Technology update

MOORE BLATCH
solicitors

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Welcome to the latest edition of the technology update which aims to provide you with up-to-date information about issues affecting businesses in the technology sector.

In this edition we discuss liability for design problems caused by following defective international standards.

We look at two recent court of appeal decisions one concerning claims for compensation under the Data Protection Act 1998 the other concerning a shareholder and director who was excluded from the business he ran with two other shareholders.

We also give an update on the UK Intellectual Property Office's new Design Opinions Service.

If you have any comments or suggestions for topics that you would like to see in future editions, please contact me on 023 8071 8078.

Kind regards

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Who is liable for a defective standard in a technology contract - client or contractor?

Who bears the risk of an industry standard being defective, leading to remedial works? Businesses engaged in the IT and Technology sectors should take note of a recent Court decision which, although relating to a construction dispute, is also likely to be relevant to complex IT/software development projects, as it is quite common for Technology development agreements to include both legal terms as well as technical specifications and standards.

The Court of Appeal (CA) overturned the trial judge's decision in MT Hojgaard A/S v E.On Climate and Renewables and decided that a contractor was not liable for the design problems of an oil rig's foundations due to the international standard it was following having a defect. The remedial costs were over €20m and the CA's decision meant that the client was responsible for such costs rather than the contractor.

Background

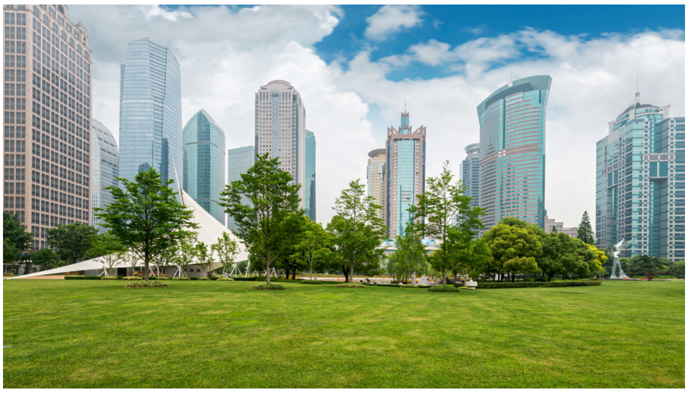
MT Højgaard (the contractor) designed and built an offshore wind farm for E.On in accordance with certain international standards without negligence. Unfortunately, the international standard was defective which required significant remedial work to the foundations.

The construction contract required the contractor to complete the Works:

- "with due care and diligence expected of appropriately qualified and experienced designers….
- in a professional manner…..in accordance with……Good Industry Practice……
- so that the Works, when completed, comply with the requirements of the Agreement
- so that each item of…the Works as a whole shall be fit for its purpose as determined in accordance with the Specification using Good Industry Practice…"
- the technical specification stated that "the design of the foundations shall ensure a lifetime of 20 years in every aspect without planned replacement…."

Decision of the CA

The CA allowed the contractor's appeal against being liable for the huge remedial costs on the basis that:



- in this case the contract did not require the contractor to achieve a "service life" of 20 years;
- most references in the contract were for the contractor to deliver a "design life" of 20 years and the CA felt that the distinction between "design life" and "service life" was significant;
- the obligations in the contract did not impose an absolute obligation of quality on the contractor when interpreted correctly;
- the contractual references to the foundations needing to be "fit for purpose" referred to matters such as "Good Industry Practice" and using "reasonable skill and care" – this was not consistent with the argument that the contractor had promised to deliver foundations that could last 20 years (which would amount to a warranty).

As a result of this reasoning, the CA concluded that neither the contract nor the technical standards imposed an absolute obligation on the contractor to guarantee the foundations for 20 years – such an obligation would have required an express warranty, which was lacking.

Commentary

In applying the Court's approach to the IT and Technology sectors, the following lessons should be remembered:

1. ultimately, whether a contractor has an absolute legal obligation to deliver a particular deliverable even if a relevant standard/specification is defective will depend on the specific language used;
2. where the IT developer is employed to create a technical specification it will be legally liable if the specification is defective due to its negligence or poor performance;
3. however, when the contractor is not at fault, a clear distinction must be drawn between those obligations which are absolute which a contractor must comply with as opposed to those obligations where it must exercise "reasonable skill and care" – in the latter case, a contractor will not be liable for failing to deliver a deliverable provided that it has complied with its contractual obligations and not been negligent;
4. if some form of absolute obligation (ie warranty) to deliver is required by the client, it should be stated expressly as the court may well be reluctant to imply or uphold one if such wording is not present; similarly, contractors should seriously consider stating expressly that they will not be responsible for any deficiencies in specifications/standards they are working to so that they are not liable for any remedial actions/costs;
5. where there is more than one contractual document to consider, it would also assist interpreting the underlying obligations if a clear hierarchy between the competing documents is set out;
6. in many technology projects the contractor's risks are limited by ensuring that both parties sign off the technical specifications as agreed contractually in which case the contractor will only run the risk of a specification being defective if it has been negligent in drawing it up.

John Warchus, Partner

Stack V Ajar - Tech Ltd

Ajar–Tech had been formed in 2005 to supply audio – visual equipment by 3 individuals, Mr Martin, Mr Keane and Mr Stack. Mr Martin had experience in marketing 360° cameras, Mr Keane was a financial adviser who introduced Mr Martin to Mr Stack, who was experienced in running a business and was looking for a project to invest in.

Mr Martin, Mr Keane and Mr Stack were all appointed directors and had broadly equal shareholdings. Mr Martin was employed by the company and was paid a salary under PAYE. Mr Keane did not work for the company. Mr Stack did work for the company but it was not a formal arrangement, he did not have a contract and he did not receive a salary. The understanding was that he would receive payment for his services at the same level as Mr Martin, backdated to when he began working, once the company was able to afford to pay him.

In 2009 Mr Martin and Mr Keane decided to exclude Mr Stack from the business.

Mr Stack claimed that he was an employee and had been unfairly dismissed and the matter finally came before the Court of Appeal.

The somewhat surprising conclusion was that despite the fact that Mr Stack did not have any formal contract of employment with the company and had not been paid, he was nonetheless an employee, on the basis that he had been under an obligation to work for the company and to carry out the work personally and that he had done so in the expectation of receiving payment.

Mr Stack presumably pursued the claim that he was an employee for tactical reasons. The claim that he was an employee was dealt with in the employment tribunal where there are very rarely any adverse costs orders made, so he was at much less risk, if he lost the case, of having to pay his opponents costs. If he succeeded, he would be entitled to a significant amount of back pay.

An alternative would be to claim that his exclusion from the business had unfairly prejudiced his rights as a shareholder and to seek a "buyout" at a fair price.

Ajar–Tech appears to have been what is known as a quasi-partnership company on the basis that there had been a relationship of mutual trust and confidence between the 3 shareholders when they started out in business together and Mr Stack clearly had an expectation of being involved in the management of the company.

As Mr Stack was excluded from the business by Mr Martin and Mr Keane, he would, on the face of it have good grounds to petition the court that his rights as a shareholder had been unfairly prejudiced on the basis that being excluded from a quasi-partnership is accepted as being unfairly prejudicial conduct; alternatively he could petition for a just and equitable winding up of the company.

These claims are still open to him but, having succeeded in establishing that he was an employee has probably put him in a strong position to settle all his claims, including his claims as a shareholder.

Paul Whitaker, Partner

New approach to compensation claims for breaches of the data protection act 1998

The Court of Appeal has recently reversed a decade of caselaw during which it has been difficult to bring successful claims for compensation under the Data Protection Act 1998: from now on, barring any successful appeal, claims can be made for distress caused by a breach of the Act even though no financial loss has been suffered.

Until the decision in Google Inc. v Vidal-Hall, the English Courts had interpreted Clause 13 as meaning that compensation was only available where a Claimant had suffered some sort of financial loss and this had the consequence that most breaches of the Act (which relate to emotional distress) could not be the subject of a claim, as there was no financial loss suffered.

That has all changed: in an eye-catching ruling, the CA have decided that Clause 13(2) of the Act is legally invalid on the basis that it is incompatible with Articles 7 and 8 of the EU Charter of Fundamental Rights (protecting the right to family life and the protection of personal data). In reaching its decision, the CA decided that statements by the CA in an earlier case were not binding on them and, looking at the express wording of the EU Data Protection Directive which the UK implemented by the Data Protection Act, there was no justification for the distinction in Clause 13 between financial loss and non-financial loss. Indeed, the CA referred to the broad aims and background of the Directive which was to protect personal privacy – against this legislative background, the CA felt that it was irrational to draw a distinction between financial and non-financial loss, particularly as it is the latter which is the more likely result of a breach.

The decision is likely to have a number of potentially wide-ranging implications, including:

- the likelihood that there will be more claims for compensation under Clause 13 now that there is no requirement to show financial loss;
- although the CA commented that it was likely that individual awards of compensation would be relatively modest (so far they have been in the low thousands of pounds), there could be a growth of class actions in which a large number of individuals have suffered emotional distress or invasion of privacy, leading to larger overall damages awards;
- data Controllers will have an even stronger incentive to comply with data protection rules on the basis that they could be faced with costly class actions;
- the CA's decision is also consistent with the likely future trend of data protection legislation – the draft EU Data Protection Regulation (which is likely to come into force in the next couple of years) expressly states that there should be no distinction between compensation for financial loss or non-financial loss.

John Warchus, Partner

New design opinions service to help resolve disputes

The UK Intellectual Property Office (IPO) is hoping to introduce a new Design Opinions Service.

The new service will provide non-binding opinions on questions relating to registered and unregistered designs. There will be a fee of around £200. The service will be similar to the Patent Opinions Service introduced by the IPO in 2006.

Opinions issued by the service will focus on:

1. Whether a design is being infringed or potentially infringed;
2. Whether a design is valid;
3. Whether design right subsists in a particular design;
4. The duration of any unregistered design right.

The service aims to enable those with limited funds, such as small businesses, to make an informed decision on how to use and enforce their design rights and how to avoid infringing the rights of others, without the need for litigation. Where litigation is required it is hoped the opinions issued will help parties focus on the real issues, thus reducing time and cost.

A consultation on the service closed on 15 May 2015 and the IPO is currently analysing the feedback received. A summary of the responses is expected to be published shortly, and the final rules will be laid before Parliament. The IPO hope to have the service in place by October 2015.

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