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SOFTWARE AS GOODS

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Case: St Albans City and District Council v International Computers Ltd [1996] 4 All E.R. 481 (CA (Civ Div))

Legislation: Convention on Contracts for the International Sale of Goods 1980 (United Nations)

Sale of Goods Act 1979

Subject: COMMERCIAL LAW. Other related subjects: Contracts. Information technology. International trade. Sale of goods

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Abstract: Outlines the arguments in favour of characterising software as "goods " under the Convention on Contracts for the International Sale of Goods 1980 and the Sale of Goods Act 1979. Reviews the current uncertainties over the legal status of software, case law concerning the movability and tangibility requirements for products to be classed as goods and the range of contracts pertaining to software. Outlines why an approach that seeks to establish whether software transactions are licensing agreements or sales transactions, or contracts for goods or services is misguided, and suggests an alternative system which considers the context of each agreement.

*161 Introduction

Software is a term used to describe the collections of instructions and data (also referred to as programs), that allow computers to operate. Without software, computers are redundant vessels, unable to perform any dynamic functions. From a legal point of view, software is remarkable for two principal reasons. First, its unique characteristics mean that it is not truly analogous to any conventional chattel with which the law is familiar. Secondly, despite the fact that it is one of the most ubiquitous commodities of our commercial age, it has no readily discernible legal identity. It is surprising, for instance, that even the most venerable legal texts currently devote only a few paragraphs to this commonplace product and its place within the law relating to the sale of goods. [FN1] This, combined with the relative paucity of judicial authority on the matter, means that it is not clear what manner

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of legal treatment should apply to disputes involving software. This uncertainty manifests itself in the question of whether software should count as goods for the purposes of the Sale of Goods Act 1979 (SGA) or the 1980 United Nations Convention on the International Sale of Goods (CISG). It is the purpose of this article to make the case for software to be classed as goods, under both the SGA and the CISG, where the circumstances are appropriate.

The problem

The lack of clarity surrounding the legal approach to software is both conceptually arbitrary and commercially inconvenient. Currently, parties to transactions concerned primarily with the transfer of software [FN2] are denied predictability in *162 terms of the legal response to any problem they may encounter, whereas such predictability is taken for granted by those contracting for conventional products. Add to this the fact that there is no convincing reason why software should be excluded from the statutory protection afforded to other items subject to sales, and it becomes increasingly apparent that the law's failure properly to tackle this issue is unsatisfactory and needs to be addressed: "Liability under a sale of goods is associated primarily with compensating a purchaser in respect of unfulfilled expectations..." [FN3]

Purchasers of software have, in general, the same expectations of fulfilment as those individuals purchasing items with which the law is more comfortable. A refusal to classify software as "goods" has the effect of failing to recognise the need for these expectations to be protected. The SGA [FN4] and the Sale and Supply of Goods Act 1994 (SSGA) function so as to provide legal assurances to those contracting to buy "chattels personal other than things in action and money". [FN5] Whether software is covered by this definition depends upon its classification as a chattel personal, as distinct from a thing in action. Such an interpretive question is one for the common law, but the common law provides no easy answer. The situation is somewhat similar in the context of the CISG. Although the question of whether software is goods within the CISG has arisen on a greater number of occasions than it has in English common law, it remains unresolved. One reason for this is that neither of these regimes was developed with a view to governing transactions in software. Another reason is that the rapid growth in the commercial and social significance of software has outpaced comparable developments in the legal understanding of the relevant technologies. It cannot (and should not) be denied that software is a unique phenomenon, so attempts to understand its nature through analogy with existing concepts are not always helpful. In order for software to receive an appropriate legal treatment, therefore, either our legal taxonomy, or the criteria we use in relation to it, needs to be revised. The discussion that follows demonstrates how important it is to recognise that, in determining the most appropriate classification of a product, the context in which it is being considered, and its capacity within that context are often more relevant considerations than are the intrinsic characteristics of that product.

"The word [goods] is of very general and quite indefinite import, and primarily derives its meaning from the context in which it is used." [FN6]

To fail to recognise this is to fail to distinguish between the (potentially) several nature of interests in goods, each one requiring separate legal treatment. Money, *163 for instance, in its most common and recognisable form, is a medium of exchange and so is unable to constitute the subject-matter of a sale. It is, however, only excluded from the ambit of "goods" once it has passed into currency. [FN7] As a physical note or coin, money can behave like goods when it is kept and exchanged for its own intrinsic value. This simple example shows just how dependent legal classification is (or should be) upon contextual considerations.

Methodology

We examine both the SGA and the CISG for several reasons. First, these are both influential in the international legal environment [FN8] and, considering the importance of software for today's economy, it is important that there is clarity regarding its treatment under these regimes. Secondly, despite the fact that the United Kingdom has not ratified the CISG, it is beneficial for the English commercial community to be aware of developments in relation to it, since UK merchants may find themselves bound by it [FN9] and UK courts may sometimes be obliged to apply it. [FN10] Thirdly, the relationship between domestic and international developments has been aptly described as "symbiotic" [FN11] and there may be, therefore, some valuable lessons

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for the two systems to learn from each other.

In attempting to identify what it is about the legal concept of a sale of goods that has caused such confusion to arise in relation to software, we begin by examining two characteristics of the products themselves, namely "tangibility" and "movability" (variously identified as being necessary for products to have in order for them to count as "goods"). Next we look at the contracts to which software is subject, a context in which the question posed so often seems to take the form of asking whether "software transactions" are contracts for goods or for services, or whether they are licensing agreements or sales. Such an approach, we suggest, is not helpful; there is no reason to suppose that all software contracts should be of a common type. Rather, the law should look to the context of each individual agreement, just as it does with other products, in order to identify the precise nature of the contract at issue, and to deal with it appropriately. Our principal contention throughout this article is simply that it is possible to classify software as goods, and that, in the appropriate context, this is what should happen.

*164 Tangibility

Under some legal regimes, the criterion of tangibility is crucial for determining whether the object in question is goods. [FN12] Tangibility is usually defined as having a physical form or being capable of being perceived by the senses. [FN13] This notion has played a significant role in the current debate and it has even been stated that tangibility is the "stumbling block" to the classification of software as goods. [FN14] Furthermore, in *St Albans DC v International Computers*, [FN15] Sir Iain Glidewell distinguished between software per se and software contained on a computer disc. In his opinion, instances of the former would not be "'goods' within the statutory definition", whereas a:

"computer disc onto which a program designed and intended to instruct or enable a computer to achieve particular functions has been encoded"

would be. A clear implication of this decision is that, to be treated as goods, software must be contained on a tangible medium.

By contrast, the way the CISG has been interpreted by courts and commentators is much less categorical. There is no apparent uniformity as to whether the tangibility/intangibility dichotomy is a relevant consideration. In one case, [FN16] the court ruled that custom-made software was not tangible and, on that basis, implied that it was not goods within the meaning of the CISG. [FN17] Another court, however, took a much more liberal approach by stating that the notion of "goods" under the CISG includes all tangibles and intangibles that might be the subject of an international sales contract. [FN18] There is also academic disagreement on the matter; some argue that goods do not have to be tangible under the CISG, [FN19] while others maintain that it governs only tangible goods. [FN20] Finally, some commentators take a somewhat ambiguous position by stating that the CISG generally governs tangible *165 objects, but also suggesting that the term "goods" should be interpreted broadly so as to include all kinds of software. [FN21]

Relevance of the distinction to the question whether software is goods

In establishing whether this distinction is relevant for the purposes of classifying software, it is necessary to determine why tangibility is ever required of a good. It is probably because of the requirement that property must pass under a sale. Most legal systems define a sales contract as an agreement for the transfer of property in goods for money, usually called the price, [FN22] and such a transfer generally requires a transfer of possession. In the case of pure intangibles, however, it is often argued in both common and civil law systems that either an alienation [FN23] or a possession of an intangible is impossible or that intangibles are not capable of being owned because they cannot physically be possessed. [FN24] It would seem, therefore, that some form of tangibility requirement is indeed necessary. Our primary contention on this point, however, is that legal notions of tangibility be updated in order to accommodate the digital age. A fundamental mistake, commonly made when classifying software, is the drawing of a qualitative distinction between hardware and software. In actual fact, there is no legally relevant distinction to be made between them. As will be demonstrated below, components of hardware differ physically

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from components of software only in terms of their size. They both have a corporeal form, but whilst hardware can be perceived by the unaided senses, software cannot.

This does not alter the fact that software is a tangible product, as the Supreme Court of Louisiana recognised when it agreed that:

"[i]n defining tangible, 'seen' is not limited to the unaided eye, 'weighed' is not limited to the butcher or bathroom scale, and 'measured' is not limited to a yardstick".

Hall J. then asserted:

"The software itself, i.e. the physical copy, is not merely a right or an idea to be comprehended by the understanding. The purchaser of computer software neither desires nor receives mere knowledge, but rather receives a certain arrangement of matter that will make his or her computer perform a desired *166 function. This arrangement of matter, physically recorded on some tangible medium, constitutes a corporeal body." [FN25]

This corporeal body takes the form of massive strings of "bits". [FN26] If a program is stored permanently on a CD ROM, [FN27] each "bit" is represented by either the presence or absence of a pit on the disc's surface. When a program is stored in a less permanent form, such as on a computer hard disc, it takes the form of a series of magnetic switches, positioned at either "I" or "O". Even in the case of an electronic transfer or "download", [FN28] when a program is in its most transient state, it still has a corporeal form because it exists as a series of electrical pulses. As electronic communication is merely a form of linking up hardware, any software that is received on a computer has not been plucked out of the ether, but has come from another machine located elsewhere.

Since software has this tangible form, it is capable of being alienated and possessed. In proving this assertion, it is important to note that the notions of property and possession are inextricably linked. As Bridge explains:

"[i]n the law of personal property, possession is the relationship between a person and a chattel based upon both the fact and intention of excluding all others from effective control of the chattel." [FN29]

If something cannot be possessed, then an aspiring owner cannot exclude others from it. In order to be possessed, software must exhibit two particular features. First, the notion of exclusivity requires that software be capable of being controlled. Since software exists as a physical attribute on hardware, it can be controlled, [FN30] and exclusive access to it can be maintained. [FN31] Secondly, software must be movable, because if it is not, it cannot be transferred without losing the capacity to be exclusively possessed. [FN32]

A failure to recognise the true nature of software is likely to lead to the unfortunate situation in which the law applicable to a particular transaction will depend on whether software has been delivered on a disc or downloaded online, [FN33] even though the purpose of such transactions will often be the same. No doubt parties to these transactions, and particularly those who contract as consumers, [FN34] would be surprised to learn that their chosen medium of delivery could have *167 significant consequences for their legal rights. [FN35] Under English law, the rights and obligations of the parties to a transaction not classed as a sales transaction, would be governed by common law rather than the SGA. [FN36] A contract found not to be a sales contract under the CISG would require judges and arbitrators to determine the law applicable to the dispute. [FN37] Either way, such a result could be regarded as unfair and contrary to the reasonable expectations of software buyers. [FN38]

Movability

Something that is not movable cannot be transferred without losing its capacity to be exclusively possessed. Unless it can be so possessed, its aspiring owner cannot exclude others from it. Bridge illustrates the point by comparing a diamond ring with information: the transferor of information "retains the information that was transmitted which denies one of the features of a property right, namely its exclusivity", whereas "a diamond ring cannot support two wearers at the same time". [FN39] Thus, the movability of a product would seem to be a good indicator of its ability to be classed as goods for sales purposes.

Software is movable. [FN40] Choses in action are not. A chose in action, such as a copyright, cannot be moved. If the holder of that copyright has it infringed, he or she has not had that right removed and transferred to

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the infringer. On the contrary, the right crystallises and enables him or her to take legal action. Another sort of chose in action, such as the "know how" to create a program, is not physically movable either because, although it might be communicated from one mind to another, it does not thereby leave its origin; a copy is made, but the original remains where it is. Such things necessarily travel with those who have ever shared in them, and remain with them; they are copied and distributed, but not moved. It is entirely possible to remove, however, a piece of software from one piece of hardware to another. Of course, such a thing can be copied and distributed, (and often is), but the same can be said of almost any conventional chattel. The essential *168 distinction between those things that are movable and those that are not is the possibility of deleting them from their source. [FN41] Movability is directly relevant to the requirement of delivery. According to the SGA, "'delivery' means voluntary transfer of possession from one person to another" [FN42] and it is clear that "delivery" under the CISG is also intended to include acts which would enable the buyer to have possession over the goods. [FN43] This is something that can occur in relation to software, distinguishing it once more from choses in action, which cannot be delivered. Since the performance of a sales contract is epitomised by the delivery of those goods, [FN44] it is clear that deliverability is an essential characteristic for any goods purporting to be the subject of a sale.

A further indicium of software's movability is that, regardless of the medium on which it is supplied, it is usually "intended to be furnished as a distinct chattel". [FN45] In other words, when it is incorporated into another object (such as a computer hard disc), it is not an accession to that other object in the true sense of the term. This is because it can be added to and taken away from its medium without causing any material damage to that host object. [FN46]

It is perhaps significant that Art.2 of the US Uniform Commercial Code has explicitly moved away from a definition of "goods" which employs the term "chattels personal" and adopted one that reads "all things (including specifically manufactured goods) which are movable at the time of identification to the contract for sale". [FN47] This explicit reference to the criteria of movability and identification effectively pinpoints the characteristics of products most relevant to the question of whether they can be goods.

As far as the CISG is concerned, although it does not expressly require that in order to be "goods" an object must be movable, its various provisions reflect that such a requirement does in fact exist. [FN48] The corresponding section of the SGA, [FN49] which has adhered to the use of the term "personal chattels", could be regarded as being less specific and, consequently, less immediately helpful; after all, whilst some personal chattels will be capable of constituting the subject-matter of a sale, others will not. It would perhaps be more effective to identify from the outset *169 those things to which the statute will attach, rather than to refer to a genus from which exceptions must then be made. This is particularly true where, as here, [FN50] such a genus is beset by conceptual baggage.

Goods/services distinction

It has been argued that software transactions are contracts for the supply of services, rather than sales of goods, thus relying on a distinction recognised by many legal systems. [FN51] In such systems, different legal regimes apply, depending on how a particular contract is classified.

A number of attempts to explain the difference between goods and services have been made. For instance, it has been pointed out that service contracts, unlike sales transactions, are based on a continuing relationship and call for close co-operation and interaction between parties. [FN52] These two phenomena, however, can also be applicable to sales transactions, some of which are themselves performed over a long period and may also require mutual co-operation. [FN53]

It has also been argued that services are not capable of being stored, [FN54] and this point perhaps reflects the main difference between goods and services, namely the intangible nature of the latter. [FN55] It is possible that the law treats goods and services differently on pragmatic grounds because of the different ways in which they are traded. Thus, as far as tangible products are concerned, the emphasis is placed on the product itself "because it is

