Is there a contract?

It is not unusual for work to begin on a contract for the development of software before the precise details of the contract have been properly agreed and formalised. The modern pressures of business life may make it tempting to commence work before the 'legal stuff' has been sorted out but it is a temptation that should be avoided if at all possible. After committing resources or carrying out work, the other party may claim that there is not a contract. Even if it is accepted that there is a binding contract, there may be some uncertainty as to the precise terms of the contract and there is a limit to how much the courts may be willing to imply. Uncertainty itself can be a factor in making a purported contract void and unenforceable.

The case of ***Prudential Holborn Ltd* v *Fraser Williams (Southern) Ltd*** (unreported) 14 May 1993 provides an example of the dangers and difficulties which might ensue if work begins before a contract is properly in place. Fraser Williams submitted a proposal to Prudential to develop software. It was dated 3 March 1989 and was expressed as being 'subject to contract'. Two telephone calls from Prudential on 7 and 9 March 1989 confirmed that the claimant had got the job and a letter was sent on 10 March 1989 confirming this, though the letter showed that there were still some things to be resolved, in particular how responsibilities would be shared between Fraser Williams and an independent consultant engaged by Prudential in respect of the software. On 13 March 1989, at the invitation of Prudential, Fraser Williams commenced work and on 5 April it sent its standard form contract to Prudential. Subsequently, Fraser Williams raised three invoices which were paid by Prudential, but on 5 May 1989 Prudential informed Fraser Williams that it was terminating the relationship and requested that Fraser Williams vacate the defendant's premises immediately. Fraser Williams complained in writing about the alleged breach of contract by Prudential but the correspondence remained unanswered until, on 27 November 1989, Prudential's solicitor wrote to Fraser Williams asserting that there was no contract between them. It was argued that the letter of 10 March 1989 was merely a letter of intent and, even if it were an acceptance, there was still no contract as Fraser Williams' 'offer' was expressed to be subject to contract.

At first instance the judge held that there was a binding contract but the Court of Appeal overturned this on a majority decision. The phrase 'subject to contract' when used by experienced business persons meant more than simply requiring acceptance to be in writing. The standard form contract had not been agreed by Prudential and there remained important matters to be decided such as the boundary between the work to be done by Fraser Williams and the independent consultant. Lord justice Kennedy considered that the letter of 10 March 1989 was no more than an acceptance that, in the light of Fraser Williams proposals, the parties should go a stage further.

It had also been argued that a contract could be implied on the basis of the parties' conduct as in ***Brogden* v *Metropolitan Railway Co*** (1877) 2 App Cas 666 where the conduct of the parties in supplying and paying for coal over a period of time in accordance with a draft contract could only be explained on the basis that they approved of the contract. The present case differed. Although the work commenced at the invitation of Prudential this could be

explained by concluding that the parties expected a formal contract would be agreed. Of course, Fraser Williams was entitled to payment for the goods and services supplied at the invitation of Prudential until 5 May 1989 (on the basis of a quantum meruit, see below).

The dangers inherent in embarking on work without a formal contract in place are fairly obvious. In the above case, if the court had held otherwise, the software developer would have found it difficult to obtain any recompense for the work it carried out. One possibility is under a quantum meruit. Another difficulty is determining the precise nature and scope of the contractual terms. If, eventually, in the above case, an administrative decision was taken assigning responsibility between the software developer and the independent consultant, it could have been detrimental to the software developer. It could, for example, reduce the total job value for the software developer or increase the amount of work to be completed in an already tight timescale. However, where there is some uncertainty as to the precise terms of the contract, the terms implied by the Supply of Goods and Services Act 1982 or common law may save the contract. Otherwise, if there is a previous course of dealing between the parties, that may provide some clue as to the precise scope of the parties' rights and obligations under the contract. The courts will not, however, write the contract for the parties and, as HH judge Richard Seymour QC said in ***Co-operative Group (CWS) Ltd* v *International Computers Ltd*** [2003] EWHC 1 (TCC):

> If satisfied that parties did indeed intend to enter into a binding agreement and sought to do so, it is no part of the function of the court to seek to frustrate that intention. At the same time it is no part of the function of the court to impose upon the parties a contract which they did not, objectively, make for themselves.

In ***DMA Financial Solutions Ltd* v *BaaN UK Ltd*** (unreported) 28 March 2000, BaaN originally provided training to customers of its accounting software. BaaN decided to outsource its training and wanted DMA to take over this role, as BaaN's authorised training provider. Negotiations began between BaaN and DMA for this purpose. Negotiations went well and both sides seemed confident that there would be final agreement. Eventually, BaaN started closing down its training facilities and DMA began recruiting staff to provide training. BaaN passed on training enquiries to DMA but there was still no formal written contract, as BaaN's lawyers were preoccupied with other matters. Eventually, BaaN's lawyers started raising objections about what had been agreed by the negotiators and eventually sent DMA its standard form contract which differed in many respects from what had been agreed. After a number of exchanges, DMA’s position was that a binding contract existed whilst BaaN, which had changed its mind about outsourcing its training, argued that there was not a binding contract.

As to whether the negotiations resulted in a binding contract before a formal written agreement had been executed, Mr justice Park thought that three possibilities existed:

1. The negotiations were not intended to result in a contract even if fully concluded until such time as a written contract had been drawn up and executed by both sides. This was equivalent to the usual practice when negotiating to buy a house where the phrase 'subject to contract' was commonly used.

2. The negotiations were such that a contract could exist before the execution of a formal written contract- the negotiations resulted in complete agreement.
3. As 2 above but the negotiations did not get far enough for there to be sufficient agreement for a contract to exist.

The judge said that there was no evidence to satisfy him that, in the computer software industry, it was the generally understood usage that agreements are never binding until they have been drawn up by the lawyers and signed. In this particular case, the phrase 'subject to contract' had not been used during negotiations. All the main terms were agreed including the price of $250,000, payable in six quarterly instalments. If some point was not raised in negotiations but was not an essential point, that would not prevent a contract coming into existence. An example was the applicable law for the contract. The fact that this had not been raised did not matter as, although it was certain that BaaN's lawyers would insert such a term in the formal written contract, it was highly unlikely that DMA would have complained about it on the basis it had not been previously agreed. Therefore, the judge held that a valid binding agreement existed between the parties.

The fact that there have been extensive negotiations does not, of course, automatically mean that a contract exists. It depends on whether all the terms considered to be important by the parties have been agreed. In ***Co-operative Group (CWS) Ltd* v *International Computers Ltd*** [2003] EWHC l (TCC), the claimant alleged that there was a contract between it and the defendant (ICL). It was true that there had been extensive negotiations between the parties and that both expected that agreement would be reached. However, no agreement as to liquidated damages for late delivery had been agreed, amongst other things. CWS had insisted that liquidated damages were included in the contract but ICL was unwilling to accede. The inclusion of liquidated damages in a contract to write software is usually a very important term and failure to agree this was clearly fatal to the argument that there was a valid binding contract between the parties. Some of the negotiators for CWS had been unhappy about ICL's performance on other projects and the judge said that a malevolent influence hung over the negotiations. As the judge held that there was no binding contract, CWS's claim for repudiatory breach of contract was doomed. CWS had claimed no Jess than £11 m. However, CWS appealed to the Court of Appeal in ***Co-operative Group (CWS) Ltd* v *International Computers Ltd*** [2003] EWCA Civ 1955. A re-trial was ordered as a result of the apparent bias of the judge at first instance. He had made findings of bad faith and false evidence against CWS and its principal witness when no bad faith had been pleaded or suggested. This may have distorted his findings of fact and prejudiced his objectivity. There is no record of any re-trial taking place.

As negotiations for a contract to write a substantial software system can proceed over a long period of time, it is sensible for the parties to make it absolutely clear what their position is. The use of a suspensive phrase such as 'subject to contract' on documents created during negotiations should be considered. As parties to drawn out negotiations can run up considerable expenses, this seems the safest approach so that both know exactly where they stand. In some cases, the negotiations could run alongside a feasibility study or the development of prototype systems, which could be subject to a separate contract. Where the

phrase 'subject to contract' is used, the parties should ensure that a formal contract is drawn up and signed by both of them before work proceeds. Simply sending a written acceptance is not necessarily enough as shown in ***Prudential Holborn* v *Fraser Williams***, above.

Quantum meruit

Where it turns out that there is no valid contract- for example, through a lack of certainty as to the terms of the contract- the software developer may be entitled to payment on the basis of the work he has done in pursuance of what he believed was a valid contract. The law will require that the defendant pays the claimant for the 'fruit of his labour'. This is what is termed a quantum meruit (roughly translated- as much as he deserves). Of course, the defendant must have agreed to or at the very least acquiesced in the claimant carrying out the work. For example, if a software development company is appointed to write some software for a client but the purported contract between them is so vague and uncertain that it is ruled void, then if the software company has done satisfactory work for the client, it ought to be entitled to payment on the basis of a quantum meruit. Nevertheless, it is clearly preferable to have a valid and detailed contract containing all the necessary terms in writing and signed by both parties before the work commences. Writing computer software is sufficiently difficult and unpredictable without adding to the problems by having unsatisfactory legal provision for the work. An example of a software development company being entitled to a quantum meruit is the case of ***Prudential Holborn Ltd* v *Fraser Williams (Southern) Ltd***, above.

Questions:

1. What does 'subject to contract' actually mean?
2. What conditions are necessary for negotiations to result in a binding contract?
3. Explain what is a quantum meruit?

References:

Introduction to Information Technology Law (6th Edition), David Bainbridge. Chapter 15, Contracts for writing software.