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TMT Technology claim scenarios

Failed software implementation extra-contractual claims dismissed under economic loss doctrine – contract sums refunded in settlement

Factual background

A large international manufacturing firm entered into a software license and service agreement with a software company for enterprise resource planning software, including financial, manufacturing and distribution modules. After the customer installed and implemented the software, it was dissatisfied with the performance of the software on its hardware platform and ceased paying the software company under the service agreement.

Incident response

The software company offered to migrate the customer's software system to a different hardware platform - one that would have improved the software's performance. However, that offer was contingent on the customer paying any amounts outstanding under the service agreement which the customer refused to do.

Litigation / enforcement proceedings

The customer sued the software company and alleged not only breach of contract but also a number of quasi-contract and tort claims including: 1) promissory estoppel; 2) fraud; 3) unjust enrichment; 4) violation of state deceptive trade practices act; 5) theft by deception; 6) conversion and 7) punitive damages. The software company asserted various defenses and counterclaimed for breach of contract and copyright infringement (arising out of the customer's ongoing use of the software after termination of the software license and service agreement).

Outcome

The court either dismissed or entered summary judgment in favor of the software company on all of the customer's claims except its breach of contract claim. Specifically, the court upheld the software license's limitation of liability and remedy clauses thereby defeating the customer's claims that the contract was unconscionable and failed of its essential purpose. Following the court's determination that the only issue left in dispute was whether the software company had breached the software license, the parties reached a settlement for $1.7 million which was approximately what the customer had paid under software license.

Failed software implementation – Court dismisses all but breach of contract claim – Software company wins summary judgment on contract claim but defense costs high

Factual background

An international manufacturing firm contracted with three separate technology companies for different aspects of an enterprise-wide software implementation. It entered software licenses with two of the companies for software components of the system. The firm contracted with the third software developer to provide hardware and implementation services for the project. The firm claimed the system did not perform satisfactorily.

Incident response

The developers attempted to resolve the firm's issues which centered upon complaints that the main software components licensed were not interoperable. The technology companies had customized the software at the firm's request, but the firm alleged that those modifications impaired the software's functionality and performance. The firm terminated the implementation before completion of the project, claiming the software still was not operational.

Litigation / enforcement proceedings

The firm initiated a federal lawsuit against all three technology companies and alleged claims for: (1) fraud and fraudulent inducement; (2) negligent misrepresentation; (3) breach of implied warranty for services; (4) breach of express pre-contractual warranty; (5) breach of contract; and (6) violation of a state deceptive trade practices statute; and (7) joint and several liability on a theory of joint venture or partnership-by-estoppel. One of the technology companies settled with the firm shortly after the complaint was filed and was dismissed from the suit.

Outcome

Upon motions to dismiss by the technology companies, the court dismissed every claim but the firm's claims for breach of contract and partnership-by-estoppel claims. The court found that the firm's fraud, fraudulent inducement, deceptive trade practices and negligent misrepresentation claims were barred by the economic loss doctrine. The court further found that the contracts' integration clauses and conspicuous disclaimers of warranty effectively barred the pre-contractual warranty claims.

After substantial discovery, the technology companies moved for and were granted summary judgment on the remaining breach of contract claim. The court found that the firm had failed to provide evidence of any defects in the software that fell within matters expressly warranted under the product specifications pursuant to the licensing agreements. The court also found that the developers' conduct did not create joint liability through a partnership-by-estoppel theory. The firm's appeal seeking reversal of the judgment is pending.

Although the technology companies were successful at the trial court level, defense costs were estimated to exceed $4 million dollars. Software system implementations are typically labor intensive projects. Consequently, among other things contributing to high defense costs were the significant number of depositions that needed to be taken and the extensive volume of electronic mail and documents that needed to be reviewed.

Copyright infringement claim – Use of software after expiration of license

Factual background

A software company developed enterprise performance management (EPM) software that allowed customers to analyze the performance of many aspects of their business. Embedded within the EPM product was an Extract Translate and Load (ETL) software tool that the software company had licensed from a third-party software developer. The ETL tool would extract data from various application databases and load it into a data warehouse where it could be analyzed by the EPM product. The ETL tool would locate the data to be extracted by following "data maps" that, although developed by the software company, were saved in a format proprietary to the third-party developer. At some point, the software company decided to replace the ETL tool with what it believed to be a more robust tool developed by one of the third-party developer's competitors. Unfortunately, the software company was unable to migrate all of its customers to software incorporating the new tool before its license to use the original ETL tool expired. The third-party developer claimed that the software company was infringing its copyright in the ETL tool because, in the process of migrating its customers, the software company had to open and use the ETL tool to convert the data maps to a nonproprietary format. The third-party developer also claimed that the software company had improperly disparaged its ETL product when the software company announced to the public its decision to switch to the new tool and breached its confidentiality agreement by giving the third-party developer's competitor access to its proprietary software.

Incident response

The software company and the third-party developer disagreed over the interpretation of the license agreement and whether the software company's post-expiration use of the ETL tool was permissible. The software company attempted to use a neutral consultant to assist it with the customer migrations so as to insulate the third-party developer's competitor from access to the third-party developer's software.

Litigation / enforcement proceedings

The third-party developer sued the software company alleging breach of the license agreement, copyright infringement as a result of the post-license use of the ETL tool and unfair competition on account of the allegedly disparaging comments about the capabilities of the ETL tool. The software company alleged that its use of the ETL tool was permissible fair use because it used the tool only to obtain access to unprotected information.

Outcome

The software company settled the lawsuit by paying the third-party developer approximately $400,000 and offering it other business considerations. The software company estimated the total cost of the incident, including defense costs, to be approximately $1.5 million.

Network failure – Breach of contract claim with an arbitration award of consequential damages within contractual damages cap

Factual background

A major oil company and operator of 10,000 gas stations contracted with a credit card processing company to provide the technology for its point of sale system. The gas stations would rely on the system for credit card authorization and settlement services. As a result of a hardware malfunction, the processing company's network went down for six hours causing the point of sale systems in the pumps to be inoperable. The stations posted signs on their pumps inviting customers to have their transactions processed manually inside the station, but many customers drove away upon seeing the signs. The contract contained a cap on consequential damages of $10 million.

Incident response

The oil company claimed that, on average, lost 20 sales per station during the network outage at an average gas purchase of $30. It therefore claimed a total loss of $6 million. The processing company argued that the gas station could have processed the transactions manually at the pump and that, in any event, the oil company's alleged damages were too speculative.

Litigation / enforcement proceedings

The oil company filed for arbitration and asserted breach of contract and breach of warranty claims. The processing company asserted the contract's force majeure clause and challenged the oil company's damage claims.

Outcome

A three-person arbitration panel awarded the oil company $4 million in damages based on the breach of contract claim.

Failed software implementation – Court rejects extra-contractual claims – Claims settle for amounts customer paid for license fees and consulting services

Factual background

An international manufacturing firm entered into a software license and service agreement with a major software developer for enterprise resource planning software, including production planning, order promising, and enterprise planning modules. After the software developer installed the software system and assisted with its implementation, the firm was able to "go live" on the software but was never able to achieve the functionality it believed it had been promised by the software developer. Ultimately, the firm cancelled the project and licensed software from another developer.

Incident response

The firm and the software developer both made unsuccessful attempts to resolve functionality issues. The parties disagreed as to who bore responsibility for the problems.

Litigation / enforcement proceedings

The firm sued the software developer in a Pennsylvania state court and alleged claims for: 1) breach of contract; 2) unjust enrichment; 3) misrepresentation; and 4) professional malpractice. Software developer answered, asserted defenses and counterclaimed for breach of contract and quantum meruit (arising out of the manufacturing firm's failure to pay all licensing and consulting fees). The firm later sought to amend its complaint to add claims for fraud and negligent misrepresentation, but the court denied it leave to do so.

Outcome

The software developer challenged the firm's claim for malpractice based on an alleged breach of a software consultancy agreement. The court held that while it would allow the count for professional malpractice to go forward, should the firm fail to support the claim through discovery, the software developer would be entitled to its attorneys' fees to defend the count. Consequently, the firm did not pursue the professional malpractice claim.

The court also denied the software developer's motion for summary judgment but implied that the firm's tort claims would not survive at trial when it denied discovery on punitive damages because this "was a contract case."

Although the case settled shortly before trial for approximately what the customer had paid the software developer for license fees and consulting services, the court intimated that plaintiff's misrepresentation claims would have been denied either under the economic loss doctrine, the operation of the merger clause in the contract, or the "gist of the action" doctrine, a doctrine unique to Pennsylvania law that would have barred misrepresentation claims related to the performance of a contract.

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