Legal Updates & News

Bulletins

The BSkyB and EDS litigation: The Lies, The Costs and the Dog with the MBA

January 2010

by Alan Owens, Alistair Maughan

Related Practices:

- Litigation
- Sourcing
- Technology Transactions

The BSkyB and EDS litigation: The Lies, The Costs and the Dog with the MBA

A long-awaited judgment by an English court could have significant implications for the IT industry, both in the United Kingdom and globally. It also shows where to go if you want to get your dog an MBA.

In finding that the initial sales process which led to a significant IT services contract involved elements of deceit, the court opened up the service provider to a huge damages exposure, way beyond the value of the contract. In the future, customers of unsuccessful IT projects may be encouraged to seek similar remedies – and IT service providers on projects partly or wholly delivered in the UK will be wary of conduct which might lead to similar massive liabilities.

On 26 January 2010 – and after a wait of 18 months since the trial ended – the English High Court has finally ruled on the complex, long-running dispute arising out of an IT services contract between satellite broadcaster BSkyB and global IT contractor EDS (which is now part of HP). In addition to "ordinary" breaches of contract by EDS, the Court found EDS liable for a deceitful misrepresentation which induced BSkyB to contract with it, exposing EDS to potentially unlimited liability. Damages claimed were originally over £700 million (US$1 billion) although more recent estimates suggest that the figure may be closer to a minimum of £200 million (US$325 million).

The case, the first IT dispute in the UK in which deceit of this sort has been established, has potentially wide-ranging consequences for the IT and outsourcing services industry in the UK – although the effects could well be felt globally if the large multinational service providers react by adjusting their approach to the contract sales process across their entire operation. In particular, the case will affect the way in which service providers take their services to market and run bids, addressing as it does the circumstances in which: (a) a service provider can be held to account for its pre-contract sales pitches; and (b) service providers can rely on, or customers overturn, contractual limitation of liability clauses.

Background

The dispute originated in 2000 when EDS won a £48 million contract to provide BSkyB with a new customer relationship management (CRM) system. Unfortunately, the project soon ran into trouble and, in 2002, BSkyB brought a claim against EDS alleging that, during the tender stage, EDS had misrepresented its ability to deliver the project. BSkyB said that, were it not for EDS's misrepresentation, BSkyB would have awarded the contract to PwC instead of EDS. EDS countered by arguing that BSkyB had no clear idea of what it wanted from the project and had continually altered its requirements, resulting in delays and other problems (all of which are completely standard defences in claims under IT contracts).

BSkyB claimed damages of over £700 million, an amount far in excess of the maximum exposure that EDS might have contemplated on entering the contract. While the contract capped EDS's liability at a maximum of £30 million, BSkyB alleged that the misrepresentations made by EDS were deceitful (as EDS had made the representations knowing they were false or at least being reckless as to their truth) and, as a result, the contractual liability cap did not apply.

Although the court rejected certain of BSkyB's allegations of misrepresentation (including as to EDS's costing

of the project and capability), it found that EDS was deceitful, firstly, when it claimed that it had carried out a proper analysis of the time needed to complete the initial delivery and go-live and, secondly, when it claimed that it held (on reasonable grounds) the opinion that it could and would deliver the project within the promised timescales. The court found that these representations were made dishonestly by EDS's CRM Manager, who knew that there had not been the "proper analysis" and that there weren't "reasonable grounds" for the opinion that the work would be completed on time but who nonetheless made the claims.

BSkyB successfully proved that EDS breached the contract – and the court held in its favour in relation to contract damages up to the liability cap. It also proved that liability for negligent misrepresentations outside the contract were not properly excluded by the contract, but those again were subject to the liability cap.

Key to this case though is the fact that BSkyB successfully proved one deceitful pre-contract misrepresentation by EDS and it is that which blew away the contract liability cap, which everybody agreed could not apply when lies were told.

It's also important that proof of pre-contract deceit rendered redundant (for the purpose of that particular head of claim, at least) issues as to whether BSkyB had brought the project failure upon itself by not delivering on its obligations or by changing its requirements.

The case itself is notable for the fact that judgment came in 2010, 10 years after the original contract. The trial lasted for 110 days, involved 500,000 documents and 70 witnesses. Even the judgment is almost 500 pages and 2,500 paragraphs long. Legal fees are estimated at over £70 million. And, of course, with so much riding on the outcome, an appeal is likely. It illustrates why disputes in big technology contracts/projects rarely come to trial but, when they do, the issues can be very complex to deal with.

Key Implications

While the size of BSkyB's claim may have grabbed the headlines, it is the finding of deceit that will have the most far-reaching impact and may force changes to the IT services market. In an industry in which sales have always been the yardstick of success, where promises are made to clinch a deal and then worried about afterwards, in which the concept of "time" has always been taken with a pinch of salt and delays on both sides treated as the norm (and sometimes even relied on), the threat of potentially unlimited liability may force greater bid scrutiny. In particular:

- Service providers may:
    - need to become more circumspect in order to avoid the risk of misleading their customers. Sales teams will need to ensure that they do not make hasty or ill-considered promises that could sow the seeds of a future deceit claim and will need to ensure that they can deliver on promises going forward. This could result in bids becoming more cautious and considered than may have been the case to-date and may also slow the bid process to ensure complete alignment between sales and delivery teams;
    - want legal teams to audit the sales process much more closely than has previously been the case, especially on particularly large or vulnerable projects. "Vulnerable" projects are likely to include any project which touches on a customer's revenue-generating functions and which – like the BSkyB CRM system – could have huge implications on a customer's future success if it is not delivered;
    - insist on fuller documentation detailing each promise made and the timescales for fulfilment of those promises during the sales process to ensure that all potential risks are mitigated and the potential liability is made subject to any agreed cap;
    - make sure that the "entire agreement" clause in the contract works: the court in this case held that that particular clause in the BSkyB/EDS contract did not operate to exclude negligent misrepresentation;
    - become more reluctant to take on difficult or complex projects, where the risk of failure (and, therefore, exposure to damages) is higher than normal or, if they do take on such projects, will raise their prices to reflect that increased risk which, in both cases, could slow innovation;
    - be more honest and up-front with customers about delivery problems. Evidence in the case showed that, even in the early days of delivery, EDS was externally assuring BSkyB that everything was on-track while, internally, producing notes and memos attesting to rising panic and concern at the undeliverability of the project;
    - consider limiting the number of individuals with authority to make statements during the bid process in order to reduce exposure and ensure that any individual with such authority has

been through the full range of background checks to avoid rogue employees (*e.g.*, to avoid being in EDS's position and seeing a key employee's integrity destroyed – as happened when EDS's key witness was shown to have perjured himself by lying about having received an MBA from a "University" which awarded the same MBA (but with slightly better grades) to Lulu, a dog belonging to BSkyB's lead counsel in the case).

- On the other hand, Customers may:
    - be more inclined to allege deceit against service providers (which to-date have been difficult to prove and rarely successful), not least because such claims may allow customers to by-pass liability caps that would otherwise limit the amount of damages they can claim for;
    - be encouraged to push the boundaries in their claims by seeking to recover damages for financial losses (such as loss of cost savings and loss of profits) that are usually excluded by liability caps;
    - start to exercise more diligence when conducting tenders, including by asking their service providers to provide firm evidence to support statements made in tender responses, including particularly dates for delivery. As such, service providers may need to work harder to justify their sales claims;
    - document more fully the down-selection process so that decisions can be linked to specific service provider representations and show reliance on those representations. Remember that it was an important part of the case that, but for the deceitful statements, the contract would have gone to PwC not EDS.

- As a result, both parties to a proposed contract should:
    - conduct detailed pre-submission reviews of bids to ensure that all representations and assurances are detailed in the contract and, if not, are fully excluded;
    - conduct due diligence on all such representations and assurances to ensure that delivery is in fact achievable prior to final bids being submitted;
    - ensure that service provider and customer bid teams are closely aligned at all stages of the process to ensure that sales and delivery expectations are met on both sides and that the right people are on the teams;
    - consider whether or not English law is the right jurisdiction for the contract and whether a court is the right forum for a dispute to be heard, rather than arbitration, which could offer a more private resolution to a dispute without the associated reputational damage associated with public findings of dishonesty;
    - spend greater time and resource in the preparation of bids and documentation and engage in more protective restrained behaviour generally throughout the bid-process to ensure that there are no gaps or grey areas from which liability may arise.

A Note of Caution

This case has been long awaited and expectations have built up about it. The result is the one which the IT services industry feared most. Unless overturned on appeal, the case certainly deserves its "landmark" tag. But let's not get carried away by the huge numbers and the Enron-like thrill of a case turning on allegations of dishonesty.

The court hasn't created new law here – it has merely applied existing principles of English law. BSkyB was bold (in pursuing both the "normal" breach of contract claim and the more aggressive deceit claim); lucky (not everyone will have a Perry Mason moment and destroy the credibility of a key witness by proving that he committed sustained perjury); rich (to be able to gamble an estimated £40 million in fees to pursue its claim); and resourceful (to be able to come up with evidence that showed EDS's deceit and that the contract would have gone elsewhere but for that deceit).

Few wronged customers on IT contracts will be in the same boat – although others may try. Most customers will stick to the simpler task of proving a breach of contract – although even that's not easy in a complex IT project with inter-twined responsibilities. It will remain a rare event to go for – and win, as BSkyB has done – the icing on the cake of a liability cap-busting deceit claim.

And, of course, although the court's judgment has now been handed down, it will not be the end of the story, with HP (which now owns EDS) having said already that it will seek permission to appeal which is unsurprising given that it has already invested so much into the case (not least an estimated combined £70

million in legal fees). Another hearing is due in February 2010 to begin the process of assessing the exact amount of damages due.

But, even so, although new law may not have been created, this case does represent a milestone and, in the future, a service provider may be less inclined to put its money where its mouth is if it isn't sure that it's making a safe bet.

© 1998-2008 Morrison & Foerster LLP. All rights reserved.