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SAP America hit with a $500M suit

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NEWTOWN SQUARE -- SAP America Inc. is being sued for $500 million by the bankruptcy trustee for a liquidated drug distributor that once ranked among the biggest in the business.

Bart A. Brown Jr., the Chapter 7 trustee for FoxMeyer Corp., alleges in the suit that the inability of SAP's enterprise resource planning software to cope with the volume of transactions handled by FoxMeyer led to the company's demise.

The suit was filed in August in U.S. District Court in Wilmington. In a motion last week, SAP asked the court to strike damage claims in the suit, saying such claims are prohibited by Delaware court rules. (Although FoxMeyer was based in Carrollton, Texas, it was incorporated in Delaware, so its bankruptcy petition was filed there.) SAP also asked the court to dismiss the suit, saying that even if the claims are upheld, they don't prove that the company violated its contract with FoxMeyer.

Brown has until Tuesday to respond.

SAP declined to comment on the lawsuit beyond a statement by Eric Rubino, general counsel of SAP America Inc., that it released when the suit was filed. "This action is without merit and at odds with the facts," Rubino said. "The company met all of its contractual commitments and plans to vigorously defend against the claims."

In the suit, Brown accuses SAP and its German parent, SAP AG, of making promises that it knew it couldn't keep, ruining FoxMeyer in the process.

The promises concerned SAP's R/3 enterprise resource planning software, which is designed to manage all aspects of a company's business operations.

According to the suit, FoxMeyer's problems with R/3 unfolded like this:

In 1992, FoxMeyer decided to overhaul its computer systems to gain an edge on its competitors. The company was then among the biggest distributors of drug and health-care products in the United States with $3.4 billion in annual revenues. It competed with other drug distributors on its ability to process and fill orders as quickly, accurately and efficiently as possible. Like supermarket operators, it and its competitors had razor-thin margins, and so had to do a huge volume to show a profit. And, because of their large volumes, slight increases or decreases in their margins could dramatically affect their profits.

In the summer of 1993, SAP told FoxMeyer that its R/3 system would be able to handle all FoxMeyer's operations at all of its warehouses. SAP made that representation even though its R/3 system had been used primarily by manufacturers and never by a distributor, the suit said. SAP even had its employees test the R/3 software with FoxMeyer employees to prove the software could handle the volume of transactions the company did.

In September 1993, FoxMeyer contracted with SAP, Andersen Consulting and Arthur Andersen & Co. SC, to implement the R/3 software. (Brown also sued Andersen for $500 million this past July.) By the summer of '94, FoxMeyer obtained a large distribution contract that required it to add six warehouses. SAP and Andersen scheduled the implementation of the R/3 system at those warehouses for January and February of 1995, and planned to install it at FoxMeyer's other 17 warehouses immediately thereafter.

In November 1994, SAP told FoxMeyer it would only be able to implement R/3 at the new warehouses; the others, SAP said, had a greater volume of invoices than the system could process. FoxMeyer told SAP to get the system up and running at the new warehouses as scheduled and then devise a way to make it work at the old ones.

SAP came up with a method to increase the volume of transactions its R/3 software could handle, but that only enabled the software to handle 10,000 transactions per night. The system it was supposed to replace was handling 420,000 transactions per night. As a result, when FoxMeyer filed for bankruptcy protection in August 1996, its 17 old warehouses were still on the software that SAP had been contracted to replace.

Melvyn Estrin, FoxMeyer's former chief executive officer, told The Wall Street Journal that his experience with SAP and Andersen was "a spinning whirlwind." Estrin, who now heads Dallas-based Avatex Corp., did not return calls.

Although the allegations in the suit are extreme, there have been grumblings about enterprise resource planning, or ERP, software for some time.

It is designed to automate and link the various functions involved in running a business, so a company's managers can obtain up-to-the second information about all aspects of their enterprise.

But it is both expensive and time-consuming to implement. And a lot of businesses that have implemented it have been left wondering exactly what they've gained -- so many, in fact, that IMG Corp., a Swiss-based company that recently opened a U.S. branch in Lester, is carving a niche for itself by showing companies how to use the information they get from their R/3 software to improve their operations.

"We are definitely focused with [SAP] on the same result, which is having successful SAP implementations. Not that just that you turned it on and all the lights came on, but that you turned it on and you can tell what happened," Andrew Harriss, president of IMG Americas, told the Business Journal in September.

Another problem companies are experiencing with ERP software is that, by linking their business functions, it can spread erroneous information throughout their operations at lightning speed.

For example, three months after A-dec Inc., a Newberg, Ore.-based dental equipment maker, implemented ERP software from Baan Co., it began running out of materials. The problem, as reported in the Oct. 19 edition of Computerworld, was that incorrect bills of material that had been entered into the system for production uses got passed along to inventory managers.

Despite its problems, the market for ERP software is booming. SAP, the largest developer of it, posted profits of $229 million in the third quarter, up 50 percent from the third quarter of 1997. Its revenues were $1.22 billion, up 43 percent from the previous year. And it employed 18,330 on Sept. 30, 53 percent more people than it employed on the same date in last year.

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