IN THE SUPERIOR COURT OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

BLOCK FINANCIAL CORPORATION,	)	
	)	
Plaintiff/Counterclaim Defendant,	)	
	)	
v.	)	C. A. No.: 03C-04-010-CLS
	)	
INISOFT CORPORATION,	)	
	)	
Defendant/Counterclaim Plaintiff.	)	

Submitted: December 16, 2008
Decided: April 2, 2009

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PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW FOLLOWING

A NONJURY TRIAL

Scott, J.

I. Introduction

The following is the Court's findings of fact and conclusions of law following a bench trial which took place between March 31, 2008 and April 8, 2008. Briefly stated, the Court finds in favor of Inisoft on the breach of contract claim. The Court determines that the claims of fraud brought by both parties are without merit. Finally, the Court finds in favor of Block on the misappropriation of trade secrets claim.

II. Findings of Fact

a. Initial Discussions

In 2000, Block created its own software for an online tax preparation program. This was a failure.[1] Block felt it was critical for its market share that it have a successful online tax preparation program the following year. This time, it opted to utilize an outside source. In April 2000, Block and Inisoft met for the first time. The initial discussion was for a program that could be used in Canada. Later, the parties discussed an application for the United States market.

Inisoft had gone to market the previous year with a program in Canada. Of key importance to Block were stability of the system and scalability.[2] The Court finds that Inisoft indicated to Block that its software would sufficiently scale to suit

[1] "Security issues associated with the online tax program were publicly discussed by the media at large." Joint Ex. 18 at 4.
[2] Scalability refers to both vertical and horizontal scalability.

its needs. Thereafter, Block employees who made the initial visit to Inisoft recommended independent validation of Inisoft's claims to ensure that the product would meet stability and scalability requirements. Thus, despite Inisoft's assurances, Block was aware from the outset that the software might not meet its immediate needs. On April 16, 2000, Jim Rose, the Vice-President and Managing Director of U.S. Tax at Block during the relevant time period testified, sent an email to Jeff Yabuki, Block's former Chief Operating Officer, stating, "My biggest concern right now is that their product would not scale to the kind of volumes we might expect. I do [not] buy their 10,000 concurrent user number."[3]

It seems that, for Block, if Inisoft could do all it claimed, it would solve what had become a significant and costly issue. As for Inisoft, this small company had a once in a lifetime opportunity to license its product to a multinational giant. Expectations were high, but as indicated above, Block was on notice that there may be problems and it was on a short deadline of less than one year.

b. June 24, 2000 Agreement

In a June 24, 2000 email, Yabuki confirmed terms for a contemplated agreement with Rick Winston, the President of Inisoft. This agreement did not give Block the right to access Inisoft's source code. Inisoft already agreed to provide Block with access to its object code. An object code provides use only. In

[3] Joint Ex. 12.

contrast, software's source code enables a skilled user to see the manner in which the code works and manipulate the results. This initial agreement was for Block to validate Inisoft's assertions before formal licensing. The program consisted of two components, an interview development tool and a web engine. Both are necessary for the software to be functional.

A short time later, Inisoft made its first software delivery to Block. To begin with, there were problems with the interview development tool, but Block was able to work around those issues. The web engine was delivered in the programming language Visual Basic. One month later, on August 21, 2000, another version was delivered, this time written in the language C++.[4] Block claims that, by this time, it depended on Inisoft to have a program ready for the upcoming tax season.

Block had the software tested. It received a mixed report from Microsoft but dismissed some of the concerns identified because it was unsure of Microsoft's objectivity. Instead of looking elsewhere, Block decided to ask Inisoft for its source code, in order to attempt to resolve the issues on scalability and stability itself.[5]

c. Source Code Agreement Dated September 7, 2000

[4] Joint Ex. 35. "I agree with you that getting the C++ version out should be—and is—our highest priority. The goal of the VB prototype, as a part of our normal development schedule, was to demonstrate that we could scale, and not how much." Email from Marco Tabini to Block and Microsoft representatives dated August 5, 2000.

[5] See Joint Ex. 30 and 31.

Inisoft agreed to Block's request and delivered its source code to them. The agreement, entitled the "Limited Developer Source Code License Agreement" granted Block internal use of the software. The agreement provided that "the sole purpose of this license agreement is to provide Developer (Block) with a limited license for the sole purpose of commencing development work that will be the subject of a longer term software license agreement during the period that the Subsequent Agreement is being finalized."[6] The agreement also provided that "Regardless of whether any portion of the software is incorporated into the Developer Materials, Inisoft shall not obtain any right, title or interest in or to the Developer Material." As to the confidentiality of the source code, the agreement provided:

> Each party shall protect, keep in confidence and not disclose any information which it knows or should know is confidential to the other and/or its licensors . . . except to employees and consultants with a need to know who have been advised of the confidential nature thereof and who have signed its standard employee or consultant confidentiality agreement.[7]

One of the key issues at that point was scalability as Block found "[w]e can only run about 9 concurrent users successfully before we start getting errors."[8]

[6] Joint Ex. 5 at ¶2.
[7] Joint Ex. 5 at ¶7.
[8] Joint Ex. 40.

Block began to seek financial concessions from Inisoft.[9] However, the short time frame was an issue from Inisoft's perspective.[10]

d. Consultants

Nexgenix was retained by Block as early as June 1, 2000 to assess the company's options in creating an online tax program. By September 28, 2000, Block had employed Celeritas to recommend alternatives to Inisoft. Celeritas recommended that it build a new replacement web engine for Block.[11] Celeritas felt it would be successful in doing so because it had extensive knowledge of Inisoft's web engine.

The parties understood that in order for Block to obtain the source code from Inisoft, it and its consultants had to take "ownership" of the outcome.[12] On October 18, 2000, Rick Winston sent an email to Jeff Yabuki stating "if you think I'm going to be responsible for the failings of your outside consultants, we're done now. The 19th of October is tomorrow and that's when the source code agreement

[9] Joint Ex. 71, email from Jeff Yabuki to Rick Winston "We . . . need your cooperation to restructure the transaction that accounts for the changes that have been made because of the product not achieving the stability at the time we needed it to (and as we had agreed to at the time we entered into this)."
[10] "I do wish we had more time from the beginning, yet if "your decision" is to move in another direction, we'll simply try to appreciate that this is "your decision." Joint Ex. 71.
[11] Joint Ex. 75.
[12] Joint Ex. 84.

terminates."[13] With so many hands on deck, Block struggled to communicate effectively with Inisoft.[14]

In response to Inisoft's requests for additional information on "areas where we can provide assistance," Yabuki stated that "our consultants have fixed everything to date with the engine. Until further notice, you should assume that there is nothing that needs to be done."[15] In response, Winston stated "[w]ithout further direction from you, I will assume that once again, "my team" is on the sidelines."[16]

However, just one month later, Block prepared a document listing its issues with the web engine.[17] When Inisoft responded, Block determined it would ignore the issue.[18] In the interim, the parties executed the November 2 Agreement.

d. November 2, 2000 Software License Agreement

On November 2, 2000, Block and Inisoft entered into a Software License Agreement. The terms of the Agreement licensed Block to use Inisoft's software

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[13] *Id.*

[14] "I spoke with Jim today to get a heads up on the status and I learned that we have not been able to get the new C++ engine working. NOW, I also learned that no one passed that on to anyone at Inisoft so know [sic] one knows." Joint Ex. 85, email from Jeff Yabuki to Rick Winton, dated October 18, 2000. See also, Joint Ex. 90 "We heard nothing from anyone today. . . I guess no one wants to speak with us." Email from Rick Winston to Jeff Yabuki dated October 20, 2000.

[15] Joint Ex. 90.

[16] *Id.*

[17] See Joint Ex. 96 email to Rick Winston from Jim Rose at Block, "[i]n reviewing the latest release of the Inisoft forms engine, we found the release to be lacking in many areas. In fact, it is basically unusable from our perspective."

[18] Joint Ex. 99.

and source code. The Agreement superseded all prior agreements.[19] The initial term of the Agreement was from November 2, 2000 to September 30, 2003.[20] Block had the option to renew the term as its "sole discretion."

Paragraph 4.2 of the Agreement provides "as long as Inisoft is not in material breach of its obligations under this Agreement, H&R Block will not…utilize any Replacement Software in providing the H&R Service." Paragraph 1.1 defines Replacement Software as "web-based software that provides the functionality provided by the Inisoft Software or which has the effect of rendering obsolete the Inisoft Software."

Paragraph 5.2 provided that "H&R Block may advise Inisoft of deficiencies in the Inisoft Software and the Inisoft Source Code, and Inisoft shall respond as quickly as practicable using commercially reasonable efforts to promptly rectify such deficiencies."

e. Problems Going Into the 2001 Tax Season and Block's Termination Letter

On November 3, 2000, Inisoft delivered Engine release #3 to Block. Engine release #3 was to be added to Engine Release #2 in order to address some of the deficiencies in the web engine. Block performed a Code Review of Inisoft's web engine and on November 22, 2000, Jim Rose sent an email to Rick Winston

[19] Joint Ex. 1.
[20] *Id.* at 15, ¶15.1.

outlining several deficiencies with the web engine. On November 27, 2000, Winston sent a response email to Rose. In the email, Winston acknowledged that some of Block's concerns were "good points" and "would be looked into" and he requested clarification on several of the other points. Block did not respond to Winston's email and Inisoft did not make any modifications or corrections to the web engine. Block proceeded to use Inisoft's software and paid Inisoft the full license fees for the 2001 tax season.

On April 23, 2001, Block sent Inisoft a letter listing deficiencies in Inisoft's software and demanding that the problems be fixed within 30 days.[21] In the letter, Block charged Inisoft with being in "potential material breach of the [November 2] Agreement." Block also expressed concerns that it would be unable to provide Inisoft with the numbers of completed tax returns (as required by the November 2 Agreement) due to potential security law violations. On May 7, 2001 Inisoft responded to Block's letter disputing Block's characterization that it was in potential material breach of the Agreement.[22] It also questioned Block's sudden concern over disclosing the numbers of completed tax returns. Block terminated the November 2 Software License Agreement on November 5, 2001.[23]

[21] Joint Ex. 107.
[22] Joint Ex. 108.
[23] Joint Ex. 119.

III. Trial Testimony

Jeff Yabuki testified on behalf of Block regarding contract negotiations between the parties. He testified that Block was "a bit late getting in the game" of online tax preparation and that it was already a distant second in market share. The tax season begins on January 15 and runs through April 15. Block first marketed an online tax product in the year 2000, which was unsuccessful. It began to prepare new software for 2001, immediately following the preceding tax season. Yabuki testified that at his initial meeting with Inisoft he was told "it was a proven solution that had operated in Canada in the prior year with no issues, and that it had scaled and it was stable and that it would be able to meet the needs of H&R Block."[24] He testified that Block brought in Nexgenix consultants to help with the struggle to stabilize the Inisoft software in September of 2000. HRB1 was referred to as the Inisoft web engine that Block attempted to fix. HRB2 was an alternative engine. Yabuki testified that Block proceeded with both engines as a potential solution. The software provided by Inisoft consisted of both a web engine and an interview development tool; one cannot work without the other. HRB2 was designed to work with the interview development tool created by Inisoft.

Yabuki testified to the pressure Block felt to enter the market if they did not have a product ready for the upcoming tax season:

[24] Trial Tr. March 31, 2008 A.M. at 65.

> We clearly could enter the market again. We could enter – H&R Block could enter at any time. But the lead that Intuit would have had would have been insurmountable, and we would have been permanently relegated to, in the tax business, a second-class citizen.[25]

Yabuki also testified that Block is second in the market for online tax preparation as of the date of trial.

As for the October 21st email in which Yabuki told Inisoft that "our consultants have fixed everything to date with the engine," Yabuki acknowledged that it was an "awkward" email.

> I suspect that I had just seen the results of an update meeting, heard that things were going well, and really wanted our teams to be able to focus on moving the engine along and didn't want our folks to be engaged in back and forth, wanted Inisoft to fix their software and have our folks fix what needed to be done to get us to tax season.[26]

Block used the Inisoft Interview Development tool in 2001 and HRB2, the web engine that Nexgenix created using the Inisoft software. Yabuki testified that Inisoft warranted fixing "anything that does not work."[27] As for the failed efforts at communicating the issues with Inisoft, Yabuki admitted that he did not respond to Inisoft's request for clarification because "we didn't have time to address these comments that were just meant to stall."[28]

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[25] *Id*. at 108.
[26] Trial Tr. March 31, 2008 A.M. at 114.
[27] Trial Tr. March 31, 2008 P.M. at 5.
[28] *Id*. at 22.

Yabuki testified that he signed the November 2 Agreement because he wanted to ensure his consultants had continued access to Inisoft's source code.

Neal Shaw also testified on behalf of Block, he reported to Jim Rose, who in turn reported to Jeff Yabuki. Shaw was responsible for developing the tax preparation software. He testified that the term stability, as it applies to software means that the product is predictable and does not crash. Scalable means that the software can handle increased traffic and multiple users. He testified that scale is particularly important to Block's business because of its seasonal nature.

He testified that the initial version of the Inisoft web engine was given to Block in July, in Visual Basic and that it would be a waste of time for Block to test it at that point. Instead Block waited to test until it received the C++ version in August. Shaw admitted that the six month time table Block was working with was "highly aggressive."[29]

Shaw testified that, despite having received warnings regarding the difficulty of getting the Inisoft web engine to market, he did not agree with those conclusions, at that time, but later he "came to agree with that."[30] Shaw was aware of Microsoft's conclusion that "Inisoft has never participated in a project this large in scale. Their experience in the application enterprise space is low to none and should be taken into consideration when mapping out long-term strategies." He

[29] Trial Tr. April 1, 2008 A.M. at 31.
[30] *Id*. at 74.

testified that these warnings came six weeks prior to the end of August, at which point Block would have already been locked into a decision to go with Inisoft.

Shaw testified that Block spent $7 million dollars on fixing the Inisoft web engine and that most of that money went to Nexgenix.

Shaw testified that Block used HRB2 for 2001 and that after it terminated the license agreement with Inisoft, it did not use HRB2 for future years. Instead, they created a new web engine that was significantly different.

Shaw testified that he did not recall the consultants examining the Inisoft source code in order to create new code; he stated he would be surprised to learn they did. He stated that "Inisoft was aware that we were having our consultants look at their code and determining the feasibility of fixing it . . ."[31]

Interestingly, Shaw appeared surprised to learn that Jim Rose from Block sent a demand to Inisoft, requesting that it fix errors some of which Block had already solved.[32]

Next, Block called David Klausner, an expert on computer programming practices, to testify on both the breach of contract claims and the misappropriation of trade secrets claims. He assigned the errors he found in the Inisoft source code to a number of levels; fatal, severe, error and an annoyance. Klausner found a number of errors in the Inisoft source code that could cause the program to crash.

[31] Trial Tr. April 1, 2008 A.M. at 29.
[32] Trial Tr. April 1, 2008 P.M. at 72.

Of forty-five identified errors, Klausner was only able to compile the data and observe five of the listed errors.[33]

Inisoft called Rick Winston who testified regarding the business agreement with Block. He testified that the technology which was owned by Inisoft Canada changed to the Inisoft Company that was incorporated in Delaware in the first quarter of 2000. He testified that he revised the agreement in May of 2000 but did not change the date. This is in contradiction to interrogatory responses filed in this action. Winston indicated the interrogatories contained a typo.

Winston explained that Yabuki initially approached him about a Canadian application, but the next day became interested in an Australian program. Winston testified that he told Yabuki there was no documentation for the software and that Yabuki reassured him that he had a staff of hundreds, so Inisoft need not be concerned. Winston admitted that he told Yabuki during the initial meetings that the product would scale up to 10,000. In June of 2000, the parties began discussions regarding a United States tax application. Almost immediately after discussions began regarding the United States code, Inisoft began to translate its code from Visual Basic to C++. Winston stated "[T]he amount of support that was being asked of us on a daily basis was just overwhelming . . ."[34]

[33] The Court tended to discount much of Klausner's testimony. The Court was troubled by his failure to directly answer some questions.
[34] Trial Tr. April 2, 2008 P.M. at 57.

Winston further explained that he warranted fixing the software but things changed when he received a call from Jim Rose, threatening to sue him if Inisoft did not turn over the source code. Inisoft had "tremendous interest in making this thing work."[35] Winston indicated that he had no understanding that Block would take its source code and develop an alternative web engine.

Winston also testified that between the October 21 email from Yabuki, until the signing of the November 2 Agreement, he was not informed by Yabuki of any additional problems with the software. Winston also testified that while Inisoft sold the servers which housed the Inisoft source code and purged that information, he did not consider the software to be obsolete because "I knew Block had a copy of my software, my source code. I thought I could get it back from Block at any time."[36] Winston admitted that Block had no obligation under the November 2 Agreement to tell Inisoft what its consultants were doing with the source code.

Marco Tabini, the co-founder of Inisoft, testified regarding the facts of the case and as an expert on Inisoft's claimed trade secrets. He admitted that the "idea of Wizard was nothing new. There were applications that had Wizards that, you know, are step-by-step processes, but nothing to the level of complexity that we wanted to be able to achieve."[37] He also admitted that he told Block

[35] *Id*. at 62.
[36] *Id*. at 90.
[37] Trial Tr. April 3, 2008 A.M. at 101.

representatives at the outset of their relationship that he "thought the program could scale considerably."[38]

He testified about the testing procedures employed by Block prior to receiving the source code. Those tests were conducted in Kansas City. Tabini testified that the combination of software systems, also known as the stack, did not perform well. He testified that he told Block representatives that, until they understood the problems with the software stack, it would be difficult to diagnose problems with the software. He testified that there were scalability issues during that initial test.

Tabini testified that Mr. Guarini went to Houston for additional testing and that the problems persisted. He testified that once Block was given access to the source code, the relationship changed and Block stopped communicating with Inisoft about problems and resolutions. Tabini testified that after the October 21 email from Jeff Yabuki, he continued to work on the revised C++ engine which would include management tools and printing. Tabini testified that if the Inisoft software had the forty-five errors identified by Block that it would not have functioned for the tax season in which it was used. Thus indicating the errors were fixed by someone.

[38] *Id*. at 115.

As for the expert testimony offered by Tabini, he identified the trade secrets that Inisoft claims Block misappropriated. Tabini claims each item represents a secret itself, and as a whole. The claimed secrets as identified by Tabini are as follows:

1. The creation of self-looping structures for the repetition of answers. Tabini testified that self-looping means that the structure can be repeated several times, but each step does not need to be coded. The wizard created is dynamic in that it proceeds accordingly, based upon the users input.
2. The creation and handling of multiple interview wizards, repeating structures, loops, and individual question screens, as well as the unique naming convention adopted. Tabini testified that this relates to the formalization of the interview process, the manner of organizing the pages and sequence.
3. Embedding existing scripting languages to provide a rich development environment for the creation of interviews. Tabini testified that the trade secret is the "idea of using the scripting language in the context of our web engine to provide a level of support for any kind of complex operation that was required without having to have a developer write a lower level piece of code for that purpose."[39]

[39] Trial Tr. April 3, 2008 P.M. at 52.

4. A unique interview development tool for the creation of interviews in a dynamic interactive and visual way. Tabini testified this relates to the ability of a non-technical individual to build steps into the interview.
5. The separation and unserialized execution of interview, based on dynamic adaptation of the interview to the user's response Tabini testified that this also relates to the software's design and the ability of non-technical individuals to tailor the program to unique users.
6. Dynamically rebuilding the history of pages visited by the user during the course of the interview. Tabini explained that this allows the user to revisit a previous step and change the answer; the method rebuilds and maintains the history of the users' steps.
7. Capability of branding. Tabini explained that the engine was created to present different brands to the user; he claims the trade secret was in the method used to lay out the data.

Tabini also examined the source code for Block's online tax preparation software as it existed since the termination of the relationship with Inisoft. First, he noted that the 2004 source code is time-stamped as of 2001 and the author is Nexgenix. Next, he testified that he found literal copying of the function to validate the email and that there is a spacing difference between the Inisoft code and this version. He also found literal copying of the term "nullinzero." Tabini

also noted that in 2005, Block's code was written in a different language; however, the "nullinzero" function name remains. Tabini also noted that the term used for the field to capture the user's social security number is SIN rather that SSN, which in the Inisoft code was designed to capture the Canadian Social Insurance Number. He pointed out a similar finding for the field designed to capture zip codes.

Tabini pointed out, several times, that he does not think the source code contains trade secrets, but instead that it is an expression or embodiment of the claimed trade secrets.

Next, Mr. Klausner was again called by Block, this time to testify regarding the trade secret claim asserted by Inisoft. Klausner testified that none of the trade secrets asserted by Inisoft were used by Block and none of the trade secrets were actual trade secrets during the relevant time period for the purposes of this lawsuit. Counsel for Inisoft discredited the references used by Klausner by demonstrating that the publicly available information that he cited to in his report was either a poor source or not available for view at the time of trial.

Finally, Inisoft called Ken Pugh to testify regarding the trade secret claim. Specifically, he testified regarding literal copying of Inisoft's source code by Block. Pugh stated that while the literal copying that he found does not, by itself, represent the claimed trade secrets, it represents a "DNA indication that the Block

source code, in essence, had traces of Inisoft DNA in the source code itself."[40] He opines that this proves whoever wrote the Block software had access to the Inisoft source code, because the likelihood of the same lines by chance is "awfully low."[41] He identifies sixty-nine common lines of code between the programs, but acknowledges that this is a small percentage of the program.[42]

The parties submitted the deposition testimony of K.P. Hari, Robert Cossins, Antonio Lamanna, Maurizio Guarini, and Jim Rose for the Court to review in chambers.

The Court notes that K.P. Hari, who was working for Nexgenix during the relevant time period had access to the Inisoft source code and that the teams working on HRB1 and HRB2 were not prohibited from talking to one another. He recalls that work on HRB1 concluded sometime in November.

Robert Cossins, CEO of Celeritas, testified that on September 21, 2000, Block asked his company to develop a replacement for the Inisoft software.

Antonio Lamanna testified as the accountant for Inisoft, both the U.S. and Canadian entities. He recalled discussions of a technology transfer from the Canadian company to the U.S. company either in the fall of 1999, or the Spring of 2000. Inisoft Canada never received the full fee for the technology.

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[40] Trial Tr., April 7, 2008 A.M. at 11.
[41] *Id.*
[42] *Id*. at 93-94.

Maurizio Guarini, an owner of Inisoft, was unsure whether the employees who built the software are or were subject to confidentiality agreements. He testified that no work had been done on Inisoft's source code after March of 2001. He also testified regarding the specific aspects of the Inisoft source code that manifest the claimed trade secrets. Finally, he acknowledged that Inisoft did not seek to market or sell the various features of the program which it claims as its valuable trade secrets.

Jim Rose testified that at the time of the November 2 Agreement, Block was certain it would use the Interview Development Tool component of the Inisoft software, but it was unsure about the web engine. He acknowledged receiving the criticisms from Microsoft regarding Inisoft's ability to deliver. As for Block's request for the source code, he stated "Block requested and received the Inisoft source code so that we could assist Inisoft in fixing their source code in making it work, and by putting more resources to bear on getting it fixed." He also testified regarding limited security breaches during the 2001 tax season.

IV. Preliminary Conclusions of Law

a. Choice of Law

In its Proposed Findings of Fact and Conclusions of Law, Block asserts that for its claims of fraud, negligent representation and promissory estoppel, that Missouri law applies. "A choice of law analysis would therefore likely result in

application of Missouri law. That said, there is no reason at this time for the Court to engage in a choice of law analysis with respect to these particular claims."[43] It is unclear why Block believes the choice of law analysis is unnecessary but the Court determines that Delaware law applies as the contracts select Delaware law and the entities are both Delaware corporations.[44]

b. Expert Testimony

At trial, none of the experts offered their opinions to a reasonable degree of scientific certainty. The Court asked the parties to address this point in their post-trial briefing. Inisoft, citing *In re Asbestos Litigation*, argues this is irrelevant because our rules do not require "such an incantation."[45] Block claims that the Court should afford no weight to the expert testimony. The expert testimony relates exclusively to Inisoft's claim of misappropriation of trade secrets.

This is a bench trial and neither side asked their experts whether their opinions were stated to a reasonable degree of probability. As such, the Court will treat the testimony of all experts as offered by them to a reasonable degree of

[43] D.I. 134 at 35.
[44] See D.I. 1 at ¶ 1; D.I. at ¶ 2; Jt. Tr. Ex. 1 at § 17.1.
[45] See Inisoft's Proposed Findings of Fact and Conclusions of Law on its Counterclaims at 17, citing *In re Asbestos Litigation*, 911 A.2d 1176, 1199.

probability—particularly as the concern was raised by the Court and not by either party, thus no objection was raised.[46]

V. Breach of Contract Claims

Block seeks rescission of the November 2 Agreement on grounds of (1) economic duress, (2) fraudulent inducement, and (3) inducement through negligent misrepresentation.

Block seeks declaratory judgment that Inisoft's actions constituted a material breach, that Block was entitled to develop its own web engine and other software, and that Block was entitled to terminate the November 2nd Agreement.

Inisoft has counterclaimed for breach of contract and breach of the implied duty of good faith and fair dealing.

The parties agree that 6 Del. Code § 2-101 *et. seq*. controls the contracts at issue.78

a. Conclusions of Law Regarding the Limited Developer Source Code Agreement

The Limited Developer Source Code Agreement[47] became effective on September 7, 2000 and granted Block access to Inisoft's source code for seven days. The parties agree that the agreement was extended several times, up until the

[46] See *Pawtucket Mut. Ins. Co. v. J.B. Research, Inc.*, 2000 WL 1611079 *2 (Del. Super.). "The Court is satisfied that the [expert]'s official conclusion as to the fire's origin was held by him to the appropriate degree of probability."
[47] Joint Ex. 5.

execution of the November 2nd Agreement. The Agreement provides, in part, as follows:

> Inisoft hereby grants Developer (Block) a non-exclusive, royalty free, non-transferable license, for a period not to exceed seven days to use internally the Software solely to commence development of software applications ("Applications"), which shall consist solely of the Software integrated with Developer's proprietary software and information ("Developer Materials").
>
> > It is acknowledged and agreed that the sole purpose of this license agreement is to provide Developer with a limited license for the sole purpose of commencing development work that will be the subject of a longer term software license agreement (the "Subsequent Agreement") during the period that the Subsequent Agreement is being finalized.

As to ownership, this agreement provides that:

> For further clarification, regardless of whether any portion of the software is incorporated into the Developer Materials, Inisoft shall not obtain any right, title or interest in or to the Developer Material.

As to confidentiality, the agreement states:

> Each party shall protect, keep in confident and not disclose any information which it knows or should know is confidential to the other and/or its licensors ("Confidential Information"), except to employees and consultants with a need to know who have been advised of the confidential nature thereof and who have signed its' standard employee or consultant confidentiality agreement. The foregoing shall not apply to Confidential Information which is in the public domain without breach of this Agreement, was known to the non-disclosing party prior to its first receipt from the disclosing party, or has been rightfully received by non-disclosing party from a third party without breach by any party of any confidentiality limitations.

Inisoft claims that Block breached the Limited Developer Source Code Agreement. Specifically, it alleges that "Block materially breached that contract by, among other actions, keeping Inisoft's source code beyond the term of the agreement."[48] At trial and in post briefing, Inisoft's theory appears to be that: (1) Block violated this agreement by breaching the confidentiality provision in revealing the source code to its consultants and (2) by developing a replacement or alternative web engine.

As to the first theory, the Court finds that there was no breach by Block as the parties admit the agreement was extended while they negotiated the November 2 Agreement. As to the second theory, the Court concludes that Block did not breach this agreement by revealing the source code to its consultants. The parties' course of conduct indicates that Inisoft was aware that Block was revealing its source code to consultants in an effort to get the product to work. Inisoft received copies of reports from the various consultants who viewed the source code. Moreover, while Celeritas, the only consultant for which Block did not obtain a confidentiality agreement, was working for Block during the relevant time-period, the invoices do not reflect that it had access to the source code.[49] Additionally, the deposition testimony of Robert Cossins, also does not establish that Block granted

[48] D.I. 2 at 35.
[49] See Joint Ex. 122, HRB003764

Celeritas access to the source code.[50] Block, in keeping with this agreement, obtained confidentiality agreements from Microsoft and Nexgenix. Accordingly, there is no breach on this theory.

Finally, much was made at trial regarding the difference between designing a replacement engine and an alternative engine. The Court finds that it need not address this issue with regard to this agreement because the agreement states that its purpose is to allow Block to commence "development work that will be the subject of a longer term software license agreement." Whether that development work would result in an alternative or replacement is not defined by the parties. However, the course of dealing indicates that Inisoft was aware that its product was not scaling to Block's requirements and that all parties were working long hours, with the help of consultants, to develop a program that would work. This agreement does not contemplate whether the final, working product would be a replacement or alternative—and the Court concludes that the parties, at the relevant point in time, were unsure about the nature of the fix required.

b. Conclusions of Law Regarding the November 2, 2000 Software License Agreement

The November 2 Agreement was the culmination of a great deal of negotiation and, during trial, a great deal of attention. Both parties allege breach of

[50] See generally deposition designation of Robert Cossins.

this Agreement by the other party. The Court concludes that the Agreement was breached by Block, but not Inisoft.

Section 2.3 of the Agreement states that Block is granted a license to develop an online tax program and that "all such development shall be deemed to be modification of the Inisoft Software." Such *modifications* are permitted, and in fact, the purpose of the Agreement. However, section 4.2 prohibits Block from developing or utilizing *replacement* software so long as Inisoft is not in material breach of the Agreement.

Block may not "cause or permit reverse compilation or reverse assembly of all or any portion of the Inisoft Software."[51] Inisoft retained intellectual property rights, however, Block was to own any modifications that it made to the software.[52] Within the same provision, Block acknowledged that the software constituted valuable proprietary information.[53] Block was given the power to release Inisoft's confidential information to contacts "who required access to it for the purposes of this agreement," which as indicated above, was to permit the development of online tax software.[54]

[51] Joint Ex. 1 at 6, ¶2.6.
[52] *Id.* at 7, ¶3.1.
[53] *Id.*
[54] *Id.* at 12, ¶10.2.

Inisoft was required, for the first year, to provide to Block, any corrections to the software that Block diagnoses as errors.[55] However, the contract also indicates that the software is deemed accepted by Block, with the exception of "minor changes."[56] Such changes are to be reported to Inisoft and Inisoft was to act "as quickly as practicable . . .to rectify such deficiencies."[57]

Section 15.2 provides the parties can terminate the Agreement in the event of a material breach by the other. The contract constitutes the entire agreement between the parties.[58] Inisoft warranted that it had the power and legal right to enter into the agreement with Block. Finally, there is no mention of the implied warranty of merchantability.

The Court concludes that the November 2 Agreement did not appropriately disclaim the implied warranty of merchantability as required by our statute, as the warranty must be expressly disclaimed, and the Agreement does not even mention the term "merchantability."[59] To be merchantable, the statute requires that the

[55] Joint Ex. 1. at 6, ¶2.5.
[56] *Id.* at 8, ¶5.1
[57] *Id.* at ¶5.2.
[58] *Id.* at 18, ¶17.10.
[59] See 6 Del. C. § 2-314 and 2-316(2) stating that "to exclude or modify the implied warranty of merchantability or any part of it the language must mention merchantability and in case of a writing must be conspicuous."

goods would pass in the trade without objection and are fit for the ordinary purpose for which the goods are used.[60]

The goods in this case are (1) the interview development tool and (2) the web engine. The web engine is the portion of the software which required the most modification by Block in order to properly interface with the interview pages which were developed by Block, using the Inisoft program. In order to establish that the warranty of merchantability was breached, Block needed to provide evidence and testimony regarding the expectations in the trade for a web engine. There was evidence provided that the software was not stable and did not scale to Block's requirements. There was testimony from all sides that a web engine must be stable to pass muster in the trade. However, the course of dealing between the parties indicates that Block was well aware of the limitations of the software and yet chose to sign this new agreement with Inisoft.

Of particular importance is that Block, a sophisticated party, accepted the web engine at the time of the Agreement. In fact, it made such acceptance conditional only on Inisoft's promise to remedy "minor" deficiencies. Given the testimony of Block representatives at trial, stability and scalability were not minor—and yet, Block accepted the software with the knowledge of its limitations.

[60] There are other statutory requirements to meet merchantability requirements, however, they are not relevant to the goods in this case as they are not fungible, were not sold in bulk, and no labeling was produced at trial. See 6 Del. C. § 2-314(b), (d), (e), and (f).

While the stability of the Inisoft web engine would not meet trade standards to be immediately brought to market, the Agreement contemplates that Block would *develop* an online tax program. So, while the industry standard might be that a web engine would be stable before going to market, the Agreement between the parties indicates that Block was using the software as a basis on which to develop a program for market. Thus, the goods were merchantable for the purpose of this Agreement.

Next, Block claims that Inisoft breached the Agreement by failing to remedy the diagnosed and reported errors. The Court disagrees. The software was accepted on receipt and Inisoft promised only to fix "minor" errors. Block representatives testified that the problems with stability and scale were significant, and in no way, minor. There is no promise in the Agreement to fix any and all problems Block reported, particularly when the Court considers that Block was well aware of the problems and yet accepted the software on receipt anyway.

Inisoft claims breach of this Agreement because it argues Block developed a replacement engine, which was prohibited under the Agreement. Block counters that it developed a modification or fix. The Court agrees with Block. The Agreement contemplates that Block would develop an online tax program using the Inisoft Source Code.[61] Block and its consultant, Nexgenix, did exactly that

[61] Joint Ex. 1 at 5, ¶2.3.

with HRB2. For a significant portion of the limited time Block had, it worked on multiple options to get a product to market. It, prudently, had contingency plans. HRB2 was such a plan. Inisoft does not seriously dispute that the engine it delivered did not meet Block's requirements. Replacement software is defined in the Agreement as that which renders the Inisoft Software obsolete; however, the Inisoft Software consisted of two components, the interview development tool and the web engine. HRB2 was designed to work with the interview development tool that Inisoft delivered—as such, it could not have rendered the Inisoft software obsolete.

Using the web engine delivered by Inisoft as a basis, Block developed an online tax program—that is exactly what Block negotiated for in the Agreement at issue. The Court rejects Inisoft's claim that Block breached the November 2nd Agreement by developing replacement software.

VI. Conclusions of Law Regarding the Fraud Claims

Both parties allege the other committed fraud. Block also claims promissory estoppel. Inisoft alleges that Block committed fraud in the November 2 Agreement because, it claims, at the time Block entered the Agreement, it had no intention of using the Inisoft web engine. The Court concludes that even if this allegation was true, it would not constitute fraud because the Agreement contemplates that Block

would use the Inisoft software to develop an online tax program—which it did through HRB2.

In Delaware, the implied covenant of good faith and fair dealing "attaches to every contract."[62] Block asks the Court to hold that Inisoft had a duty to exercise reasonable care in making its representations and that, by failing to do so; Inisoft breached the implied covenant of good faith and fair dealing. The Court need not make such a determination at this point because it finds Inisoft did exercise reasonable care in making its representations. Inisoft had a product that it took to market the prior year, Marco Tabini's statements at the initial meeting with Block representatives regarding scale were estimations based on his intimate understanding of the software. Regarding the stability issues, the Court is not convinced that, during the tests in Kansas City and Houston, the stability issues were with the Inisoft software and not other software within the software stack used to conduct the testing.

Block also asserts a claim for promissory estoppel. The elements of promissory estoppel are as follows:[63]

(1) a clear and unambiguous promise

(2) reasonable and foreseeable reliance

(3) injury sustained

[62] *Dunlap v. State Farm Fire and Cas. Co.*, 878 A.2d 434, 441 (Del. 2005).
[63] *Vornado PS, L.L.C. v. Primestone L.P.*, 821 A.2d 296 (Del. Ch. 2000).

The Court concludes that Block cannot succeed on its claim for promissory estoppel because (1) there is no conclusory evidence of a clear promise regarding scale and stability, and more importantly, (2) any reliance Block placed on Inisoft's representations should have been tempered by the fact that Block employees themselves immediately questioned Inisoft's claims. While Block states that it was impressed that Marco Tabini prevailed in a dispute with Microsoft and that it questioned other consultants' reviews of the Inisoft web engine. The fact remained, that Block had warning and its own employees doubted the claims purportedly asserted. Thus, any such blind reliance was unreasonable and Block cannot succeed on its claim of promissory estoppel.

VII. Conclusions of Law Regarding Trade Secret Claims

Inisoft claims Block misappropriated its trade secrets. The party asserting a misappropriation of trade secrets has the burden of proof. Inisoft must establish: [64]

(1) A trade secret existed,

(2) It was communicated to Block by Inisoft,

(3) There was an implication that secrecy would be maintained,

(4) Block improperly used or disclosed the secret.[65]

[64] *Vornado,* 821 A.2d 296.
[65] *EDIX Media Group, Inc. v. Mahani*, 2006 WL 3742595 *5 (Del. Ch.).

Trade secret law protects (1) information that (2) derives an independent economic value from not being generally known, which (3) the party has taken reasonable steps to protect the secret.[66]

The Court concludes that Inisoft's claimed trade secret, the ideas embodied in its source code, is not protected under Delaware law because Inisoft did not take reasonable steps to ensure its secrecy. The primary reason is that Inisoft's co-owner Maurizio Guarini did not recall if he was subject to a confidentiality agreement regarding the trade secrets. Additionally, Inisoft produced no evidence that its employees that worked on the source code and software were subject to confidentiality agreements.[67] Moreover, the Court accepts the testimony of Block's expert over that of Marco Tabini regarding the existence of the trade secrets. Tabini did not testify regarding the novelty of his purported trade secrets during the relevant time period, instead he testified regarding their novelty during the time he initially developed the software—1999. Because the Court concludes the purported trade secrets are not protected under the applicable law, the Court finds in favor of Block on this claim.

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[66] 6 Del. C. § 2001(4). See also, *Smithkline Beecham Pharmaceuticals Co. v. Merck & Co., Inc.*, 766 A.2d 442, 448 (Del. 2000).

[67] See *Technicon Data Sys. Corp. v. Curtis 1000, Inc.*, 1984 WL 8268 *6 (Del. Ch.) wherein the Court cited to the fact that employees were required to execute confidentiality agreements to establish that reasonable measures had been taken to maintain secrecy.

VIII. Conclusion

The Court finds that Inisoft did not materially breach the November 2 Agreement, as such, Block's termination was wrongful and it is required to pay the requisite contractual damages. The parties are to submit written arguments to the Court regarding the calculation of contract damages pursuant to the attached Order. The Court finds that neither party has established their various fraud claims. Finally, the Court finds in favor of Block on the misappropriation of trade secrets claim.

IT IS SO ORDERED.

Judge Calvin L. Scott, Jr.