Legal Risks in Reseller Relationships
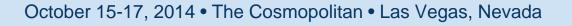
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- Who needs SPLA?

- What is "commercial hosting"?

- Licensing alternatives for commercial hosting rights

- Defending SPLA audits

- Estimating SPLA-audit exposure

- Negotiating SPLA-audit settlements

Who Needs SPLA?

- Licensing model originally released in 1999
- Standard retail and volume licensing terms prohibit the use of MS software for "commercial hosting services"
- Primary purpose of SPLA-licensed products must be the delivery of hosted or rental software services
- Typical SPLA customers:
- Data hosts (HaaS, website hosts, file-sharing)
- Application providers (hosted BDR, hosted CRM, hosted messaging)
- Scott & Scott LLP
- Allows businesses to license MS products on a month-to-month subscription basis, rather than committing to an up-front license purchase

What is "commercial hosting"?

Microsoft:
"*You may not host the products for commercial hosting services.*"
(Product Use Rights, *et al.*)

- Standard-form EULAs and Product Use Rights do not define "commercial hosting services"

- Additional guidelines in the form of licensing briefs, charts, etc. may not be directly enforceable against MS, but:
  - they often help to illustrate more subtle licensing concepts, and
  - if a court were to determine that the agreements are ambiguous, they likely would be admissible as extrinsic evidence regarding intent

- Example: SPLA Qualification Road Map
  - Flowchart to help guide licensing decisions for Microsoft products
  - Last revision in 2011

SPLA Road Map Core Questions

Assuming non-anonymous third parties are accessing the hosted solution, the most critical questions pertaining to "commercial hosting" for most businesses are:

#4: "*Is the licensee providing access to software application(s) used for third party business operations?*"
    (Data or applications?)

#5: "*Is the third party using the software application as a way to acquire goods or services from the licensee?*"
    (Means to an end? Example: Amazon.com)

#7: "*Does the licensee own the business logic, content, or data and deliver the service under its own brand?*"
    (Outsourcer?)

SPLA Road Map Guidance

Microsoft's guidance regarding licensing scenarios:

#4
"_Scenario Yes:_ _Company A provides a software application for Company B to use._"
"_Scenario No:_ _Company A hosts Company B's website._"

#5
"_Scenario Yes:_ _Customers of ABC Bank use the bank's online banking service, which is built on Microsoft software products, to conduct their banking online._"
"_Scenario No:_ _Company A provides a customer relationship management (CRM) application for Company B to support its customer engagements._"

#7
"_Scenario Yes:_ _A travel company with an online presence is using its own brand to sell its travel services._"
"_Scenario No:_ _Company A is a travel company with an online presence that delivers a corporate travel portal branded in the name of Company B._"

SPLA Road Map Outcomes

Three principal outcomes for most businesses:

Internal Use
Third-party access (if any) is anonymous / unauthenticated
No external client licensing is required

Internal Use with External Connectors
Third-party access requires client licensing (CALs, ECs or processors)
Services do not require "commercial hosting" rights

"Commercial Hosting"
Third-party access requires client licensing
That access requires "commercial hosting" rights via SPLA **or** via Self-Hosted Applications
benefit with Software Assurance

Self-Hosted Applications

- Benefit <u>included with Software Assurance</u>, but requirements are specific:

- Available only for products for which product-specific terms in the PUR state:
  "*Self-Hosting of Applications Allowed: Yes*" (Note: SQL Server and Windows Server <u>are</u> included)

- MS products must be used exclusively in connection with a "Unified Solution"

- Licensee's software must:
  - *add significant and primary functionality to the Self-Hosted Applications that are part of the Unified Solution (**dashboards, HTML editors, utilities, and similar technologies are not a primary service and/or application of a Unified Solution**);*

(continued next page)   **January 2013 Product Use Rights, Appendix 2**

(continued)

- Licensee's software must:
  - *be the principal service and/or application, and sole point of access, to the Unified Solution;*
  - *be delivered over the Internet or a private network from your datacenter to end users. The Self-Hosted Applications component may not be loaded onto the end user's device; and*
  - *be owned, not licensed, by you, except that your software may include non-substantive third party software that is embedded in, and operates in support of, your software*

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<u>All client access must be licensed</u> (*i.e.*, licensee still is required to purchase CALs, ECs and/or processor licenses)

Example: Provider writes a file-sharing application running on Windows Server hardware and incorporating a SQL Server database.

SPLA License Types

If the business chooses to pursue SPLA, it is necessary to choose between two principal SPLA license types:

Subscriber Access Licenses (SALs)
- Assigned to authorized users
- Permit unlimited software deployments, as long as they are accessed only by users to whom SALs have been assigned
- Require strict, centralized server administration (to avoid unauthorized access) and the ability to accurately measure access

Processor Licenses
- Assigned to hardware
- Permit access by an unlimited number of users to each properly licensed server
- More expensive and can entail somewhat more complicated accounting, but much easier to administer

Defending SPLA Audits

Newer SPLAs and Microsoft Business Agreements / Business and Services Agreements grant Microsoft broad audit rights.

Critical initial steps:

- Examine the signed agreements to confirm that the scope and entity(ies) identified in the audit notice letter are correct

- Obtain an agreement from Microsoft and its auditors (usually Deloitte, PwC, KPMG or E&Y) regarding the confidentiality of the audit data and the process to be followed during the audit

Estimating SPLA – Audit Exposure

SPLA-audit exposure sources:

- Past unreported software usage / extrapolated counts
- "Roll-forward" findings
- Penalty percentage
- Inspection fees

Past exposure can be difficult to estimate:

- Absent historical data, extrapolation factor typically applied to audit "snapshot"
- Active Directory user counts often used as basis for calculated SAL requirements
- Licensing models may have changed over time (*e.g.*, Windows Server)

Negotiating SPLA – Audit Settlements

Before negotiating on amounts, it is critical to establish factually accurate assumptions underlying the compliance costs.

Settlement terms:
- Installment payments
- Release of liability
- Audit forbearance
- Confidentiality

Consequences of not settling:
- Termination of SPLA (switching costs)
- Litigation (possible injunctive relief)

QUESTIONS?