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Chapter 49

Corporate Information Technology Transactions and Disputes

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I. INTRODUCTION

§ 49:1 Scope note

This Chapter discusses the role of corporate and outside counsel in the implementation of major information technology (“IT”) projects for the business client, the outsourcing of IT systems, and common disputes arising from the implemen-

tation and performance of IT agreements. IT projects include implementing new systems; contracting for consulting services to integrate hardware, software, and telecommunications systems from disparate vendors; and the outsourcing to an external service provider of key information systems that previously were managed internally or are being re-outsourced.

Why a separate Chapter on information technology transactions, outsourcing, and disputes?¹ Over the past 25 years, many companies have developed sophisticated information management systems that are an integral part of their businesses, and make possible significant competitive advantages or opportunities. Reflecting this importance, companies are committing significant capital and operating budgets to support their information systems (for billing, inventory control, order fulfillment, production and process control, and a host of other purposes), and have become more frequent purchasers of the hardware, software, and services that are necessary to support them. IT transactions and disputes are becoming significant strategic issues that demand the attention of a company's most senior executives.

In this Chapter we explain the role of corporate counsel and outside counsel in connection with both IT transactions (including outsourcing) and IT disputes. We consider the importance of an assessment of business objectives in information technology projects,² the players involved,³ managing the transaction,⁴ dealing with the business and technical integration of disparate systems, typical contract provisions,⁵

[Section 49:1]

¹Chapter 48 "Transactions" (§§ 48:1 et seq.) of this treatise discusses transactional practice generally and Chapters 50 to 56 cover particular types of transactions. In addition, Chapters 59 to 67 of this treatise cover various phases or aspects of litigation. Accordingly, this chapter is focused on corporate information technology transactions and disputes, and does not address subjects covered in other chapters except to the extent necessary to put corporate information technology transactions and disputes in context.

²See § 49:3.

³See §§ 49:4 to 49:11.

⁴See §§ 49:12 to 49:32.

⁵See §§ 49:33 to 49:54.

and information technology disputes.⁶ We believe this will help corporate counsel work effectively with outside counsel in organizing and managing both information technology projects and disputes.

II. INFORMATION TECHNOLOGY TRANSACTIONS AND OUTSOURCING

§ 49:2 What is information technology?

Information Technology, or “IT”, is the use of computers and telecommunications to run applications and software to store, retrieve, transmit and manipulate data. The term is commonly used as a synonym for computers and computer networks, but it also encompasses other information distribution technologies such as television and telephones. Although humans have been storing, retrieving, manipulating and communicating information for hundreds of years, the term ‘Information Technology’ in its modern sense first appeared in a 1958 article published in the Harvard Business Review.¹

In a business context, the Information Technology Association of America has defined information technology (IT) as “the study, design, development, application, implementation, support or management of computer-based information systems.”² IT specialists assume responsibility for selecting hardware and software products appropriate for an organization, integrating those products with organizational needs and infrastructure, and installing, customizing, and maintaining those applications for the organization’s computer users. Examples of these responsibilities include the installation of networks; network administration and security; the design of web pages; the development of multimedia resources; the installation of communication components; the oversight of e-mail systems; maintenance of cloud computing networks; and the planning and management of the technol-

⁶See §§ 49:55 to 49:75.

[Section 49:2]

¹Harold J. Leavitt & Thomas L. Whistler, Management in the 1980s, 36 Harvard Business Review 41, 41 (1958).

²Proctor, K. Scott (2011), Optimizing and Assessing Information Technology: Improving Business Project Execution, John Wiley & Sons.

ogy lifecycle by which an organization's technology is maintained, upgraded, and replaced.

§ 49:3 Business objectives of major information technology projects

Corporations and other business entities often commission large-scale IT projects, which, if successful, can provide significant benefits to a company by automating manual processes or improving existing automation. These projects can improve quality of service, reduce costs, and increase performance.

Business entities are often interested in the rapid implementation of computer and telecommunications systems to achieve a competitive advantage or to meet the increasing capabilities of their competitors. This requires rapid contracting as the initial step to timely implementation. But speed can cause businesses to overlook complex issues or restrict counsel from fully developing the contractual protections the company would otherwise demand if given more time. Consequently, at the outset of an information technology project, inside and outside counsel should seek to understand their clients' business objectives; how those objectives will be aided by the target systems or project; and, to the extent necessary, how the technology works. Part of learning about the technology is understanding how the technology typically is acquired, how it was (or is being) developed, and the pitfalls in installing and using it. Typically, the vendor in an information technology transaction has a preferred way of selling or licensing the system (often involving a team of preferred hardware, software, and, increasingly, telecommunications providers) and preferred forms of contracts.

In contrast, corporate and outside counsel may want to avoid a vendor's preferred form agreement. Despite that seemingly intuitive point, corporate users often adopt much, if not all, of the vendors' language. Users may perceive less delay and less friction with vendors in simply adopting the vendors' approach. This attitude may change as users become more familiar with the pitfalls inherent in information technology projects.

While speed is often the key to achieving users' business objectives, counsel must be sure that a host of performance

issues are covered in a way that facilitates practical enforcement during the project's course. The enforceability of an agreement is high on counsel's list of objectives, because rapid, efficient enforcement will be of great utility to their clients, the corporate users who will be managing the project. More effective enforcement and disengagement techniques can be negotiated and included in the contract with the technology providers, and the inclusion of these provisions can help identify and minimize problems as they develop.

In a variety of IT transactions, the corporate client is likely to confront significant changes in technology, and related business changes, during the lifetime of the contract and/or the systems acquired. Indeed, dynamic changes to the particular technology may actually occur during the contractual implementation period or even during the contract negotiations themselves. Accordingly, anticipating the capacity to manage change in technology, including business changes brought about by new technology, is an essential element of these projects and the contracts that frame them. In entering into agreements in which the technology will inevitably change, it is vital that counsel appreciate the evolutionary timeline of the relevant technology, both before the point of contract and any anticipated enhancements. IT contracts often include a requirement that the vendor's services evolve over time, and this key business objective is best pursued by counsel who understands the timeline of the relevant technology.

The technical and commercial risks in information technology transactions are significant. Among other things, computers break down and software fails (*e.g.*, causing bills not to be accurate, or not sent on time or at all, or a vital production process to shut down); employee or customer data may be inadvertently revealed to third parties or the general public; service providers may have trouble delivering integrated systems that perform as promised; technology and systems change may require the installation of new computer systems; and business requirements themselves (such as inventory control, classification of various transactions for tax or accounting purposes, or streamlined order-entry processes) may change during the lifetime of an agreement with a service provider.

Because of these issues, information technology transactions tend to be difficult to negotiate. And while the contrac-

tual issues raised in these transactions are similar to the issues many in-house counsel deal with on a regular basis, they require a special understanding of existing technology; likely technological developments in, or in competition with, the technology of choice; intellectual property rights; the services to be rendered by the vendor; the commercial terms of the transaction (the gamut of price and performance obligations and entitlements); potential performance problems that are likely to occur; and sometimes regulatory schemes that may impact the transaction. Due to these issues, corporate counsel should consider engaging outside counsel with experience in these types of transactions to supplement the internal legal team. Corporate counsel may also want to engage outside counsel with IT outsourcing experience to help anticipate and navigate the challenges presented by structuring long-term contracts that require multiple entities to work closely together, and dealing with the risk that a problem may arise for which none of those entities is contractually obligated to address or remedy.

§ 49:4 The players in major IT transactions

Major IT transactions typically involve a variety of participants and relationships. The corporation will have one or more groups of affected users (depending on its business and structure). Sometimes the user groups are aligned, but in some cases their objectives can be, to some extent, at cross-purposes (*e.g.*, production groups want faster performance while risk managers want to avoid any streamlining that may increase the odds of exposure to liability). Corporate counsel plays an important role in identifying the conflicts among these groups and insisting that the project manager or senior management reconcile the project-related goals and expectations of internal groups.

In any large scale corporate IT transaction, the success of the project from the company's perspective depends in large part upon all the players having defined roles and responsibilities, accepting the challenges accompanying them, and maintaining their individual focus on their roles and responsibilities while keeping overall company objectives in mind.

§ 49:5 The players in major IT transactions— Executive sponsor

Whatever the nature of the particular IT transaction, the

company's top management should be fully engaged in the project from the outset. Top management sets the company's goals and objectives for the project, outlines broadly the company's parameters for acceptance of risks, establishes budgets, and determines the project's priority. The executive sponsor of the project acts as liaison between the company's top management and the contract negotiation team. She frequently will be the company's chief information officer, but may also be the director of procurement or administrative services director. The executive sponsor is directly responsible to top management for ensuring that the company's goals and objectives are achieved, that the risks the company has assumed fall within the guidelines established by top management, and that the project is accomplished on time and within budget. The executive sponsor is also directly responsible to top management for ensuring that the systems and processes resulting from the project are properly integrated into the company's existing structures. The executive sponsor is also likely to be the company's representative on any steering committee established to oversee implementation of the project.

**§ 49:6 The players in major IT transactions—
Negotiation team**

Besides the executive sponsor,¹ the contract negotiation team will include technical leads who will manage the detailed technical issues, and the commercial leads who will manage issues such as price, transaction or processing volume, and delivery of the completed, tested system. Additional skills may include: human resources staff to manage employment issues,² which are particularly prevalent in large outsourcing transactions or wholesale systems conversions, and tax leads to address matters like the place and manner of payment for goods and services, or sales and use taxes.³

[Section 49:6]

¹See § 49:5.

²See § 49:43.

³See § 49:32.

§ 49:7 The players in major IT transactions—Legal team

The discussion in §§ 49:4 to 49:6 leads us to the legal team. The legal team, comprised of in-house and outside counsel, facilitates the negotiation process by advising the contract negotiation team as to appropriate legal strategies, helping the team appreciate the consequences of particular action or inaction to the company's risk management structure, and managing the evolution of the contract documents as the negotiations progress. The legal team also may advise the negotiation team as to technical issues such as performance measures and service levels, and commercial issues such as unit pricing, minimum processing volume commitments, and service credits. Frequently, a lawyer is one of the principal negotiators, and sometimes serves as the chief negotiator.

The most important role the legal team plays, however, is that of author and editor of the documents that ultimately reflect the agreements among all parties involved in the project. It is the legal team's responsibility to ensure that the contract documents accurately and thoroughly reflect the deal that has been struck with the vendor. Although the legal team may not prepare all of the pieces that go into the finished product, and indeed the typical scenario will have the technical team preparing contractual provisions relating to the hardware and software requirements, specifications, and schedules, the legal team will have to ensure that the completed package fits together properly.

§ 49:8 The players in major IT transactions—Legal team—Role of outside counsel

In-house counsel may choose to heavily involve outside counsel in contract negotiations. Outside counsel may be well suited for that role due to her legal acumen, technical experience, and price negotiating experience. In addition, outside counsel may be well equipped to maintain and control the document production process. For instance, large law firms typically have staff and infrastructure designed to maintain and control documents of significant size and complexity. In our experience, the retention of experienced outside counsel may also increase the corporate user's negotiating leverage because the vendor knows it is likely to work with outside counsel again, thus fostering better communication and disclosure.

§ 49:9 The players in major IT transactions—Legal team—Role of in-house counsel

While outside counsel may lead the legal team in the negotiation and contract drafting processes, in-house counsel must be sufficiently involved in both of these processes to develop a thorough understanding of both the deal that is struck with the vendor, and the contract that reflects it. In-house counsel must live with the document after the closing; must help manage the administration of the contract on a day-to-day basis; must help business and technical managers on the project team interpret or explain the contract to top management and others when questions arise; and will be the first called upon when legal difficulties arise. Although both transactional and litigation counsel are hopefully never far away and can respond when summoned, it is this daily contract management that most notably differentiates in-house from outside counsel's relationship to the project.

By developing the required familiarity with the contract and the underlying deal, in-house counsel can respond to the particular needs of the negotiation team, identifying and marshaling the company's internal resources for use by the team, assuring that the negotiation team remains within the boundaries of the company's policies and procedures, drafting portions of contract documents when called upon to do so, reviewing drafts in a timely fashion, and generally helping to keep the overall document production process on track. Most importantly, in-house counsel must not lose sight of the fact that she is the leader of the legal team, because she ultimately will be responsible to the company's management for the quality of counsel provided by the legal team. Clearly, an informed, hands-on involvement in the project by in-house counsel will maximize the legal team's chances of successfully representing the client in large corporate IT transactions.

§ 49:10 The players in major IT transactions—Secondary vendors

Complex projects also typically involve other vendors besides the principal vendor. These other vendors will supply hardware, software, or telecommunications products or services that may be essential to the success of the project. The contracts for the project must describe the responsibili-

ties of each vendor so that there is minimal overlap of responsibility, and no gaps in responsibility in order to make possible the client's effective project management and, when necessary, enforcement of the agreements. This is especially true in projects where more than one vendor has responsibility for systems integration.

§ 49:11 The players in major IT transactions— Implementation consultants

Implementation consultants can play multiple, sometimes conflicting, roles. They may be helpful in defining the project, identifying vendors, and suggesting ways for efficient implementation. They may also take on certain supervisory, systems integration, or similar tasks once the project gets underway. Counsel should be rigorous in helping the project team to define whether a consultant's role is just advisory, or whether to some extent it is operational. In the latter case, the consultant is functioning as a vendor, and its relationship to the project's other vendors requires careful definition, both to deal with potential conflict of interest issues for the consultant and to provide a definite mechanism for ongoing client review of the consultant's project management decisions. In either case, the consultant's share of the project's risk, if any, should be dealt with as explicitly as possible in negotiations before the consultant begins to act.

§ 49:12 Managing the deal

Sections 49:13 to 49:32 discuss various aspects of managing the transaction, including project timelines,¹ selection of counsel,² RFPs and vendor selection,³ specifications,⁴ structural negotiations,⁵ and hardware and software-related considerations.⁶

[Section 49:12]

¹See § 49:13.

²See § 49:14.

³See § 49:15.

⁴See § 49:16.

⁵See §§ 49:17 to 49:20.

⁶See §§ 49:21 to 49:32.

of disputes (and the fact that many adjudicative disputes are resolved in arbitration), there are a limited number of cases that specifically involve substantial IT disputes. The disputes that have arisen are often contract disputes governed by the parties' detailed contracts. But, with the growth in litigation over IT agreements, different theories of recovery have been employed by parties. In particular, in addition to claims for breach of contract, parties to IT contracts have claimed misrepresentation at the contracting stage and at the billing stage.² And, at least one client claimant has asserted that an IT vendor has a fiduciary duty to its client.³

§ 49:76 Practice checklists

Key considerations when you are managing an IT transaction:

- Project timelines. (*See* § 49:13)
- Selection of counsel. (*See* § 49:14)
- RFPs and vendor selection. (*See* § 49:15)
- Specifications. (*See* § 49:16)
- Structural negotiations. (*See* § 49:17)
 - Preliminary selection of vendors. (*See* § 49:18)
 - Timing considerations. (*See* § 49:19)
 - Third-party maintenance. (*See* § 49:20)
- Hardware and software considerations. (*See* § 49:21)
 - Cloud-based services. (*See* § 49:22)
 - “Sizing” the hardware and software. (*See* § 49:23)
 - Long-term IT strategy of client. (*See* § 49:24)
 - Roles of corporate counsel, outside counsel, and client's IT staff. (*See* § 49:25)
 - Hardware leasing. (*See* § 49:26)
 - Software licensing. (*See* § 49:27)
 - Keeping the project “on time”. (*See* § 49:28)

²*See, e.g.*, BSKyB Ltd. v. HP Enter. Serv. UK Ltd., [2010] EWHC 86 (TCC) (claim by client of misrepresentation by vendor, pre-contract); Hamilton County Emergency Communications Dist. v. Orbacom Communications Integrator Corp., 2006 WL 120157 (E.D. Tenn. 2006) (claim by client under state statute based on misrepresentations).

³*Metavante Corp. v. Emigrant Savings Bank*, 2008 WL 5099619 (E.D. Wis. 2008), order amended on reconsideration, 2008 WL 5263046 (E.D. Wis. 2008) (finding, under the facts, no fiduciary duty owed from vendor to client).

- Limitation of liability. (See § 49:29)
- Support and maintenance services. (See § 49:30)
- Use of consultants to configure, implement, or train. (See § 49:31)
- Tax considerations. (See § 49:32)

Key considerations when you are negotiating an IT transaction:

- Contract scope. (See § 49:34)
 - Master services agreement. (See § 49:35)
 - Term. (See § 49:36)
 - Statements of work. (See § 49:37)
 - Sweep clauses. (See § 49:38)
 - Change orders. (See § 49:39)
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 - ARCs/RRCs. (See § 49:41)
 - Benchmarking. (See § 49:42)
 - IT asset/staff transfers and transition. (See § 49:43)
 - Transformations. (See § 49:44)
 - Exclusivity. (See § 49:45)
 - Termination provisions. (See § 49:46)
 - Dispute resolution provisions. (See § 49:47)
 - Governance procedures. (See § 49:48)
- Service levels. (See § 49:49)
 - Response times. (See § 49:50)
 - Success rates. (See § 49:51)
 - Levels of availability. (See § 49:5.)
- Security/confidentiality. (See § 49:53)

Key considerations when you are involved in an IT dispute:

- The forum. (See § 49:69)
- Specified relief. (See § 49:70)
- Document issues. (See § 49:71)
- Experts. (See § 49:72)
- Presentation challenges. (See § 49:73)
- Avoiding litigation. (See § 49:74)
- Claims. (See § 49:75)