

# PRODUCT LIABILITY IN THE DIGITAL AGE

Position paper of the Federation of German Consumer Organisations (vzbv)

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# I. SUMMARY

Product liability law in the European Union is outdated and in need of an overhaul. As software becomes increasingly relevant as a cause of damage, the law must make clear that software is a product within the meaning of the Product Liability Directive. It should not be possible for multiple potentially liable parties to shift responsibility to each other within ecosystems that lack transparency. Instead, they must take responsibility for resolving damage events. Ultimately, producers must always be liable, in the sense of strict liability, if their product causes damage when used as intended.

# II. CURRENT SITUATION

Digital voice assistants, robot vacuum cleaners, smart TVs: internet-connected hardware is an established part of everyday life. However, their level of security varies greatly from model to model. Some of them are incorrectly programmed or easy to hack. When damage occurs, consumers are often left to deal with the consequences.

The German Product Liability Act (Produkthaftungsgesetz) governs the circumstances under which producers are liable for damages caused by defective goods. It is based on an EU directive from 1985. At that time, there were no digital voice assistants or internet-enabled appliances. Correspondingly, the legal situation today is inadequate. Only hardware items are explicitly considered to be products. Whether software can also be a product is currently disputed. The law only covers damage to people or property. It remains unclear who is liable for data losses or infringement of personality rights.

The Federation of German Consumer Organisations (vzbv) calls for a fundamental reform of product liability law. To protect consumers, the provisions must be adapted to the requirements of the digital world.

# III. VZBV'S PROPOSALS

## 1.1 Update the definition of a product

The extent to which software falls within the scope of the directive is controversial. At the time the directive was passed, software as used by consumers was of little relevance. The situation is different today. Even when buying hardware, consumers often see the integrated software as a central aspect of the purchase. This is why it is important to establish clarity. In vzbv's view, the Product Liability Directive should be adapted to this reality. Algorithms and software are capable of causing damage that is just as severe or even more than that caused by mechanical products. Therefore, producers must be just as liable for defective software and the damages it causes as they are for moveable goods.

### **VZBV DEMANDS:**

The scope of product liability legislation must in future also include software, regardless of whether it is integrated into a physical product or not. The law must take a

broad approach to technology and cover not just hardware but also algorithms and artificial intelligence.

## 1.2 Obligation to update and modernisation of the definition of a defect

The definition of a defect in the Product Liability Directive is based on the concept that a product is completely detached from the producer once it has been placed on the market. According to this concept, the producer no longer has direct influence over the functionality of the product after that date. As a logical consequence, it is assumed that the producer is not liable for defects that were not present, or that the producer could not have known about, when the product was placed on the market (Art. 7 b) and e), Product Liability Directive).

Neither assumption corresponds to today's reality. Producers of connected products have the option to keep these up to date and secure by means of updates. They can retroactively fix security flaws and correct defects. This is essential because, in complex systems in particular, there is no such thing as error-free software. Security flaws and defects in connected devices are usually only identified after some time. Once a defect has been discovered, it can be exploited for attacks. However, this is also the point at which it can be fixed by the producer – and it is usually only the producer who can do so. This means there can only be product safety for connected devices if the producer continues to take responsibility for the updating of the product after it has been placed on the market.

With Directive (EU) 2019/771 on certain aspects concerning contracts for the sale of goods and Directive (EU) 2019/770 on certain aspects concerning contracts for the supply of digital content and digital services, European legislators introduced an update obligation for products with digital elements and for digital content and services. vzbv believes this should be taken as a model for the codification in product liability law of an obligation for producers to provide security updates. The duration of the update obligation should be based on the expected product lifespan.

In addition, where automated or autonomous systems are used, it is generally not possible for the user to precisely understand how a product works. This is a desirable situation for producers, as the source code that ensures the functioning is part of the trade secrets they would like to protect. However, this also means that it is nearly impossible to distinguish between poorly programmed systems and one-off malfunctions. If a defect which meets the definition of the directive occurs on the software side, it is thus simply impossible for the consumer to prove. From the consumer's perspective, it is not acceptable that the producer's recourse to protection of trade and business secrets makes it impossible for consumers to assert their rights in the event of damage. As such, producers must take responsibility regardless of a verifiable defect.

In vzbv's view, therefore, the definition of a defect is unsuitable altogether for connected devices.

### **VZBV DEMANDS:**

Just like contract law, product liability law should also contain an obligation to provide updates.

Regardless of any defect, the producer should bear a strict liability if a product causes damage within the intended use.

### 1.3 Reversal of the burden of proof

Under the Product Liability Directive, the burden of proof e.g. for causality fall disproportionately on the injured party. In the event of damage, however, it can be difficult for consumers even in the analogue world to identify the defective product and hence the liable producer. In the realm of digital technologies, injured parties often have little chance to figure out the defect and product and to demonstrate the causalities.

The problems resulting from digitalisation thus have a disproportionate impact on consumers. This shift in the balance of liability requires a political correction of the distribution of the burden of proof in the Product Liability Directive.

The burden of proof for the absence of defects in digital products should instead be shifted to the producer. The producers could free themselves from this burden of proof by complying with standards and documentation obligations.

#### **VZBV DEMANDS:**

The burden of proof, provided products are used as intended, should be shifted to the producer. In the event of doubt, the producer should have to prove that the damage was not caused by a software defect.

### 1.4 Attribution where multiple parties are involved

Users of connected hardware often cannot identify precisely which device is responsible for which process when damage occurs. To make their products attractive, producers and operators of connected hardware make use of complex eco-systems in which the interaction of processes is usually completely opaque for the consumer. The only process that can be identified is the one that is actually visible from outside. If this leads to an instance of damage during the intended use, producers must not be able to use the opacity of operator networks and eco-systems to shield themselves from liability.

#### **VZBV DEMANDS:**

In ecosystems of connected systems, all parties involved in the provision of the product to the consumer should be jointly liable.

The producers are subject to an obligation to document how the system components they provide function. They should be able to free themselves from liability in relation to the other producers if they are able to describe and prove the circumstances that exonerate them.

### 1.5 Expansion of the definition of damage

According to the Product Liability Directive, the producer is currently liable only for injury to life or health, and damage or destruction of an item other than the defective product. However, even this is subject to restrictions (Art. 9). This fails to do justice to the fact that data and software are becoming increasingly important as products. For example, if a piece of software, as a result of a malfunction, deletes valuable data belonging to the consumer this causes real, tangible damage. It is currently unclear whether this falls under the definition of damage in the existing Product Liability Directive. There is a need for a clarification and expansion of the definition of damage

here. Without this, the concept cannot keep up with the definition of a product (see above).

In a context of increasing importance of data and software, the definition of damage should be expanded to include immaterial damages to the consumer or third parties. This must explicitly include the consumer's stored data.

In addition, there must be a discussion about the extent to which financial losses need to be compensated under product liability law.

## 1.6 Ten-year limitation period

The Product Liability Directive provides that after ten years from the date on which the product is placed on the market, all claims emerging from this directive become time-barred. However, damages can often only be identified after this period, especially for products with relevance to health (e.g. medication, chemicals, genetically modified food, nanotechnology).

### **VZBV DEMANDS:**

Irrespective of digital innovations, the limitation period of ten years (Article 11) should be significantly extended. The ten-year period poses the risk of a complete obstruction of access to legal recourse, in particular, in the context of medicines, chemicals, genetically modified foods or nanotechnology.

## 1.7 Optional liability limits

According to applicable law, Member States can limit the liability for the same defect by introducing a maximum limit. This ceiling can be set as low as 70 million euros (Art. 16 para. 1). The limit is alien to the system and gives the impression of being simply a tactical exemption from the harmonised product liability to consumers in the European Union.

Even if the optional upper limit to liability is to be kept in order to guarantee the insurability of any new strict liability provision, under applicable law, it is significantly too low. Within global mass production processes, this threshold is far below any potential liability sum that could result from a single defect for many producers with strong global market penetration. It also seems unjustified when put in relation to the turnover of such producers. The liability threshold must therefore be increased to a value that accounts for the possible damage scenarios but also enables insurability for producers.

The optional upper liability limit of 70 million euros for personal injury should be removed. If a liability limit continues to be considered necessary for reasons of insurability, the limit should be increased to a value that adequately takes the potential damage scenarios into account.

In order to hedge the producer's insolvency risk, an obligation to take out product liability insurance should be introduced.

With regard to mass production in particular, it is important to note that collective compensation for consumer damages must be made easier to obtain. To make this happen, collective compensation procedures are needed at the level of the Member States, and these must also be applicable to product liability cases.

## 1.8 Responsibility of online marketplaces under liability law for the import of unsafe products

Product liability law should protect consumers from suffering damage from a defective product and then having no responsible party within reach. The recitals to the Product Liability Directive contain the following clauses:

“Whereas protection of the consumer requires that all producers involved in the production process should be made liable, in so far as their finished product, component part or any raw material supplied by them was defective; whereas, for the same reason, liability should extend to importers of products into the Community and to persons who present themselves as producers by affixing their name, trade mark or other distinguishing feature or who supply a product the producer of which cannot be identified;”

The digital market economy has created a situation in which there are new actors – online marketplaces – which play a central role in providing consumers with products. A core element of the business model of such online marketplaces is that consumers are brought into contact with vendors that they would otherwise never encounter. At the same time, online marketplaces refuse to accept legal responsibility in the event that consumers suffer damage due to inferior goods obtained in the purchase they brokered<sup>1</sup>.

These third parties increasingly include vendors from outside the European Union that do not comply with import and safety legislation and that are hard to engage for an injured consumer in the event of damage. Thanks to the brokering service provided by online marketplaces, consumers come into contact with providers from all parts of the global market. Consumers expect that the safety rules will be complied with, but in many cases the traders have never even heard of these. For consumers in this situation to be left with the damage and no recourse falls short of a fair balance of interests.

### **VZBV DEMANDS:**

Where operators of online marketplaces broker sales of products from non-EU countries, they must be liable for compliance with legal requirements in terms of product safety and for damages suffered by consumers as a result of defective products.

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<sup>1</sup> See, for example, No. 11 of the Amazon Conditions of Use and Sale (accessible at [https://www.amazon.de/gp/help/customer/display.html?ie=UTF8&language=en\\_GB&nodeId=201909000](https://www.amazon.de/gp/help/customer/display.html?ie=UTF8&language=en_GB&nodeId=201909000)): “Amazon does not assume any responsibility or liability for the actions, product, and content of all of these or any other third parties.”