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Death by software

By John Murphy

(originally published in Computing Magazine)

The Internet gets all the publicity but in the corporate IT world the biggest development of the 1990s has been Enterprise Resource Planning (ERP) packages.

A hotchpotch of disparate systems can be thrown out and replaced with a single package which does every administrative task for billion-dollar multinational corporations in a fully integrated way. They cost the earth and are devils to install but the benefits of integration and the cost saving they achieve make it all worthwhile.

Two pillars of this modern IT wisdom are SAP, the German package supplier has been the fastest growing in the world and Anderson Consulting, the world-wide professional services organisation with an army of up to 10,000 people dedicated to integrating and installing SAP's R/3 package.

A whole industry surrounds SAP and ERP generally. This world was rocked last month when SAP and Anderson Consulting were sued for $500 million each over claims that the R/3 package, poorly implemented by Andersen, was a significant cause of the collapse of FoxMeyer Drug, a $5 billion US pharmaceutical distributor.

It is possibly unique that a company has tried to blame its complete collapse on a packaged software supplier. Bobby Cameron, head of Forrester Research's packaged applications service believes this is going to be an increasing trend as companies move to electronic commerce and depend on their IT systems for everything.

The demise of FoxMeyer two years ago was the largest Chapter 7 liquidation in US bankruptcy history. SAP supporters would like to depict the law suit as a desperate piece of ambulance chasing by eager lawyers working for a bankruptcy trustee who has nothing to lose and suing the parties with the deepest pockets. After all how can a software package alone bring a large company down, especially one with 15,000 apparently satisfied users around the world - surely the company's management are the architects of their own demise.

While the latter is probably largely true the former is not. The case is being brought by Mark Ressler of the top Manhattan litigation boutique Kasowitz, Benson, Torres and Friedman.

Ressler say of SAP's and Anderson's vociferous protestations of innocence: "That is a pretty typical reaction from someone who is being sued for half a billion dollars." He is well used to big game hunting, as a former US Attorney in East Manhattan he worked in the same office as the team that brought down Mafia Godfather John Gotti.

In his complaint against SAP in the District Court of Delaware says that SAP officials told FoxMeyer management that the system would work, despite there being no comparable high volume distribution installation at the time. If they said that, it is not a view shared by analysts who watch SAP. The complaint said the legacy mainframe system could do 420,000 transactions a day while the SAP system could only do 10,000. If SAP officials said R/3 could do 420,000 transactions a day they then that view is not held by other. Forrester's Cameron said: "It is well known that R/3 has a problem with scalability, not because of anything wrong with the software but its transaction rate is limited by the speed of the underlying database." An R/3 transaction is more complicated because it has to update every module of the integrated package every time you turn the handle. Large SAP installations have been achieved but only by splitting companies up into multiple units each running their own systems. Cameron finds it hard to believe that SAP would have made any such promises. Others in the software industry have confirmed that they would rather walk away from a contract than sign one which contained a performance guarantee. Not least because performance is determined by factors which are outside the direct control of the software vendor. One development director of a leading unconnected software vendor said: "We know our software works because it works elsewhere. If a customer has problems then it is down to how that software is implemented or used. If they bought the wrong package then it is rather churlish for them to blame us for that."

In a separate complaint before the district court of Harris County, Texas, FoxMeyer's trustee claims that Andersen consulting portrayed itself as the being the leading implementer of R/3 with trained staff who would provide a "professional and workmanlike service". The complaint says that Andersen's charged FoxMeyer $30 million but effectively used the company as a training school, bringing in untrained consultants to get some SAP experience before pulling them out to work on other projects. Andersens called these claims "outlandish and at odds with the facts." A spokesman added that Andersens had been paid for their work and it had been signed off by FoxMeyer. However the complaint further alleges that Andersens threatened to pull out of the project before it was completed unless it was paid in full and remaining work paid for on an hourly basis, and unless the management agreed to sign a statement of satisfaction which had been drawn up by Andersens.

The main question to be answered in court is whether the system would ever have worked? The answer is probably not. The next question is whether FoxMeyer's management would have gone ahead and continued with the project if SAP or Andersen had told them it would never work?

Complaints made initially in a case are obvious yet to be proven and it will be for Ressler to produce evidence that will satisfy a jury. The threat of embarrassment is obviously a useful tool in extracting a settlement but neither SAP nor Andersens will discuss the allegations in detail.

SAP simply put out a statement from Eric Rubino, SAP America's vice president and general counsel which said: "This action is without merit and at odds with the facts. The company met all its contractual commitments and plans to vigorously defend against the claims." It will not disclose what facts the complaint is at odds with. Neither will it reveal if it normally offers any warranty with its software nor would it reveal any benchmarks of transaction volumes attained with R/3, information which Computing would normally expect a software company to provide - if it hadn't mentioned the magic word FoxMeyer.

In August 1994 in the searing heat of Orlando, Florida, some 4000 senior figures in the corporate IT world assembled for the first SAFFIRE SAP user conference. Among the announcements made was an award of Excellence to Andersen Consulting for its SAP projects. It was credited with installing four of the first eight R/3 packages in the US. Elsewhere consultants were warning that the shortage of SAP implementation and integration skills were the main factor holding back the company's growth.

Another announcement was that FoxMeyer

Drug was going to replace its mainframe-based system with client server architecture and R/3 software. FoxMeyer CIO Robert Brown was quoted as saying: "We are betting our company on this." It was reported that R/3 was part of an extensive evaluation of other client/server application offerings, but it bested the competition in volume processing. Those words were to haunt Brown and FoxMeyer.

FoxMeyer one of the favourite "poster children" of the IT industry. It was in the business of buying stocks of drugs from manufacturers and then quickly supplying order to corner drug stores or hospital pharmacies. Competition was intense and all its rivals charged similar prices. There was very little opportunity to add value and very thin margins. From the late 80s it had been looking to IT to fix its problems. In 1993 it announced "Project Delta" which would use every piece of IT it could eat including a fully automated robotic warehouse and ERP, to cut costs and improve customer service. It boasted constantly in magazines and TV programmes about how wonderful it would be when Project Delta was finished. When it went bust it was the IT equivalent of the Marlboro Man who died of lung cancer.

Those on the outside were a little more cynical of its claims that the SAP system would be the answer to its prayers.

"I remember at the time the FoxMeyer management appearing in the news and saying what visionaries they were," said Jim Shepherd, vice president of ERP analysts Advanced Manufacturing Research. "No IT system is going to achieve the kinds of result they were talking about. People were also skeptical about putting an ERP system into a distribution environment which previously never had anything except custom systems.

"People tend to shoehorn ERP systems into all sorts of environment because of the benefits of integration but in distribution it would not then and is not now a perfect fit."

Shepherd said: "ERP systems are designed for manufacturing companies which have very complex transactions but nowhere near the volume you would get in a very large wholesale distribution operation. If they had done any due diligence at the time they would have realised that there were no reference sites of companies who had ever even attempted to achieve that volume. At that time you would not have expected any client-server system to process that volume. One wonders why FoxMeyer made the decision to buy it and one wonders why Andersen and SAP agreed to go along. I think it was ill-advised on the part of all three.

"Do SAP and Andersen have some responsibility for having taken a bad piece if business? Yes they absolutely do. But does that amount to a billion dollars worth of legal liability between them? I'm not so sure."

Forrester's Cameron agrees that R/3 is not designed for very high volume transaction applications. He said: I have heard that a lot of people are having problems with scaling and that those difficulties are because of database limitations and also because R/3 doesn't distribute. Monsanto is running a distributed operation but I think it is the only one. Chevron has the biggest set of users in production and they have ten stand-along instances of R/3. But in my experience SAP is very good at estimating the capacity of its systems and every user I have spoken to has said that they have known the limitations of the system.

"SAP is common in distribution industries but people tend to mix it with other products for warehouse and transportation. For example in retail there is a package called Manhattan which is popular. One of the biggest weakness R/3 has from a functionality standpoint is its monolithic nature but they are working their butt's off to fix that. Sales related activities requires increasing amounts of flexibility. They have announced a sales order configurator for delivery later this year but interestingly it is not built using standard r/3 technology, such as ABAP4 or ABAPOO, it is built using C++ and talks to the R/3 repository as a retrofit add-on.

SAP is unlikely to be affected by the FoxMeyer case because it is covered by product liability in any instance. Cameron believes that the bad publicity is unlikely to swerve large corporations away from its software because it has got too big and there are so many users who have claimed benefits. He said: "I don't think anything is going to scare people off the SAP bandwagon".

Ends

Box out

Project Delta

FoxMeyer Drug hoped that automation would give it a competitive edge so it developed a strategy to use technology for everything - known as Project Delta. Some of the simpler unit included a system for sorting through manufacturers promotions and another to give its purchasing department a better visibility of stock.

A third project involved a fully automated warehouse which cost $15 million from from the day it was switched on scrambled customer orders. Order had to be recalled and even air freighted at FoxMeyer's expense because they were needed urgently and that fiasco cost it $16.5 million.

At the same time it was implementing R/3 in a project which was supposed to save it $40 million a year when implemented in its 23 warehouses. When the company lost a customer which accounted for some 15 percent of its turnover someone had a bright idea to win new customers. Why not take the $40 million saving as read and factor that into reduced prices. The R/3 installation was only ever rolled out to six small warehouses out of 23 and the savings never materialised. When the R/3 system was first tried it too corrupted customer data costing more lost orders and disgruntled customers. On top of installing R/3 it then had to clean up its database, something which according to its court complaint Andersen's originally said it would cover the cost of but was eventually charged to FoxMeyer.

The court complaint against SAP claims that the company realised during the project that it was not going to work and FoxMeyer managers were invited to SAP headquarters in Walldorf, Germany to discuss a fix which was called "Split SD". The idea was to use separate modules on separate processors. The complaint claims this fix was never delivers.

By August 1996 FoxMeyer was going down the plug hole. Project Delta had failed and its suppliers were restricting its credit and pressing it for payment. It went into Chapter 11 Bankruptcy at the end of August and a reorganisation plan created which called for an investment of $775 million to get it back on its feet. This never happened and it had no alternative but to go into Chapter 7 liquidation.

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