusual or seldom occurring. In *Patrice Di Pinto*, case C-361/89,³⁶ the Court of Justice felt that it could not draw a distinction between the “normal acts” of a business and those which were “exceptional in nature”.

²⁹ Regulation 3.

³⁰ There is an exception to the ‘natural person’ restriction in the Regulations where arbitration clauses are the subject of scrutiny. This is discussed further below at 12.4.11.

³¹ Discussed above in chapter 11.5.

³² In contrast with Scotland where they have legal personality.

³³ For example, a computer software buyer, who purchases a piece of software from a retail outlet as a present for his son. The purchase surely *relates* to the individual’s trade business or profession.

³⁴ For example, once acting outside his capacity as a tradesman, businessman or professional, activities are no longer for the purpose of his trade, business or profession.

³⁵ August 2000, in the discussion of ‘consumer’ at para 4.4.

³⁶ [1991] ECR I-1189 at para 15 of the judgment.

12.2.2 Seller or Supplier

For the Regulations to apply, the other party to the transaction must be a “seller or supplier”. A “seller or supplier” is defined in regulation 3 as

“any natural or legal person who, in contracts covered by these Regulations, is acting for purposes relating to his trade, business or profession, whether publicly owned or privately owned.”

The inclusion of natural or legal persons in this definition gives it a broad scope. It covers all parties whatever their legal status if they enter into contracts with consumers for purposes which relate to their trade, business or profession. The phrase “acting for purposes relating to” would appear to encompass a wide range of activities, indicating that the ‘purpose’ of the contract does not need to have a strong connection with the business itself. In the broadest sense “relating to” could encompass a computer engineer selling his home computer, i.e anything that relates to that profession or business per se. This is arguably a rather too wide interpretation bringing certain transactions inappropriately within the scope of the Regulations. However, the terminology of the regulation would appear to require a less restrictive approach to that adopted under the Unfair Contract Terms Act. The phrase “in the course of a business”, used to distinguish consumers and non-consumers, has been given a narrow interpretation, requiring that the transaction be either integral to the business or occurring with a sufficient degree of regularity.³⁷ In the context of the Regulations an appropriate interpretation would require that the specific activity must relate to the trade business or profession rather than the nature or subject matter of that activity.

In the 1994 Regulations the definition referred to ‘a seller of goods’ and a ‘supplier of goods or services’. This definition had the potential to restrict the scope of the Regulations by excluding transactions involving items which do not fit easily into these categories. A key example would be computer software, often the subject of electronic transactions, but not clearly categorised as ‘goods’ or ‘services’.³⁸

³⁷ *R & B Customs Brokers v United Dominions Trust* [1988] 1 All ER 847. Discussed in chapter 11.5.

³⁸ See *St Albans City and District Council v. International Computers Ltd* [1997] F.S.R. 251. See the discussion below in chapter 13.2.

12.2.3 Terms Subject to the Regulations

The Regulations are not restricted to particular 'types' of term in the same way that UCTA is restricted to exemption clauses. However, only terms which have "not been individually negotiated" are subject to the test of fairness.³⁹ Clauses are not individually negotiated if they have been drafted in advance and the customer has not been able to influence the substance of the term.⁴⁰ This phrase clearly encompasses the vast majority of consumer contracts and would also cover the situation where a seller or supplier offers a choice of two or more contracts.⁴¹ A typical example of this approach would be the situation found in photographic stores for developing and printing services, where the consumer may choose between a standard and a deluxe service. Under the deluxe service a higher price is paid but in the terms and conditions the service provider accepts greater liability. Equally, simply offering a customer various levels of after sales service such as on-site service or on-line helpdesk does not mean that the term is individually negotiated.⁴² The negotiation of a number of terms in what is otherwise a pre-formulated contract will not take the contract beyond the scope of the Regulation.⁴³ It is for the seller or supplier to show that a term has been individually negotiated with the consumer.⁴⁴

12.2.4 Excluded Terms

The most important exclusion from the scope of the Regulations is the exclusion of 'core' terms of the contract.⁴⁵ However, the Regulations do not apply to contractual terms reflecting mandatory statutory or regulatory provisions applicable in the United Kingdom or provisions or principles of international conventions to which the UK or EC are party.

The 1994 Regulations contained a list of certain excluded types of contract, including contracts relating to employment and succession rights, rights under family law or the incorporation and organisation of companies or partnerships.⁴⁶ These exclusions were removed from the 1999 Regulations although they were a clear reflection of the

³⁹ Regulation 5(1).

⁴⁰ Regulation 5(2).

⁴¹ See, Bragg, R. "Implementation of the E.C. Directive on unfair terms in consumer contracts: the Department of Trade and Industry Consultation Document." [1994]2(2) *Consum. L.J.* 29-38.

⁴² However, these factors may be relevant to any assessment of the fairness of a particular term in the contract.

⁴³ Regulation 5(3).

⁴⁴ Regulation 5(4).

⁴⁵ See below at 12.2.5.

⁴⁶ Found in Schedule 1 of the 1994 Regulations.

approach envisaged by the Directive.⁴⁷ However, the nature of the contracts subject to the exclusion found in the 1994 Regulations may indicate that such contracts are not between a consumer and a seller or supplier. Contracts relating to land or property are not excluded from the Regulations and it would appear that the courts are willing to accept that a contract between a landlord and a tenant could constitute a contract between a seller or supplier and a consumer.⁴⁸

12.2.5 The 'Core' Term Exclusion.

Terms relating to the definition of the main subject matter of the contract or to the adequacy of the price or remuneration will not be subject to the assessment of fairness under the Regulations so long as they are in "plain intelligible language".⁴⁹

The "core exclusion" maintains a level of freedom of contract, preventing interference with the central elements of the parties bargain. However, difficulties in determining what will constitute a 'core term', or the 'main subject matter of the contract' leaves room for uncertainty. The House of Lords considered this exemption from the scope of the Regulations in *Director General of Fair Trading v. First National Bank Plc*.⁵⁰ Lord Steyn felt that the term in question was a "subsidiary" one and not defining the main subject matter of the contract.⁵¹ Lord Bingham indicated that terms which "express the substance of the bargain" should be distinguished from those "incidental" terms which surround them. The former would fall within the exemption whereas the latter would not.⁵² The court felt that in general a narrow interpretation of the 'core exemption' was important to the ability of the Regulations to fulfil their objective.⁵³

Nevertheless, a term "expressing the substance of the bargain" has to be in 'plain intelligible language' to be excluded from the scope of the Regulations.

12.2.5.1 "plain intelligible language"

The use of inaccessible language has been identified as a problem by the courts for some time and the Regulations have been seen as an opportunity to rid, consumer contracts at least, of complex legal terminology and 'small print'. In *The Zimnia*⁵⁴ the

⁴⁷ See recital 11.

⁴⁸ See *Margaret Peters v. Fairclough Homes Limited* [2002] WL 31961996 (Ch D) at para 58.

⁴⁹ Regulation 6(2).

⁵⁰ *Director General of Fair Trading v. First National Bank Plc* [2002] 1 A.C. 481.

⁵¹ At p 499.

⁵² At p 491.

⁵³ Per Bingham L.J. at 491.

⁵⁴ *Stag Line Ltd. v. Tyne Shiprepair Group Ltd. and Others, (The 'Zimnia')* [1984] 2 Lloyds Rep 211.

judge observed that he was tempted to hold an exclusion clause in a commercial contract “unreasonable” because it was so complicated and prolix that one almost needed a law degree to understand it.⁵⁵ The Office of Fair Trading (OFT) took the opportunity to express an opinion at an early stage. In their second Bulletin on unfair contract terms they stated that;

“The use of small print and obscure language (so often found together) is fatal – if not counter productive – and should be jettisoned.”⁵⁶

The impact of the phrase “plain intelligible language” on the fairness test is considered further below.⁵⁷ For the purposes of the ‘core exemption’, failure to use plain intelligible language renders what would be an excluded ‘core term’ subject to the fairness test in the Regulations. The interpretation of “plain intelligible language” is less than clear. The OFT have indicated that the terms must be plain and intelligible to “the ordinary consumer without legal advice” and that the legal ‘jargon’ found in normal commercial contracts would be wholly inappropriate for use in contracts with consumers.⁵⁸ This would appear to suggest that an objective approach should be taken, ascertaining whether the language used in the term would be plain and intelligible to the average person.⁵⁹

The provisions of the Regulations cannot be evaded by a choice of law clause stipulating the law of a non-EU state. Regulation 9 reads:

“These Regulations shall apply notwithstanding any contract term which applies or purports to apply the law of a non-Member State, if the contract has a close connection with the territory of the Member States.”

⁵⁵ *Ibid* at p 222.

⁵⁶ OFT Unfair Terms Bulletin 2.

⁵⁷ At 12.2.5.1.

⁵⁸ *Ibid*. Where legal terminology is necessary the OFT suggested the inclusion of explanations.

⁵⁹ Such an approach would allow scope for a consideration of the nature of the contract and whether it was the type of contract where legal advice would usually be obtained.

12.3 The Assessment of Unfair Terms

An unfair term is not binding on the consumer, but the contract will continue to exist if practicable.⁶⁰ The test applied to determine whether a contract term is unfair is found in regulation 5:

“A contractual term which has not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties’ rights and obligations arising under the contract, to the detriment of the consumer.”

In assessing the fairness of a term, the nature of the subject matter of the contract, all of the other terms of the contract, and all of the circumstances attending the conclusion of the contract will be taken into consideration.⁶¹ This assessment will include a consideration of the ‘core terms’ of the contract and whether the language used in the contract was ‘plain and intelligible’.⁶² An indicative and non-exhaustive list of terms which may be regarded as unfair can be found in Schedule 2 of the Regulation.⁶³

The key elements of the test are the significant imbalance in the parties’ rights and obligations, to the detriment of the consumer, and that the imbalance is contrary to the requirement of good faith. In *First National Bank*, Lord Steyn explained that while there are three elements to this test, the element of detriment to the consumer “may not add much” serving primarily to indicate that the Directive was aimed at protecting the consumer against an imbalance rather than the seller or supplier.⁶⁴ He continued by asserting that the “twin requirements of good faith and significant imbalance will in practice be determinative”.⁶⁵

⁶⁰ Regulation 8.

⁶¹ Regulation 6(1).

⁶² Regulation 7(1) requires the seller or supplier to ensure that “any written term of a contract is expressed in plain intelligible language” and any doubt as to interpretation will be determined in favour of the consumer. It is not expressly stated that failure to fulfil this requirement will be a consideration in the fairness test, but it the courts may see it as contrary to the requirement of ‘good faith’.

⁶³ Regulation 5(5). The Schedule is also known as the ‘grey list’.

⁶⁴ *Director General of Fair Trading v. First National Bank Plc* [2002] 1 A.C. 481. at p 500 para 36.

⁶⁵ *Ibid.*

12.3.1 “Significant imbalance”

In *Director General of Fair Trading v. First National Bank Plc.*⁶⁶ the House of Lords stated that the requirement of significant imbalance will be met if a term is “so weighted in favour of the supplier as to tilt the parties’ rights and obligations under the contract significantly in his favour.”⁶⁷ The imbalance should be assessed in the light of circumstances at the time of the contract to establish whether it is significant. Whether there is an imbalance in the parties’ rights and obligations to the detriment of the consumer is assessed against the potential for creating an imbalance.⁶⁸

The OFT has indicated that the assessment may be approached by considering whether rights conferred on the seller are balanced by corresponding rights for the consumer. However, there are some terms which cannot be balanced by a mirroring term. In addition, attempting to weigh up the rights and obligations of the parties may be time consuming and not particularly productive. A low price may be the consequence of a particularly harsh term but that should not automatically make the term fair.⁶⁹ Ultimately the assessment of whether there is a significant imbalance will be a factual determination based upon the circumstances and context within which the term is being, or intended to be, used.

12.3.2 The Requirement of “Good Faith”.

The OFT has stated that the requirement of good faith does not equate to an absence of subjective “bad faith” in the sense of dishonesty but rather requires the supplier to behave fairly and equitably.⁷⁰ The 1994 Regulations contained a Schedule providing guidance on the requirement of good faith based upon recital 16 of the Directive.⁷¹ The guidance does not feature in the 1999 Regulations but the factors in recital 16 may be given consideration in appropriate circumstances. The first three factors contained in recital 16 are familiar to lawyers in the United Kingdom because they closely resemble factors relevant to the requirement of reasonableness in UCTA:

“whereas, in making an assessment of good faith, particular regard shall be had to the strength of the bargaining positions of the parties, whether the consumer had

⁶⁶ *Ibid.*

⁶⁷ *Ibid* at 494.

⁶⁸ OFT Bulletin 1 para. 1.2.

⁶⁹ Beale, H. “Unfair Contracts in Britain and Europe.” [1989] 42 *C.L.P.* 197.

⁷⁰ OFT Bulletin no 2.

⁷¹ Schedule 2.

an inducement to agree to the term and whether the goods or services were sold or supplied to the special order of the consumer.”

The recital continues that the requirement of good faith may be seen as satisfied where the seller or supplier deals “fairly and equitably with the other party whose legitimate interests he has to take into account”. In the 1994 Regulations the reference to the taking account of the legitimate interests of the consumer was omitted and it has been suggested that this element is essential to the adoption of a suitably high standard of ‘good faith’.⁷²

In *First National Bank* Lord Bingham considered the ‘good faith’ element of the fairness test as requiring fair and open dealing with no taking advantage of the consumers’ weaker position, whether deliberately or unconsciously. The terms of the contract should be expressed fully, clearly and legibly containing no concealed pitfalls or traps for the consumer.⁷³ On a more general note he stated that the requirement of good faith “looks to good standards of commercial morality and practice”.⁷⁴

The judgment in *First National Bank* is not without criticism, but it does provide some practical guidance to the application of the fairness test under the Regulations.⁷⁵

12.4 The Indicative or “Grey” List

The indicative list of terms which may be regarded as unfair provides some guidance but as the OFT has emphasised, clauses of this nature will still be assessed against the test of fairness and are by no means blacklisted. The OFT has nevertheless stated that “if a term appears in the list then it is under substantial suspicion”.⁷⁶ In *First National Bank* Lord Steyn described the list as a “check list of terms which must be regarded as potentially vulnerable” to a finding that they are unfair.⁷⁷

The list refers not to specific terms or their form but rather to the object or effect of the term in a broad way. Nevertheless, there are some familiar ‘types’ of term

⁷² Macdonald, E. “Scope and Fairness of the Unfair Terms in Consumer Contracts Regulations: *Director General of Fair Trading v First National Bank*.” [2002] 65 *M.L.R.* 763 at 769.

⁷³ *Op cit* fn 63 *per* Bingham L.J. at 494. Lord Steyn reiterated the “the notion of open and fair dealing” at p 500.

⁷⁴ *Ibid.*

⁷⁵ It has been suggested that in not requesting a preliminary ruling on the meaning of ‘unfair’ from the ECJ, the court infringed the interpretative monopoly of the ECJ in the area of Community law. See Dean, M. “Defining Unfair Terms in Consumer Contracts – Crystal Ball Gazing?” [2002] 65 *M.L.R.* 773.

⁷⁶ OFT Bulletin 4 at p 22.

⁷⁷ *Op cit* fn 63 above at p 500, para 36.

contained in Schedule 2. For example; paragraphs (a), (b) and (q) can be broadly categorised as exemption clauses;⁷⁸ paragraphs (d) and (e) encompass terms which would fall within the common law rules on penalty clauses and related issues;⁷⁹ and paragraphs (j), (k) and (l) relate to the conferment of a discretion on the seller or supplier in relation to his performance under the contract which could fall within s 3(2)(b) of UCTA. Certain terms contained within the list may be particularly relevant to electronic contracts. These terms will now be highlighted.⁸⁰

12.4.1 Excluding or limiting consumer's rights on suppliers breach of contract - including the right of set-off.

(b) inappropriately excluding or limiting the legal rights of the consumer vis-à-vis the seller or supplier or another party in the event of total or partial non-performance or inadequate performance by the seller or supplier of any of the contractual obligations, including the option of offsetting a debt owed to the seller or supplier against any claim which the consumer may have against him.

This paragraph has a broad applicability to exemption clauses or general disclaimers relating to liability for breach of contract.⁸¹ For example, clauses stating that a supplier “will not accept any responsibility whatsoever in the event that adverse side-effects are caused by using our product” are *prima facie* unfair.⁸² Such clauses are particularly common in electronic contracts for downloading media and software from service providers because of risks of viruses or bugs in software which could result in harm to the consumers system. Likewise, contract terms seeking to exclude or restrict liability for unsatisfactory goods or workmanship, or delay in performance are likely to be treated as *prima facie* unfair.⁸³

In May 2002 the well known travel and leisure website ‘lastminute.com’ was investigated by the OFT and found to be using no less than eight terms falling within this

⁷⁸ See, Macdonald, E. *Exemption Clauses and Unfair Terms* (Butterworths: London, 1999) at p 202 *et seq*.

⁷⁹ On penalty clauses generally See Koffman, L. and Macdonald, E. *The Law of Contract* 4th ed. (Tolley, 2001) at chapter 10.

⁸⁰ It must be remembered that the OFT only gives guidance on terms that are likely to be unfair, only the courts can decide what is unfair on basis of fairness test. (Bulletin 3, p. 50)

⁸¹ And to that extent is similar to s. 3 of UCTA.

⁸² See “GP Care Supplies” case study in Bulletin 3 at p 51.

⁸³ *Ibid* at p. 53 – 57. There is considerable overlap here with s. 6 of UCTA.

category, including one for negligently providing inaccurate information to consumers, amongst sixteen amendments or deletions recommended by the OFT.⁸⁴

12.4.2 Agreements which bind the consumer but not the seller.

(c) making an agreement binding on the consumer whereas provision of services by the seller or supplier is subject to a condition whose realisation depends on his own will alone.

Terms which make an agreement binding on the consumer but not on the seller until a condition, which the seller controls, is fulfilled will also be *prima facie* unfair. For example, a seller will control the point at which goods are despatched from his warehouse. A term that states that the seller is not bound until the goods are despatched, but that a consumer may be irrevocably bound before that point may fall within this paragraph. In attempting to retain complete control over the contractual process many website operators are using terms to this effect and are, in the process, creating an imbalance in rights and obligations against the consumer.⁸⁵

12.4.3 Retention of deposits

(d) permitting the seller or supplier to retain sums paid by the consumer where the latter decides not to conclude or perform the contract, without providing for the consumer to receive compensation of an equivalent amount from the seller or supplier where the latter is the party cancelling the contract.

A term allowing a seller or supplier to retain a deposit paid by a consumer if the consumer cancels the contract is likely to be treated as unfair unless the sum retained reflects actual losses or costs incurred by a supplier and the consumer has an equivalent claim should the supplier cancel the contract. In 2002 the OFT encountered terms of this nature on the “easycar.com” website and recommended the revision or deletion of twenty five terms.⁸⁶

⁸⁴ In recent years British Telecom’s Internet service, Tesco Stores Ltd and the Toys ‘R’ Us website have all been found to contain exemption clauses falling within para 1(b) by the OFT and OFTEL.

⁸⁵ <http://www.ofc.gov.uk>.

⁸⁶ Bulletin 20 p. 11.

12.4.4 Unequal termination rights

(f) authorising the seller or supplier to dissolve the contract on a discretionary basis where the same facility is not granted to the consumer, or permitting the seller or supplier to retain the sums paid for services not yet supplied by him where it is the seller or supplier himself who dissolves the contract.

Many clauses of this nature are found in contracts for the provision of Internet and mobile phone services. They are popular because they provide the supplier with complete discretion as to when, where and how he provides the service, allowing him to adapt to changes in the market. However, the consumer is placed at a considerable disadvantage with no equivalent discretion in his contract.

The Britannia Rescue Services Ltd case study⁸⁷ provides a useful indication of the OFT's approach to this type of clause. As a result of intervention by the OFT a term allowing Britannia to cancel contracts on a discretionary basis, and thus to get out of a bad bargain and also permitting Britannia to retain money paid for a service which had not yet been provided, was amended.

12.4.5 Termination without notice

(g) enabling the seller or supplier to terminate a contract of indeterminate duration without reasonable notice except where there are serious grounds for doing so.

This type of clause is also popular with service providers in the electronic environment for similar reasons to the preceding paragraph. In September 2001, One.Tel, an Internet Service Provider, had clauses allowing them to terminate service contracts without notice amongst sixteen potentially unfair terms.⁸⁸

12.4.6 Extension of contracts

(h) automatically extending a contract of fixed duration where the consumer does not indicate otherwise, when the deadline fixed for the consumer to express his desire not to extend the contract is unreasonably early.

⁸⁷ Bulletin 3, p. 26.

⁸⁸ Bulletin 18 p. 52.

The use of 'rolling contracts' which continue and renew unless the consumer takes steps to cancel the agreement have been problematic for some time.⁸⁹ The OFT have indicated that such terms may be deemed unfair particularly where the consumer may not know of or understand the effect of the clause.⁹⁰

12.4.7 Binding the consumer

- (i) irrevocably binding the consumer to terms with which he had no real opportunity of becoming acquainted before the conclusion of the contract.

In chapter 9 the incorporation of terms into contracts by 'reasonably sufficient notice' was considered. This paragraph indicates that a term may still be challenged as unfair even if it is incorporated at common law, because the consumer has had no real opportunity to become acquainted with it. It would appear to require that the supplier do more than is required at common law to ensure that the consumer has the opportunity to be fully aware of the implications of the contract he is signing. In the Country Holidays case study⁹¹ the small print and language used in the term in question led the OFT to conclude that the consumer had no real opportunity to become acquainted with the terms effect.⁹² The lack of an opportunity to become acquainted with the term, rather than the content of the term itself, creates the unfairness.

12.4.8 Unilateral alteration of products or services

- (k) enabling the seller or supplier to alter unilaterally without a valid reason any characteristics of the product or service to be provided.

Clauses of this nature are common in electronic and traditional contracts, and arguably they are an important element of any contract entered at a distance enabling a supplier to adapt to product developments and changes. This would appear to provide a 'valid reason' for altering the product delivered.⁹³ Nevertheless, a clause to this effect will

⁸⁹ This form of 'inertia selling' is outside of the scope of the Unsolicited Goods and Services Act 1971.

⁹⁰ See the 'Bradleys Estate Agents Ltd' case study in Bulletin 3, at p. 25.

⁹¹ Bulletin 3, p. 28.

⁹² In addition the term fell foul of the requirement that terms must be written in plain and intelligible language.

⁹³ See the OFT case study 'GP Care Supplies' – clause had potential for unfairness since it enabled the company to change the characteristics of what was supplied. This right has now been limited and the consumer now has the right to withdraw if fundamental changes are made to the goods (Bulletin 3, p. 33).

usually also allow consumers to reject the substitute if he desires and under the Distance Selling Regulations⁹⁴ this is now a statutory requirement in distance contracts.⁹⁵ In May 2000 the ISP 'Total Web Solutions Ltd' were investigated by the OFT and as a consequence an 'entire agreement clause' was removed.⁹⁶

12.4.9 Commitments undertaken by agents – Entire agreement clauses

(n) limiting the seller's or supplier's obligation to respect commitments undertaken by his agents or making his commitments subject to compliance with a particular formality.

This paragraph could be of particular importance to website traders, the majority of whom attempt to disclaim any liability for statements or commitments made on his website. An interactive website can act as advertising, shop-floor and sales assistant and as such acts as the 'agent' of the supplier.⁹⁷ Terms, particular entire agreement clauses, which attempt to exclude any commitments made in statements made on a website, may have the potential to create unfairness. In the Vodacall Ltd case study an entire agreement clause which excluded representations made by Vodacall's agents on which the consumer could have relied, and substituted terms which the consumer had probably not read or understood was deemed potentially unfair by the OFT and as a result deleted.⁹⁸ Where statements are made on websites with the intention that consumers will rely on the information contained within those statements, any term seeking to limit the seller's liability for the lack of truth in those statements will potentially be unfair.⁹⁹

12.4.10 Transfer of rights and obligations under the contract

(p) giving the seller or supplier the possibility of transferring his rights and obligations under the contract, where this may serve to reduce the guarantees for the consumer, without the latter's agreement.

⁹⁴ The Consumer Protection (Distance Selling) Regulations 2000 (S.I. 2000 No. 2334).

⁹⁵ *Ibid* regulation 19(7).

⁹⁶ Bulletin 12 at p. 31.

⁹⁷ For a general discussion of this issue see chapter 3.2 above.

⁹⁸ Bulletin 3 at 49. See also the 'Chromearch Ltd / Nationwide Driveways' case study at p. 27 in the same Bulletin.

⁹⁹ Terms excluding or limiting such liability may also be challenged under s. 3 of the Misrepresentation Act 1967 (as amended by UCTA).

In the volatile commercial climate of the Internet and information technology in general, this occurrence, and terms allowing for this occurrence, are common place. For example, over the past few years many Domain Name Services (DNS) have ceased trading or sold their business interests and the contracts have been passed on to other service providers. The consumer is often only aware of this when he receives an e-mail from the new service provider and as such he is not given the opportunity to go elsewhere for the services. Terms allowing for this occurrence clearly place consumers at a significant disadvantage, particularly when they have no knowledge of the assignment.¹⁰⁰

12.4.11 Restrictions on legal remedies.

(q) excluding or hindering the consumer's right to take legal action or exercise any other legal remedy, particularly by requiring the consumer to take disputes exclusively to arbitration not covered by legal provisions, unduly restricting the evidence available to him or imposing on him a burden of proof which, according to the applicable law, should lie with another party to the contract.

Alternative methods of dispute resolution are particularly important for electronic commerce, to provide speedy and efficient solutions to disputes without excessive cost. However, it is equally important that consumers should not be forced to take this route to uphold their rights under a contract. A contract term intended to inhibit the consumer's right to take legal action by for example, requiring disputes to be taken to compulsory arbitration, would be *prima facie* unfair.¹⁰¹

12.4.11.1 Arbitration clauses

It is appropriate to comment at this point on the involvement of UTCCR in the control and use of arbitration clauses in consumer contracts. Compulsory arbitration clauses in consumer contracts were previously considered undesirable because they may be used to deter consumers from pursuing valid claims by requiring binding and sometimes expensive arbitration. Hence, before 1996 such terms were not binding on the consumer if they were entered into before a dispute arose, by virtue of the Consumer

¹⁰⁰ See the case study of 'Orange Personal Communications Services', in Bulletin 17 at p.44.

¹⁰¹ See the case study of 'Town & Country Driveways Plc' in Bulletin 3 at p. 44.

Arbitration Agreements Act 1988.¹⁰² In effect such clauses were wholly ineffective in law.

A general reform of English Law on arbitration was undertaken in the 1990's resulting in the repeal of the 1988 Act on the introduction of the Arbitration Act 1996. The provisions relating to consumer arbitration agreements can now be found in section 89 – 91 of the 1996 Act. A term which constitutes an arbitration agreement¹⁰³ will now be subject to the Unfair Terms in Consumer Contracts Regulations, and the test of fairness. There are however, two elements of this provision which are of particular interest.

The first is an apparent digression from the basic premise that to be a 'consumer' under the Regulations a party must be a 'natural person'. Section 90 of the Arbitration Act states that:

“The Regulations apply where the consumer is a legal person as they apply where the consumer is a natural person.”

Businesses, including limited companies may now advance an argument that an arbitration clause is unfair under the Regulations.

Secondly, section 91 the Act appears to create a 'black list' to add to the 'grey list' in the Regulations:

“A term which constitutes an arbitration agreement is **unfair** for the purposes of the Regulations so far as it relates to a claim for a pecuniary remedy which does not exceed the amount specified by order for the purposes of this section.”¹⁰⁴

Hence, arbitration agreements, where the dispute relates to a sum, at present not exceeding £3000, will be conclusively presumed to be unfair. Sums below this amount are not considered appropriate for reference to, a potentially expensive, arbitration process.

¹⁰² Section 1.

¹⁰³ Section 89: “For this purpose “arbitration agreement” means an agreement to submit to arbitration present or future disputes or differences (whether or not contractual).”

¹⁰⁴ Emphasis added.

12.5 Conclusion

The Regulations have had a significant impact on the terms used in consumer contracts in the traditional environment and there is no reason why they should not have the same impact on the contents of electronic consumer contracts. The majority of credit for that impact must go to the role provided to the OFT and other bodies by the Regulations. The examples and case studies included in the discussion do however indicate that the general use of unfair terms in the electronic environment is common. It is submitted that as the use of electronic commerce and electronic contracting increases, more sites will be found to be using potentially unfair terms and become the subject of the OFT scrutiny. The difficulty will be keeping pace with the rapidly changing electronic environment and the increasing number of sellers and suppliers entering contracts with consumers. Since the introduction of the 1999 amendments the OFT is now helped with the workload by other bodies such as regulatory bodies like OFTEL and the Consumers Association.

The Regulations, or more correctly the Directive, has the added advantage of having cross-border influence. By providing a minimum level of consumer protection throughout the European Union the provisions will help develop consumer confidence in entering cross-border electronic contracts.

The role of adverse publicity due to the publication of OFT investigations should not be underestimated. Publicity of this nature not only informs consumers about errant suppliers but also instils confidence because consumers can see that their interests are being protected. Perhaps most importantly the risk of bad publicity can act as a deterrent to sellers and suppliers to using unfair terms against consumers. The only criticism of the approach adopted at present would be the limited distribution of the information in the bulletins when a higher profile dissemination would probably result in greater changes in contractual terms. The information in the OFT Bulletins would indicate that even well known names are using contractual terms, either naively or intentionally, which are potentially unfair under the Regulations. It must be questioned whether suppliers are continuing to use unfair terms until they are politely asked to amend them by the OFT, or whether the approach adopted under the Regulations is really winning the battle against the use of unfair terms.¹⁰⁵ For electronic commerce the removal of potentially unfair terms from electronic consumer contracts is essential if the desired trust and confidence is to be obtained.

¹⁰⁵ See Bright, S. "Winning the battle against unfair contract terms" [2000] 20(3) *L.S.* 331-352

Implied Terms

A contract, be it formed and performed in the electronic environment or in a more traditional manner, may be subject to the implication of terms not stated or perhaps even contemplated by the parties themselves. This may occur by virtue of a statutory provision or by the courts implying a term at common law. The terms implied may have a significant effect on a party's obligations and liabilities and therefore, a degree of certainty in relation to the implication of terms is desirable. In this chapter the implication of terms at common law and by statute are considered and the potential uncertainties for parties entering electronic contracts highlighted.

13.1 Terms Implied at Common Law

At common law the implication of terms is often subdivided for convenience into those implied in fact, in law or by custom. The intention of the parties has a variable impact on the implication of a term. Terms that would appear obvious or that are necessary "to give such business efficacy to the transaction as must have been intended"¹ by the parties are implied on the basis of the contracting parties' 'intention' (in fact).² The basis for this form of implication is strict as can be seen from the words of Lord Pearson, in *Trollope & Colls Ltd v. N.W. Metropolitan Regional Hospital Board*:³

"An unexpressed term can be implied if and only if the court finds that the parties must have intended that term to form part of their contract; it is not enough for the court to find that such a term would have been adopted by the parties as reasonable men if it had been suggested to them; it must have been a term that went without saying, a term which, though tacit, formed part of the contract which the parties made for themselves."

¹ *Moorcock, The* (1889) 14 PD 64, per Bowen L.J at p 68.

² *Shirlaw v Southern Foundries Ltd* [1939] 2 KB 206. The 'officious bystander' test.

³ [1973] 1 W.L.R. 601 at 609.

The emphasis in the judgment is on a clear indication that the courts are not re-writing the parties' bargain.

Terms are also implied on the basis that they are 'necessary'⁴ in the particular 'type'⁵ of contract in question and not based on the intention of the parties (in law). Such terms have been described as "... incidents attached to standardised contractual relationships"⁶ operating as "default rules".⁷ It has been indicated that terms implied on this basis may have a particularly important role to play in relation to certain common 'types' of electronic contracts.⁸

Where certain terms are customary in a particular trade, profession or locality the courts are willing to imply that the contract is subject to that term.⁹ However, there must be "evidence of a universal and acknowledged practice of the market".¹⁰ In the modern, and relatively 'new', electronic market one might suggest there has been insufficient time to establish such a custom or practice; however, this does not prevent a term, customary to a particular profession from being implied into an electronic contract.

As a general rule terms will not be implied into a contract at common law in the face of an express contrary term,¹¹ or even in the face of very detailed, although not contradictory, express terms.¹²

13.2 Terms Implied by Statute

The most significant statutory implied terms for the purposes of this discussion also relate to contracts of a particular 'type'. Such terms are usually the result of legislative intervention into a contractual relationship within which there is an imbalance of bargaining power. The statutory implied terms found in the Sale of Goods Act 1979

⁴ *Liverpool CC v Irwin* [1976] 2 All ER 39.

⁵ See *El Awadi v Bank of Credit and Commerce International SA* [1989] 1 All ER 242 at p 253.

⁶ *The Society of Lloyds v Clementson* [1995] CLC 117, per Steyn LJ at p 131.

⁷ *Malik v Bank of Credit and Commerce International* [1997] 3 All E.R. 1, per Steyn LJ at p 15.

⁸ See the discussion below at 13.2; the possibility of terms equivalent to the Sale of Goods Act being implied at common law.

⁹ See *Hutton v Warren* (1836) 1 M & W 466, and *National Bank of Greece v Pirios Shipping Co* [1990] 1 All ER 78.

¹⁰ *Baker v Black Sea Insurance* [1998] 2 All ER 833 at p 842 the House of Lords supporting the words of Millett LJ. In the Court of Appeal ([1996] LRLR 353 at 362).

¹¹ *Johnstone v Bloomsbury HA* [1991] 2 All ER 39. However, in this case the court indicated that the express term may be classed as an exclusion clause and subject to the Unfair Contract Terms Act 1977 (discussed above in chapter 12). See Macdonald, E, "Exclusion clauses: the ambit of s 13(1) of the Unfair Contract Terms Act" (1992) 12 LS 277.

¹² *Trollope & Colls Ltd v. N.W. Metropolitan Regional Hospital Board* (1973) 1 W.L.R. 601.

(SGA)¹³ and the Supply of Goods and Services Act 1982 (SGSA)¹⁴ will be relevant to many electronic contracts. The terms implied by the Sale of Goods Act require that goods sold 'in the course of a business' match their description (s 13), or a sample(s 15), are of satisfactory quality (s 14(2)) and reasonably fit for the buyer's purpose (s 14(3)). When dealing with a consumer, the implied terms are classed as conditions and therefore any breach would entitle the consumer to repudiate the contract (s 14 (6)). When dealing with parties who are not consumers, the terms are also classed as conditions save for the situation where the 'breach is so slight that it would be unreasonable for him [the purchaser] to reject them' (s 15A); instead the terms are treated as warranties.¹⁵

There is no need to demonstrate that the breach is due to negligence on the part of the supplier and hence the terms are often labelled as 'strict liability'.¹⁶ The terms relating to the quality and fitness of goods provide significant opportunities for redress should the goods be defective in some way. By contrast, the implied terms found in the Supply of Goods and Services Act require that contracts for the supply of a service are carried out with reasonable care and skill (s 13).¹⁷ Clearly the standards required of goods passing under a contract of sale are stricter than those implied in a contract for the supply of a service. There is also a greater burden of proof under the SGSA with the need to demonstrate the reasonable care and skill has not been taken.

Hence, establishing whether a contract is for the sale of goods or the supply of a service is fundamental to identifying the potential liabilities of the supplier and corresponding rights of the customer. The existing common law and legislative definitions and their application to electronic contracts must be considered.

In the electronic environment, whilst many contracts are entered into for 'traditional tangible products', many concern the supply of material which can be accessed from, or downloaded directly to, a customer's PC or other device, with no 'tangible' items passing. In such circumstances, will the customer benefit from the stricter requirements as to quality and fitness found in the SGA or is the supplier only

¹³ Sections 13 – 15 imply terms into contracts for the sale of goods, sold 'in the course of a business', that they must match their description (s 13), or a sample(s 15) and that the goods should be of satisfactory quality(s 14(2)) and reasonably fit for the buyer's purpose (s 14(3)).

¹⁴ Sections 8 – 10 relate to the hire of goods implying similar terms to those found in SGA and s 13 implies a term requiring services to be carried out with reasonable care and skill.

¹⁵ A breach of which entitles the injured party to claim damages but not to repudiate the contract and reject the goods.

¹⁶ Atiyah, P.S. *et al The Sale of Goods* 10th ed. (Longman: Pearson Education, 2001), chapter 6.

¹⁷ "In a contract for the supply of a service where the supplier is acting in the course of a business, there is an implied term that the supplier will carry out the service with reasonable care and skill." Goods passing incidentally under a contract for services attract equivalent terms to those found in the SGA (SGSA s2 – s4).

obliged to provide the material and facilitate the download with reasonable care and skill? Alternatively, the possibility that the transaction cannot be categorised in the traditional way must be considered.¹⁸ The statutory regimes contained within SGA and SGSA will not apply to the contract which would appear to leave customers, and of particular concern consumers, without the protection of any implied terms as to the quality of the item or the standard of performance of the supplier. Such a conclusion would arguably be unacceptable because the 'thing' being contracted for is identical, only the carrier medium has changed. Allowing the carrier medium to dictate the rights and liabilities of the parties is surely inappropriate and it is submitted that this occurrence would not be tolerated by the courts. But what principles will the courts apply to avoid such a dichotomy?

To a limited extent the courts have grappled with this dilemma in relation to computer software and this will be returned to below.¹⁹ First, the principles which have been adopted by the courts to distinguish contracts for the 'sale of goods' from contracts for the 'supply of services' must be considered.

13.2.1 Distinguishing Contracts for the Sale of Goods and Supply of Services at Common Law

At common law, the distinction between a contract for the sale of goods and a contract for the supply of services, or work and materials, has been the subject of some debate, particularly in relation to books,²⁰ body parts or fluids,²¹ and computer software.²² In *Lee v. Griffin*²³ the subject matter of the contract was a set of false teeth. In concluding that the contract was for the sale of goods Blackburn J felt that in order to correctly classify the contract the court had to decide whether the result of the contract could be the subject matter of a sale. If it could, then the contract was for the sale of goods; if it could not, then the contract would be for work and labour done.²⁴ In *Robinson v. Graves*²⁵ the Court of Appeal indicated that to correctly decide the issue, the 'substance' of the contract had to be established. If the 'dominant element' of the contract was the skill

¹⁸ Perhaps placed in a class of its own, *sui generis*, for example. (Discussed further below).

¹⁹ A popular subject matter of contracts concluded in the electronic environment.

²⁰ See Lloyd, I. "A Rose By Any Other Name" (1993) *Jan J.B.L* 48-54.

²¹ See *Perlmutter v Beth David Hospital* 123 NE 2d 792 (1955). *Cf. Dodd v Wilson* [1946] 2 All E.R. 691, which is difficult to distinguish on grounds of legal principle.

²² See the discussion below at 13.2.2.3.

²³ (1861) 1 B & S 272.

²⁴ This judgment has been doubted in later cases, see *Robinson v. Graves* below. Atiyah suggests that the decision may be "indicative of the regard in which dentists were held in the mid-nineteenth century!" *op cit* fn 16 at p. 28 n 93.

²⁵ [1935] 1 KB 579. The dicta of Blackburn J. was doubted in this judgment.

and expertise of a party, then the contract was one for the supply of a service and any goods passing were incidental to that contract.²⁶ The case before the court concerned the commissioning of an artist to paint a portrait. The contract was held to be one for work and materials, the substance of which was the skill of the artist, with the canvass and paint being materials passing incidentally under that contract.

More recently in *James Ashley v. Sutton London Borough*²⁷ Scott Baker J expressed the view that;

“...what one has to do, it seems to me, is to look at the essential nature of the transaction and see what in reality it was, that was being provided to the customer.”

Hence, it would appear that if the substance or dominant element of the contract is the supplier's skill and labour a contract for services exists; if on the other hand the substance or dominant element of the contract is the end result, then the contract is one for the sale of goods. Although in principle this distinction is quite clear, its application to the particular facts of an individual case can prove problematic.

In *Cammell Laird & Co Ltd v Manganese Bronze and Brass Co Ltd*²⁸ a contract for the construction of two ships propellers was held by the House of Lords to be 'unquestionably' a contract for the sale of goods, even though a great deal of skill and labour had gone into their manufacture.²⁹ Likewise, in *Lockett v A & M Charles Ltd*³⁰ a contract for the supply of a meal in a restaurant was considered a contract for the sale of goods. It is at least arguable that although the end product, the meal, was important, the contract is comparable to the one in *Robinson v. Graves*, in that the 'dominant element' of the contract is the skill, expertise and labour of the chef.

The House of Lords took an arguably more realistic approach to contracts of this nature in *Hyundai Heavy Industries Co Ltd v Papadopoulos*.³¹ Here a contract for the manufacture of a ship was considered a sale of goods but not necessarily a pure contract of sale. The contract contained two parts: 1) the contract for the supplier to make the ship was a contract for services and, 2) a contract under which the supplier agreed to sell

²⁶ The goods passing incidentally would, nevertheless, have to satisfy the implied terms as to quality and fitness.

²⁷ *Ashley v Sutton London Borough* [1995]14 Tr Law 350, The Times 8 December 1994, 139 SJ LB 1.

²⁸ [1934] AC 402.

²⁹ This can be seen as similar to the set of false teeth in *Lee v. Griffin*.

³⁰ [1938] 4 All E.R. 170.

³¹ [1980] 1 WLR 1129.

the completed ship which was, in effect, a contract for the sale of goods. The court recognised that the transaction was complex and could not be simply classified as a contract for the sale of goods *or* the supply of services.

The principles discussed in the preceding cases can be applied to subject matter common to electronic contracts. With downloaded material such as a film, music or proprietary software the 'end result' is the dominant element of the contract. Even though skill and labour went into the initial production of the work, the copies downloaded are for distribution to a mass market. Alternatively if the material is a 'personalised' composition, or bespoke or customised software the skill and labour would appear to be the dominant element of the contract and more akin to the provision of a service.³²

However, even if the 'dominant element' or 'substance' of the contract is the movie, the album or the piece of software, it is debateable whether such 'intangible' items can be correctly defined as 'goods'. This potential difficulty will now be considered.

13.2.2 The Definition of 'Goods'

The natural starting point would appear to be the relevant statutory definition of 'goods' in the Sale of Goods Act. Section 61 states that;

“ 'goods' includes all personal chattels other than things in action or money.”

Atiyah points out that the definition, although it appears 'virtually all-embracing' clearly excludes non-physical items such as company shares, which are 'things in action' and also items of 'intellectual property'.³³ Equally clearly, goods can exist which contain or embody work that is the subject of intellectual property rights.

Books, music, movies and computer software are all very popular online purchases. However, each of these items can be delivered in a number of forms – on paper, magnetic tape, CD or DVD, or electronically downloaded to the hard drive on a PC or other electronic communications equipment. When a customer purchases a 'hard copy' of a book, tape, CD or DVD in a shop, few would argue that he is not purchasing 'goods' from the retailer.³⁴ When items are downloaded directly to a customer's computer, the transaction includes no 'tangible' items. For the purpose of the statutory

³² Although there may be a transfer of the final product which may, in effect, be a sale of goods.

³³ *Op cit* fn 16 at p. 66.

³⁴ Including the retailer himself!

implied terms it must be considered whether these transactions are a sale of goods, a supply of services, or 'none of the above'? Ultimately, the crucial question is whether the method of delivery of the material should dictate the liabilities of the supplier and the rights of the customer? The logical answer would be a simple no:

“The basic argument that the rights of the parties should not depend upon the medium of supply must be right. But the point has to be made that there is the possibility that *any* original copyright work can, at the present stage of technological development, be delivered either on a physical medium or on-line. Does the fact that the contents of a book can be delivered on-line, or the image of a painting, mean that sales of books and paintings must now be treated as *sui generis* and thus outwith the Sale of Goods Act? Surely not...”³⁵

However, as the debate surrounding computer software indicates the solution may not be quite so straightforward. To date much of the discussion about the issue of 'intangible' products has related to computer software, as have the few cases wherein the issue has been discussed, albeit *obiter*. However, it is submitted that many of the arguments discussed in relation to computer software can be applied to other 'intangibles' purchased in the electronic environment.³⁶

13.2.2.3 Computer Software – Goods? Services? Or *Sui generis*?³⁷

Although the actual cases where this issue has been discussed are few, and the comments *obiter*, the issue has been hotly debated and as a consequence the limited judicial comments have been analysed with some rigour. The relevant arguments in relation to computer software and the potential consequences of adopting those arguments in the wider context of electronic contracts as a whole will now be considered.

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. The second argument is that software is

³⁵ *Op cit* fn 16 at p. 68.

³⁶ Although some of the submissions have as their basis the differences between computer software and other media. These will be discussed in due course but it should be noted at the outset that these arguments have been developed to attempt to 'fit' computer software into the 'goods' category by distinguishing it from 'mere information'. Although this distinction is clearly valid it is respectfully submitted that it is an unnecessary and somewhat artificial solution to the problem.

³⁷ The classification of the software and other electronic media may also have an impact on protection afforded and liabilities incurred under the Consumer Protection Act 1987 and the Trade Description Act 1968.

'intellectual property' and hence a 'thing in action' and therefore specifically excluded by the definition in s 61 SGA.³⁸

13.2.2.4 The Arguments:

'Software is Merely Information'

Scott³⁹ puts forward the argument that as software is simply coded information⁴⁰ it is "altogether different in nature to personal property".⁴¹ The English authorities, culminating in the House of Lords decision in *Boardman v Phipps*⁴² suggest that information "is not property in any normal sense"⁴³ and is therefore incapable of being personal property or a personal chattel. In *Oxford v Moss*⁴⁴ 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.⁴⁵

This is an accurate technological analysis and if this analysis is accepted then it is submitted that all digitally and magnetically recorded media is simply coded information.⁴⁶ 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 has the rather unfortunate and arguably unacceptable consequence that only the 'carrier', the piece of plastic or magnetic tape, is subject to the strict standards of the implied terms of the SGA. 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, in general the law is not, and arguably should not, be based upon detailed and microscopic technological analysis. If it is, then there is an equally

³⁸ A 'choses in action' is a proprietary right in personam, in contrast with a 'choses in possession'.

³⁹ Scott, A.P. "Software as 'goods': Nullum Simile est idem." (1987) 3(4) *CL. & P.* 133-136.

⁴⁰ As indeed a movie or music album may be when downloaded.

⁴¹ *Op cit* fn 39 at p 135.

⁴² [1967] 2 AC 46.

⁴³ *Ibid* per Lord Upjohn at p. 128.

⁴⁴ [1978] 68 Cr App R 183.

⁴⁵ *Op cit* fn 39 at p. 136.

⁴⁶ DVD's and CD's essentially contain a series of bumps 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.

microscopic and technological analysis available to counter the argument that software is simply 'information'.

The physical or metaphysical argument – microscopic analysis.

Macdonald⁴⁷ argues that in relation to computer software, when it is contained on a physical medium, the contention that it is simply information can be met from two perspectives, a physical one and a functional one. While the physical argument can be extended to movies, music and other material the functional argument does not transfer as readily.

The physical argument relates to the fact that when embodied on a physical medium, the software takes a 'physical form', albeit only at the microscopic level. 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 'information'.⁴⁸ In the context of the Criminal Damage Act 1971⁴⁹ Lord Lane LCJ concluded that the data or information stored on a disk, and the consequent orientation of the magnetic particles, could constitute 'property of a tangible nature' for the purpose of a charge of criminal damage.⁵⁰ By analogy the *effect* that the computer program has on the storage medium is tangible.⁵¹ Unfortunately this analysis does not address the situation whereby no tangible storage medium is involved, which may result in a contract for the same subject matter being treated differently due to the method of transfer. Once again the transfer medium would have a potentially disproportionate and inappropriate impact upon the rights and liabilities of the parties.

The 'function' performed by that information.

The 'functional' argument relates to the fact that as the software "interacts directly, with the hardware",⁵² 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*⁵³ 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

⁴⁷ In Rowland, D & Macdonald, E, *Information Technology Law* 2nd Ed. (Cavendish: London, 2000) at p 175.

⁴⁸ This follows the line adopted by Sir Iain Glidewell in his *obiter* comments in *St Albans City and District Council v. International Computers Ltd* [1997] F.S.R. 251 at 265.

⁴⁹ To this point now amended by the introduction of the Computer Misuse Act 1990.

⁵⁰ *R. v Whiteley (Nicholas Alan)* (1991) 93 Cr. App. R. 25 at p 28.

⁵¹ Equally, a movie, music or text would have a tangible effect upon the storage medium.

⁵² Atriyah, P.S. *op cit* fn.16 at p. 178.

⁵³ 938 F 2d 1033 (9th Cir 1991).

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. 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.⁵⁴ 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.

The analogy with certain types of books has been used in relation to the supply of computer software and hardware together. Although the 'physical' argument discussed above could be of equal application. Where computer software is sold in a package with the hardware⁵⁵ 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*⁵⁶ 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."⁵⁷

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.⁵⁸ 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.

⁵⁴ *Op cit* fn.16 at p. 68.

⁵⁵ As is becoming increasingly common with Microsoft's domination of the software market.

⁵⁶ [1983] 2 NSWLR 48.

⁵⁷ *Ibid* at p 51. This description was adopted in the *St Albans* case by Scott Baker J.

⁵⁸ s 14. *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.

Atiyah believes that the analysis in the *Womell* case is far from satisfactory, especially when applied to computer software.⁵⁹ He explains that software being described as a 'set of instructions to a computer'⁶⁰ 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."⁶¹

There has been some debate regarding books and their content distinguishing the liability associated with the book's manufacture (the pages and printing etc) and 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.⁶²

"A book would certainly be regarded as goods but information or advice therein would be subjected to a due care standard"⁶³

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. Lloyd makes a convincing case for this suggestion.⁶⁴ 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

⁵⁹ *Op cit* fn 16, at p. 69, n 18.

⁶⁰ Citing Macdonald [1995] MLR 585 at 590.

⁶¹ *Op cit* fn 54.

⁶² 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 being liable under the SGA for missing pages or poor manufacture but not liable in respect of erroneous information contained within the book. See Bridge, M. G. *The Sale of Goods* (Oxford University Press, 1998) at p. 31.

⁶³ *Ibid.*

⁶⁴ See Lloyd, I. "A Rose By Any Other Name" (1993) Jan *J.B.L* 48-54.

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.

Intellectual property

Where computer software is involved there has been a tendency to focus upon the intellectual property embodied in the software. Intellectual property rights are 'things in action'⁶⁵ and as such are excluded from 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, distribution of the work and certain other activities are prohibited without the permission of the rights owner.⁶⁶ 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. Arguably this distinguishing feature of computer software led Lord Penrose to classify a contract for the supply of proprietary software as *sui generis* in *Beta Computers (Europe) Ltd v Adobe Systems (Europe) Ltd*.⁶⁷ 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'. In the US this point was recognised by Weiss J in *Advent Systems Ltd v Unisys Corp*.⁶⁸

“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 to the observation that, at a microscopic level, when stored on a medium such as a magnetic disk, the software takes on a perceptible physical

⁶⁵ *Torkington v Magee* [1902] 2 K.B. 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.”

⁶⁶ In the computer software context this was recognised by Steyn J in *Eurodynamics Systems v General Automation Ltd* (1988) unreported 6th September LEXIS.

⁶⁷ *Beta Computers (Europe) Ltd v Adobe Systems (Europe) Ltd* [1996] FSR 387 at p 396.

⁶⁸ 925 F 2d 670 (1991).

or tangible form. 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.

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 pass. Even if the argument that the contract is for the supply of 'mere information' can be defeated, it is at least uncertain whether data 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

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 programme is written".⁶⁹ However, Napier argues that such a conclusion, in relation to software, would offend common sense and defeat a purchaser's expectations.⁷⁰ In *St Albans* 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."⁷¹

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 physical medium to dictate the legal message. But if we say 'no' we face a much greater evil..."⁷²

⁶⁹ Bridge, M.G. *The Sale of Goods* (Oxford University Press, 1998) at p.21.

⁷⁰ Napier, B. "The Future of Information Technology Law." [1992] 51(1) *CLJ* 46.

⁷¹ *St Alban's City and District Council v. International Computers Limited* [1995] F.S.R. 686 at 699.

⁷² *Op cit* fn 69 at p. 48.

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 whereby the software is embodied on a disc or some other medium, ignoring the possibilities of transfer via a non-tangible medium.⁷³ 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.⁷⁴

Fitting computer software and other intangible items 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 designed to encompass. While it is true that computer software is different to other 'goods', it would not be the first time that computer software was perhaps labelled inappropriately because an existing statutory regime is considered 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. 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.⁷⁵ The same could be said of music, films or electronic books. This line of reasoning follows the approach adopted by Lord Penrose in *Beta v Adobe*.⁷⁶ In his *obiter* comments he felt that the reasoning that software was goods was unattractive because

⁷³ Direct down loading from the Internet for example.

⁷⁴ See *St Albans City and District Council v. International Computers Ltd* [1997] F.S.R. 251 at 265.

⁷⁵ *Op cit* fn 16 at p. 185.

⁷⁶ *Op cit* fn. 67.

“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.”

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,⁷⁷ and the views expressed by Steyn J in *Eurodynamics Systems plc v General Automation Ltd*⁷⁸ 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*.⁷⁹

“...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.”⁸⁰

Although this conclusion is convenient, to the extent that it avoids the difficult issues raised by, as Lord Penrose put it, inappropriately forcing computer software into an existing category, it does raise difficulties of its own. In *St. Albans City and District Council v. International Computers Ltd*⁸¹ Scott Baker J felt that if computer software fell outside the definition of goods the purchaser would find himself, “unprotected by any statutory regime.” On the same basis Brian Napier concluded that if computer software is not

⁷⁷ *Ibid* p, 608 – 609. See also, Reed, C. & Angel, J. *Computer Law*. 4th ed. (Blackstone Press Limited: London, 2000) at p. 44.

⁷⁸ 6th September 1988 (unreported) LEXIS.

⁷⁹ *Beta Computers (Europe) Ltd v. Adobe Systems (Europe) Ltd* [1996] FSR 367.

⁸⁰ *Ibid*.

⁸¹ [1995] FSR 686.

categorised as goods then the 'legal analysis' would defeat purchasers 'common sense expectations'.⁸² 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 1977.⁸³ 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. Where the contract is between a supplier and a consumer, the Regulations on Unfair Terms in Consumer Contracts⁸⁴ would also remain relevant. 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.⁸⁵ 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. In *Dodd v. Wilson*⁸⁶ 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, (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 dicta of Sir Iain Glidewell in *St Albans City and District Council v. International Computers Ltd*,⁸⁷ in the Court of Appeal;

"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."⁸⁸

⁸² Napier, B. "The Future of Information Technology Law." [1992] 51(1) *CLJ* 46.

⁸³ See chapter 11.

⁸⁴ See chapter 12.

⁸⁵ See Macdonald, E & Rowland, D. *Information Technology Law*, 2nd ed. (Cavendish: London, 2000) chapter 4.

⁸⁶ [1946] 2 All ER 691.

⁸⁷ The Times 14 August 1996. (Heard 26 July 1996, by Nourse LJ, Hirst LJ and Sir Iain Glidewell).

⁸⁸ *Ibid.*

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.

13.3 Conclusion

The approach adopted at common law to the implication of terms produces no specific problems for electronic contracts. In fact terms implied by the courts at common law may have a particularly important role to play in some electronic contracts because of the difficulties associated with classifying contracts for intangible items.

The statutory implied terms of the Sale of Goods Act and the Supply of Goods and Services Act are stalwart examples of Parliamentary policy towards certain types of business transactions, and transactions with consumers in particular.⁸⁹ They are as important to electronic contracts as they are to any other. Unfortunately there are two issues which are capable of creating uncertainty as to their application in the electronic environment and the rights and obligations of the parties to certain types of electronic contracts.

The first issue is of general importance rather than being unique to electronic contracts; the classification of a contract as one for the sale of goods or alternatively for work and materials, or services. This classification will determine whether the stricter terms implied by the SGA are applicable to the contract. The case law demonstrates that there is a discernable level of flexibility in the tests adopted by the judiciary. However, the focus on the 'dominant element' or 'substance' of the contract appears logical and in *Hyundai Heavy Industries* the House of Lords appeared to take a pragmatic approach to the analysis of a complex contract, recognising the practical realities of the situation. The case also highlights the important point that contracts do not have to be 'either/or' but can be a combination as the facts of the case dictate.

The approach adopted at common law can be readily applied to electronic contracts and their subject matter. For example, in a contract for the download of a movie or a piece of mass produced software the dominant element, or substance, of the contract is the finished product, the movie or the computer program. A transaction for a bespoke piece of software and service contract is more likely to be treated as a contract

⁸⁹ See the judgment of Potter L.J. in *Stevenson and Another v. Rogers* [1999] 1 All E.R. 613, [1999] 2 W.L.R. 1064, [1999] Q.B. 1028.

for work and materials or a combined contract encompassing the sale of goods and the provision of services. The difficult question appears to be whether intangible items like a downloaded movie or software can be properly called 'goods'.

There are a number of arguments, supported by some judicial comment, that an intangible item such as computer software or a computer program and by analogy other intangible products, cannot be classified as goods. These arguments are capable of being met with sustainable counter arguments however, it is submitted that such arguments are unnecessary.

The suggestion that computer software is intellectual property⁹⁰ and therefore outside the definition of 'goods' in s. 61 SGA does not recognise the nature of the majority of transactions entered into for software and media. The contracts will usually be for a copy of a work protected by intellectual property rights and rarely for the transfer of the intellectual property rights themselves.

To describe computer programs and electronic media as merely information is arguably an accurate description, but it does not recognise the interactivity of computer software with its environment or the fact that when such 'information' is placed on a disc or other carrier medium the contract is considered a sale of goods.

The technical argument that computer programs and by analogy downloaded media have no 'physical presence' and can therefore not be called 'goods' can be met with the equally technical counter argument that a 'physical presence' does exist, albeit at a microscopic level.

However, in analysing the transaction in this way it is easy to become consumed with arguably unnecessary technical debate and lose sight of the reality and true nature of the transaction and the purpose of the relevant legislation. As Professor Atiyah suggests:

"... it is less important to worry about how we should slot software into existing legal categories, than what we think the respective liabilities of the software house or of any intermediary supplier to the purchaser should be. Once the latter is decided, other questions are relatively straightforward."⁹¹

Once the transaction is approached in this way it becomes easier to analyse transactions for digital products or 'dematerialised goods'. A service provider supplying a movie, pop album or digital publication should not be liable for the abstract 'quality' or 'fitness for

⁹⁰ An argument, which could be extended to forms of downloaded media.

⁹¹ *Op cit* fn 16 at p. 67.

purpose' of the material, in the same way that a retailer in the traditional sense should not be subject to a claim that, for example, a comedy movie was not fit for its purpose because it was not particularly funny or a pop CD is not of satisfactory quality because the music and lyrics are dreadful. The liabilities should relate to the functioning of the item. Can the movie be viewed or the music listened to without distortion or gaps? Is the publication complete without 'pages' or words missing? These liabilities relate to quality, but they are the liabilities for which a traditional retailer would expect to be responsible and it is submitted that they are the liabilities for which a service provider of digitally downloaded items should be responsible. Faults of this nature do not always relate to a problem with the physical transfer medium and it would be inappropriate to confine the application of the implied terms of the SGA solely to these tangible items. This approach avoids any metaphysical debate and focuses on the expectations of the parties and allocation of liability.

However, if the courts do not accept the proposition that intangible items can be categorised as goods, then the possibility exists for the supplier of an item such as a feature film to have different levels of liability depending on the means used to deliver the film to the customer. To this end it is submitted that the courts would imply equivalent terms at common law necessary to create parity and consistency between identical items, albeit supplied via different media. Any alternative conclusion would surely lead to an unacceptable dichotomy in the implied terms applicable to what are essentially identical transactions.

Conclusion

In this section the ability and extent to which parties can dictate their rights and obligations in electronic contracts or exclude or restrict their liability under a contract have been examined. While it is important for sellers and suppliers to control their risks and potential liabilities by the use of contractual terms it is equally important to protect weaker parties against unfair or unreasonable terms. In the electronic environment these often competing needs are emphasised because parties are entering new and different contractual relationships. The potential effects of the common law rules on the incorporation of terms and overriding legislation such as UCTA and UTCCR must be predictable sufficiently certain to create confidence in the use of electronic contracts.

The common law rules of incorporation provide the courts with the opportunity to declare contractual terms ineffective because they have not become part of the contract. As is the case with the common law rules on contract formation, although the principles are flexible enough to be applied to electronic contracts the uncertainty created by having to speculate as to how the courts may apply principles to the electronic environment does not provide the predictability required to promote confidence.

The Unfair Contract Terms Act has the ability to protect both business parties and consumers against the use of exemption clauses. The greater protection afforded to those who 'deal as consumer' under the Act is extended to business parties and companies entering contracts which are not part of their usual business activity.¹ This added protection may be particularly important for smaller businesses looking to take advantage of the electronic environment by entering electronic contracts with more dominant trading partners.

The Unfair Terms in Consumer Contracts Regulations have become an important weapon against the general use of unfair terms against consumers. The consumer confidence created by the publicised and pro-active discouragement of unfair terms by the OFT and other bodies is vitally important to the development of consumer trust in entering electronic contracts. In the more recent reports the investigation of sellers and suppliers using the electronic environment is becoming more evident. This will ultimately benefit the sellers and suppliers as much as the consumer because the

¹ i.e. Integral to or incidental to, but occurring with sufficient regularity.

increased consumer confidence can only lead to greater involvement in electronic commerce.

The proposed amendment or amalgamation of these instruments would be welcomed if it codified and clarified the provisions without removing any of the protection afforded the business party under UCTA. One of the options mooted by the consultation to-date is the extension of UTCCR provisions to business-to-business transactions. It is submitted that although this suggestion may attract criticism for introducing further 'red tape' to interfere with business transactions it would ultimately create a fairer and more stable legal environment for business and for electronic commerce in particular.

The implied terms as to quality and fitness for purpose under the SGA and the reasonable care and skill required of service providers by the SGSA are vitally important elements of contracts falling within the scope of those pieces of legislation. This is demonstrated by their specific inclusion in measures found in UCTA and the recent discussions of computer software in the Court of Appeal. It is submitted that their extension to 'dematerialised goods' and 'intangibles' or 'data-products' is not only vital to promote confidence in, what will become the largest single subject matter of electronic contracts, but also to maintain legal consistency. The legal status of an item should not be dictated by the medium by which it is delivered.

V

Conclusion

Conclusion

This thesis has set out to demonstrate that the legal environment applicable to electronic contracts lacks the certainty, consistency and predictability required to promote their use.

The approach adopted in this thesis has been to analyse the key legal provisions applicable to electronic contracts. Common law and regulatory principles have been examined to assess their potential impact on electronic contracts and more generally electronic commerce. Areas of legal uncertainty, inconsistency and unpredictability have been highlighted to illustrate the potential difficulties encountered when applying existing principles to electronic contracts.

In the introduction three key elements were identified as required for the creation of a stable and predictable legal environment for electronic contracts:

- 1) The removal of legal 'barriers' to the use of electronic contracts;
- 2) A non-discriminatory or medium neutral approach to contracts formed and performed by electronic means; and
- 3) The creation of legal certainty in the principles and legislation applicable to contractual relationships created in the electronic environment.

It was also emphasised that in addition to these elements the cross-border potential of electronic commerce and hence electronic contracts must be taken into account.

These criteria have been employed in the body of this work to identify the legal principles capable of having a detrimental impact on the use of electronic contracts. It is logical therefore that they should be considered first.

The removal of legal 'barriers' to the use of electronic contract

Legal barriers to electronic contracts may take a variety of forms and as the discussion in chapter 7 indicates, may come from a variety of sources.

Traditional requirements of form, such as 'writing' and 'signature', have been considered the main potential barriers to electronic contracts because of doubts as to whether electronic forms of communication can satisfy those requirements. Formal requirements in the legislation of England and Wales are unlikely to cause significant problems for electronic contracts for a number of reasons. First, few requirements of form that exist apply to contracts in general and as such are unlikely to inhibit the use of electronic contracts. Secondly, if the courts adopt a purposive approach to the interpretation of the requirements then in the majority of situations the electronic forms of communication will probably be accepted as satisfying the requirement. However, the main problem for electronic contracts is created by the uncertainty surrounding whether electronic communications can satisfy formal requirements, rather than by the requirements themselves.

In recognition of the uncertainty created by formal requirements the European Commission introduced measures to combat the problem at Community level. Article 5 of the Electronic Signatures Directive was intended to create legal certainty in relation to electronic signatures and Article 9 of the Electronic Commerce Directive had the object of requiring Member State governments to remove potential legal barriers to electronic contracts. As Directives, the method of implementation of these measures is left to the discretion of the Member States. Arguably, the approach adopted in the United Kingdom does not go far enough to create legal certainty sufficiently quickly. The piecemeal nature of the approach in section 8 of the Electronic Communications Act is slow and the lack of statutory recognition of advanced electronic signatures as functionally equivalent to their traditional counterparts leaves legal uncertainty as to their standing.

Potential barriers to the use of certain forms of electronic communication have also been introduced in legislation intended specifically for electronic commerce. They can also be found in legislation addressing related issues, such as distance selling. In a number of situations additional requirements can be justified because of the need to maintain safeguards for parties entering contracts in the electronic environment. For example, information requirements introduced to address the problem of identification in the electronic environment. However, even where new requirements are justified it is

submitted that sufficient consideration has not been given to the nature of the electronic environment and electronic contracts. For example the introduction of requirements which may be difficult to fulfil or ambiguous to interpret such as the requirement that information be provided in a 'durable form' or be 'permanently accessible'. These requirements have the potential to lead to disputes about their interpretation and application to various technologies, resulting in uncertainty and a lack of confidence in the use of electronic contracts.

A non-discriminatory or medium neutral approach to contracts formed and performed by electronic means

Naturally, formal requirements which create barriers to the use of electronic contracts may also be considered discriminatory measures and their removal can provide a medium neutral approach. There are also a number of measures of a discriminatory nature which have been introduced in legislation relevant to electronic communications. The measures are discriminatory because they require higher standards of electronic communications than their paper-based counterparts. For example; the levels of reliability and security expected of electronic signatures go beyond anything expected of traditional signatures; the requirement that contract terms are provided in a manner allowing for their storage and reproduction is not something usually required of traditional contracts. Higher standards may be justified because of the nature of the electronic environment, but if they are, they need to be explicitly clear and the higher standards should be reflected in the legal status of the communication.

An area of particular concern in relation to discriminatory treatment of electronic contracts was identified in chapter 13 in relation to statutory implied terms. Traditional definitions of 'goods' and 'services' have the potential to discriminate against dematerialised goods or data products, denying them the benefit of the statutory implied terms. It was suggested that the courts may imply equivalent terms at common law to prevent purchasers from being 'unprotected'. However, even if they are there may still be discrimination because specific measures such as section 6 of UCTA will not apply.

The creation of legal certainty in the principles and legislation applicable to contractual relationships created in the electronic environment

A lack of legal certainty has been identified by this thesis as the most common and potentially damaging deterrent to the use of electronic contracts. Although a lack of legal certainty may be found in many areas of the law it is particularly detrimental in an

area new to the majority of individuals and businesses. Areas of legal uncertainty have been found in the common law and legislation.

Common law sources of uncertainty

The application of common law principles is never an exact science because the principles developed by the courts are intended to be flexible and transferable. It is due to this flexibility that those principles transfer readily to the electronic contracts. However, predicting the courts' interpretation and application of those principles in the electronic environment is somewhat more problematic. Two vitally important steps of the contractual process, formation and the incorporation of terms, which remain the domain of the common law have elements which require statutory attention if legal uncertainty is to be removed.

In the formation process the point of contract formation, in particular the point of effective acceptance of the offer, is a major source of uncertainty. However, it is not the question of whether the postal rule should apply or not that is the source of the uncertainty but rather the question of when an electronic communication of acceptance is received. Regulatory attempts to address this issue, in the form of the draft Electronic Commerce Directive, resulted in a rather confused and unhelpful Article which was ultimately discarded. Unfortunately the issue will now produce an equally confused debate in the courts at a point in the near future. The UNCITRAL Model Law probably provides the clearest set of rules on the matter, but Parliament was not persuaded to move the issue away from the courts.

It could be argued that a regulatory measure has already addressed the issue *vis-à-vis* regulation 9(1) of the Electronic Commerce (EC Directive) Regulations 2002, wherein it is stated that service providers shall clearly inform customers of "the different technical steps to follow to conclude the contract". However, this approach has been adopted by many suppliers for some years because of the uncertainty surrounding the application of the principles of contract formation to electronic contracts. It is submitted that this approach has demonstrably led to attempts by suppliers, in their 'terms of website use' to distort the contract formation process significantly in their favour to the detriment of the consumer. For example:

"No contract will subsist between you and [...] for the sale by it to you of any product unless and until [...] accepts your order by e-mail confirming that it has

dispatched your product. That acceptance will be deemed complete and will be deemed for all purposes to have been effectively communicated to you at the time [...] sends the e-mail to you (whether or not you receive that e-mail).”¹

It is submitted that rather than aiding clarity this approach in reality harms the consumer.

The common law rules on incorporation, particularly by ‘reasonably sufficient notice’ are a cause of uncertainty primarily because of the multitude of ways in which customers can be given notice of terms in the electronic environment. However, it is conceded that the position is no less certain for electronic contracts than it is for more traditional ones. Suppliers are aware that the notice they give of their terms must give the customer the opportunity to acquaint himself with the terms and it is submitted that the technology available to the supplier may play a role in any adjudication. For example, a simple hypertext reference at the bottom of a webpage may not be considered reasonably sufficient when a pop-up scroll box could be used without any detriment to the use-ability of the site.

In the light of recent judicial comments and the increased risk of identity fraud in the electronic environment there is an undeniable need for the much maligned doctrine of mistaken identity at common law to be unravelled by Parliament. As a matter of policy there must be a system of justly allocating loss in the event of fraud. If losses were distributed in accordance with fault then a useful caveat will also be created for sellers to take steps to ensure the identity of their contracting partner.

Whilst the common law is flexible and therefore capable of adapting to technological and societal change, the speed of that change is inadequate to meet the immediate need for legal certainty in electronic contracts. As a consequence the legal uncertainty created has the potential to at least result in costly precautionary steps to be taken by those entering electronic contracts and at worst deter parties from using electronic contracts stifling the development of electronic commerce. The fact that common law *can* accommodate the technological changes does not necessarily mean that it *should*.

Sources of uncertainty in legislation.

This thesis has identified two key sources of uncertainty in legislative measures applicable to electronic contracts; the first is the application of existing principles which

¹ ‘Amazon’ terms and conditions of sale, available at: <http://www.amazon.co.uk>.

are inappropriate for the electronic environment and the second is the introduction of regulatory measures which do not take sufficient account of the nature of the electronic environment and electronic contracts.

There is no better demonstration of both of these problems than the rules on jurisdiction.

Many of the difficulties highlighted with the Brussels Convention are caused by the reliance on the search for some form of 'physical' presence in many of the provisions, which is an inappropriate base in the electronic environment. For example, the 'place of performance of the obligation in question' is potentially difficult to assess online; the need for a consumer to 'take steps necessary for the conclusion of the contract' in his home state creates a potential problem with mobile technology; and from the case law, the existence of a secondary establishment has implications of a physical presence. While a physical presence has traditionally been an important factor in jurisdiction issues, the concept may need some re-consideration in the light of electronic communications and the Internet in particular. The consumer protection measures in the Convention are an additional source of uncertainty because of the debate surrounding 'advertising' and whether websites could constitute advertising targeting a consumer's jurisdiction for the purpose of the Convention.

The new Regulation was introduced with the expressed objective of clarifying a number of these uncertainties, but it is submitted that insufficient account was taken of the nature of the electronic environment in the development of the new measures. While the retention of the basic need for a physical presence is understandable, it is unfortunate that this need was not qualified in the context of an electronic or 'virtual' presence. For example, the clarification of 'place of performance' only deals with the supply of goods or provision of services, which would appear to leave uncertainty in the case of 'data products'. The 'clarification' introduced for the provision of services does not account for the fact that the services may be 'provided' on a remote device which could be located anywhere. The use of a virtual presence such as a website as a secondary establishment was not considered, although the potential impact of such a presence in a particular jurisdiction is identical to that of a physical 'branch, agency or other establishment'. Perhaps the most concerning omission in the new Regulation is an explanation of the replacement of 'advertising' in the consumer protection provision with 'directing or pursuing... activities'. The clear intention behind the provision was to extend consumer protection to cases where interactive websites are in use, and the

provision is capable of being interpreted in that manner. However, the lack of any clarification in the final instrument means that this potentially vital issue for the development of consumer trust and confidence in cross-border electronic contracts is left uncertain and for interpretation by the Member State courts.

Legislation such as UCTA and UTCCR is extremely important for the promotion of confidence in electronic contracts and electronic commerce. There are a number of references in UCTA to formal requirements which could raise questions in the electronic environment, however, it is submitted that the courts will adopt a purposive approach to the interpretation of those requirements. With the amendment and possible combination of these instruments on the horizon, there would appear to be an ideal opportunity to remove any unnecessary references to writing and clarify certain provisions. However, for the promotion of small business use of electronic commerce it is hoped that the valuable protection provided by UCTA is not eroded but clarified and expanded in the revised provisions.

To-date, where 'new' measures have been introduced with the objective of accommodating new methods of communication and electronic contracts, insufficient consideration has been given to the nature of the electronic environment to produce regulation which is sufficiently clear to provide the legal certainty and favourable legal environment desired.

Electronic contracts are just contracts formed and often performed by modern means of communication. If the message creating an electronic contract, or indeed the subject matter of that contract, is the same as a traditional contract then its legal significance should not be affected by the medium through which it is sent. However, electronic contracts are sufficiently different in nature, to challenge the application of existing legal principles. At present, this challenge is not being met by the law and the stable, predictable and consistent legal environment required to promote the use of electronic contracts is not in place.

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