

**A report on the legal implications of
International Business Networks
entering into a project to provide
Anti Trust Solutions Ltd
with hardware and software.**

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1. Introduction

To be as professional and successful as possible, IBN always has to highlight legal risks before entering projects.

In this special case we are about to enter a project with a SME company called Anti Trust Solutions Ltd, also based in England. We know that they are dependant on our right hardware and software solutions (development framework as a licence agreement) and that they may develop software used in expert systems with it.

In case of the project with Anti Trust Solutions Ltd there are some legal considerations in the following matters:

- Distinctions between hardware and software contracts
- Legal aspects for selling hardware and software (Supply of Goods and Services Act)
- Liability for defective software
 - Liability for expert systems developed by Anti Trust Solutions Ltd

This report investigates the most relevant issues to keep in mind before starting such a project as for example the possibility of claims against us.

For reasons of easier reading, the abbreviation ATS is used for Anti Trust Solutions Ltd.

2. Legal distinction between HW and SW contracts

Due to the type of project, an evaluation of these contracts is necessary to understand their legal aspects.

It seems that hardware is kind of useless without software and most of the time they are sold as a bundle anyway. However, in English law different legal rules apply for hardware and software.

First I want to difference the most common used ways of selling hardware and software:

- Hardware only (without assembling or installations)
- Hardware with assembling or installations
- (Hardware hiring)

- Software developed exclusively and sold with copyrights
- Software provided in licence

- Hardware with software on it (i.e. CD with software on it)

2.1. Acts according to hardware

According to Bainbridge (2008), there is only one major issue the Sales of Goods Act 1979 applies in our context and that is when only hardware is sold - without any assembling or installations. The hardware has to be of satisfactory quality since the Sale and Supply of Goods Act 1994 replaced some important parts. (The good had to be merchantable before)

In case of hiring hardware, the Supply of Goods and Services Act 1982 applies because ownership is not transferred.

Because the Sales of Goods Act 1979 defines “goods” as ‘... all personal chattels other than things in action...’ and copyrights are such ‘things in action’, the Sales of Goods Act 1979 cannot apply to copyrights or other intellectual properties. (Like software, see 2.2 Acts according to software)

There might be a collateral sale of goods contract if the software is i.e. installed on a Computer and sold with it. This contract will be governed by the Sales of Goods Act 1979 and the Services Act 1982.

2.2. Acts according to software

Typical contracts of writing software are controlled by the Supply of Goods and Services Act 1982. (assignment of copyright)

Licence Agreements

In case of licence agreements, where the ownership of the software is not transferred, the contract should include the duration and the scope of the agreement to avoid misunderstandings. According to *Linden Gardens Trust Ltd v Lenesta Sludge Disposal Ltd* [1993] burdens aren't transferable but benefits are if not prohibited in the contract.

Copyrights / Intellectual Property

In some cases of selling software, also the Copyright, Designs and Patents Act 1988 applies.

2.3. Breach of Contract

In software and hardware contracts there is also a division in conditions and warranties. Only in case of conditions, the aggrieved party could abandon the contract but also has the possibility to seek damages. In case of warranties, they cannot end the contract and if innominate terms appear, it depends on the breaches seriousness.

According to Bainbridge (2008). "...late delivery is normally a breach of condition, but in a contract of writing software, it is more likely a warranty especially if there" He also states that software usually contains errors and errors aren't necessarily a reason of condition breach. Contracts can provide clauses that developers will fix errors.

3. Effect of the Supply of Goods and Services Act

This Act implies three important terms to projects like ours:

- The supplier has to provide reasonable care and skill.
- The supplier has to carry out the service in a reasonable time if performance time is not part of the contract anyway.
- If fees are not mentioned within the contract, the supplier gets paid a reasonable amount.

Furthermore, the Act mentions expert systems and the possibilities of liability.

Bainbridge (2008) describes two cases of contracts in the context of expert systems: a contract between the person acquiring a copy and the dealer OR a contract between the person acquiring a copy and the software company itself (the dealer acts like a company agent). If our contract is covered by the Contracts (Rights of Third Parties) Act 1999 and the second case (ATS deals with our software) applies, there is a risk that we could be liable to ATS clients.

3.1. Liability: Anti Trust Solutions

To figure out what ATS needs, we should recommend an external consultant to design the specifications with them. That should save us from coming up with the wrong HW and SW. In case the consultant is wrong, ATS has a claim against him, not us.

Bainbridge (2008) recommends independent professional supervision by a member or fellow of the British Computing Society for important contracts. I do not think that this is necessary if an external consultant designs the specifications.

According to *Stewart v Reavell's Garage* [1952] 2 QB 545, the professional giving advice using the ATS expert system should satisfy himself to reliability of the software.

Charnock v Liverpool Corporation [1968] 1 WLR 1498 is a case that shows the liability in terms of the Supply of Goods and Services Act 1982 if the contract is not performed in reasonable time. Therefore, we are liable to ATS for late delivery for example.

Concerning software bugs and quality warranties, we have the duty to correct possible errors in our software after delivery (*Saphena Computing Ltd v Allied Collection Agencies Ltd* [1995] FSR 616). According to Bainbridge (2008) this warranty concerning bugs can be limited in time and it is usual to keep money in the budget for error correcting.

Because the project is about replacing hardware, we are liable for the professional disposal of the old equipment.

Limiting Liability

The possibility of exemption clauses exists but they should be managed with care. In this project, we have bigger bargain power and that would be considered in case of a reasonableness test. In the case *Flamar Interocean Ltd v Denmac Ltd (The Flamar Pride)* [1990] 1 Lloyd's Rep 434, Potter J created these guidelines. These guidelines were also used in the case *The Salvage Association v CAP Financial Services Ltd* 1005 FSR 654 to show that limiting liability to unreasonable amounts is not possible.

Furthermore, *St Albans City & District Council v International Computers Ltd* [1997] FSR 251 shows that limiting liability to much (unreasonable) would end in an unfair contract and therefore the Unfair Contract Terms Act 1977 would apply.

3.2. Liability: 3rd parties

No I do not think we are liable to 3rd parties in general.

Also if we act like a subcontractor for ATS, their clients do not have claims on us because ATS has the duty for satisfying themselves as to the veracity and reliability of our system.

Economic Loss

The case *Caparo Industries plc v Dickman* [1990] 2 AC 605 states criteria for imposing duty of care. In my interpretation, damages are not foreseeable for us and there is no reasonableness of imposing a duty of care. Also in negligence there would be a doubt about proximity. But there is a possibility of remedy if these three criteria apply and our software provided a 3rd party with defective information.

Bainbridge (2008) says that decisions based on economic loss are unlikely because there is the burden of proof as well.

Expert Systems

If the claim is about an indirect statement, the 3rd party would have to prove that they relied on a statement provided by our software. Due to the fact that our software is not able to make statements or give advice (because it is only a framework) it is impossible to get sued for “wrong” indirect statements by any 3rd parties. (*Abbott v Strong* [1998] 2 BCLC 420) and (*Williams v Natural Health Foods Ltd* [1998] 2 All ER 577)

We know that they probably develop expert systems with our software framework and use the hardware purchased from us to do it. In the case that death or personal injuries are a result of our negligence and ATS acted negligent as well it is possible that we are partly guilty.

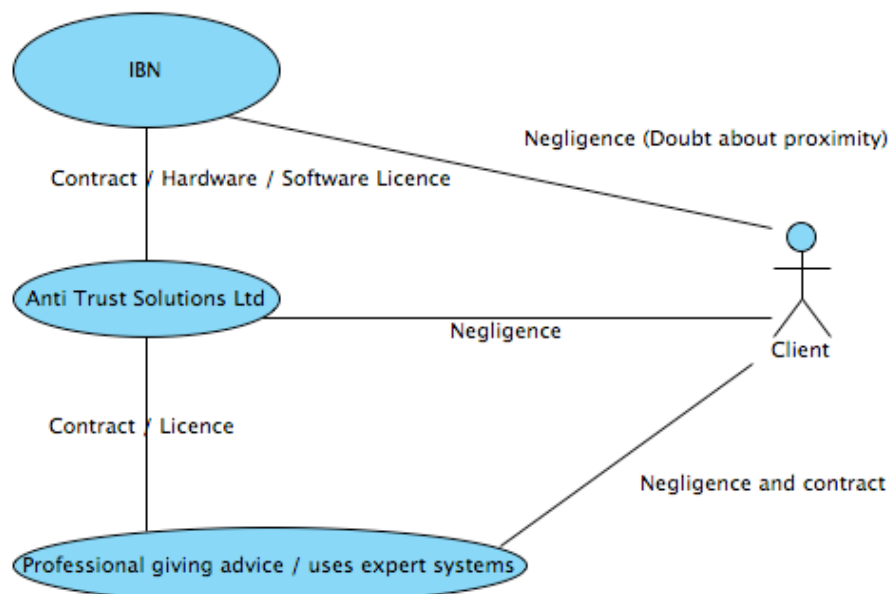


Figure 1: Possible Scenario

4. Conclusion and Recommendations

The legal situation is not that clear – we will have to make use of some legal options to protect our company from any accuses.

I recommend a BCS supervisor or at least an external consultant to design the specifications for the project. These specifications should include a benchmark to measure the acceptance of the project.

We have to set up a written contract with ATS where we can bring in the needed clauses and terms to carry out a fair project. Without any contract, we would be very vulnerable to claims.

It would be easier to have more contracts to divide hardware from software because different Acts apply:

- Hardware (only) purchase contract (Sales of Goods Act 1979)
 - HW maintenance contract
- Software licence agreement (Supply of Goods and Services Act 1982)
 - SW maintenance contract
- Disposal contract for old hardware

According to the Supply of Goods and Services Act 1982 we also should include deadlines and fees in these contract to avoid obscurities.

If we try to limit our liability in our contract with ATS, we should be aware of the Unfair Contract Terms Act 1977. But we can try to limit it to 1.000.000 Pounds (if that is a reasonable amount) and obtain insurance for it. Bainbridge (2008) says that is a common used amount in computing contracts.

Because we know that ATS may develops expert systems and any harm is done to a human because of a malfunction of our software (underlying the ATS expert system) we could get sued if they proof our negligence and there is enough proximity.

Bainbridge (2008) also says that it would be a good idea to allocate risks of the project together and obtain an insurance to cover possible losses.

In the SW maintenance contract we should provide ATS with error correcting updates for the software to avoid breaches of quality warranties. (Saphena Computing Ltd v Allied Collection Agencies Ltd [1995] FSR 616)

Furthermore we can set up a disclaimer and ensure that ATS is aware of any limitations in liability.

According to Bainbridge (2008) an arbitration or alternative dispute resolution (ADR) clauses should be included.

5. Bibliography and References

Bainbridge, D. (2008) Introduction to Information Technology Law, Pearson Education Limited: Harlow

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6. List of Supporting Cases

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