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# Drafting IT Master Services Agreements: Guidance for Purchaser and Vendor Counsel

Defining Project Scope and Obligations, Negotiating Pricing and Payment Terms, Minimizing Risks

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TUESDAY, OCTOBER 7, 2014

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

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Today's faculty features:

Julie Machal-Fulks, Partner, **Scott & Scott**, Southlake, Tex.

Robert Scott, Partner, **Scott & Scott**, Southlake, Tex.

Michael T. Krueger, **Bowles & Verna**, Walnut Creek, Calif.

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# Drafting IT Master Service Agreements

PRESENTED BY:

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# Key Provisions in IT Master Services Agreements

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# Importance of Written Agreements

- Memorializes the parties' obligations
- Identifies potential misunderstandings at the beginning of the relationship
- Contains provisions to protect each parties' rights
- **If Agreements are done correctly, they can be sales tools!**

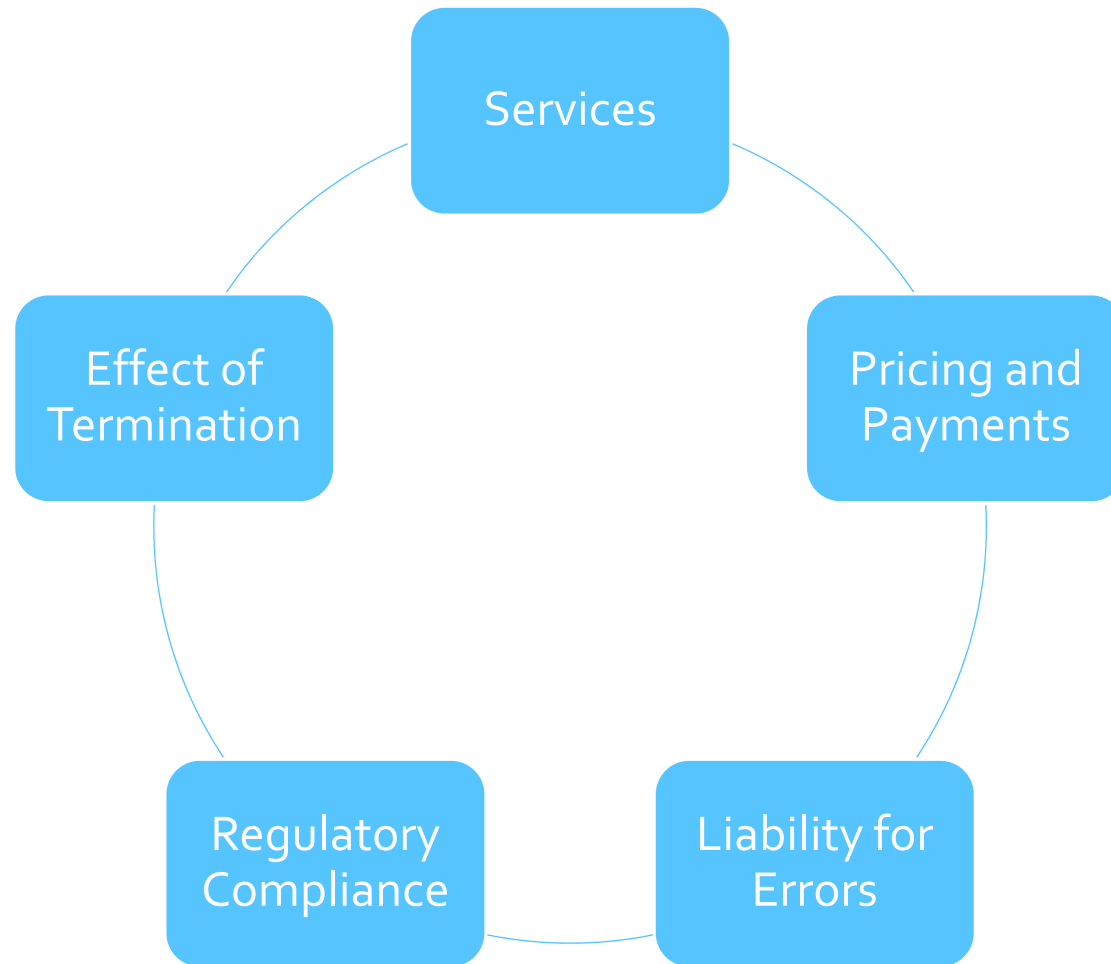


## **Typical End User Concerns That Should be Addressed in the Contract**

- What do I get for my money?
- What will be required from my team?
- How will I be protected?
- What happens if there is a problem with the services?
- Do you have a guarantee, if so what is covered and not covered?



# Key Provisions in Master Services Agreements





# Services

- Important to add services that are included
- Helpful to include a list of services that are excluded
- To keep document sets short, have a Master Agreement that contains general terms and conditions and shorter services agreement that can be included on an as-needed basis
- Identify any assistance that the end user will have to provide (restarting machines, notifying of outages, etc.)



# Pricing and Payments

- Clear and easy to understand pricing terms
- Include information about invoices and due dates
- Consider making pricing an addendum that gets updated once per year
- Keeping pricing section separate allows an increase in pricing without a re-negotiation of all the terms and conditions
- Include provisions for late payments and delinquencies



# Liability for Errors and Omissions

- Provision should cover all types of potential outages – data breach, unscheduled downtime, natural disasters, etc.?
- The provider should have insurance coverage in an appropriate amount
- If the customer possesses provider-owned equipment, it needs to be covered
- What is the limitation of liability?



## Regulatory Compliance

- Provisions should address major regulatory requirements that impact the end users' businesses
- Document the processes and procedures developed to protect client information
- Price the services after considering costs of compliance with regulatory requirements and still make a profit



# Effect of Termination

- How will any data be transferred from provider back to the end user?
- Will there be a charge for the transition?
- If so, what will the charge be?
- Can provider remove access to hosted servers without notice?
- Is it clear how access can be restored?



## Importance of Legal Review

- Always advisable to get input from an attorney
  - Familiarity with / ability to research applicable law
  - Check for consistency across client-facing and other documents

# Purchaser Considerations

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# Risks Inherent in IT Relationships

- Business Continuity Risks
  - Service interruption
  - Post-termination data rights
- Regulatory Compliance Risks
  - Data privacy and security statutes
- Intellectual Property Risks
  - Use and disclosure of information
  - Ownership of software
  - IP ownership at termination
- Liability Risks



# Business Continuity Risks

- Service Interruption – define service levels, metrics, and remedies in the SLA
- Termination of the Agreement – ensure data is owned by and returned to customer in a usable format upon termination



# Intellectual Property Risks

- Use and disclosure of information
  - Ensure both parties understand the nature of the data stored in the cloud
  - Specifically personally identifying information and trade secrets



# Intellectual Property Risks

- Intellectual property ownership
  - Define ownership of any software customizations
  - Exclusivity of customizations during term of engagement
- IP ownership at termination – work for hire or vendor-owned code



# Regulatory Compliance Risks

- Industry-specific regulation
  - FTC Red Flags Rule – Financial
  - Gramm-Leach-Bliley Act – Financial
  - HIPAA & HITECH – Healthcare
  - PCI Compliance – Payment Systems
- Broad regulation – Massachusetts Data Privacy Law



# Liability Risks

- Risk Balancing
  - Vendors disclaim all liability – this is unacceptable to the customer
  - Insurance as a tool for risk balancing
  - Indemnity as a tool for risk balancing



# Liability Risks

- Striking the Balance
  - Specifically address liability issues regarding data risks
  - Risk should be commensurate with the value of the cloud service



# Risk Mitigation Strategies

- Require vendors to legally assume all liabilities associated with the service
- Specify insurance coverage requirements including forensics, breach response, regulatory response and consumer claims
- Use indemnity provisions to protect against liability
- Edit limitation of liability provisions that would limit access to coverage



# Vendor Considerations

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# Drafting IT Master Services Agreements

## Key areas of concern for Vendors in IT Master Services Agreements

1. Do you have the correct parties signing the agreement?
2. Is the Statement of Work (SOW) accurately reflecting the engaged services?
3. Is the Term and Termination clear?
4. When does your client get paid?
5. Who owns the IP?
6. Is your client protected?

## 1.) Do you have the correct parties signing the agreement?

THIS MASTER SERVICES AGREEMENT (the “*Agreement*”) is made and entered into this 7th day of October, 2014, by and between ABC Apps, LLC, a California limited liability company (hereinafter referred to as “*Service Provider*”) and Tech Savvy Realtors, Inc., a Delaware corporation (the “*Company*” and collectively “*Parties*” and each a “*Party*”).

# 1.) Do you have the correct parties signing the agreement?

- Signature Page

IN WITNESS WHEREOF, the Parties have executed this Agreement as of the Effective Date.

Service Provider  
ABC Apps, LLC  
A California limited liability company  
corporation

Company  
Tech Savvy Realtors, Inc.  
A Delaware

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ABC Apps, LLC  
By: Mary Member  
Its: Managing Member  
President

Tech Savvy Realtors, Inc.  
By: Bob Boss  
Its: CEO and



## **1.) Do you have the correct parties signing the agreement?**

- This item seems too obvious to necessitate its own slide in a CLE. However, many of the vendors that retain our firm end up in sticky litigation issues because they were not consistent in signing agreements, they failed to sign on behalf of their own entity, the individual signing on behalf of the client had no authority to sign, or the owner of the entity cancelled the entity under the name a lawsuit was initiated believing the vendor agreement was his own personal services agreement.

## 2.) Does the Statement of Work (SOW) accurately reflect the engaged services?

- This is a typical layout of the scope of services in an IT MSA.
- The assumption is that your client is going to be providing a lot of services for a lot of different clients. Your client would prefer to only pick up the phone to call you when this agreement needs to be modified.
- The best result you can provide your client is a strong agreement where only the services, term and fees change with each new client.

### ARTICLE 1 SCOPE OF SERVICES

1.1 **Description of Services.** Service Provider shall perform for the Company the services described in Exhibit “A”, Scope of Services, attached hereto and incorporated herein by this reference (hereinafter, the “*Scope of Services*”).

1.2 **Additional Services.** The Company may request Service Provider to perform additional services not covered by the specific Scope of Services set forth in this Agreement, and Service Provider shall perform such services and will be paid for such additional services when they are mutually agreed to and made part of this Agreement by written amendment.

## **2.) Does the Statement of Work (SOW) accurately reflect the engaged services?**

1. Planning & Discovery Phase
2. Content Guidelines/Deliverables
3. Development Milestones/Projected Dates

It is your responsibility to ensure that the services your client will be providing the client are included in this agreement, and no additional services.

Depending on the type of IT your client is providing, the SOW will be broken into different phases. However, these four steps are typically universal

## 2.) Does the Statement of Work (SOW) accurately reflect the engaged services?

- Planning Discovery Phase

If your client is engaged to identify a specific problem with a system, this section may be the entire scope of services. However, this is where a lot of clients can run into issues if they don't have the scope of services clearly identified.

In this example my client was utilizing LabVIEW software to improve a camera function on a device and improve the user interface. The first two phases were to identify the issues.

CONSULTANT will provide software engineering services to Client on improving and further developing the LabVIEW software for a Client design qualification system that allows R&D and manufacturing quality assurance staff to manually perform visual inspections for defect characterization of the Product consumables.

The project will be performed in two phases

### **Phase I - Upgrade software to support new camera**

2.1 CLIENT will provide CONSULTANT with a camera and PC (with Camera Link card installed) for testing driver at CONSULTANT'S location.

CLIENT will provide SVN access to source code to CONSULTANT developer(s) working on the project. Goal is to update driver and integrate changes with Scan and Sample Filling applications.

### **Phase II - software user experience improvements**

3.1 CONSULTANT will work with CLIENT to identify improvements for the software user experience for operators in manufacturing support roles. CONSULTANT will create user interface mockups and will review code to identify high value areas of the application for improvements. The list of changes will be captured and prioritized with CLIENT so that only changes that CLIENT specifically requests will be implemented in this phase.



## 2.) Does the Statement of Work (SOW) accurately reflect the engaged services?

- Content Guidelines

Content guidelines is another area where the client can get into some issues that will spark the Intellectual Property ownership issues.

I recommend that my clients identify their use of reuse libraries or any other stock products to protect them from IP disputes and content guidelines. The use of reuse libraries significantly reduces the amount of time a client will spend on implementing IT services rather than create all new code.

### Reuse libraries

#### 4.1 **Using CONSULTANT reuse libraries with a prior written consent from CLIENT**

4.1.1 CONSULTANT will (potentially) use it's own software libraries and frameworks as well as third party libraries and frameworks to deliver to software deliverables upon written prior approval from Client. Applicable CONSULTANT software license agreement or third party software license agreement will be used to cover the usage of the libraries and frameworks.

## 2.) Does the Statement of Work (SOW) accurately reflect the engaged services?

It is important to identify the time frame in which a project must be completed. Depending on the size of the project, the timeline could dictate if your client will be paid timely, a reduced fee or if the delay will be considered a material breach.

- Development Milestones/Projected Dates
- So long as CONSULTANT has delivered the completed deliverables bi-weekly time sheets for a project milestone on or before the milestone date (and CONSULTANT's deliverables time sheets fully conform to the performance benchmarks for said deliverables as set forth in this Schedule and the Appendices hereto), then CLIENT shall pay to CONSULTANT the invoice for said milestone time sheet at the full COMPENSATION RATE specified above.

### 3.) Is the Term and Termination clear?

This section has been raised by different jurisdictions where service providers must be given written notice of termination pursuant to state laws that supersede the agreement.

These sections are appropriate in an IT MSA because the termination is not confusing, it is clear how each party may terminate and requires all termination notices to be delivered in writing and the date upon which termination is effective.

- Termination by Client upon 30 days notice; or
- Termination by either PARTY by delivery to the other PARTY of a written notice of termination in the event that the latter PARTY is in breach of any obligation under this AGREEMENT and has received written notice thereof and has failed to cure such breach within the time period specified in such notice of breach, which time period shall not be less than 15 days; or.
- Termination by either PARTY by delivery to the other PARTY of a written notice of termination in the event that a Force Majeure event, which extends to the performance by one of the parties hereto of all, or substantially all of such party's obligations hereunder, continue for more than sixty (60) days as provided in Section 11.12 below

### 3.) Is the Term and Termination clear?

These terminating clauses are not appropriate in an IT MSA because they can be misleading.

- Avoid automatically renewing clauses
- Avoid termination language where the termination date is uncertain
- These two sections raise issues because the termination date or expiration date may be defined elsewhere in an agreement.
- The term of this Agreement shall commence on the Effective Date and shall expire on December 31<sup>st</sup> (the "Initial Term"), and shall automatically renew for successive one (1) year terms (each of which, and "Extended Term"), unless the Agreement is terminated pursuant to section VI of this Agreement, or a party provides written notice to Client no less than ten (10) days prior to the expiration date that it does not wish to renew.
- Either party may terminate this Agreement, with or without cause, by giving written notice of termination to the other party at least ten (10) days prior to the termination date, by registered or express mail, return receipt requested.

## 4.) How does your client get paid?

This section should be simple and straight forward. I do not like to have this section too wordy because it is referencing invoice timetables and additional schedules. Remember that the benefit of the MSA structure is the flexibility of changing out the SOW and Fee Tables while maintaining the structure and content of the Master Agreement itself.

- **4.1 Consulting Fee.** CLIENT shall pay CONSULTANT pursuant to the compensation rate and invoicing timetable set forth in Schedule 1.
- **4.2 No Additional Compensation.** CONSULTANT acknowledges and agrees that the sole and sufficient compensation for CONSULTANT's consulting services under this AGREEMENT shall be the payment by CLIENT of the compensation set forth in Schedule 1 and that CONSULTANT shall receive no other compensation for such consulting services.

## 4.) How does your client get paid?

Additional services and expenses should be included in the Master Agreement, but again, keep this section simple and reference the attached schedules.

**Compensation Upon Early Termination.** In the event of termination of this AGREEMENT prior to the term hereof or any extension thereof, CONSULTANT shall be entitled only to the compensation payable to the date of termination and CONSULTANT shall not be entitled to any compensation after such date.

**Expenses.** CLIENT shall reimburse CONSULTANT for reasonable out-of-pocket expenses incurred by CONSULTANT while traveling away from CONSULTANT's above-written address in connection with the consulting services, provided such expenses itemized and supported by appropriate receipts.

## 4.) How does your client get paid?

### A. Compensation Rate.

This section is often negotiated between the vendor and the customer prior to an attorney's involvement if the vendor is bidding a project. However, that does not mean that everything was discussed prior to the attorneys getting involved. Prior to reviewing this section for my client there were ten other provisions that would go into effect in the event the client was late on work product. We addressed those issues in other sections of the agreement, but it would create ambiguity as to the rate of pay if several different rates were listed here.

CONSULTANT shall be paid at a rate of \$100 per hour for each full hour of work performed for CLIENT on the projects listed in this Schedule and the Appendices hereto (the "COMPENSATION RATE"). Work performed by CONSULTANT on any additional projects within the CONSULTING PERIOD shall be compensated at the same COMPENSATION RATE. CONSULTANT shall be paid at the COMPENSATION RATE for time spent during visits to CLIENT and other sites if such visits are requested and pre-approved by CLIENT.

#### **Payments.**

#### **On Time Delivery of Work Product.**

If CONSULTANT has delivered the completed bi-weekly time sheets and CONSULTANT's time sheets fully conform to the performance benchmarks for said deliverables as set forth in this Schedule and the Appendices hereto), then CLIENT will pay to CONSULTANT the invoice for said time sheet at the full COMPENSATION RATE specified above.

## 5.) Who owns the IP?

The important part to remember is that if you do not identify the proprietary information or products that your client is bringing into the services your client is at risk of issuing a license to use that information or product.

Each party hereby acknowledges that, except as expressly provided in this Agreement, it does not have, and will not acquire, any interest in any of the other party's products, technology or Intellectual Property Rights as a result of this Agreement or the performance of any obligations hereunder.

The Consultant Technology is the exclusive property of Consultant, and Consultant retains all right, title and interest, including all Intellectual Property Rights relating thereto (subject to the licenses granted in Section 4.2.1 and 4.2.2 of this Agreement), including all such rights in or to any enhancements, updates, modifications, changes or derivatives thereof or thereto made by or on behalf of either party.

Consultant Reuse Libraries Consultant grants to Customer a limited, worldwide, fully-paid, non-exclusive, irrevocable license (unless terminated for breach) to use, copy, and modify the source code version of the Reuse Libraries solely for Customer's internal software development purposes.



## 5.) Who owns the IP?

Remember that your client is a service provider. The additional licenses may be avenues of additional services and revenue.

- Except as specifically provided in herein or in the Statement of Work, no other license to, or right in the Technology is granted to Customer under this Agreement. Any license from Consultant to Customer of the Technology other than the Reuse Libraries shall be provided under a separate software license agreement between Consultant and Customer. Customer will not incorporate Consultant's Technology other than the Reuse Libraries within the scope of Services or related deliverables under this Agreement without the prior written consent of Consultant.

## 6.) Is your client protected?

Indemnification clauses are the tip of the iceberg, but they should be in every MSA.

I typically try to use indemnification agreements that require the Consultant to look to any insurance policies in place prior to triggering any indemnification clause, but those don't always apply in smaller companies. It is also important to weigh the cost/benefit of mandatory insurance policies for IT services.

- **Obligations.** Each of us (“Indemnitor”) shall indemnify, defend and hold the other (and its affiliates, employees and agents) (“Indemnitee”) harmless against all losses, damages, claims, liabilities, and expenses (including reasonable legal fees) (each a “Claim”) resulting from Indemnitor’s breach of this Agreement, negligent acts or omissions, or willful misconduct in performing under this Agreement. Each of us is responsible under this section for the actions of its employees, agents, and subcontractors. Neither of us will be responsible under this section to the extent a Claim resulted from the other’s breach, negligence, or willful misconduct.
- **Procedures.** Indemnitee must notify Indemnitor within 10 days after learning of a Claim. Failure to notify within 10 days will not affect the right to indemnification unless Indemnitor can show harm caused by the late notice. Indemnitor may take over the defense of a Claim by notifying Indemnitee. In that case, Indemnitee shall not admit liability or settle the Claim. If Indemnitor chooses not to take over an indemnified Claim, then it must pay the Indemnitee’s external counsel’s fees and expenses. Indemnitor will pay indemnified Claims within 15 days of Indemnitee’s written demand for payment. Any indemnification payment not made when due will bear interest at the annual prime rate as published by the Wall Street Journal (or other publication specified in the relevant APD) on the payment due date, for each day from due date until paid.

## 6.) Is your client protected?

Your client might not have any services that will require a warranty, but typically the service provider is also selling a maintenance package for ongoing services. In these circumstances the limitation of liability might not be feasible, or could terminate the ability of the client to provide future services.

### **WARRANTY AND LIMITATION OF LIABILITY.**

Consultant warrants that any Services provided to Customer under this Agreement will be consistent with generally accepted industry standards. This warranty shall be valid for ninety (90) days from performance of the applicable Services. If after the expenditure of such reasonable efforts, Consultant is unable to correct the Services such that they comply with the foregoing warranty, Customer may, at its option, terminate such Services and, Consultant, in full satisfaction of all Customer's claims relating to such noncompliance, shall refund the pro rata portion of the fees Customer has paid with respect to such nonconforming Services.

Consultant warrants that the Reuse Libraries as originally delivered by Consultant to Customer consist of original works of authorship or works with respect to which the copyrights (or license rights thereto) have been assigned to Consultant. Consultant further warrants that, to Consultant's actual knowledge, the licenses granted to the Reuse Libraries as originally delivered by Consultant to Customer do not infringe the copyright or trade secret rights of any third party.

## 6.) Is your client protected?

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# Panel: Anticipating Common Drafting Issues and Streamlining Negotiations

MODERATOR: ROBERT J. SCOTT

PANEL: MICHAEL T. KRUEGER  
AND JULIE MACHAL-FULKS



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# Q&A

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# *Thanks.*

Please join us for our next conference, “Drafting Indemnification and Hold Harmless Provisions in Commercial Contracts - Negotiating Scope and Exclusions, Overcoming Enforcement Hurdles, Navigating Interplay With Insurance Coverage,” scheduled on Tuesday, October 14, 2014 starting at 1pm EDT.

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