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Caveat Emptor in digital times

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Citation

Nieuwenhuis, J. H. (2003). Caveat Emptor in digital times. *E-Commerce Law, National And Transnational Topics And Perspectives*, 89-92. Retrieved from <https://hdl.handle.net/1887/3243>

Version: Not Applicable (or Unknown)

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Note: To cite this publication please use the final published version (if applicable).

Caveat emptor in digital times

Hans Nieuwenhuis

1 DID YOU EVER SEE TWO COMPUTERS MAKE A FAIR AND DELIBERATE EXCHANGE?

'Nobody ever saw a dog make a fair and deliberate exchange of one bone for another with another dog' Making contracts is 'common to all men, and to be found in no other race of animals' Thus, Adam Smith in his *Wealth of Nations*¹

No race of animals other than the homo sapiens? How about computers?

Did you ever see two computers make a fair and deliberate exchange?

This seems to be a piece of cake. A valid contract can be concluded by two 'electronic agents', i.e. 'computer programs used independently to respond to electronic messages without intervention by an individual at the time of the response'

The electronic agent of a bookseller, finding out that there are only three copies of 'An Introduction to Comparative Law' in stock, spontaneously buys fifty copies from the electronic agent of the Oxford University Press. Electronic contracts can, of course, also be concluded between a human being and an electronic agent. This will be the case if I add *Bleak House* to my 'on line shopping cart' provided by Amazon.com

Everyone agrees that electronic agents are not real agents as understood by the law of agency. You can only act as an agent, representing your principal at the conclusion of a contract, if you are a person, be it a natural person or a legal person.

The responses made by the electronic agent show a close resemblance to the reactions of a Pavlov dog. This may be a very intelligent dog, performing very complicated tasks, but its choices are not its own. His master's voice is all there is to obey. Its behaviour is completely determined by the way in which it is programmed. Likewise, an electronic agent may be able, far better than I am, to find out whether Alitalia offers lower prices for flying from Amsterdam to Rome than KLM, but only I am able to decide whether it is advisable for me to fly to Rome, rather than buy a new dishwasher.

Some key concepts of Contract Law seem to be linked exclusively to human nature: the principle of good faith and fair dealing, for instance. This principle is one of the cornerstones of the new Principles of European Contract Law.

Each party must act in accordance with good faith and fair dealing (Article 1:201)

It may not be absurd to speak of a dog being faithful and fair, but as regards an electronic agent, the requirements of good faith and fair dealing can only apply to the person employing this agent and to the ways in which he has programmed it.

1 Adam Smith, *An inquiry into the nature and causes of the wealth of nations*, ch. 2

How is one to instruct an electronic agent in order to have it act in accordance with good faith and fair dealing? Take for instance the concept of fundamental mistake in the Principles of European Contract Law:

A party may avoid a contract for mistake (...) if the other party knew or ought to have known of the mistake and it was contrary to good faith and fair dealing to leave the mistaken party in error. (Article 4:103).

The principle of good faith and fair dealing is especially tailored for face-to-face situations. If I have reasons to believe that the person wanting to buy my farm is mistaken about the number of pigs he is allowed to breed there, I may have to inform him, even if he did not question me on this point. The homely wisdom, 'Ask me no questions and I will tell you no lies' is not a safe guideline in Contract Law.

What applies 'Off line', should also apply 'On line'. This is a recurrent theme in the debate on the law relating to e-commerce. Legal principles and norms governing the 'Off-line' situation, where both parties are physically present when negotiating a contract, should also apply if the contract is concluded 'On line'.

Amazon.com ought to know that several people are seriously mistaken about their ability to understand and appreciate 'Finnegans Wake' by James Joyce. Should Amazon give them the opportunity to test their ability by confronting them with the first sentence?:

riverrun, past Eve and Adam's, from swerve of shore to bend of bay, brings us by a commodius vicus of recirculation back to Howth Castle and Environs?²

Irrespective of whether the contract is to be concluded 'Off line', or 'On line', Contract Law should try to strike a fair balance between two opposing principles: on the one hand, the principle of *Caveat Emptor*, let the buyer beware, and on the other hand, the altruistic principle that you have to inform the other party if you know him to be mistaken. *Caveat Emptor* tells a person wanting to buy a second-hand car to have this car properly inspected **before** concluding the contract. But in some cases, for instance, if the seller is a professional seller of second-hand cars, Dutch Contract Law requires that the seller inform the buyer that this car has been involved in a serious crash and that the damage has been repaired rather inadequately.

2 CAVEAT EMPTOR 'ON LINE'

What's the meaning of *Caveat Emptor* 'On line'? Browsing the web, you discover an attractive KitchenAid Ultra Power Food Processor priced at €199. But you are not sure whether you can handle this high-tech device. At this point a Directive of the European Community comes to your aid:

2 In fact, <www.amazon.com> offers the opportunity to inspect, not only the front and back covers and table of contents, but also some eight sample pages of *Finnegans Wake*.

For any distance contract the consumer shall have a period of at least seven working days in which to withdraw from the contract without penalty and without giving any reason. The only charge that may be made to the consumer because of the exercise of his right of withdrawal is the direct cost of returning the goods. The period for exercise of this right shall begin: in case of goods, from the day of receipt by the consumer (...) (Directive 97/7/EC, Article 6).

The consumer has ample opportunity to heed the warning: *Caveat Emptor*. Seven days and seven nights he can test the Ultra Power Food Processor and in the end decide: I prefer my old set of kitchen knives. He can then withdraw from the contract without giving any reason.

Can we still call this European consumer distance contract a contract? What is left of the binding nature of a contract if one of the parties is allowed to withdraw from it at will? Medieval civil lawyers, commenting upon Digest 19,1,13,29, would call this arrangement a *negotium claudicans*, a limping contract:

si quis a pupillo sine tutoris auctoritate emerit, ex uno latere constat contractus.

If a man buys from a *pupillus* without his tutor's authorisation, a contract arises on one side only. (translation A.Watson).

There is, however, an important difference between the merchant in Roman times and the modern dot.com firm. The Roman merchant could easily avoid concluding contracts with pupilli (boys younger than fourteen). Modern e-commerce firms, on the other hand, can hardly be expected to avoid doing business with adult consumers. Is this unconditional right to withdraw from the contract fair to the seller? One could object that it is not so much a question of fairness, but of Law and Economics.

Economics first: any higher level of consumer protection is in the end paid by the consumers. Every 'On-line' seller will estimate the percentage of goods that will be returned by consumers deciding to withdraw from the contract. In those cases he not only loses the costs of shipping these goods to the consumer, even if it were agreed that the consumer should pay these costs, but he will also be unable to resell these returned goods – food processors for instance – as new and unused. In calculating the price of his products, he will have to take these losses into account.

Now, turning to the law: how is one to 'withdraw' from the contract?

According to the American singer Paul Simon there are fifty ways to leave your lover, some quite subtle: hop on the bus, Gus; make a new plan, Stan.

In Dutch Law there are two distinct, far less subtle, ways to leave a contract. The first uses retroactive force: annul the contract. The contract is considered to have been null and void from the start (*ex tunc*). If ownership has been transferred, it automatically returns to the seller. The second way in which to leave a contract is to terminate the contract *ex nunc*. The contract stays valid for the period preceding its termination. If ownership has been transferred, it must be transferred back.

Implementing the Directive, the Netherlands have opted for the second technique. On receiving the goods bought 'On line' ownership is transferred to the buyer. If after seven days he decides to terminate the contract, the buyer must transfer the ownership back to the seller.

The fact that during the trial period of seven days the buyer, and not the seller, is

the owner of the goods causes problems in case of bankruptcy of the buyer. A bankruptcy will block the transfer of ownership back to the seller.

Can the seller forestall these complications by simply stipulating a retention of ownership (reservation of title)?

Under Dutch law a retention of ownership by the seller is only valid if it is meant to ensure payment by the buyer (Article 3: 92 Civil Code). Buying 'On line' the consumer will normally have paid before receiving the goods. A retention of ownership is therefore ineffective.

What's the most effective remedy for chronic headaches?

The guillotine, without any doubt. Chop off your head and your headache will most certainly disappear. But the most effective remedy is not always the best. It might contain some overkill. New developments in law often contain a considerable amount of overkill. Take the development of a non-possessory security for movables in German and Dutch law. It started as a fiduciary transfer of ownership in combination with a delivery per constitutum possessorium. Thus, the goods could remain with the transferor. Next it became urgent to trim this fiduciary ownership to reasonable proportions in order to protect the rights of third parties. The *Hoge Raad* did this in an impressive series of decisions. This opened the way for a more balanced device for non-possessory security on movables in our new Civil Code: a right of pledge which can be established without bringing the goods under the control of the creditor (Article 3: 237 Civil Code).

A similar development in the way in which we construe the right to withdraw from the 'On-line' contract is very likely. Again, the law concerning 'On-line' contracts should follow the example offered by the 'Off-line' world as closely as possible.

A voice from the real world: A wants to sell his caravanette for € 10,000 to B (**caravanette**, a motor vehicle with a caravan-like rear compartment for eating, sleeping etc.; Concise Oxford Dictionary). The price is no problem for B, but he would like to test whether he can handle the car. In order to win him over A allows B to try the caravanette during the weekend. After the weekend B tells A that he thoroughly disliked the eating and sleeping facilities. B hands the caravanette back to A.

No one would deem it necessary to construe these facts in such a way as to imply that on Friday A sold the caravanette to B and transferred the ownership thereof, and that on Monday B terminated the contract and transferred the ownership back to A. Far more realistic is the view that on Friday A made an offer to B, and on Monday B declined this offer.

Likewise, we should construe the response of the electronic agent of an 'On-line' seller and the subsequent shipping of the goods as an offer which is irrevocable during a period of seven days after receipt. In this way a serious problem will disappear. Both in 'Off-line' and in 'On-line' commerce we should keep two activities clearly apart: one, finding out whether a proposed contract suits us, and two, concluding the contract. The *Caveat Emptor* principle belongs to the former and should not cross borders with the latter. Once the contract has been concluded another principle should reign: *Pacta sunt servanda*.