

Ghosts in the Machine?

Scary Things in Software Licensing



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Overview

➤ Introduction

➤ Types of Licenses

- ❖ End User License Agreement (EULA)
- ❖ Click-Through / Click-Wrap Agreements / Shrink Wrap Agreements - "take it or leave it"
- ❖ Negotiated software license agreements executed by the licensor and licensee
- ❖ Software license terms included in negotiated agreements involving the purchase and sale of hardware or services
- ❖ OEM
- ❖ Reseller
- ❖ Note: There is no "one-size-fits-all" software license agreement. Each deal will be different based on a number of factors.

Key Factors

➤ What is the business deal?

- ❖ Who's using what, how, for how long?
- ❖ What is the leverage?
 - How critical is the licensed software to the business?
 - Is there another source for the functionality?

➤ How Licensed?

- ❖ Per user/seat, per CPU, limited to a type of hardware or facility
- ❖ License fee + maintenance and/or support
- ❖ Subscription - monthly fee for usage

U.S. Copyright Act

- Exclusive rights granted to owner of the copyright
 - ❖ To reproduce
 - ❖ To prepare derivative works
 - ❖ To distribute copies
 - ❖ To perform
 - ❖ To publicly display

- Software constitutes a literary work

Software Patents / U.S. Patent Act

➤ Why used?

- ❖ Copyright law only protects the expression of the idea but not the idea itself
- ❖ Generally, courts are reluctant to interpret this right broadly

➤ Patents can be used to prevent others from creating a competing program that uses the same ideas in an existing, patent-protected program

- ❖ Limited due to bad patents where prior art was not adequately considered

License Grant

➤ Terminology

- ❖ Subject to the terms of this Agreement, Licensors grants to Licensee a perpetual, irrevocable, personal, non-assignable, non-exclusive license to use the Software in object form only solely for Licensee's internal business purposes in the Territory.

License Grant

Be Specific Defining Licensee's Rights

Licensee gets right to

➤ Use

- ❖ Use may be limited to a specific purpose e.g. Licensee's internal business only

➤ Reproduce

- ❖ Reproduction may be limited to archival purposes or a specified number of copies

➤ Modify

- ❖ Modification may be limited to specific purpose or a particular application so it is compatible with the system
- ❖ Determine which party owns the modifications

➤ Distribute

- ❖ Right to distribute or redistribute may include rights to sublicense, promote or market
- ❖ Licensor may want to limit to redistribution as a bundled product, stand alone, in a territory at a certain price limit
- ❖ Which party is liable for claims in relation to end-users?

License Grant

Be Specific Defining Licensee's Rights

What words – not included

➤ Exclusivity Rights

- ❖ Means the ability of Licensee to exercise its rights to the exclusion of all others, including Licensor
- ❖ Based on specified amount of royalties or
- ❖ Scope: Territory, duration or particular fields of use

➤ Perpetual

- ❖ Unlimited duration or duration of the Licensor's underlying intellectual property rights
- ❖ What effect does the termination of the Agreement have?

➤ Irrevocable

- ❖ Licensee may want to ensure that Licensor can't take back its rights after having paid for the Software
- ❖ Licensor may "Subject to the terms of this Agreement" and will condition any permanency on Licensee's compliance

License Grant

Definition of Licensee

- **Scope of License**
 - ❖ **Definition of Licensee - include affiliates**
 - ❖ **Adequate to cover business needs?**
 - **Object code only**
 - **Source code - right to modify**
 - **Hosted / ASP?**
- **Can Affiliates use it?**
 - ❖ **Assignable - exclude affiliates so Licensee may grow by M&A (watch transfer clause in grant clause too)**
- **Specified IP Rights**
 - ❖ **Is Grant under Licensor's patents and copyrights?**

License Restrictions

- Copy only for Archival Purposes
- Licensee will not reverse engineer, decompile, disassemble or otherwise try to get the source code
- Licensee will not transfer, sublicense, distribute, sell or use for service bureau use
 - ❖ Transfer to unaffiliated third parties only? Means affiliated entities can use it – may expand scope of license or number of users
- No Implied License Rights
 - ❖ May include language
 - "Licensee may not use the Software except as expressly set forth in Section ____, License Grant."*
 - ❖ Licensee generally obligated to reproduce all proprietary notices on copies of Software

License Fees

- **One-time license fees**
- **Monthly or annual subscription fees**
- **Each of these can be based on the number of computers, users, facilities, concurrent users, etc.**

Delivery & Acceptance

- **Go hand in hand with payment structure**

- **Considerations**
 - ❖ Up front license fee
 - ❖ Installment payments on monthly or quarterly basis
 - ❖ Subscription style

- **Delivery**
 - ❖ Determine when Licensor is to deliver the Software
 - ❖ Which version
 - ❖ Does install occur at one time or in multiple installations?

- **Acceptance Testing – Licensor wants to put a fence around this**
 - ❖ What rights does Licensee have to test and for what period?
 - ❖ Software may be deemed accepted after certain number of days
 - Or upon use by Licensee in production
 - What notice of acceptance / non-acceptance is required?

- **Remedy**
 - ❖ May limit to a refund of monies paid if Software fails acceptance test
 - ❖ Exclusive remedy may be Licensor's obligation to to repair, replace or somehow fix the Software without providing a refund

Custom Code - Issue in Professional Services or Consulting

➤ **Ownership**

- ❖ **Works made for hire**

- ❖ **License Back**

- ❖ **Royalties**

- **Licensor pays Licensee royalties on subsequent licenses on custom portion of the code**

Warranties

- Consider what is disclaimed
- If third party or Open Source Software is embedded in the Software
 - ❖ Warranties should match the heightened risk
 - ❖ Determine responsibility for the security of data – particularly important if personally identifiable information is touched
 - ❖ Is licensor acting as insurance company for Licensee?
- Licensor represents and warrants that:
 - ❖ Neither the Software, nor any component thereof, shall infringe any Intellectual Property, personal or other proprietary rights of any third party;
 - ❖ Licensor has the full authority to enter into this Agreement, it has the right to grant the rights set forth in this Agreement and that entering into this Agreement does not violate or conflict with any prior agreements with or other obligations owed by Licensor to any third parties;
 - ❖ Licensor is the owner of or otherwise has the right to use and distribute all materials and any third party products use by Licensor or provided to Customer in connection with this Agreement; and
 - ❖ Licensor will comply with all applicable federal, state and local laws as required by Customer and communicated in writing by Customer to Licensor in the performance of this Agreement.

Warranties continued

➤ Performance Warranty:

- ❖ Licensor warrants that the software will function in a specified manner for some period of time
 - Substantially in compliance with documentation provided to Licensee
- ❖ Warranty period typically begins upon Acceptance
 - 90 Days
 - Term of Agreement
- ❖ Licensor should consider the warranty of performance when 3rd party software is included in the software (e.g., open source)
- ❖ Warranty that software system will operate within service level parameters
 - Remedy: pre-agreed service level credits (liquidated damages)
- ❖ Warranty that the Licensor is the owner of the software and has the right to grant the licenses granted (no infringement). What about Third Party code or Open Source embedded?
- ❖ No viruses, time bombs, trap doors or other harmful or disabling code
- ❖ Licensee might want to seek a warranty that Licensor has no plans to discontinue software
- ❖ Licensors will want to disclaim implied warranties
- ❖ Remedy: repair or replace the software, with a refund if replace/repair remedy fails
- ❖ Licensors will want to limit the warranties to things within its control (e.g., not a failure of the computer system on which the software is running)

Limitation of Liability

- Breach of Confidentiality
- Licensor will want to limit its liability under the Agreement, including disclaiming consequential damages and capping overall liability
- Licensee may also want to limit its liability
- Pricing the risk
 - ❖ Increasing Licensor's potential liability likely raises Licensor's price
- Cap on liability – key what is not covered
 - ❖ Exclusions - means unlimited liability
 - Indemnity
 - Breach of Confidentiality
 - Valid only if software approved or provided by Licensor or used in accordance with the terms of the Agreement (no unauthorized use)
 - ❖ Cover data loss?

Indemnity

- **IP Infringement**
- **Exclusions: Any Licensee modification to the software, Licensor modifies at the Licensee's request, Licensee uses an old version, use of the software with third party software/hardware.**
- **Licensor will want the right (even at its own cost) to make software noninfringing, obtain a license, provide functionally equivalent software or refund the license fees at its discretion**
- **Control of defense**
 - ❖ **Licensee wants to pre-approve any settlement that obligates it**
- **Privacy / PII data breach**
 - ❖ **Excluded from cap on liability?**
 - ❖ **May be limited to breach of third party IP rights within a defined Territory or for example to breach of a U.S. Patent**
 - **This excludes indemnity for any other type of IP right in other jurisdictions and for copyright violation**

Support & Maintenance

- **How long will Licensor provide support and maintenance for the software?**
 - ❖ While Licensee pays fees
 - ❖ Licensee: for so long as the Licensee is using the software
 - ❖ Licensor: a reasonable period of time
 - ❖ Licensees will also want to control support fee escalation over time. Limit the Licensor's ability to increase support fees to some annual maximum

- **Support Fees (0% of license fees) and Service Credits**

Escrow

- When Licensee has license for object code only that is critical to its business
- Release Conditions are key. Depositor and Beneficiary agree that a Work Request for the release of the Deposit Material shall be based solely on one or more of the following conditions:
 - (i) Depositor's breach of the license agreement or other agreement between the Depositor and Beneficiary regulating the use of the Deposit Material covered under this Agreement; or
 - (ii) Failure of the Depositor to function as a going concern or operate in the in the ordinary course; or
 - (iii) Depositor is subject to voluntary or involuntary bankruptcy.
- Does Licensor have an obligation to deposit updates, enhancements and new releases into escrow?

Software Licensing Checklist

- **License Grant**
- **License Restrictions**
- **License Fees**
- **Delivery & Acceptance**
- **Ownership / Custom Code**
- **Warranties**
- **Limitation of Liability**
- **Indeminty**
- **Support & Maintenance**
- **Escrow**
- **Software License Checklist – Valuable Tool**