

AUGUST 2016

DEVOTED TO
LEADERS IN THE
INTELLECTUAL
PROPERTY AND
ENTERTAINMENT
COMMUNITY

VOLUME 36 NUMBER 7

THE *Licensing*
Journal

Edited by Gregory J. Battersby and Charles W. Grimes



Contract Corner

Stephen F. Pinson

Negotiating Software Contracts

A warranty is one of the most important contract provisions in a software contract. The warranty section deals with the performance of the software and what the licensor promises the software will or will not do. In a software contract, these performance warranties should be heavily negotiated, but usually they are overlooked. Because so many factors can affect the performance of the software, publishers seek to limit their warranty, and provide limited remedies in the event of a breach. It is important for businesses that license software to have a strategy in place to successfully negotiate this section. But, what exactly are the pitfalls when negotiating a warranty provision, and how do you successfully navigate it?

Successfully Negotiating a Warranty Section

One of the major pitfalls in negotiating a warranty is contained in the structure of the contract provision itself and the intent of the software licensor. Many contracts include boilerplate language, requiring contract negotiators to develop a systematic way to review the language and then develop a strategy to address the warranty concerns for their side of the deal. To do this, the parties must first understand the risks involved with a particular software license and negotiate for the specific risk type.

The best way to put this into action is to review the warranty language and put the language

into a more concrete roadmap to negotiate the contract by asking the following questions: (1) what are the licensor's objectives in the warranty section; (2) what are licensee's objectives in the warranty section; (3) what is a checklist of provisions that should be negotiated in a warranty section; and (4) what is a general checklist of provisions that should be included in a warranty section?

The Licensor's Objectives in a Warranty Section

Licensors typically want to limit what they promise in their warranties as much as possible, and some limit their warranties to the most restrictive warranty possible, which is an "as-is" warranty: The Software is provided "as-is" without any warranties. This type of warranty should never be accepted, and a warranty like this always should be negotiated for greater protections and promises that the software and services will perform.

The Licensee's Objectives in a Warranty Section

At the very least, the licensee's objective in the warranty section should be the following warranties:

- **Title:** That the licensor owns the software or, at least, has a license to use it.
- **Performance:** Simply, that the software will work.
- **Virus:** That the software does not contain any harmful code.

However, there are risks in seeking the bare minimum warranties

listed above. When most licensees see these general warranties, they usually do not negotiate more than what is listed here. Remember, the warranty section is the contract provision dealing with how the software will perform and how the services will be performed. These are very important concepts because a whole host of things can go wrong (*e.g.*, there could be errors, down time, or failure to perform, etc.).

Additionally, licensees must realize that software is an integral part of how a company does business. If the software does not perform in the way the licensee expects, or wants, then it can have detrimental effects to the bottom line of the business. Therefore, there must be a systematic checklist that a licensee can review to make sure they are negotiating the warranty section correctly. There are a number of questions that should be answered by a licensee who is negotiating the warranty section.

Checklist of Questions That Should Be Asked When Negotiating Performance Warranties

1. Does the warranty clearly state the standard to which the vendor is subject (*e.g.*, free from material defects; performs substantially in accordance with end user documentation for software)?
2. Does the warranty specify the time period within which the customer must notify the vendor of any warranty claims?
3. Does the warranty include appropriate exclusions (*e.g.*, exclusions for software errors that cannot be reproduced, which occur in an unsupported hardware and system software environment, or have

- been modified by the customer or any third party)?
4. Does the warranty include appropriate conditions precedent to the vendor's obligation to provide a remedy for failure of performance (e.g., a requirement that the vendor be able to reproduce the error or demonstrate the occurrence or a statement of the costs the customer will be required to bear for fixing the issue)?
 5. Does the warranty include sole and exclusive remedies for breach of warranty (such as "the exclusive remedy for breach of warranty is to fix or repair the software")?
 6. Does the warranty include an alternate exclusive remedy in the event the first remedy fails of its essential purpose (e.g., "refund of the purchase price")?
 7. Typically in a limited warranty section, does the Agreement contain a conspicuous disclaimer of the implied warranty of merchantability and does it also disclaim the implied warranty of fitness for a particular purpose, the warranty of title, or a warranty of non-infringement?
 8. Is there a warranty that the licensor has taken the necessary precautions to excluded viruses?
 9. Are the limitations of liability set forth in a separate section of the agreement from the warranty?

10. Does the agreement contain an acknowledgment by the customer that the purchase price or license fee reflects the negotiated warranty provisions?

Provisions That Should Be Included in a Typical Warranty Section

Based on the answers to the questions in the above checklist, the warranty section should include some of the following warranties. Licensor warrants that:

- The Software shall substantially conform to the Functional Specifications.
- The software or service provider has necessary equipment and trained personnel to perform the services consistent with industry standards.
- The software will be free of material or hidden defects.
- The services will be performed in a workmanlike manner.
- The services will be performed in accordance with industry standards.
- The software or service provider will comply with all applicable laws.
- The software or service provider warrants that it maintains an information security process with physical safeguards appropriate for the sensitivity of customer information.

- The warranty will have a time period, such as thirty (30) to sixty (60) days.

****This is not an exhaustive list****

Remember, warranty sections are contractual promises on how the software or services will perform. It is always important to seek advice from experienced legal counsel in order to understand all the risks involved when negotiating software and service contracts.

Stephen F. Pinson is an attorney at Scott & Scott LLP, a business, intellectual property, and technology law firm, in Southlake, TX. He represents clients involved with intellectual property and technology disputes. Specifically, he assists clients with corporate and technology transactions. He also defends clients in software licensing and copyright infringement matters. Prior to joining the firm, Mr. Pinson practiced in high-stakes securities litigation, regulation, and enforcement actions. He spent the majority of his time prosecuting and defending large corporate clients, institutional investors, and Wall Street firms. Before entering the legal profession, he was a financial analyst for a large international investment bank. He may be reached at spinson@scottandscottllp.com.

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