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Subject:	Proposal for a Directive of the European Parliament and of the Council on certain aspects concerning contracts for the supply of digital content (First reading) - Policy debate

I. Introduction

1. On 9 December 2015, the Commission adopted two proposals for Directives relating to contract law: a proposal for a Directive on certain aspects concerning contracts for the supply of digital content ('Directive on the supply of digital content' or 'DCD')¹ and a proposal for a Directive on certain aspects concerning contracts for the online and other distance sales of goods ('Directive on online sales of goods')².

¹ 15251/15 JUSTCIV 290 CONSOM 220 DIGIT 116 AUDIO 40 CODEC 1731 + ADD 1 + ADD 2.

² 15252/15 JUSTCIV 291 CONSOM 221 CODEC 1733 + ADD 1 + ADD 2.

2. At its meeting on 9 and 10 June 2016, the Council (Justice and Home Affairs) held a policy debate on the proposal for a Directive on the supply of digital content, and Ministers agreed on a number of basic principles and endorsed a set of political guidelines for the ongoing work on the draft Directive at technical level³.
3. The proposed Directive on the supply of digital content is part of the 'Digital Single Market Strategy for Europe'⁴. The Slovak Presidency therefore put great priority on the negotiations of this proposal.
4. Building on the political guidelines endorsed by the Council in June 2016 and based on a joint Dutch-Slovak Presidency revised text of the proposal, the Council Working Party on Civil Law Matters (Contract Law) in an intensive meeting schedule (12 meeting days) held in-depth deliberations on the individual provisions and the underlying concepts of the Directive on the supply of digital content, as well as on its relationship to other sectoral and horizontal legislation.
5. The discussions were very constructive and good progress was made on a number of technical aspects. However, given the complexity of the proposal and its interrelation with other legislation, discussions also brought to light a number of additional issues that require further consideration at technical level.
6. The Presidency has identified three policy questions which would benefit from guidance from the political level at this stage. To pave the way for further substantial progress to be made on the proposed Directive on the supply of digital, the Presidency wishes to submit these three questions for a policy debate of the Council.

³ 9768/16 JUSTCIV 160 CONSOM 137 DIGIT 67 AUDIO 76 CODEC 809.

⁴ 8672/15 COMPET 185 TELECOM 109 AUDIO 11 DIGIT 32 RECH 107
MI 291 PI 32 IND 72 ECOFIN 308 ENER 139 DATAPROTECT 70 CYBER 31 JUSTCIV
101 E-JUSTICE 56 CULT 29 EDUC 122.

II. Questions for the policy debate

The Council (Justice and Home Affairs), at its meeting on 8 and 9 December 2016, is invited to hold a policy debate on the following questions, taking into account the background information set out in the annex to this note:

- 1) Which of the two options concerning 'embedded digital content' should be the basis for further work?
 - **Option A** - to apply the 'goods rules' also to embedded digital content
 - **Option B** - to apply the 'digital content rules', by way of a rebuttable assumption, also to the tangible good
- 2) Should 'other data' (data other than personal data) be considered as a possible counter-performance under the proposed Directive on the supply of digital content?
- 3) Do you agree with the modified approach regarding the balance between subjective and objective conformity criteria for the conformity of digital content as described in section C, point 33, of the annex to this note?

A. Which rules should apply to 'embedded digital content'?

1. Background

1. More and more goods contain embedded digital content. The diversity of products is vast and the extent to which the digital content contributes to the functioning of such products also varies (simple household appliances, the 'Internet of things', 'smart goods', 'wearables', 'smart cars', 'smart homes', etc.).
2. The range stretches from household appliances, such as washing machines, where the digital content basically 'only' controls the primary function of the item (to run the washing cycle in the example of the washing machine) to goods which are equipped with additional applications that make such goods 'smart products' (e.g. a smart fridge that, in addition to cooling its content, checks the stock and creates a shopping list or even orders the shopping). Such products also include goods where the digital content could be considered predominant compared to the tangible part of the product (e.g. a 'smart home' device which controls the heating, air conditioning, etc.).
3. Therefore, the question of whether, in the event of a defect, it would be more appropriate for such products to be subject to the rules/remedies designed for the sale of goods or those designed for the supply of digital content is a crucial aspect for the creation of a regulatory regime that corresponds to the technical reality, is future-proof, and that allows a simple and, where necessary, flexible application in practice.
4. The Commission proposal suggested that the Directive on the supply of digital content ('digital content rules') should *not* apply to 'digital content, which is embedded in goods in such a way that it operates as an integral part of the goods and its functions are subordinate to the main functionalities of the goods'⁵. This would mean that the rules on sales of goods ('goods rules') would apply to such digital content embedded in goods.

⁵ See recital 11 of the Commission proposal.

5. 'Goods rules' in this context refers to the rules of the Consumer Sales and Guarantees Directive 1999/44/EC⁶, and/or the new rules of the proposed Directive on the online and other distance sales of goods⁷ (subject to its adoption).
6. Following the political guidelines approved by the Council in June 2016⁸, the Working Party on Civil Law Matters (Contract Law) considered three options which can be broadly outlined as follows:
 - (1) to apply the 'goods rules' to the embedded digital content;
 - (2) to take a 'split approach' and apply the 'goods rules' to the good itself in which the digital content is embedded, while applying the 'digital content rules' to the embedded digital content;
 - (3) to apply the 'digital content rules' to both the digital content and the good in which it is embedded, coupled with an exception giving the supplier the possibility to prove that the defect lies in the hardware of the good, in which case the 'goods rules' would be applied when remedying such a defect.
7. In the discussions in the Civil Law Working Party, the second option received little support as it was considered to be difficult to apply in practice. The other two options (labelled as options A and B below) each met with the support of several Member States. However, so far no clear majority has emerged for either of those alternatives.
8. In the light of this, the Presidency invites Ministers to indicate to the Civil Law Working Party which of the two options should be taken as a starting point for further work at the technical level.

⁶ Directive 1999/44/EC of the European Parliament and of the Council of 25 May 1999 on certain aspects of the sale of consumer goods and associated guarantees, OJ L 171, 7.7.1999, p. 12.

⁷ See document 15252/15 JUSTCIV 291 CONSOM 221 CODEC 1733 + ADD 1 + ADD 2.

⁸ See point 12 of ANNEX of document 9768/16.

9. When deciding on this question, Ministers are invited to bear in mind that according to draft Article 3(3) of the proposed Directive on the supply of digital content (as proposed by the Commission proposal and supported by a majority of Member States at Working Party level) the remedies contained in the 'digital content rules' would also apply to any tangible medium (i.e. a good⁹) '*incorporating digital content in such a way that the tangible medium serves exclusively as a carrier of digital content*'. The most illustrative examples of such 'tangible media' are CDs, DVDs, and USB sticks.
10. It should also be noted that, as regards delivery and the failure to deliver, the rules of the Consumer Rights Directive 2011/83/EU would continue to apply to both 'tangible media' (as described in the previous point) and 'goods with embedded digital content' (under both options A and B).

2. Options on embedded digital content

Option A - apply the 'goods rules' to the embedded digital content as well

11. This option would mean that the supply of goods containing embedded digital content would fall only under the 'goods rules'. Thus the specific standards required for digital content under the 'digital content rules' (e.g. the conformity criteria of Articles 6 and 6a of the proposed Directive on the supply of digital content, such as on *qualities, functionality, interoperability, accessibility, continuity* or *the requirement that digital content needs to be supplied along with any accessories and instructions that the consumer may reasonably expect to receive*, etc.) would not apply to embedded digital content.
12. This option would reflect the understanding that the 'thing' in which the digital content is embedded is a 'good' and would provide for a regime that is easily foreseeable from the average consumer's perspective, given that, unlike option B, it does not provide for an assumption, but a rule that applies in any case. Under this option the goods rules would apply even if the defect clearly lies in the embedded digital content.

⁹ In this context, see also recital 19 of the Consumer Rights Directive 2011/83/EU.

Option B - apply the 'digital content rules', by way of a rebuttable assumption, to the good as well

13. This option would mean that the 'digital content rules' would apply to both the digital content and the good in which it is embedded. It would be coupled with an exception giving the supplier the possibility to prove that the defect lies in the hardware of the good, in which case the 'goods rules' would be applied when remedying such a defect.
14. This option aims to allow for flexibility to apply those rules that are most appropriate, depending on the location of the defect. By taking the application of the digital content rules as a starting point, this option intends to take account of the fact that in an increasingly digitised world the functioning (and thus also potential defects) of goods are likely to be increasingly dependent on digital processes and the specificities resulting from the digital nature of their components. By applying the digital content rules only as a default rule, this option allows for the application of the goods rules in cases where this would be more appropriate, because the defect lies in the hardware. The burden of proof for this would be on the trader/supplier.

Illustrating example - see footnote ¹⁰

¹⁰ **Illustrating example**, taking the example of a modern car where, for instance, the breaks are controlled electronically:
If the brakes are not functioning, under option A, the conformity criteria and rules for remedying the defect designed for goods would also be applied to the software controlling the brakes. Under option B, it would be assumed that the defect lies in the embedded digital content and therefore, by default, the conformity criteria and rules for remedying the defect designed for digital content would be applied, unless the trader/supplier proved that the source of the defect lies in the hardware, e.g. a damaged/broken brake disc.

B. Scope: Should 'other data' (data other than personal data) be considered as a possible counter-performance under the proposed Directive on the supply of digital content?

15. Acknowledging the increased value of personal data in modern business models, the political guidelines approved by the Council in June 2016¹¹ expressed support in principle for the idea of including contracts where digital content is supplied in exchange for personal data in the scope of the proposed Directive on the supply of digital content. At the same time they emphasised that 'any interference with the application of the EU General Data Protection Regulation ('GDPR') needs to be avoided¹².
16. During the Slovak Presidency, considerable time has been dedicated to clarifying the relationship between the GDPR and the proposed Directive on the supply of digital content ('DCD'). However, discussions on that interplay have proven to be complex and brought to light additional issues that require further considerations at technical level.
17. The CLS has been asked to provide a written opinion on some of the questions raised in this context. Moreover, some delegations suggested seeking further input from data protection experts in order to get more clarity on the data protection related aspects.
18. Without prejudging any decisions on the questions relating to personal data as a possible counter-performance, discussions at technical level would benefit from a clarification at the political level of the question as to whether or not provision by the consumer of 'other data' should be considered a possible counter-performance under the proposed Directive on the supply of digital content.

¹¹ See point 13 of ANNEX of document 9768/16.

¹² See point 8 of ANNEX of document 9768/16.

19. In line with the political guidelines approved by the Council in June 2016¹³, discussions in the Civil Law Working Party tried to shed more light on the concept of 'other data'.
20. The examples mentioned by the Commission of 'other data' that could be monetised by the supplier included:
 - photos of a mountain, recipes, songs or poems created by the consumer, etc., which are anonymised and could be used by the supplier, e.g. for advertising purposes;
 - combined anonymous data about a group of individuals (such as persons with an interest in the same sport or hobby) which does not refer to identified individuals, to be used for marketing purposes;¹⁴
 - information about which websites or app stores consumers have visited, or which digital content they have enjoyed, without collecting information about their identity, used to develop more popular products.¹⁵
21. Discussions in the Civil Law Working Party and, in particular, the exchange held with the IT experts on 19 October 2016 have shown that practically any data provided by consumers in exchange for the supply of digital content can be traced back to a specific person. It can therefore be broadly concluded that, in the context of the DCD, in most cases the data provided by consumers in exchange for the supply of digital content would be of a personal nature ('personal data' as defined by the GDPR, the definition of which is reused in the DCD).
22. Discussions also showed that, even if there were data that would not be covered by the broad definition of 'personal data', the scope of such 'other data' would be rather limited.

¹³ See point 14 of the ANNEX of document 9768/16.

¹⁴ For instance, information collected about TV series that consumers watch online, which contain no information on their identity and are used to identify the preferences of large groups of consumers (in a non-individual manner) to allow more popular, and hence profitable, TV series to be developed.

¹⁵ For example, a business offering online games could conclude on the basis of such data that certain types of in-game purchases (e.g. game characters or trophies) are more popular than other types, and could re-design a game by introducing a wider variety of the more popular characters into the game.

23. In any event, the delineation between 'personal data' and 'other data' appears to remain difficult in practice, and would depend on a subtle case-by-case *e contrario* interpretation of the definition of personal data.¹⁶ Concerns were expressed that the concept of 'other data' would cause legal uncertainty in view of the broad definition of 'personal data' under EU law on the protection of personal data.
24. Some delegations saw these difficulties as an argument for not making a distinction between 'personal data' and 'other data' and for considering the idea of bringing all kinds of data into the scope of the DCD as possible counter-performances. Another argument put forward by the Commission in support of also considering 'other data' as a possible counter-performance was that the inclusion of non-personal data in the scope of the DCD would remove the possibility of circumventing the Directive by simply anonymising the data.
25. From an economic perspective, doubts however were expressed about whether such 'other data' as counter-performance given by the consumer would have an economic value that would justify putting the supplier under the obligation to provide for the contractual remedies laid down in the DCD in the event of a defect in the digital content.
26. While several Member States could support the inclusion of 'other data' 'as a counter-performance in the scope of the DCD, several other Member States were opposed to the idea.

¹⁶ As explained by the Article 29 Data Protection Working Party (see Opinion 4/2007 on the concept of personal data - WP 136, p. 24, http://ec.europa.eu/justice/policies/privacy/docs/wpdocs/2007/wp136_en.pdf), "...in different circumstances information may be considered not to be personal data. This is the case where the data cannot be considered to relate to an individual, or because the individual cannot be considered to be identified or identifiable." Determining whether this is the case or not requires a case-by-case test, taking into account all means that are reasonably likely to be used to identify a person through the information provided. However, "...this test is a dynamic one Identification may not be possible today, with the means likely reasonably to be used today" (see p. 15 of Opinion 4/2007). But this would not rule out such possibility becoming available in the future.

27. To bring work on this matter forward, it would be beneficial to receive guidance from the Council on how to proceed on this question in further negotiations at technical level.
28. The question addressed to Ministers is intended to get guidance as to whether 'other data' (other than personal data) should be considered a 'counter performance' that would justify putting the supplier under the obligation to provide for the contractual remedies laid down in the DCD.
29. This question does not relate to any 'data created or stored by the consumer by using the supplied digital content or service', such as storage of (personal and non-personal) data by the consumer in a cloud. As concerns 'data created or stored by the consumer by using the supplied digital content or service', the Directive will (have to) provide for rules on the return of such data to the consumer when a contract is terminated (in this regard, further technical discussions will be needed on Article 13a(3) of the revised Presidency text, 10231/16), regardless of the policy choice made as regards the inclusion of 'other data as counter-performance' in the scope of the Directive.

C. Balance between subjective and objective conformity criteria

30. In reaction to the concerns expressed by Member States in relation to the concept of the initial Commission proposal that gave precedence to subjective conformity criteria (i.e. criteria agreed in the contract) over objective conformity criteria (i.e. criteria stipulated by law), political guidelines approved by the Council in June 2016¹⁷ held that for greater balance the digital content needed to be assessed against both the contract terms and a set of objective conformity criteria as defined by EU law.
31. Following those directions, the Dutch and Slovak Presidencies suggested significant modifications to the conformity provisions putting subjective and objective criteria on an equal footing. This approach and the modified wording of the new Articles 6 and 6a met with broad support.
32. However, the extent to which it should be possible to deviate from the objective conformity criteria, and the conditions under which this should be possible, remain undecided despite intensive and constructive discussions in the Civil Law Working Party.
33. As a compromise to this question the Presidency suggests to follow broadly the philosophy of Article 2(3) of Directive 1999/44/EC, by introducing a rule in the proposed Directive on the supply of digital content according to which there shall be no lack of conformity, if, at the time of the conclusion of the contract,
- (a) the consumer knew that a specific characteristic of the digital content was deviating from the objective conformity requirements, and
 - (b) the consumer expressly accepted this deviation when concluding the contract.

Under this rule, the burden of proof for both aspects (a) and (b) shall be on the supplier.

¹⁷ See point 21 of the ANNEX of document 9768/16.