

TEXAS LAWYER

An **ALM** Publication

texaslawyer.com | JUNE 6, 2016

The Importance of Escrow Agreements in Software and Technology License Agreements

BY JULIE MACHAL-FULKS

SOME OF THEIR MOST integral software applications businesses use are under another party's control.

When each party is upholding its end of the licensing bargain, these relationships can be long-lasting and useful.

But, in some instances, the licensee can no longer access software on which it relies because the licensor is unable or unwilling to continue ensuring meaningful access. When this occurs, the licensee needs a remedy that will actually provide it with some assurance that its business operations will not be interrupted.

The kinds of events that cause licensees to become nervous about the ability of the licensor to deliver or support the critical technology include insolvency, bankruptcy, business discontinuation, loss of data, and litigation.



If one of these events occurs, the licensee must be able to continue its own operations.

One way to minimize the risks inherent in the purchase of technology services is to consider an escrow agreement. There are several types of escrow agreements depending on

how the licensor delivers the technology.

SOURCE CODE ESCROW

Licensees using software solutions on their own premises and hardware should consider whether to include a software escrow provision in the license agreement.

In a typical on-premises solution, the publisher's software is located on the licensee's hardware. The licensee often pays support and maintenance fees to the publisher to ensure that the software is updated to work with later releases of operating systems and newer hardware. The payments usually include access to technical support.

If the publisher stops supporting the product, ceases business operations, or otherwise fails to provide necessary updates for the products, a licensee could lose the ability to meaningfully use the product. When the product is mission-critical, the licensee may not have a good option without an escrow agreement.

A software escrow agreement allows the licensee to request that the escrow agent release the source code of the product to the licensee so that the licensee may, at its own expense, make the necessary adjustments to the software to allow it to operate properly.

These escrow provisions can be especially critical in a software license dispute. Some escrow provisions are so broad they could potentially allow the licensee to request the source code in the event that the publisher attempts to

terminate the software license for alleged breach.

TECHNOLOGY ESCROW

In an on-premises solution, the licensee controls the hardware, and thus, a copy of the software. In that instance, it is often difficult for the licensor to physically restrict the ability to access the licensed products.

When the product is delivered on-line in a cloud or hosted solution, the risks become even greater. The licensor now has control of all of the licensee's data as well as its right to use the software solution.

The licensor can eliminate the licensee's ability to access either the software, or the licensee's data that resides with the provider. In this situation, a strong escrow agreement can provide comfort to the licensee that it will still be able to access the software or its data from the escrow agent in the event that one of the identified triggers occurs.

To ensure that the technology escrow is meaningful and updated, the licensor periodically deposits source code and a copy of the resident data into escrow.

If the licensee makes a legitimate request for the escrowed materials, and if the requisite circumstances exist, the escrow

agent will then release the materials to the licensee. The licensee will then have to find a way to use the source code and data to continue operations.

A technology escrow agreement offers protection for many of these risks for annual costs that typically range from \$1,000-\$5,000, depending on the size and complexity of the service offering and the data retained by the escrow agent.

CONCLUSION

For companies that are considering a new technology transaction, or expanding or renewing an existing technology relationship, part of due diligence should include an evaluation of the risks of using the software, and whether the delivery of the software or data is dependent on the ability of the provider to continue business operations.

An escrow agreement may help minimize the risks associated with lost data or a licensor's intentional or unintended termination of access to the software and data.

Julie Machal-Fulks is a partner in Scott & Scott in Southlake, where she leads a team of attorneys in representing and defending clients in legal matters relating to information technology.