H. Ward Classen

Mr. Classen has been Assistant General Counsel of Computer Sciences Corporation since November 1996 and was General Counsel of CSC Intelicom, Inc. from December 1990 to March 1998. He was previously Associate General Counsel and Assistant Secretary for International Mobile Machines Corporation (now Interdigital Corporation) from 1987 to 1990, and an Associate with Weinberg and Green (now Saul, Ewing) from 1985 to 1987. He has a Bachelor of Arts in economics from Trinity College (Connecticut); a Juris Doctor of law from Catholic University; and a Master of Business Administration from the Wharton School of the University of Pennsylvania. Mr. Classen was a member of the *Catholic University Law Review* and Editor in Chief of *The Journal of Contemporary Health Law and Policy.*

Mr. Classen serves on a number of business, professional and civic boards, including the Editorial Board of *Business Law Today,* the Board of Advisors of *The Intellectual Property Counselor*, as well as *The Commercial Law Advisor*, and is an Adjunct Professor at the University of Baltimore Law School. He is the author of the three volume set *Classen's Commercial Forms* as well as *Classen's Merger and Acquisition Forms*. Mr. Classen has written and spoken extensively in legal journals and before professional groups both domestically and internationally. His recent articles address technology licensing, export controls, law department management and managing inside/outside counsel relationships.

FUNDAMENTALS OF SOFTWARE LICENSING

Fifteenth Annual Advanced Licensing Institute
Franklin Pierce Law Center

H. Ward Classen, Esq.

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License vs. Sale

- The First Sale Doctrine
  - The purchaser of a copy may use such copy for what ever purpose it likes (i.e. use, re-sell, etc.). (17 U.S.C. §109(b))
  - The first sale doctrine does not apply when software is licensed rather than "sold".



License vs. Sale

- Transfer of Intellectual Property Rights
  - License: A license provides for a transfer of *limited* rights. *An exclusive license is an assignment of the copyright but only to the extent granted in the license.*
  - Assignment: An assignment transfers ownership.



Grant of License

- Terminology of the License Grant:

"Subject to the provisions of this Agreement, Licensor grants to Licensee a perpetual, personal, non-assignable, non-transferable, non-exclusive object code license to use the Software solely for Licensee's (and its Affiliates?) internal business purposes in the United States."



Terminology of the License Grant

- Use of Software
  - Definition of the "Licensee/Licensor" and "Affiliates"
    - limit definition to restrict use of software
    - list Affiliates to avoid disputes
    - consider export issues
    - Who is the Licensor?



Terminology of the License Grant

- Term of License
  - should begin on delivery of the software
  - length of term not always significant as most software is obsolete within 10 years, i.e. perpetual vs. a term of years
  - if no term stated, under Copyright Act term will be either 75 years from year of first publication or 100 years from year of creation, whichever expires first (17 U.S.C. §302(c))



Terminology of the License Grant

- Use Restrictions
  - for Licensee's internal business purposes only
- Protect against
  - service bureau use (BPO)
  - outsourcing
  - access by third party consultants



Terminology of the License Grant

- Assignability/Transferability
  - Depending on the type of license granted, the Licensee may or may not be able to assign the license.
  - If the license is non-exclusive, it is not assignable unless the license agreement expressly provides otherwise. If the license is exclusive, it will generally be assignable if it resembles an assignment of the underlying intellectual property (i.e. copyright).
  - An exclusive licensee is considered to be a copyright owner only to the extent of the exclusive rights granted by the license (17 U.S.C. §201(d)(2))



Terminology of the License Grant

- Payment/Performance
  - Is a guarantee needed to ensure payment by Licensee or performance by Licensor?
  - Tax issues
    - Corporate address
    - Delivery address



Terminology of the License Grant

- Geographic Restrictions
  - Pricing Issues
  - Export Considerations
  - Intellectual Property Rights Indemnification



Terminology of the License Grant

- Object Code and Source Code Licenses
  - If a source code license is granted, the Licensee can only use one copy of the source code.
  - Third parties (i.e. contractors, customers) should not have access to the source code/software.
- Non-exclusive license
- Is exclusivity important to Licensee?
  - Competitive advantage
  - Payment for development



Representations and Warranties

- Representations create legal risk of fraud claims regarding the licensor's sales puffery (tort).
- Warranties give rise to liability for damages equal to the value of what was not delivered (contract).



Standard Warranties

- Licensee's Perspective
  - Licensor has authority to enter into agreement
  - Agreement does not conflict with any other obligation of Licensor
  - All work performed in a professional and workmanlike manner
  - Software will not infringe on any third party intellectual property rights
  - Software will contain no virus' or trap doors, etc. (knowledge representation vs application of virus/spy ware program)
  - Licensor owns software or has right to grant license
  - No open source code



Standard Warranties

- Licensor's Perspective
  - Licensee has authority to enter into agreement
  - Agreement does not conflict with any other obligation of Licensee
  - Licensee has the ability to pay all amounts when due



Warranty Disclaimer

- **Both Parties** should disclaim all warranties except those expressly made in the license agreement. (UCC §2-316)
- Warranty disclaimers relating to merchantability must be in writing, be conspicuous and contain the word "merchantability." The UCC also requires that warranties relating to fitness for a particular purpose be conspicuous and in writing. (UCC §2-316)
- UCITA has different requirements.
- Include an "Integration" clause.



Warranty Disclaimer

- **Both Parties** should disclaim liability for special, incidental and consequential damages. (UCC §2-719)
- Licensors should provide for an exclusive remedy of a monetary refund if a "repair or replace" remedy fails in its essential purpose. If not, a court may void the licensor's exclusion of consequential damages.
- Licensor should clearly state software will not be error free.



Length of Warranty

- Licensees should seek a warranty that begins on date of acceptance rather than on the date of shipment or installation.
- Licensors should avoid granting long warranties, and alternatively provide XX months of free maintenance under a separate maintenance agreement.



General Indemnification

- Usually covers **only** personal property damage and personal bodily injury
- Potentially allows recovery in a contributory negligence jurisdiction and recovery of legal fees
- Licensor should not agree to indemnify for negligence especially for third party claims



Intellectual Property Indemnification

- Limited to:
  - a specific licensee
  - existing U.S. intellectual property (copyright the exception)
- If infringing, Licensor at its option should:
  - make non-infringing,
  - obtain 3rd party license or
  - provide comparable software
- In full satisfaction of all liability (otherwise unlimited liability)
- If impracticable, the right to grant refund, which may be prorated for time of use
- Licensee must have right to assume defense if Licensor fails to do so



Limitation of Liability

- Consequential/Special/Indirect punitive damages should be disclaimed.
  - Parties can not limit consequential damages for personal bodily injury in consumer transactions. (UCC §2-719(3))
- **Both Parties** should limit liability
  - **Licensor - to amount received**
  - **Licensee - to multiple of amount payable by Licensee**
- Limit on damages usually does not apply to:
  - intellectual property indemnification (subject to exclusive remedy)
  - personal bodily injury and personal property damage
  - breach of the confidentiality provisions
  - payment obligations of customer
- Any damage limitations can not be unconscionable
- Reduce Statute of Limitations (usually to two years)



Significant Clauses

- Breach and Termination
  - Licensor needs minimum 30 day cure period.
  - Licensee is entitled to 30 day cure period except for misuse of software.
  - All breaches which justify termination must be material breaches.



Remedies

- Licensor Remedies
  - Termination of Agreement
  - Recovery of Monetary Damages
  - Attorney's Fees
  - Equitable Relief
    - Injunctive Relief
    - Self Help



Remedies

- Licensee Remedies
  - Termination of Agreement
  - Recovery of Monetary Damages
  - Equitable Relief
    - Injunctive Relief
    - Specific Performance
  - Right of Set Off
  - Transition Rights
  - Cover
  - Access to Source Code
  - Access to Licensor Employees and Contractors
  - Attorney's Fees



Significant Clauses

- Governing Law and Forum
  - New York favors Licensors.
  - Texas favors Licensees.
  - Has UCITA been adopted?
  - Compromise: Choice of forum decided by the party who does not initiate the legal action to discourage the parties from bringing claims.
  - Governing law in international transactions should be laws of United States, England and Wales (UK) or Sweden.



Alternative Dispute Resolution (ADR)

- ADR vs. Judicial System
  - Arbitration
    - Potentially quicker, but defendant can delay progress
    - Not viable for some issues such as indemnification and violation of confidentiality provisions; opt for judicial relief in those cases
  - Mediation
    - Usually suited for performance issues
  - Judicial System
    - Right to injunctive relief
    - Lack of privacy



Arbitration Necessities

- Scope of Disputes to be Arbitrated
- Number of Arbitrators
- Qualifications of Arbitrators
- Arbitration Rules
- Administrated v. *ad hoc* Arbitration
- Place of Arbitration



Escrow Agreements

- Licensor's Perspective
  - Source code held by Licensor
  - If source code held by third party, Licensee pays all costs
  - Released only upon Licensor's proven non-performance
  - Released subject to license terms
- Licensee's Perspective
  - Source code and documentation held by independent third party
  - Source code and documentation updated quarterly
  - Released immediately upon qualifying events
  - Access to Licensor's employees
- Reality: Source code alone will not allow Licensee to fully operate the software.



Other Issues to Consider

- Work Made for Hire Doctrine
  - General Principle: Unless the work performed by an independent contractor falls into one of nine enumerated exceptions, the copyright will be owned by the independent contractor. The employer will be deemed to have a non-exclusive license unless the contractor assigns its rights to the employer. Community for Creative Non-Violence v. Reid, 490 U.S. 703(1989).



Other Issues to Consider

- Ownership of Custom Developed Software

  4 Possibilities:

  - Licensor owns custom software/enhancements - licensee has limited license (licensor may or may not have the right to license with or without royalties).
  - Licensee owns custom software.
  - Licensee owns custom software with licensor having the right to re-license, with or without payment of royalties to licensee.
  - Licensor and licensee have joint, unrestricted ownership. (with or without the obligation to account to the other)



Other Issues to Consider

- Functional Specifications
  - incorporation of RFP and RFP response
  - should be very detailed and complete
  - agreed to prior to contract signature
  - Must be easily understood by independent third party (i.e., judge, jury or arbitrator)
- Acceptance and Acceptance Test Procedures
  - initial draft should be completed by licensor
  - should be as detailed as possible
  - "substantial" compliance issue
  - should be used in conjunction with service levels



Other Issues to Consider

- Liquidated damages
  - good faith estimate of damages suffered
  - unreasonably large amounts void as penalty
  - usually agreed to for late delivery
  - Licensor: should be tied to delivery not acceptance as Licensee controls acceptance
  - Licensee: should be tied to acceptance as Licensor may deliver bad code just to avoid damages
  - make mutual
  - If one party seeks to collect, it will most likely ruin the parties' relationship



Other Issues to Consider

- Customer Obligations
  - payment
  - provide support and assistance
  - site ready for installation (hardware, third party software, electricity, A/C, skilled/trained employees)
  - other special obligations (visas, etc.)



Other Issues to Consider

- Maintenance
  - minimum period in which to offer
  - maintain two most recent releases/versions
  - release of source code if maintenance no longer offered or breach of maintenance agreement
  - cap on annual price increase
  - use of separate agreement



Proprietary Information Clauses/Agreements

- Term: Seven years from the later of date of last disclosure or when licensor is no longer marketing the proprietary information.
- Software: All software shall be considered proprietary and confidential regardless of whether it is marked proprietary or confidential.



Uniform Computer Information Transaction Act (UCITA)

- NCCUSL drafted and approved in July 1999 a new uniform act, the Uniform Computer Information Transactions Act (UCITA)
- Enacted in Maryland effective October 1, 2000 and enacted in Virginia effective July 1, 2001
- Revised by NCCUSL in 2002 to address pro-licensor concerns



Uniform Computer Information Transaction Act (UCITA)

- UCITA is intended to govern all transactions involving "computer information"
- UCITA provides for:
  - express recognition of electronic records
  - Implied warranties
  - Provision of default rules
  - Exclusive license
  - Transferability
  - Self help under controlled circumstances
- A number of its provisions differ significantly from the UCC and common law. Carefully consider any decision to accept UCITA.

