Computer Litigation: Tactics and Remedies

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The computerisation of business has led to an increase in information technology related disputes, relating to matters such as business functionality, performance and adequacy of systems. In general, lawyers and the Courts are not comfortable or familiar with the subject matter of such disputes. This article examines how IT disputes fit into the traditional characteristics of a litigious environment and provides some suggestions about strategies to be adopted in IT litigation.

PARTIES TO AN IT DISPUTE

There are two distinct groups who will most likely end up in an IT dispute.

Firstly, there is the IT vendor and the inexperienced purchaser. Disputes between these parties are characterised by businesses with little experience in IT development, manufacturing or services, purchasing a product or suite of products to increase efficiency and productivity. The inexperienced purchaser relies heavily on the expertise and experience of the IT vendor to define the products and services which will satisfy the purchaser's requirements and objectives. In these "one-off" transactions there is often no previous commercial history between the parties.

The seeds of such disputes are often in the negotiation for the purchase of products and services. Issues that may show up later down the litigation pathway will include:

> the alleged failure of the IT vendor to understand the business of the purchaser;
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> representations about whether the vendor's products could be adapted (if they ever could) to the purchaser's business;
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> the extent to which the purchaser did rely or ought to have been reasonably expected to rely on its own, or the IT vendor's, skills and experience in identifying whether the product in dispute was the correct product for the required purpose;
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> failure to communicate required functionality and performance requirements to the IT vendor in clear and unambiguous terms, leading to a common misunderstanding of the purpose for which the products were to be used.

The second group of likely litigants is the IT vendor and IT purchaser. Both parties are sophisticated in terms of their understanding of the dynamics of the IT market and will usually have products or services which purportedly complement each other. Disputes between these parties often revolve around the failure of the parties to understand their own and the other parties products. Sales and purchasing officers may conclude a deal based upon inadequate or assumed knowledge of the technical aspects of the products which they wish to sell or purchase. With ever changing upgrades and releases of new versions of hardware and software, minor misunderstandings as to the ability of a product to perform at a specified level can flow through to become a showstopper event for the end user.

Another situation likely to be a feature of litigation between experienced IT vendors/purchasers is the knowledge levels (or the lack thereof) of persons purporting to conduct development of hardware and software applications. A dispute will often result when a party represents it has skill levels to conduct certain work when it doesn't.

PLEADINGS/CAUSES OF ACTION

Defining the nature of the relevant IT dispute is a difficult task. Drafting pleadings in an IT dispute involves taking detailed instructions to identify the real complaint. It can be difficult to identify relevant malfunctions. The complainant has an obligation to inform the defendant of the precise nature of the complaint. A complainant may need to retain experts at the commencement of the proceedings to identify the precise problems with a product. Such action may be warranted to prevent a defendant striking out those parts of a claim which are imprecise.

If there is a contract, an allegation of breach will generally be at least one cause of action. It is common to also incorporate the use of "implied terms" into a contractual dispute. By way of example, the complainant may plead that it was an implied term of the contract that an IT vendor would do everything that was reasonably necessarily to ensure that the product which the purchaser has received under the contract will not be diminished in value in an way or that the products were fit for purpose.

Often there are no terms in the contract dealing with such matters such as acceptance testing. In these cases, the complainant will need to "construct" a contract, which may be a combination of correspondence, invoices and discussions. The difficulty here is identifying which pieces of evidence are relevant to defining the terms of the contract.

As most IT contracts limit matters such as damages, consequential losses and the like, complainants will usually resort to claims under the Trade Practices Act 1974. The most popular provisions in this regard are Sections 51A, 52 and 53 of the Act. The types of actions that will be pleaded under these provisions are:

that a representation was made as to future conduct (eg. as to the capacity of a computer system) which was not reasonable when it was made. This cause of action is available under section 51A. The advantage of this cause of action is that the onus of showing that the representation was reasonable shifts to the party who is alleged to have made the representation;

a claim that conduct was misleading or deceptive under section 52. It is rare to see a pleading involving commercial matters (whether related to the computer industry or not) which does not have a section 52 pleading in it in the modern era;

false representations in relation to the supply of products and services relating to matters such as the performance characteristics of the services. Various causes of action are available under section 53.

In its pleading, a claimant may characterise the dispute in a manner wholly inconsistent with the defendant's recollection or interpretation of events. The defendant may respond to the complainant generally admitting, not admitting or denying the allegations made. Alternatively, the defendant may seek to characterise the dispute in its own terms, pleading what is known as a positive defence.

Positive defences can be particularly useful in IT disputes. For example, the common saying in the IT community that a software bug is in fact a "feature", reflecting the industry experience that no piece of software is immune from being corrupted, should be kept in mind when drafting defences. The acknowledgment in a positive defence of matters such as this may well serve to narrow the issues so as to identify the real nature of the dispute. It is also important for any defendant in an IT case who is prepared to admit matters that may seem to be controversial to lead evidence demonstrating that such admissions are not in fact general admissions of liability, if such matters are a standard industry occurrence or practice.

A useful aid that can be used in IT pleadings is a Scott Schedule type document summarising the precise failures alleged. Such a schedule may allow the court to understand the matters which are said to be deficient, which otherwise may become lost amongst voluminous pleadings and particulars.

DISCOVERY

Discovery, unless properly handled can and often does lead to the costly and time wasting production of voluminous amounts of irrelevant documents. Nowhere is this more the case than in IT disputes. The categories of documents may need to be discovered in IT disputes will include:

(a) contract documents;

(b) pre and post contractual correspondence between the parties (including letters, facsimiles and e-mails)

(c) timesheet (usually kept by the persons providing services);

(d) customer call logs;

(e) systems specifications set out in reports (including user requirements, functional specification and technical design and associated plans and notes);

(f) correspondence and reports generated through dealings with third party contractors;

(g) file notes, memoranda and internal and external e-mails;

(h) the equipment the subject of the dispute, including hardware and software (if possible).

In many organisations, e-mail has replaced the use of letters and facsimiles as a communications tool. E-mail is not always printed to hard copy and filed as a business record. E-mail, like other computer documents, is subject to deletion at the simple press of a button. Once a dispute arises with a party, instructions should be sent to all employees concerned, to retain all e-mail and print hard copies, if that has not already been done. In many cases, even if an employee has deleted e-mail, the system will be backed up by tape which will contain a record of all e-mail. Such e-mails can then be recovered and discovered.

LAY STATEMENTS

Evidence adduced by parties in IT litigation generally extends beyond the traditional annexing of correspondence. If a system or product is no longer intact, evidence will need to be adduced from officers of the parties as to their recollection, whether by way of contemporaneous documents or not, of the nature of the deficiencies (or lack thereof) associated with that product.

Defining in the traditional statement form the nature of problems with IT equipment can be difficult, in particular given the terminology used in the industry. If a Court (and one must assume Courts to be inexperienced) is to understand the nature of the dispute, the lawyer will act in an interpretative role identifying those areas which must be explained in plain English to make sense of a matter.

EXPERTS STATEMENTS

Technical issues in IT disputes will be resolved upon the acceptance of the best expert evidence available. Appropriate independent experts should be retained at the commencement of proceedings. Experts will need to review lay evidence, discovered material and if possible, the actual products themselves (if they remain intact). The assumptions that an expert works with must be supportable and unimpeachable.

It is important that the chosen expert have particular qualifications in the field which is the subject of the proceedings. Even if an expert produces a fine report, challenges

may be made on the basis of the expert's curriculum vitae as to his/her basis for reaching the conclusions in the report if the relevant experience is not there. Anticipating the quality of an opponent's experts will be useful in determining the appropriate expert to present your client's case.

Using experts who have had previous court experience is preferable. Whilst some experts may have written clarity, such experts may (like many lawyers) be unable to maintain that clarity under cross examination.

DAMAGES

The general remedy for breach of contract is to put a party who has suffered damage as a result of the breach in the position it would have been had the contract been performed. The amount of damage will be determined by taking into account whether the defendant or a reasonable person in its position would have realised that such damages were likely to result from the breach.

In *Alexander v Cambridge Credit Corporation Limited* (1987) 9 NSWLR 310 McHugh JA (as he then was) commented that parties need not contemplate the degree or extent of the loss or damage suffered by the Plaintiff, nor the fact that the parties need contemplate the precise details of the events that give rise to such loss. His Honour found that it was sufficient that the parties contemplate the kind or type of loss or damage which had been suffered.

The types of damage which may be recoverable in a breach of contract may include:

(a) loss of profits which would have been made if the products had worked as required;

(b) loss in value of products purchased;

(c) replacement costs;

(d) loss of consequential income that would have been earned if the products operated as required;

(e) mitigation costs.

The type of loss recovered will depend on the particular circumstances of the case. In some cases a party will need to elect whether reliance losses or expectation losses will be pursued.

Under the *Trade Practices Act* damages are generally assessed on a tort basis. The object of damages under Section 82 and in tort is to place the Plaintiff in the position which it would have been had the conduct or tort not been committed. However, the Plaintiff may recover for loss of opportunity if it can show that, had it not relied on the misleading representation or conduct, it *could* and *would* have entered into an alternative contract which would have generated profits. This concept was considered by the High Court in *Gates v City Mutual Life Assurance Society Limited* (1986) 160 CLR 1 at 13.

The High Court case of *Poseidon Limited v Adelaide Petroleum NL and Ors* (1994) 68 ALJR 313 has qualified some of the matters raised in Gates' case. In Poseidon the High Court found that in assessing damages for lost opportunity, the Court must assess the value of that opportunity by reference to the degree of probabilities or possibilities of that opportunity. In Poseidon there was evidence before the Court that the Plaintiff would have entered into an alternative agreement but for reliance upon the Defendant's statements. Where damages are sought by an IT Purchaser, evidence may be adduced of the various responses to the tender for services in identifying such an alternative supplier.

It can be seen, therefore, that there still exists and assortment of damages which may be recoverable by the Plaintiff under Section 82 of the Trade Practices Act should the Plaintiff be able to prove in evidence viable alternatives other than the contract entered into with the Defendant. Some damages, such as the costs of replacing deficient hardware and software will not, however, be recoverable and the Plaintiff will only be able to recover the value of the goods purchased from the Defendant (which may in any event be valued at $0.00 therefore allowing the Plaintiff to recover the whole purchase price).

Parties may also seek orders under Section 87 of the Trade Practices Act. Section 87 provides a Court with a statutory discretion to order specific forms of compensation including:

(a) the refund of money or return of property to the person who suffered loss or damage;

(b) an order that payment be made to the person who suffered loss or damage in the amount of that loss or damage;

(c) an order that the contravening party, at its own expense, supply specified services to the party who suffered, or is likely to suffer the loss or damage.

A party who is seeking damages has a duty to mitigate its loss. This is particularly relevant to IT disputes. It is not open to a party who is seeking damages to simply do nothing about repairing defective products if repairs or replacements can easily be made. If a repair or replacement is undertaken, the following ought to be noted:

(a) the party who is alleging the loss ought to carefully document the process by which the repair or replacement takes place. This will include:

keeping correspondence;

keeping accurate records of all testing.

It may be prudent to engage an independent expert to keep those records and provide an opinion prior to the repair or replacement taking place so that this may be relied upon in later proceedings;

(b) if the problem relates to software, keeping a copy of the source code for that software at the relevant time;

(c) if the problem relates to hardware, the replaced product ought to be kept for a later analysis by experts.

The types of damages recoverable in an IT dispute was considered by

Woodward J of the Federal Court of Australia in *Westsub Discounts Pty Limited v Idaps Australia Limited* (1990) 17 IPR 185. Westsub entered into a contract with Idaps for the supply of a computer system to be used in Westsub's video rental business. Idaps agreed to modify an existing software package to meet Westsub's requirements. Difficulties were experienced in implementation of the system and ultimately Westsub chose to replace the system with a new system two and a half years later. Westsub commenced proceedings against Idaps under Section 52 of the Trade Practices Act and for breach of contract. The Court found that although a breach of contract had not been proved, Idaps had contravened Section 52 of the Trade Practices Act. The Court's assessment of damages which Westsub was entitled to provides an interesting review. Outlined below is a list of the damages claimed by Westsub and the basis upon which the Court either allowed or refused the claim:

(a) Costs for third party maintenance support for hardware - The Court found that Westsub's claim for support of hardware costs was recoverable as there was a causal link between the misleading conduct and damage which continued until Westsub could assess the situation and make alternative arrangements with a new systems supplier.

(b) Payments to Idaps for software support and certain miscellaneous hardware were recoverable. The amounts paid by Westsub were done so under compulsion because "Westsub could not allow the system to collapse".

(c) Hardware and borrowing costs of hardware. As there was no evidence before the Court of the then current value of the hardware, the Court found that Westsub should return the hardware to Idaps and Westsub should be refunded the purchase price. The Court allowed borrowing costs as it was foreseeable that Westsub would have to borrow to pay for the equipment.

(d) Telecom charges for the rental of a telecom line used by the computer system to connect an office. The Court allowed this claim on the basis that no break in the causal link had been established.

(e) Staff recruitment for data processing - The Court refused to this on the basis that it was not a charge properly incurred.

(f) Stationery and repairs costs which were incurred due to the Idaps system failing to operate as required. There was no evidence which indicated that the amount for stationary and repairs was thrown away because of the failure of the system. The claim was disallowed (240).

(g) Insurance of the hardware. This claim was allowed (241).

(h) Additional Staff - That amount was calculated by comparing the staff required when the new system was functioning smoothly and the staff in place when the Idaps system was in use. The Court found that under Section 52, Westsub was not entitled to a claim for an additional savings that might have been achieved if the Idaps system had worked as represented. That claim was a contractual claim. It appears that the Court may have reached an alternative conclusion if Westsub had been required to employ additional staff as a result of the failure of the Idaps system.

(i) Loss of profits - There was no evidence to support the claim that at the time of making the representations, Idaps knew Westsub was planning a large expansion in to the Sydney market and would require the computer facilities for that purpose. The claim was disallowed.

(j) Lost opportunity - Westsub claimed an amount for the lost opportunity of entering into an alternative contract for the supply of hardware and software. There was no evidence that Westsub was prepared to spend any more on a system than they did with Idaps and as such refused to make any allowance by way of damage for lost opportunities to invest in a better system.

The ultimate damages award was, as noted by the court, a long way short of the Applicant's exaggerated claim.

Conclusion

Matters such as the Westsub case, clearly illustrate the need for well defined IT contracts between Vendors and purchasers. Contracts which include matters such as acceptance testing and clearly defined obligations for each party can often prevent the parties resorting to litigation based on representations, the truth of which can only be substantiated through a protracted litigation process.

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