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Software Licensing

by LONNIE FINKEL

INTRODUCTION

Software has transformed the way we conduct business and is quickly transforming the way we live our lives. It runs many of the devices we use every day—from the computers we use to gather and disseminate information via the Internet, to the personal digital assistants and telephones we use to communicate with colleagues and friends, to the cars we drive, to the coffee makers we use to prepare our morning coffee, to the toys our children use to learn basic language skills. The design, development, reproduction, marketing, maintenance, and servicing of software is extremely expensive. The need to develop new generations of software to satisfy customers' demands and remain competitive in the marketplace increases costs and results in constant pressure to reinvest revenues back into software companies.

The principal method software companies use to generate revenue is to license their software. By licensing on a nonexclusive basis rather than selling its software, a software company can grant to multiple licensees the right to use the software in exchange for a fee from each licensee.

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At the same time, the software company retains complete ownership of all proprietary rights embodied in the software, which in turn allows it to license the software to additional licensees and thus generate additional fees. If a software company chose instead to sell its software, it would transfer some or all of its ownership interest in the software on consummation of the sale and lose the right to exploit the software, or at least those transferred rights, for further financial gain.

There are many types of software licenses in use in commerce today. One-size-fits-all shrink-wrap licenses are used to license software purchased off the shelf at computer retail stores by individuals and small businesses. Customized license agreements negotiated by corporate customers are used to license more complex software that can be tailored to an enterprise's specific needs, installed on multiple computer terminals, and used by numerous end users at the licensee's facilities. Joint software development agreements are even more complex license arrangements frequently entered into by technology companies for the purpose of developing a completely new software product or technology in which each of the participating companies will have an ownership interest.

The Computer Software Act of 1980 explicitly applied the Copyright Act to computer programs, and added a definition of "computer program" that encompasses software.

This article first discusses the law that applies to license agreements entered into in California, focusing on the federal Copyright Act (17 USC §§101–1101) and state contract law. To the extent that software developers have sought to protect their products under federal law, they have most frequently sought protection under the Copyright Act. Although software can be protected and licensed under federal patent law, historically most software has not been patented. While software can be protected as a trade secret under California's Uniform Trade Secrets Act (CC §§3426–3426.11), pure trade secret licenses are rare. Second, this article discusses the major differences between exclusive and nonexclusive licenses, and object code and source code licenses. Third, the article provides a form of license agreement that can be used as a template to prepare a software license. In setting forth the license provisions, the article discusses and offers suggestions for resolving the most significant issues that arise in negotiating and drafting a software license. The form of license provided in this article is intended to, and should only be used for, the specific transaction for which it is prepared.

COPYRIGHT LAW AND TYPES OF LICENSES

Copyright Law

Copyrightable Material

Software has been recognized as copyrightable material protectable under the federal Copyright Act since the early 1960s. Under the Act, copyright protection exists only for "an original work of authorship fixed in any tangible medium of expression, now known or later developed, from which the work can be perceived, reproduced or otherwise communicated, either directly or with the aid of a machine or device." 17 USC §102(a). For a work of authorship to be eligible for copyright protection it must be: (1) an original (2) work of authorship (3) fixed in a tangible medium.

For a work to be original it must be created by the independent efforts of its author and must not be copied from another person's work. The quantum of originality required to support a copyright is extremely low. "Original, as the term is used in copyright, means only that the work was independently created by the author (as opposed to copied from other works), and that it possesses at least some minimal degree of creativity." *Feist Publications, Inc. v Rural Telephone Serv. Co.* (1991) 499 US 340, 345, 113 L Ed 2d 358, 369, 111 S Ct 1282. To be original (*Drop Dead Co. v S.C. Johnson & Sons* (9th Cir 1963) 326 F2d 87, 92):

> [t]he author must have created the work by his own skill, labor and judgment, contributing something "recognizably his own" to prior treatments of the same subject. However, neither great novelty nor superior artistic quality is required.

Works of authorship include literary works. 17 USC §102(a)(1). The Act defines "literary works" as "works . . . expressed in words, numbers or other verbal or numerical symbols or indicia, regardless of the nature of the material objects, such as . . . tapes, discs or cards, in which they are embodied." 17 USC §101. Literary works include computer programs to the extent that they incorporate the physical expression of the programmer's ideas as opposed to the ideas themselves. H Rep No. 94–1476, Part 1, 94th Cong, 2d Sess (1976), reprinted in 1976 US Code Cong & Ad News 5659, 5676. The Computer Software Act of 1980 explicitly applied the Copyright Act to computer programs, and added a definition of "computer pro-

gram" that encompasses software. H Rep No. 96–1307, Part 2, 96th Cong, 2d Sess (1980), reprinted in 1980 US Code Cong 7 Ad News 6460. A "computer program" is "a set of statements or instructions to be used directly or indirectly in a computer in order to bring about a certain result." 17 USC §101. Both before and after passage of the 1980 amendments, the courts have found that a computer program is a "work of authorship" subject to copyright protection. *Apple Computer, Inc. v Franklin Computer Corp.* (3d Cir 1983) 714 F2d 1240, 1249; *Tandy Corp. v Personal Micro Computers, Inc.* (ND Cal 1981) 524 F Supp 171, 173 (applying 1976 Act prior to 1980 amendments). The courts have also found that copyright protection is afforded to human readable source code as well as machine-readable object code. See *Apple Computer, Inc. v Franklin Computer Corp., supra*; *Sony Computer Entertainment, Inc. v Connectix Corp.* (9th Cir 2000) 203 F3d 596, 602.

A work is fixed in a tangible medium of expression when its embodiment in a copy, by or under the authority of the author, is sufficiently permanent or stable to permit it to be perceived, reproduced, or otherwise communicated for a period of more than transitory duration. 17 USC §101.

> It makes no difference what the form, manner or medium of fixation may be—whether it is in words, numbers, notes, sounds, pictures or any other graphic or symbolic indicia, whether embodied in a physical object in written, printed, photographic, sculptural, punched, magnetic, or any other stable form, and whether it is capable of perception directly or by means of any machine or device 'now known or later developed.'

H Rep No. 94–1476, Part 1, 94th Cong, 2d Sess (1976), reprinted in 1976 US Code Cong & Ad News 5659, 5676.

It is clear from the statute, legislative history, and case law that software meets the criteria of copyrightable subject matter. A software developer who writes a software program by creating a sequence of commands in a computer language has created an original work of authorship as long as that work is the fruit of his or her own intellectual labor and has not been copied from another person's work. Once the programmer reduces the sequence of commands to a tangible medium, like a magnetic disk or computer hard drive, the original work of authorship is fixed in a physical medium and may be protected under the Copyright Act.

Exclusive Rights of Copyright Owner

Under the Copyright Act, the owner of a copyright has the exclusive right to do and authorize others to do the following with the copyrighted work: (1) reproduce, (2) prepare derivative works, (3) distribute, (4) perform, and (5) display. 17 USC §106.

Right to Reproduce. The reproduction right consists of the right to reproduce the copyrighted work in copies or phonorecords. 17 USC §106(1). A copy is a material object in which the work is fixed (*i.e.,* computer disk, hard drive, or server) by any method now known or later developed. 17 USC §101. The right to reproduce a computer program means "the right to produce a material object in which the work is duplicated, transcribed, imitated or simulated in a fixed form from which it can be perceived, reproduced or otherwise communicated, either directly or with the aid of a machine or device." S Rep No. 473, 94th Cong, 1st Sess (1975). Loading copyrighted software onto a computer results in making a copy, and if not authorized by a license, constitutes infringement. *Stenograph L.L.C. v Bossard Assocs.* (DC Cir 1998) 144 F3d 96, 100. Loading copyrighted software from a storage medium into the memory of a central processing unit creates a copy, and in the absence of a license or ownership of the copyright, constitutes infringement. *MAI Sys. Corp. v Peak Computers, Inc.* (9th Cir 1993) 991 F2d 511, 517.

A copyright owner's exclusive right to reproduce copyrighted software is not without its limitations. The owner of a copy of the software can make a new copy or adaptation of the program if making such copy or adaptation is (1) an essential step in the use of the computer, or (2) is made for archival purposes only. 17 USC §117(a). Congress created these exceptions to the copyright owner's exclusive reproduction right for several reasons. An owner of a copy of software should be able to install the software onto its computer without being subject to a claim of infringement as long as it acquired the software legally and installing such software is necessary to operate the computer. National Commission on New Technological Uses of Copyrighted Works (CONTU), Final Report 1, p 13 (1979). Moreover, the owner of a copy of software should be allowed to adapt the software to its computer to the extent necessary to use the software on the computer. The magnetic media on which software is stored is inherently unstable, and thus a back-up copy should be permitted without running the risk of an infringement claim. The Act also allows the owner or lessee of a machine to make a copy of a computer program if such copy is made solely by activating the machine and is used only to maintain or repair the machine. 17 USC §117(c). Congress created this exception to ensure that independent service providers who maintain and repair computers are not liable for copyright infringement

when they activate a client's computer to service the machine, and in doing so, copy the software.

Right to Distribute. The Act reserves to the copyright owner the exclusive right to "distribute copies of the copyrighted work to the public by sale or other transfer of ownership, or by rental, lease or lending." 17 USC §106(3). To infringe the distribution right, a person must engage in the actual dissemination of copies of the work. *National Car Rental Sys., Inc. v Computer Assocs. Int'l, Inc.* (8th Cir 1993) 991 F2d 426, 434. The distribution right is limited by the first sale doctrine, which states that once a copyright owner consents to the sale of a particular copy of its copyrighted work, it may not, absent a contractual provision to the contrary, control or direct the further distribution of that copy. 17 USC §109(a); *Bobbs-Merrill Co. v Straus* (1908) 210 US 339, 350, 52 L Ed 1086, 28 S Ct 722. The first sale doctrine applies to any transaction in which title to a copy of the work is transferred, but does not apply to transactions in which the copy is simply rented, leased, or lent.

Congress created an exception to the first sale doctrine for computer programs. Unless authorized by the copyright owner, a person in legal possession of a computer program may not dispose of or authorize the disposal of the program by rental, lease, or lending if it is done for commercial gain. Outright sales of computer programs are unaffected by this exception. The prohibition does not apply to the rental, lease, or lending of such computer programs if they are used for nonprofit purposes. 17 USC §109(b)(1)(A). The prohibition also does not apply to (1) computer programs that cannot be copied during the ordinary operation of the machines on which they are installed, or (2) computer programs installed on machines that play video games. 17 USC §109(b)(1)(B). The rental, lease, or lending of these types of software remains permissible under the Act.

Right to Perform. The copyright owner possesses the exclusive right to publicly perform its literary works. 17 USC §106(4). To perform a work means to "recite, render, play, dance or act it, either directly or indirectly by means of any device or process." 17 USC §101. A work is performed publicly if it is performed "at a place open to the public or at any place where a substantial number of persons outside a normal circle of a family and its social acquaintances are gathered." 17 USC §101. The devices and processes used to perform the work can include "all kinds of equipment for reproducing or amplifying sounds or visual images, any sorts of transmitting apparatus, any type of electronic retrieval system, and any other techniques and systems not yet in use or even invented." H Rep No. 94–1476, Part 1, 94th Cong, 2d Sess (1976), reprinted in US Code Cong & Ad News 5659, 5676. The public performance of a literary work without authorization from the copyright owner infringes the copyright. The Act limits the copyright owner's exclusive right to perform the copyrighted work when the work is performed for educational, governmental, religious, or nonprofit purposes. 17 USC §110.

Congress created an exception to the first sale doctrine for computer programs. Unless authorized by the copyright owner, a person in legal possession of a computer program may not dispose of or authorize the disposal of the program by rental, lease, or lending if it is done for commercial gain.

Right to Display. The copyright owner possesses the exclusive right to publicly display its literary works. 17 USC §106(5). To display a work means to "show a copy of it, either directly or indirectly by means of film, slide, television image, or any other device or process." 17 USC §101. Display includes "not only showing a copy directly, but also by projection of an image on a screen, or other surface by any method, and the transmission of an image by electronic or other means, as well as the showing of an image on a cathode ray tube, or similar apparatus in connection with computers or other devices. H Rep No. 94–1476, Part 1, 94th Cong 2d Sess (1976). The public display of a copy of a software program—like its projection on a screen so employees of a licensee company can be trained in its use—invokes the exclusive right to display the software, and requires authorization from the copyright owner. The unauthorized display of the software program constitutes infringement unless the display is nonpublic. *Thomas v Pansy Ellen Prods. Inc.* (WD NC 1987) 672 F Supp 237, 240.

The copyright owner's exclusive right to display its copyrighted work is limited in situations where a person has acquired ownership of a lawfully made copy of the work. 17 USC §109(c). Such person has the right to publicly display or authorize the public display of the copy either live or by projection. If the copy is displayed by projection, it must be projected one image at a time, and the viewers must be present at the place where the copy is located. Like the performance right, the Act limits the copyright owner's

exclusive right to display the copyrighted work when the work is displayed for certain educational, governmental, religious, or nonprofit purposes. See 17 USC §§110(1), (2), (3).

Right to Prepare Derivative Works. The last exclusive right held by the copyright owner is the right to prepare derivative works based on a copyrighted work. 17 USC §106(2). A derivative work is a work based on one or more preexisting works that recasts, transforms, or adapts the preexisting works into a new work. 17 USC §101. To be a derivative work, the new work must substantially copy from the original work, and the original work must itself be capable of being copyrighted. *Micro Star v Formgen, Inc.* (9th Cir 1998) 154 F3d 1107, 1111; *Lewis Galoob Toys, Inc. v Nintendo, Inc.* (9th Cir 1992) 964 F2d 965, 968. A derivative work will be copyrightable if the original aspects of the derivative work (1) are original, and (2) do not in any way affect the scope of any copyright protection in the preexisting material. *Durham Indus., Inc. v Tomy Corp.* (2d Cir 1980) 630 F2d 905, 909. With respect to the first criteria, to satisfy the Constitution and the Copyright Act, the author must contribute something more than a merely trivial variation on the original work. See *Entertainment Research Group, Inc. v Genesis Creative Group, Inc.* (9th Cir 1997) 122 F3d 1211, 1221 (quoting *Sid & Marty Krofft Television v McDonald's Corp.* (9th Cir 1977) 562 F2d 1157, 1163 n5. With respect to the second criteria, copyright protection is not granted to a derivative work that is virtually identical to the original work, to ensure that the original copyright owner can exercise all of its rights in the copyright and to prevent the first derivative copyright holder from interfering with the creation of subsequent derivative works from the same underlying work. *Gracen v Bradford Exch.* (7th Cir 1983) 698 F2d 300, 305. A derivative work of software uses an existing software program to develop a new piece of software, and in the course of doing so incorporates significant portions of the original program into the new program. An object code license typically does not include the right to prepare derivative works. A source code license frequently grants the right to prepare derivative works, because the preparation of such works is one of the primary reasons for entering into such a license.

Infringement and Remedies

In the absence of a valid license, or a statutory or common-law defense, a person who uses copyrighted material in a manner expressly reserved for the copyright owner infringes the copyright. 17 USC §501(a). A licensee infringes the owner's copyright if the licensee's use of the software exceeds the scope of the grant clause contained in the license. *S.O.S., Inc. v Payday, Inc.* (9th Cir 1989) 886 F2d 1081, 1088. To succeed on a claim of infringement, the plaintiff must prove (1) ownership of a valid copyright, and (2) copying of the constituent elements of the work that are original. *Feist Publications, Inc. v Rural Tel. Serv. Co.* (1991) 499 US 340, 361, 113 L Ed 2d 358, 379, 111 S Ct 1282. The unlicensed use of copyrighted material in any manner reserved exclusively for the copyright owner—reproduction, adaptation, distribution, performance, or display—satisfies the second element of an infringement claim. *S.O.S., Inc. v Payday, Inc.* (9th Cir 1989) 886 F2d 1081, 1085 n3. An exclusive licensee has standing to sue in its own name to recover for infringement of the specific rights it has licensed from the copyright owner; a nonexclusive licensee does not. *Essex Music, Inc. v ABKCO Music & Records, Inc.* (SD NY 1990) 743 F Supp 237, 241.

A copyright owner who prevails in an infringement action is entitled to recover the actual damages suffered as a result of the infringement, and any of the infringer's profits that are attributable to the infringement and not taken into account in computing actual damages. 17 USC §504(b). The primary measure of actual damages is the extent to which the market value of the copyrighted work at the time of infringement has been injured or destroyed by the infringement. *Frank Music Corp. v Metro-Goldwyn-Mayer, Inc.* (9th Cir 1985) 772 F2d 505, 512. If the infringement has destroyed the entire value of the work, damages will equal the full value of the work. *Cream Records, Inc. v Jos. Schlitz Brewing Co.* (9th Cir 1985) 754 F2d 826, 828. One method courts have used to calculate the magnitude of the injury suffered by the copyrighted work is to determine the copyright owner's lost profits attributable to the infringement. *Big Seven Music Corp. v Lennon* (2d Cir 1977) 554 F2d 504. California law specifically allows recovery of lost profits. *Glovatorium, Inc. v NRC Corp.* (9th Cir 1982) 684 F2d 658, 664. In the absence of malicious intent or willful misconduct, punitive damages will not be awarded for statutory copyright infringement.

In addition to actual damages, the copyright owner is entitled to recover from an infringer those profits earned by the defendant that are attributable to the infringement and not taken into account when computing actual damages. *Transgo, Inc. v Ajac Transmission Parts Corp.* (9th Cir 1985) 768 F2d 1001, 1023. While case law varies considerably on the calculation of the defendant's profits, virtually all of the cases focus on whether the defendant's profits are attributable to the acts of infringement or are too

remote or speculative to be considered part of the infringement. *Frank Music Corp. v Metro-Goldwyn-Mayer, Inc.* (9th Cir 1989) 886 F2d 1545, 1553.

As an alternative to recovering actual damages and defendant's profits, the plaintiff can recover statutory damages. 17 USC §504(c)(1). Within the monetary limits set forth in the Act, a court will award statutory damages in an amount it considers just. *Harris v Emus Records Corp.* (9th Cir 1984) 734 F2d 1329, 1335. While courts have considered various factors when calculating statutory damages, at least one court has found that such damages should be based on "the expenses saved and the profits reaped by the defendants in connection with the infringements, the revenues lost by the plaintiffs as a result of the defendant's conduct, and the infringers' state of mind, whether willful, knowing or merely innocent." *N.A.S. Import Corp. v Chenson Enters., Inc.* (2d Cir 1992) 968 F2d 250, 252.

When determining whether a person has engaged in copyright misuse, courts typically focus on whether the copyright owner's behavior is anticompetitive.

In addition to legal remedies, the Act allows a copyright owner to pursue equitable relief—including preliminary and permanent injunctions—to prevent or restrain infringement of its copyrighted work. 17 USC §502(a). A court has authority to order the destruction or other reasonable disposition of all copies of the copyright owner's work that have been made or used in violation of the copyright. 17 USC §503(b). A court has the discretion to award to either party the costs of an infringement suit, and to the prevailing party reasonable attorney fees. 17 USC §505.

Any person who infringes a copyright willfully and for the purpose of commercial advantage or private financial gain has committed criminal copyright infringement. 17 USC §506(a). Penalties for criminal copyright infringement can include both fines and imprisonment, and are imposed, in part, on the basis of the work infringed and the type of infringement. On a conviction of criminal infringement, the court must order the forfeiture and destruction or other disposition of all infringing copies and all implements, devices, and equipment used in the manufacture of the infringing copies. 17 USC §506(b).

Copyright Misuse

The doctrine of misuse is an equitable defense to a claim of infringement that originally arose in the context of patent law but has recently been applied to copyright law. In this context, the doctrine states that a copyright owner who uses its limited copyright monopoly in a manner that violates the public policy embodied in the grant of the copyright may be liable for misuse of the copyright. *Lasercomb Am., Inc. v Reynolds* (4th Cir 1990) 911 F2d 970, 978. When determining whether a person has engaged in copyright misuse, courts typically focus on whether the copyright owner's behavior is anticompetitive. Thus far, the courts have found copyright misuse under several circumstances. A copyright owner that includes a covenant in a license that prohibits the licensee from independently developing or assisting others in developing a competing good is guilty of per se copyright misuse. Similarly, a copyright owner that imposes a covenant in a license that prohibits the licensee from using or dealing in competing goods engages in per se copyright misuse. *Practice Mgmt. Info. Corp. v American Medical Ass'n* (9th Cir 1997) 121 F3d 516, 521. A copyright owner that prohibits a licensee from copying its software onto the licensee's equipment, and in doing so prevents the licensee from developing competing equipment, unlawfully uses its copyright to maintain a patent-like monopoly over nonpatented technology, and thus commits per se copyright misuse. *DSC Communications Corp. v DGI Technol., Inc.* (5th Cir 1996) 81 F3d 597, 601. In addition to those actions considered per se copyright misuse, there are other acts in which a copyright owner can engage that may expose it to a claim of copyright misuse. These acts include: (1) using a copyright to maintain a resale price maintenance scheme; (2) using a copyright to violate antitrust laws; (3) contracting with a licensee for the payment of royalties after the copyright expires; (4) conditioning the grant of a license for copyrighted material on the sale of noncopyrighted material; (5) requiring a licensee to license a portfolio of copyrights in order to license the single copyright it wishes to license; and (6) charging royalties for a copyright on the basis of the licensee's total sales.

The consequences of misuse are draconian. If a court finds copyright misuse, the owner of the copyright may not enforce the copyright, or any agreement or license that relates to the copyright, until the misuse has been purged from the marketplace. This means that the copyright owner may not file an action to enjoin acts of infringement or pursue damages for breach of a license. Copyright misuse can be asserted directly by the licensee against whom the misuse has been perpetrated, or collaterally by any licensee, or

even a third party, that may otherwise be an infringer of the copyright. To purge the adverse effects of copyright misuse, the copyright owner must abandon the offending practice and the anticompetitive effects of that practice must be completely eliminated from the marketplace. Eliminating the anticompetitive effects of misuse requires allowing all potential competitors to re-enter the market and allowing the market to return to its natural, competitive state. Under copyright law, purging the effects of the misuse can take many months, if not years, to complete, and during that entire time the copyright remains unenforceable.

Types of Software Licenses

There are many different types of software licenses. With respect to the legal rights that flow from a software license, however, there are two principal types: exclusive and nonexclusive. While both types of licenses may be structured in similar ways, they grant significantly different rights to the licensee, and expose the licensor to significantly different risks. From a business standpoint, there are two principal types of software licenses: Object code and source code. The majority of software licenses in use in commerce today are nonexclusive, object code licenses limited by time, geography, and field of use.

Exclusive Versus Nonexclusive Licenses

An exclusive license transfers to the licensee ownership of some or all of the exclusive rights owned by the copyright owner. 17 USC §201(d). While the grant may be limited to a particular time, place, and field of use and still constitute an exclusive license, it must be in writing. 17 USC §204; *Imperial Residential Design, Inc. v Palms Dev. Group, Inc.* (11th Cir 1994) 29 F3d 581, 583. An exclusive license should be filed with the Copyright Office to provide constructive notice that ownership of the rights granted under the license has been transferred to the licensee. The Act contains a bona fide purchaser provision that requires an assignee to record its assignment within a specific period of time or risk losing its ownership interest in the copyright to a subsequent assignee that gives value and records first. 17 USC §205(d). The Act does not require consideration to effect a transfer of copyright ownership under an exclusive license. Absent a contractual limitation to the contrary, an exclusive licensee can reconvey or sublicense to a third party the rights granted by the copyright owner. An exclusive licensee has standing to sue in its own name for infringement of the exclusive rights granted to it under a license. 17 USC §501(b).

An exclusive license should be filed with the Copyright Office to provide constructive notice that ownership of the rights granted under the license has been transferred to the licensee.

A nonexclusive license does not transfer to the licensee an ownership interest in any of the exclusive rights held by the copyright owner. Instead, it authorizes the licensee to exercise the rights granted in the license during a specific period of time, in a particular geographic region, and in a particular field of use. When the totality of the parties' conduct indicates an intent to grant permission to use copyrighted material, the result is a nonexclusive license. *Michaels v Internet Entertainment Corp.* (CD Cal 1998) 5 F Supp2d 823, 831. A nonexclusive license need not be in writing and may be granted orally or implied from conduct. *Effects Assocs. v Cohen* (9th Cir 1990) 908 F2d 555, 558. A nonexclusive licensee may not sublicense, transfer, or assign any of the licensed rights unless specifically authorized by the license. Absent a provision in the license authorizing the licensee to enforce the copyright, a nonexclusive licensee has no standing to sue in its own name for infringement of any rights granted to the licensee under the license. Even if the licensee is authorized to bring suit to enforce the copyright, it will likely have to join the licensor, because the licensor is a necessary party under Fed R Civ P 19.

Object Code Versus Source Code Licenses

While source code and object code licenses are similar in form and content, there are major differences that must be kept in mind when preparing a license agreement. Source code is the human-readable form of the software written in a computer programming language like Basic or Java. It is comprised of a series of commands and instructions that the computer uses to execute its various functions. Object code is the machine-readable form of the software that is comprised of an endless stream of zeros and ones that can be read and understood only by the computer. After source code is developed it is run through a compiler program that translates it into object code. The computer reads the object code when executing the software's functions and applications.

In general, software companies enter into object code licenses to generate revenue. After spending considerable time and resources developing what it hopes will be a blockbuster software program, a company will be reluctant to disclose its source code to

potential competitors and lose the competitive advantage it has gained by bringing its product to market. Maintaining the confidentiality of its source code ensures that the company will have the exclusive right to develop and license new and improved versions of the software and use the existing software as a platform for developing new products. It also allows the company to maintain complete control over the technical support and maintenance it provides to its licensees, and in doing so allows the company to generate additional revenue that can be reinvested in the company for operations and research and development.

While technically difficult, skilled computer programmers can reverse-engineer a software program's object code to discover the underlying source code. When preparing an object code license it is crucial to expressly prohibit the licensee from reverse-engineering, decompiling, or disassembling the software. Under certain circumstances, courts have found that reverse-engineering does not constitute infringement. *Sony Computer Entertainment, Inc. v Connectix Corp.* (9th Cir 2000) 203 F3d 596, 602. Thus, including in the license a provision that expressly prohibits the licensee from reverse-engineering the object code will ensure that the licensor can pursue a breach of contract claim against the licensee if it attempts to reverse-engineer the software, even if the licensor is unable to pursue a claim of infringement.

A software company enters into source code licenses to reduce costs or pursue strategic business opportunities. A successful software company may be growing so quickly that it cannot adequately support its customers, and consequently may seek to outsource some of its support and maintenance operations to a third party provider. To do so, it must license its source code to a third party that is technically capable of supporting, maintaining, and, in some cases, upgrading the software for the company's customers. Or, an opportunity may arise that allows a software company to enter into a strategic business relationship with another company for the purpose of developing a new software product. The nature of this working relationship frequently requires both parties to disclose copyrighted source code or trade secrets to successfully develop the new product. Regardless of whether the parties enter into a license for the purpose of providing technical support or developing a new software product, the license must clearly and concisely define the specific rights in the source code that the licensee may exercise, and the restrictions limiting those rights. For example, the licensor may wish to allow the licensee to use a single copy of the source code and prohibit the licensee from making any additional copies. The licensor may also wish to authorize the licensee to make only certain types of modifications to the software and prohibit all other modifications. Similarly, because of the relative ease with which source code can be exploited for commercial gain, the licensor may want to prohibit the disclosure and distribution of the source code to unauthorized personnel and all third parties.

SOFTWARE LICENSE AGREEMENT

A combination of federal and state law governs a license of copyrighted software. All license provisions that pertain to the grant of a license, and any restrictions imposed thereon, are governed by the federal Copyright Act. State contract law governs the remaining provisions of the license. *S.O.S., Inc. v Payday, Inc.* (9th Cir 1989) 886 F2d 1081, 1088.

Introduction, Recitals, and Definitions

The first paragraph of a license agreement should set forth the names of the licensor and the licensee, and be followed by a brief set of recitals that describe the purpose of the transaction, the software being licensed and the intent of the parties. A software license may begin as follows:

THIS SOFTWARE LICENSE AGREEMENT (the "Agreement") is entered to as of _ _[*date*]_ _ (the "Effective Date") by _ _[*name of corporation*]_ _, a California corporation (the "Licensor"), and by _ _[*name of corporation*]_ _, a California corporation (the "Licensee).

RECITALS

Licensor owns all right, title, and interest in and to _ _[*name of software product*]_ _, and has the right to grant to Licensee a license to use the software in accordance with the terms and conditions set forth in this Agreement.

Licensee desires to license the object code version of the software from the Licensor, and Licensor desires to license such version of the software to the Licensee in accordance with the terms and conditions set forth in this Agreement.

NOW, THEREFORE, in consideration of the mutual promises and covenants set forth herein, and other good and valuable consideration, Licensor and Licensee agree as follows:

A definition section that contains defined terms applicable to the specific license agreement negotiated by the parties follows the introductory clause and recitals.

Section 1. *Definitions*

"Documentation" means the user manuals, training materials, and operating materials, if any, Licensor provides to Licensee under this Agreement.

"Installation Site" means the business premises owned or leased and operated solely by the Licensee, or Licensee's external hosting site, which locations are described in the Licensor's Order Form.

"Intellectual Property Rights" means any trade secrets, patents, copyrights, trademarks, know-how, moral rights, or similar rights of any type under the laws of any governmental authority, domestic or foreign, including all applications and registrations relating to any of the foregoing.

"License Fees" means the fees Licensee must pay Licensor, as set forth in Section 4, below, to license the Software from Licensor.

"Licensee Hardware" means all computers owned or controlled by Licensee and located at the Installation Site.

"Licensee Network" means Licensee's internal or externally hosted computer network, which is located at the Installation Site, comprised of Licensee Hardware and accessible only by Licensee's employees and contractors.

"Order Form" means any Licensor Order Form, with the initial order set forth in Exhibit A, and which is subject to the terms and conditions of this Agreement. In the event of any conflict between the Order Form and the terms and conditions of this Agreement, the terms and conditions of this Agreement shall govern.

"Software" means the software programs, in object code format only, that Licensee licenses from Licensor under this Agreement _ _[*pursuant to an Order Form*]_ _ **and any bug fixes or error corrections which Licensor provides to Licensee.**

"Software Support and Maintenance Agreement" means a separate agreement entered into by the Licensor and Licensee for the provision of support and maintenance of the Software.

All references in this Agreement to the "purchase" or "sale" of Software shall mean the acquiring or granting, respectively, of a license to such Software.

It is not unusual for a licensee to license software for a specific, limited purpose, and once the license is executed to forget or ignore the scope of the grant clause. Moreover, while a license may state that employees of the licensee are permitted to use the software, other parties, like affiliates, agents, consultants, subsidiaries, or parents of the licensee, may not have explicit authority under the license to do so. Indeed, many large software companies have as part of their business plan regular technology audits of their licensees to identify and collect royalties for improper uses of licensed software. The introductory sentence, recitals, and definitions should set forth clearly and precisely the parties to the license, the software being licensed, whether it is object code or source code, and the key terms that govern the parties' agreement. The licensor usually prepares the license agreement it uses to license its software, and thus any ambiguities in the license will be viewed in a light most favorable to the licensee. *Heston v Farmers Ins. Group* (1984) 160 CA3d 402, 415, 205 CR 585.

Grant Clause

The grant clause is arguably the most important provision in a license. It is the provision under which the licensor grants to the licensee the right to exercise, usually in a prescribed manner, some or all of the exclusive rights the licensor holds in the copyrighted software. From the licensor's perspective, the grant must be carefully drafted to convey only those specific rights that the parties have agreed on. From the licensee's perspective, the more ambiguously stated the grant clause, the better. A well-crafted grant clause will describe exactly what the licensee can do with the software. Under federal copyright law, all exclusive rights are reserved to the copyright owner except those expressly granted to the licensee. *S.O.S., Inc. v Payday, Inc.* (9th Cir 1989) 886 F2d 1081, 1088. If a licensee uses the software in a manner not set forth in the grant clause, it infringes the copyright and is liable to the licensor for actual damages and all profits earned by the licensee that are attributable to the infringement. The licensee may also be subject to an injunction that prohibits further use of the software, and be liable to the licensor for costs and attorney fees. The following is an example of a narrowly drafted grant clause for use of object code software:

Section 2. ***Grant of License and Ownership of Intellectual Property***

2.1 ***Grant of License.*** **Subject to the terms and conditions of this Agreement, Licensor hereby grants to Licensee for the term specified in Exhibit A, a nonexclusive, nontransferable license to (a) install the Software on Licensee Hardware; (b) allow Licensee's employees to use the Software on the Licensee Hardware or through the Licensee Network solely for Licensee's internal business purposes at the Installation Site; (c) allow the Licensee's employees to use the Documenta-**

tion to install and operate the Software on the Licensee Hardware or through the Licensee Network solely for Licensee's internal business purposes at the Installation Site; and (d) reproduce the Software and Documentation only as needed to support the permitted use of the Software by Licensee, and for archival purposes.

If you represent the licensee, request an affirmative statement in the license that grants the licensee the right to make copies of the software needed to operate the computer and serve as archival copies. While the provision is a statement of law, it will minimize infringement and breach of contract claims by the licensor, in the event the licensee makes such copies, and speed resolution of any such claims. See 17 USC §117. If you represent the licensor, and the grant clause authorizes the licensee to make copies of the software beyond those permitted under §117, make sure the license contains a provision that requires the licensee to affix the licensor's copyright notice to all copies of the software. This will help prevent the copyrighted software from being injected into the public domain and running the risk of invalidating the copyright. When representing a licensee, consider bargaining for the right to make and transfer a copy of the software to a third party who provides disaster recovery services. Many licensees request this right to protect against catastrophic losses of data due to computer system failures or unforeseen events like terrorist attacks or natural disasters. Licensors are willing to accept such a provision because it speeds recovery efforts, minimizes technical and financial losses, and reduces the risk that the licensee will file suit seeking to impose liability on the licensor for such losses.

If you represent the licensee, request an affirmative statement in the license that grants the licensee the right to make copies of the software needed to operate the computer and serve as archival copies.

If a licensor grants a licensee the right to create a derivative work, and places no restrictions on that right, the licensee will own the derivative work free and clear of any interest the licensor may claim in the work. See *Entertainment Research Group, Inc. v Genesis Creative Group* (9th Cir 1997) 122 F3d 1211, 1218. The licensor has effectively created its own competition in the marketplace for the software. In fact, the derivative work has a competitive advantage over the original software because it contains the latest functions that the original software may lack. If a licensor licenses its software, and includes in the grant clause the right to make modifications and prepare derivative works, the licensor should include a limitation on that right that states the following:

2.2 *Derivative Works.* Licensee may create derivative works; provided however that the Licensee expressly acknowledges and agrees that such derivative works shall be subject to all of the terms, conditions, restrictions, confidentiality obligations, royalty and fee obligations, and other limitations and requirements contained in this Agreement or any related agreement as if the Licensee's derivative works are part of the Software.

Because the right to make derivative works is one of the exclusive rights held by the copyright owner, to the extent that the copyright owner grants to a licensee the right to make a derivative work, it may limit the scope of the right granted in any manner it so chooses. If a licensor includes in the grant clause restrictive language similar to that set forth above, and the licensee fails to comply with the restriction, that failure constitutes both an infringement of the copyright and a breach of the contract. If the license is properly drafted, the licensor will be able to pursue claims for infringement and breach of contract and immediately terminate the license.

Restrictions on the Grant

A software license does not contain an implied negative covenant. If a licensee operates outside the scope of the grant clause, while it may infringe the copyright, it does not breach the contract unless the license includes a covenant under which the licensee expressly promises not to use the software in a manner not authorized in the grant clause. If you represent the licensor, immediately after the grant clause you should include a covenant that states that the licensee will use the software only in accordance with the scope of the grant clause. By including such a provision, if the licensee uses the software outside the scope of the grant clause, it has infringed the copyright and breached the contract. A well-crafted license will, upon the happening of such an event, allow the licensor to terminate the license. If you represent the licensor, add a sentence to the license that states that "the licensor reserves all rights not expressly granted to the licensee." While this is a statement of law, its inclusion in the license makes it difficult for the licensee to argue later that it used the software beyond the scope of the grant out of ignorance, and allows the

licensor to assert a claim of intentional infringement, which carries with it increased financial penalties and potential criminal sanctions. 17 USC §§504(c)(2), 506(a).

The following is an example of a provision limiting the licensee's use of the software to only those uses set forth in the grant clause, and retaining for the licensor all other proprietary rights in the software:

2.3 *Restrictions on Use*. Licensee shall not use the Software or Documentation in any manner whatsoever except as set forth in Sections 2.1 and 2.2. Licensee shall not disclose or distribute the Software to any person not authorized to use the Software under this Agreement. Licensee acknowledges that the Software contains Licensor's trade secrets, and accordingly Licensee agrees that it shall not cause or permit reverse-engineering, disassembly, or decompiling of the Software, or make any attempt to discover the source code of the Software. Licensee agrees not to remove, alter, or destroy any proprietary, trademark, or copyright markings or other notices placed on or contained within the Software, Documentation, or any related materials provided to Licensee under this Agreement. Licensee shall not do any of the following: (a) permit any parent, affiliated entities, or third parties to use the Software; (b) sublicense, distribute, assign, resell, or otherwise transfer the Software; (c) rent, lease, or loan the Software; (d) use the Software for commercial time-sharing or service bureau purposes; or (e) use the Software for any unlawful purpose.

Exclusive licenses possess an implied right to sublicense; nonexclusive licenses do not. An implied right to sublicense would allow a licensee to use a company's software, without its consent and without any requirement to further compensate the company for such uses, to compete with the company for customers. It would also make it difficult, if not impossible, for a software company to monitor the number of sublicensees using its software, receive royalties from such sublicensees, and control the manner in which its software is used by such sublicensees. If you represent the licensor, include a provision in the license that explicitly prohibits the licensee from sublicensing the software to ensure that the licensor can file both an infringement claim and a breach of contract claim against the licensee in the event such sublicensing occurs.

Ownership of Proprietary Rights

A licensor of software frequently demands that the license include a series of provisions designed to protect and preserve the licensor's ownership interest in the software and underlying intellectual property rights. At a minimum, the license should contain an affirmative statement that the licensee is receiving from the licensor a mere license to use the software and accompanying documentation in accordance with the terms, conditions, and limitations of the license. The license should also contain an affirmative statement that the licensor retains all ownership interests in the intellectual property embodied in the software and user documentation, and that no rights are transferred to the licensee by implication, estoppel, or otherwise. The following is a standard ownership provision:

2.4 *Ownership*. Licensor retains all right, title, and interest under its Intellectual Property Rights to the Software and Documentation. Except for the license expressly granted in Section 2.1, Licensee obtains no rights, title, or interest in the Software or Documentation by implication, estoppel, or otherwise. Licensee acknowledges that the Software and Documentation are being licensed and not sold under this Agreement, and that this Agreement does not transfer title in the Software or Documentation, or any copy thereof, to the Licensee. Without limiting the foregoing, Licensee may not sublicense or otherwise distribute or disclose the Software or any portion thereof to any third party, or permit any third party to use the Software, unless otherwise authorized by the Licensor in writing.

Delivery of Software

A well-crafted software license should clearly state the materials that will be delivered, the time and method of delivery, and the criteria for the licensee's acceptance of those materials. With respect to the delivery of licensed materials, the parties have different objectives. If you represent the licensor, it is important to seek (1) flexibility in delivering the software and documentation, (2) strict limits on the amount of software and documentation that must be delivered, and (3) absolution of responsibility for installing and integrating the software into the licensee's existing computing environment. If you represent the licensee, its important to ensure that the licensor will deliver the licensed software and documentation in good working order and in a timely manner. In particular, the licensee should request (1) prompt delivery of the software and documentation, (2) a sufficient number of copies to meet current and future needs, and (3)

quick and easy installation of the software into the licensee's existing computing environment. In addition, the licensee should require that the licensor bear all risk of loss or damage to the software and documentation during transport.

A well-crafted acceptance provision should include three elements: (1) acceptance criteria, (2) product specifications, and (3) acceptance procedures. Acceptance criteria are the simplest and most straightforward of these elements. The license should state that the software must operate in accordance with the specifications set forth in the license. Licensors frequently seek to modify this requirement by inserting commercially reasonable terms like "substantially" or "in all material respects" in the license. Because of the inherent complexity of software, licensees are usually willing to accommodate the licensor on this point.

Product specifications can vary dramatically from license to license. If the licensed software is noncustomized, the product specifications will frequently be those set forth in documentation provided by the licensor. If this is the case, the licensee should request a copy of such documentation before entering into the license to ensure that the specifications meet the licensee's needs. If the software is customized, the acceptance criteria will be complex, and thus should be the subject of considerable negotiation between the parties before the license is executed. It is imperative that the licensee's technologists participate in the development of the software specifications, because they are most familiar with the licensee's existing software and know how the software must perform to meet the licensee's computing needs. Because customized software is likely to undergo changes during its development, the licensee should request that the license allow for modifications to the schedules for delivering the software and paying fees.

The license must set forth acceptance procedures, regardless of whether acceptance takes place after a specific period of time, inspection of the software, testing of the software, installation and operation of the software, or some other objective criteria. A licensee should demand the right to test the software, because physical inspection alone cannot ensure that the software will function and process data in accordance with the licensee's needs. Any procedure agreed to by the parties should specify the amount of time the licensee will have to inspect or test the software, as well as the amount of time the licensor will have to correct any deficiencies in the software. The licensee should bargain for the right to conduct repeat inspections or testing after it has received copies of the corrected software from the licensor.

If you represent the licensor, seek automatic acceptance, unless the licensee rejects the software by a certain date or after the software has been tested in accordance with procedures established by the parties. As licensor's counsel, your primary goals should be to minimize the risk that the licensee will reject the software, accelerate the payment of license fees, and start the warranty period. The licensee, on the other hand, knows the software may not function properly when first installed, and will likely request some time to install it, integrate it, and work out the bugs. If you represent the licensee, reject the licensor's overtures to require automatic acceptance and demand that the acceptance period not begin until all of the software and documentation has been delivered by the licensor. In addition, the licensee should request enough time to test the software and train its employees in its proper use. Lastly, the licensee should consider negotiating for a self-implementing provision that extends the acceptance period if certain events take place or fail to take place. Clear acceptance procedures are crucial to both parties to the license, because on acceptance the licensee is liable for the license fee and the warranty period on the software begins to run. The following is an example of pro-licensor delivery and acceptance provisions for noncustomized software:

Section 3. *Delivery and Acceptance of Software*

3.1 *Order of Software*. Licensee shall submit orders for the Software on the order form attached hereto as Exhibit A (an "Order Form"). All Order Forms are subject to acceptance by Licensor. Licensee's Order Forms may include additional information about necessary billing and shipping information, requested delivery dates, descriptions of the Installation Site or License Hardware or Licensee Network where the Software will be installed, and the applicable fees and charges for the Software. If there is a conflict or inconsistency between the terms and conditions of this Agreement and those contained in any Order Form, the terms and conditions of this Agreement shall prevail.

3.2 *Delivery of Software*. Delivery of the Software, in object code format only, and Documentation shall be F.O.B. place of _ _[*shipment/destination*]_ _ **on or about the date requested in the applicable Order Form or otherwise agreed on by the parties. Licensor shall select the method and mode of transporting, insuring, and packing the Software.**

3.3 *Installation of Software*. Licensee shall be solely responsible for installing the Software on delivery in accordance with the applicable Docu-

mentation. Licensee shall have five (5) days after delivery of the Software to inspect the Software. Licensee shall immediately notify Licensor in writing if the Software does not conform to the Software as described in the Order Form. If the Software does not conform to the Order Form, Licensee shall promptly return the Software and all other materials, including the related Documentation, delivered to Licensee with the Software, and Licensor shall deliver replacement Software and Documentation.

Payment of Fees

There are many ways to structure the payment of fees for a software license. The structure ultimately chosen frequently depends on the licensor's revenue model for the particular software product. In general, license fees can be structured as a one-time fixed payment, a periodic royalty or license payment calculated on the basis of sublicense fees or use of additional units of the software, or some combination of an up-front fee and periodic royalty or license fee. One method favored by licensors is the payment of a fee on execution of the license and delivery of the software, and periodic payments as sublicensing royalties or for use of additional copies of the software. The initial payment is a fee for granting the license, and in certain situations, assisting with the installation and integration of the software into the licensee's existing computing environment. The periodic payments are either royalties from the licensee's sublicensing of the software or license fees for using additional copies of the software. If all or a portion of the license fee is based on royalties, it is important that the basis for paying the licensor a portion of such royalties—net sales, gross revenues, number of units—is clearly defined in the license. It is also important that the method of calculating royalty payments—fixed, variable, maximum per month, minimum per month, sliding scale—is clearly defined.

In addition to the payment provisions, the fee section should include other provisions particularly important to the licensor that pertain to payment and reporting of fees. First, the license should include a provision that sets forth the frequency of payments (*i.e.,* monthly or quarterly) and the dates on which payments are to be made. The licensor may want to consider including a provision in the license that imposes a late fee on the licensee for each day the payment is late. Second, the license should always contain a provision stating the currency in which payments are to be made, and if necessary, a method for calculating monetary conversions of such payments. Third, the license should include a provision that requires the licensee to provide the licensor with regular statements that set forth the calculations used to determine the amount of royalty payments or periodic license fees. The license should also include a requirement that the licensee keep complete and accurate records of all transactions involving the licensed software, and allow the licensor, or an independent auditor, to examine such records. Frequently, this latter provision is coupled with a provision that imposes a financial penalty on the licensee for any unpaid fees discovered during the audit and requires the licensee to pay the cost of such audit if the underpayment exceeds a certain amount or percentage of the fees owed to the licensor on an annual or monthly basis. Lastly, some licenses include a provision that allows the licensor to increase license fees during the term of the license. The following is an example of a fee provision that includes an initial fee for the license and a periodic fee for use of additional units of the software under the license:

Section 4. *Fees*

4.1 *Payment of Fees.* License Fees for the license of the Software granted under this Agreement shall include a base fee ("Base Fee") and unit fees ("Unit Fees") determined by the criteria and formula set forth on Exhibit A. Payment of all License Fees shall be made in lawful United States currency and shall in no case be refundable. Licensor shall promptly invoice Licensee for the Base Fee. Licensee shall pay such invoice pursuant to any payment terms stated on the applicable Order Form, or if payment terms are not stated on the Order Form, within 30 days of the invoice. Licensee shall report Unit Fees to Licensor on a calendar-quarter basis, by completing and submitting a report on such fees to Licensor (in such form as Licensor may specify from time to time) within 30 days after the end of each calendar quarter. Licensee shall pay with such report(s) all Unit Fees shown to then be due and owing. All payments not received by Licensor from Licensee when due shall be subject to an interest charge equal to the lesser of (a) one and one half percent (1.5%) of the overdue amount per month, or (b) the maximum rate permitted by applicable law.

4.2 *Fee Increases.* Licensor reserves the right from time to time to increase any of the fees payable under this Agreement. Licensor agrees to give Licensee not less than 90 days' notice of any proposed increase. If any such proposed increase results in a percentage increase in excess of the most recently published percentage increase in

the Consumer Price Index (all items) (or any successor comparable consumer price index) as published from time to time, Licensee shall have the right to terminate this Agreement in accordance with the provisions of Section 9.

4.3 *Recordkeeping and Auditing*. Licensee shall maintain during the term of this Agreement and for two years thereafter complete and accurate books and records of all transactions involving the Software or Documentation. During the term of this Agreement and for two years thereafter, Licensor shall have the right to have an independent accounting firm audit, during Licensee's regular business hours and subject to Licensee's reasonable security requirements, Licensee's books, records, and computer systems that contain information pertaining to this Agreement to determine that Unit Fees paid to Licensor are correct and that Licensee is in compliance with the terms, conditions, and restrictions of this Agreement. Licensor may conduct an audit no more than once every 12 months. All costs of such audit shall be borne by Licensor, except that such expenses shall be borne by Licensee in the event that any audit determines that Licensee has underpaid Unit Fees in any period in excess of five percent (5%). Licensee shall be required to pay to Licensor any underpaid Unit Fees and interest charges thereon shown by an audit.

The license should state which party will be responsible for paying taxes on the transaction. While software has traditionally been delivered on a fixed media—like a computer diskette, CD, or hard drive—it is increasingly being delivered electronically via e-mail or the Internet. The main reasons for this change are the considerable costs and the logistical challenges associated with producing and delivering software on a fixed media. Delivery via e-mail or the Internet is cheaper and easier, and reduces the risk of loss or damage to the software that either party may bear before delivery and acceptance. A second reason for this change is the avoidance of state sales tax. A prewritten computer program transferred in tangible form is subject to state sales tax. 18 Cal Code Regs §1502(f). The same program transferred electronically is not. 18 Cal Code Regs §1502(f)(1)(D). Custom-developed software is considered a service under state law and thus is not subject to state sales tax. 18 Cal Code Regs §1502(f)(2). If the value of the transaction is sufficiently great, the licensor can deliver the software and documentation via e-mail or the Internet, and the transaction will fall within the exemption for intangible personal property, allowing the parties to avoid sales tax. Regardless of how the software is delivered, it is prudent to set forth in the license the party that will be responsible for paying taxes:

4.4 *Payment of Taxes*. Unless Licensee provides Licensor with a valid tax exemption number, Licensee shall be responsible for paying all taxes, assessments, permits, and fees which are, or may be, levied on the Software and Documentation delivered under this Agreement, or their use, exclusive of franchise taxes and taxes based on Licensor's income.

Support and Maintenance

Every licensor wants its licensees to depend on it for support and maintenance, because providing these services creates an additional source of revenue for the licensor. Most software licenses exclude the provision of support and maintenance under the license itself, and instead require the licensee to enter into a separate support and maintenance agreement. The following is a typical support and maintenance provision that appears in a software license:

Section 5. *Support and Maintenance*. Licensor shall have no obligation under this Agreement to provide technical support and maintenance for Licensee's use of the Software. Licensee may elect to receive software support and maintenance after the delivery of the Software under a separate Software Support and Maintenance Agreement between Licensor and Licensee subject to payment of any applicable support and maintenance fees under such agreement.

A complete discussion of the issues that can arise under a software support and maintenance agreement is beyond the scope of this article. Nevertheless, the most important issues warrant a brief discussion. Licensees are eager to subscribe to support and maintenance agreements to ensure that the licensor will be there to fix bugs, provide work-arounds and correct errors, provide periodic upgrades, port the software to new operating systems, and do all of the other tasks required to keep the software current and useful. After all, no one knows the software better than the person who created the product. While fees for support and maintenance vary considerably, a typical support and maintenance agreement will cost the licensee somewhere between 5 and 10 percent of the initial license fee, payable on an annual basis. If you represent the licensee, support and maintenance may very well be the most important service your client receives from the licensor. After all, if the software malfunctions or fails, the cost and disruption to the licensee's business

could be considerable, even catastrophic. As licensee's counsel, you should focus on those provisions of the support and maintenance agreement that are most critical to ensuring your client's continuous and uninterrupted use of the software. For example, how quickly will the licensor respond to problems reported by the licensee? Under what conditions is the licensor obligated to provide support and maintenance to the licensee? Will the licensor provide on-site support and maintenance, or will the licensee have to pack up and ship the software to the licensor? Is the licensor obligated to provide bug-fixes, work-arounds, upgrades, and updates, and if so, how much will these services cost?

In software licenses, express warranties focus on two subjects: performance of the software and ownership of the underlying intellectual property.

If an error in the software threatens the licensee's ability to conduct business, the licensee should demand that the licensor repair the error within a definite period of time (*e.g.,* 24 to 48 hours). The licensee should further demand that the licensor service the software at the licensee's facility and not condition the provision of such services on the licensor's ability to re-create the software error on its own computers. Moreover, the rates at which the licensor agrees to provide these services should be consistent with billing rates negotiated by the parties before entering into the license, and indeed should be set forth in the license or maintenance agreement. The occurrence of a catastrophic software failure is not the time for the licensee to negotiate the terms and cost of support and maintenance services it hopes to receive from the licensor.

Reputable software companies invest considerable resources in servicing and maintaining their products. In the event of a catastrophic software failure, the licensor should be willing to provide on-site support and maintenance within a short period of time. If the error cannot be corrected, the licensor should be willing to provide a short-term work-around, supply an entirely new copy of the software, or refund the license fees paid to date. Competition in the marketplace for software provides a powerful incentive for software companies to be responsive to customers' needs. With respect to errors that do not pose a significant risk to the licensee's business, a licensor will generally agree to respond to such reported errors in a commercially reasonable time and manner. In these instances, the licensor may require that the licensee document the problem and require that the licensor be able to replicate the error at its facility and on its machines. Most software support and maintenance agreements include bug fixes, work-arounds, upgrades, and updates as part of the service, but allow the licensor in its sole discretion to determine when and if such improvements will be issued.

Warranties

California's Uniform Commercial Code recognizes two types of warranties: express and implied. An express warranty is a promise set forth in a contract for sale that the seller makes to the buyer about the goods being sold. Com C §2313. An implied warranty is a promise incorporated by law into virtually every contract for the sale of goods in California. The implied warranty of merchantability states that the goods being sold are fit for the ordinary purposes for which such goods are used. Com C §2314. The implied warranty of fitness for a particular purpose is a promise that the goods are fit for any purpose required by the buyer that the seller knew or had reason to know of at the time of sale. Com C §2315. Licensors can disclaim these implied warranties as long as the disclaimers are clear and conspicuous to the customer. *Burr v Sherwin Williams Co.* (1954) 42 C2d 682, 694, 268 P2d 1041. Express warranties can be omitted from any sales contract by simply stating that the buyer purchases the goods "AS IS." Because software is technically complex and the physical media on which it is stored is inherently unstable, and because it is not possible to know in advance all of the customer's requirements for the software, software companies frequently disclaim all implied warranties, and severely limit any bargained-for express warranties.

In software licenses, express warranties focus on two subjects: performance of the software and ownership of the underlying intellectual property. With respect to performance warranties, if you represent the licensee, you should at a minimum request an express warranty that the software will perform in accordance with the specifications set forth in the licensor's user documentation for the term of the license. The licensee may also wish to request from the licensor additional express warranties that the software (1) is free from defects in design, materials, and workmanship; (2) is delivered in good operating condition; (3) is compatible with the licensee's existing hardware and software and will function effectively when integrated into the existing computing environment; (4) meets the licensee's computing requirements; (5) completes certain functions within designated periods of time; (6) constitutes the most recent release of the software;

(7) does not contain any viruses or other defects that may corrupt or destroy any data it processes; and (8) operates free from any errors and will cause no disruptions in the licensee's business. If you represent the licensor, you know it's virtually impossible to develop software that contains no programming errors. Consequently, advise your client to politely rebuff the licensee's requested warranties, and in response offer to license the software "AS IS." If the licensee refuses to accept such a warranty, the licensor can agree to warrant the software's performance in accordance with the specifications set forth in the licensor's documentation for a specific period of time, perhaps 90 days. The substance and duration of any express warranty will depend on the relative bargaining power of the parties to the license.

To the extent that the licensor agrees to warrant the performance of its software, it should limit its obligations to repair or replace the software in the event that it fails to perform properly.

Warranty disclaimers and limitation-of-liability provisions are legal risk management techniques that allow a licensor to manage its exposure to contractual liability. A software company can also be exposed to tort liability, particularly if it fails to warn its licensees of potential harm that the software can cause to the licensees' computer systems and data. A licensor's liability for negligently failing to warn increases dramatically if a licensor knows the software contains errors that could harm licensees, but nevertheless fails to warn of that problem. To mitigate the risk of tort liability, the licensor should request that the licensee acknowledge in writing that because of the complexity of computer technology, in general, and the software, in particular, the licensor cannot and does not warrant that the software's operation will be uninterrupted and error-free. This disclaimer makes clear that the licensee is on notice of potential problems and helps to absolve the licensor of liability for failing to warn. It also helps ensure that the licensor does not have to fix every error that occurs in the software.

To the extent that the licensor agrees to warrant the performance of its software, it should limit its obligations to repair or replace the software in the event that it fails to perform properly. First, the licensor should seek to limit its obligations under the license by excluding from the warranty all instances where the licensee (1) modifies the software without the licensor's prior consent, (2) reverse-engineers, decompiles, or disassembles the software, or (3) fails to give the licensor notice of any alleged breach of the warranty. The licensor can further limit its obligations under the license by excluding from the warranty any failures in the software that are caused by persons, products, or programs that are not owned by or under the control of the licensor. In addition to narrowing the scope of the warranty, the licensor should seek to limit the licensee's remedies by bargaining for an exclusive remedy. This provision establishes specific actions that the licensor must take in response to a breach of the warranty, and sets forth the licensee's only remedies. A typical exclusive remedy provision states that the licensee's sole remedy in the event of a breach of a performance warranty is correcting the error, replacing the software, or refunding all or a portion of the license fee. Before agreeing to such a provision, the licensee should evaluate whether the exclusive remedies offered by the licensor are adequate to remedy all of the express warranties set forth in the license. In many states, if an exclusive remedy fails in its essential purpose, the licensor will have unlimited liability for all damages suffered by the licensee. *Ragen Corp. v Kearney & Trecker Corp.* (3d Cir 1990) 912 F2d 619, 623. The following provision is an example of a warranty provision commonly used in software licenses:

Section 6. *Warranty*

6.1 *Warranty*. During the initial 90-day term of this Agreement, Licensor warrants that the Software will operate substantially in accordance with the specifications set forth in the Documentation (the "Warranty Period"). Licensor does not warrant that the Software or any portion thereof is error-free. This limited warranty does not cover loss or damage for any: (a) modification or repair of the Software by Licensee or any third party; (b) failure or incompatibility of the Software with computer hardware or other software not supplied by Licensor; or (c) accident, neglect, failure of electric power, storage or use in improper or adverse environmental conditions, misuse, negligence, catastrophe, operator error, or causes other than ordinary and intended commercial use. If Licensee notifies Licensor of the material nonconformance of the Software with the Documentation during the Warranty Period, and if Licensor confirms such nonconformance, Licensor's entire liability and Licensee's sole and exclusive remedy shall be, at Licensor's option, to: (x) correct or provide a bug fix, error correction, or work-around for documented reproducible nonconformance; (y) replace the Software; or (z) refund to Licensee the License Fees received under Section 4, above.

With respect to claims of copyright infringement, a licensee may request the licensor to include a warranty in the license that states unequivocally that the software does not infringe the intellectual property rights of any third party. The licensee wants assurances from the licensor that its use of the software will not subject it to claims of copyright infringement, because the cost of defending such claims and the disruption they pose to the licensee's business can be significant. The licensor will be reluctant to provide a warranty against infringement or misappropriation of trade secrets because it simply may be unaware of a third party possessing intellectual property rights in the software that conflict with or are superior to its own, particularly if trade secrets are involved. In the event the licensee insists that the licensor give a warranty against infringement or misappropriation, the licensor can narrow the scope of that warranty in several ways. First, the licensor can qualify the warranty by stating that the software is not infringing on any third party's intellectual property rights "to the best of the licensor's actual knowledge." Second, the licensor can qualify the warranty by excluding nonmaterial or de minimis acts of infringement. Finally, the licensor can remove infringement or misappropriation from the warranty by agreeing to indemnify the licensee for losses that arise from such claims, but limit the indemnification to a certain amount of money, perhaps the amount of the licensee fee.

In addition to any express warranties set forth in the license, the implied warranties of merchantability and fitness for a particular purpose will apply if the software is considered "goods" under the state's commercial code. Software delivered on a physical media will be considered "goods" under the code. After negotiating the scope of the warranty with the licensee, the licensor should disclaim all other warranties not expressly set forth in the license and all implied warranties. To be effective, this disclaimer must be conspicuous to the licensee and thus should always be set forth in capital letters. Com C §2316. The following is the type of clause frequently found in software licenses:

6.2 *Disclaimer*. EXCEPT AS EXPRESSLY SET FORTH IN SECTION 6.1, LICENSOR DISCLAIMS ALL WARRANTIES, WHETHER EXPRESS, IMPLIED, OR STATUTORY, WITH RESPECT TO THE SOFTWARE, THE DOCUMENTATION, OR OTHERWISE, INCLUDING BUT NOT LIMITED TO THE IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, AND NON-INFRINGEMENT OF INTELLECTUAL PROPERTY RIGHTS.

Limitation of Liability

Almost every commercial contract includes a provision that limits the liability of one or both parties to the contract. Virtually all software licenses contain a limitation-of-liability provision that excludes liability for all damages except direct damages. The limitation provision typically covers all claims arising out of or related to the license or software brought in contract, tort, or infringement that seek to impose liability on the licensor. The types of damages sought under federal and state law, and the methods used to calculate those damages, differ dramatically. The following is a brief discussion of some of the types of damages licensor's counsel should seek to avoid when preparing a limitation-of-liability provision for a license.

With respect to contract claims, the measure of damages for breach of contract depends on the party that breaches the contract and the circumstances surrounding the breach. When a buyer takes possession of goods or is chargeable for the loss or diminution in the value of such goods, the seller is entitled to the contract price. Com C §2709. When the buyer repudiates the contract, wrongfully rejects the goods, or unjustifiably revokes acceptance, the seller's direct damages can be calculated as (1) the difference between the resale price and contract price; (2) the difference between the market price and contract price; or (3) if the first two methods are inadequate to put the seller in as good a position as the buyer's performance, the profits seller would have earned if the buyer had performed fully. Com C §§2706, 2708. Under each of these theories, the seller is entitled to incidental damages which include any commercially reasonable charges, expenses, and commissions incurred retrieving, transporting, caring for, and reselling the goods. Com C §2710. In general, a seller is not entitled to consequential damages under California law.

If, on the other hand, the seller fails to deliver the goods or repudiates the contract, or the buyer rightfully rejects the goods or justifiably revokes acceptance, the buyer can cover with substitute goods and recover damages equal to the difference between the cost of cover and the contract price plus incidental or consequential damages. Com C §2712. If the buyer chooses not to cover, the measure of damages is the difference between the market price and contract price plus incidental damages and consequential damages. Com C §2713. The buyer cannot recover consequential damages, however, if cover could have avoided the loss. Com C §2715(2)(a). If the seller delivers nonconforming goods, the buyer may recover its loss in any manner that is reasonable. Com C §2714(1). If the seller breaches a warranty, the buyer can recover

damages measured as the difference between the value of the goods as accepted and the value they would have had if they had been delivered as warranted. Com C §2714(2). The buyer's incidental damages include expenses incurred inspecting, receiving, transporting, and caring for goods rightfully rejected, any commercially reasonable cost incurred to cover, and any other reasonable expenses due to the delay or other breach. Com C §2715(1). The buyer's consequential damages include any loss resulting from the buyer's requirements and needs that the seller knew of, or should have known of, at the time of contracting that could not be prevented by cover, and any injury to persons or property proximately resulting from any breach of warranty. Com C §2715(2), (3).

With respect to tort claims, when a plaintiff's personal property is damaged, it can recover the depreciation value and loss of use of the property. *Hand Elec., Inc. v Snowline Joint Unified Sch. Dist.* (1994) 21 CA4th 862, 869, 26 CR2d 446. Alternatively, the plaintiff can elect to recover the reasonable cost of repairs and the loss of use of the property while repairs are being made. *Valencia v Shell Oil Co.* (1944) 23 C2d 840, 844, 147 P2d 558. When the plaintiff's property is destroyed, the plaintiff can recover the property's market value. *Hand Elec., Inc. v Snowline Joint Unified Sch. Dist.* (1994) 21 CA4th 862, 870, 26 CR2d 446.

Punitive damages are awarded to punish intentional, malicious, or oppressive conduct and to deter the defendant and other persons from engaging in similar conduct in the future. CC §3294. Punitive damages are recoverable for tort claims, but are not awarded for breach of contract claims. *Cates Constr., Inc. v Talbot Partners* (1999) 21 C4th 28, 61, 86 CR2d 855. Under the Copyright Act, as discussed in detail above, the copyright owner can recover actual damages and defendant's profits, as well as costs and attorney fees. A copyright owner can also pursue equitable relief.

With these potential damages in mind, there are several key issues the parties confront when negotiating a provision that limits their potential liability. First, does the limitation on liability extend to both parties? If the software license authorizes the licensee to (1) bundle the licensor's software with the licensee's or a third party's hardware, (2) embed the licensor's software into the licensee's or a third party's software, (3) sublicense or distribute the licensor's software, or (4) use the licensor's software to process third parties' data, then the licensee has strong grounds for requesting that the limitation of liability apply to itself. If, however, the license simply authorizes the licensee to use the software to process its own data, the licensee has scant legal or factual bases for requesting that the limitation on liability apply to itself as well as to the licensor. Even if the parties agree that the licensee's liability should be limited by the terms of the license, the licensor may want to exclude some of the licensee's obligations from the limitation-of-liability provision. If the parties agree that the licensee's liability should be capped, the licensor should insist that the licensee's payment obligations, including the payment of certain taxes, be excluded from the cap. Moreover, to avoid the possibility of a licensee copying the software, selling it, and retaining some of its profits even after satisfying its contractual liability to the licensor, the licensor should insist on excluding from the cap the licensee's liability for violations of the grant clause and confidentiality provision.

If . . . the license simply authorizes the licensee to use the software to process its own data, the licensee has scant legal or factual bases for requesting that the limitation on liability apply to itself as well as to the licensor.

Second, will the license establish a monetary cap on liability? In the event the licensee suffers an interruption in its business or a loss of data from using the licensor's software, it wants to recover from the licensor for those losses. Because of the inherent complexity of computers and computer software, and because the licensee may use third party software and hardware products over which the licensor has no control, the licensor is reluctant to expose itself to potentially limitless losses incurred by the licensee that result from its use of various hardware and software products. From the licensor's perspective, the licensee is in the best position to avoid or minimize losses that can occur from using a third party's technology. Consequently, the licensor will usually insist on establishing a cap on the amount of money for which it can be liable for claims arising from the license, and will resist the licensee's efforts to establish the cap above the amount actually paid in fees and royalties by the licensee under the license.

Third, what is the proper scope of the limitation provision? Some limitation provisions include all potential claims, while others exclude certain claims. The licensee may have sufficient bargaining power to insist on an indemnification from the licensor for any and all claims filed against the licensee for alleged infringement or misappropriation of the licensed intel-

lectual property rights. Under these circumstances, the licensor may not be able to include infringement and misappropriation claims in the limitation provision, and may be obligated to indemnify the licensee for such claims. The following is a limitation-of-liability provision that covers only the licensor, and carves out an exception for intellectual property infringement, because the licensor has agreed to indemnify the licensee for such claims:

Section 7. *Limitation of Liability*. IN NO EVENT SHALL LICENSOR, OR ITS SUPPLIERS OR LICENSORS, BE LIABLE TO LICENSEE OR ANY THIRD PARTY FOR ANY CONSEQUENTIAL, INCIDENTAL, SPECIAL, INDIRECT, OR EXEMPLARY DAMAGES ARISING OUT OF OR RELATED TO THIS AGREEMENT, THE SOFTWARE, THE DOCUMENTATION, OR OTHERWISE, INCLUDING WITHOUT LIMITATION, DAMAGES FOR LOSS OF PROFITS, BUSINESS INTERRUPTION, LOSS OF DATA, COSTS OF PROCUREMENT OF SUBSTITUTE GOODS OR SERVICES OR FOR ANY CLAIM OR DEMAND AGAINST LICENSEE BY ANY OTHER PARTY, OR OTHER PECUNIARY LOSS, EVEN IF LICENSOR HAS BEEN ADVISED OF OR KNOWS OF THE POSSIBILITY OF SUCH DAMAGES. IN NO EVENT WILL LICENSOR'S AGGREGATE LIABILITY FOR ANY AND ALL CLAIMS RELATING TO THIS AGREEMENT, THE SOFTWARE, OR THE DOCUMENTATION, WHE-THER IN CONTRACT, TORT, OR ANY OTHER THEORY OF LIABILITY, EXCEED THE FEES PAID BY LICENSEE UNDER THIS AGREEMENT DURING THE 12-MONTH PERIOD PRECEDING THE EVENT GIVING RISE TO SUCH LIABILITY, EXCEPT FOR LICENSOR'S LIABILITY UNDER SECTION 8, BELOW. LICENSEE ACKNOWLEDGES THAT THE AMOUNTS PAYABLE HEREUNDER ARE BASED IN PART ON THESE LIMITATIONS, AND FURTHER AGREES THAT THESE LIMITATIONS SHALL APPLY NOTWITHSTANDING ANY FAILURE OF ESSENTIAL PURPOSE OF ANY LIMITED REMEDY.

Some states will refuse to enforce a limitation-of-liability provision in cases in which the exclusive remedy provided in the license fails in its essential purpose. These decisions typically arise in connection with a license provision that limits the licensor's liability and the licensee's remedies to repair or replacement of the software in the event the software fails to perform properly. Under California contract law, when circumstances cause an exclusive or limited remedy to fail in its essential purpose, the injured party can seek any remedies available to it under the Commercial Code. Com C §2719(2). Moreover, in California, consequential damages can be limited or entirely excluded, unless such limitation or exclusion is found to be unconscionable. Com C §2719(3).

Indemnification

Under an indemnification provision, one party to a contract (the indemnitor) agrees to bear or reimburse all costs, expenses, and related damages owed or paid by the other party to the contract (the indemnitee). Often indemnification is limited to situations in which the damages are related to the indemnitor's negligent acts or omissions or to the indemnitor's breach of one or more terms of the contract. Often the obligation to indemnify is coupled with an obligation to defend the indemnitee against claims arising out of the contract or transaction as long as the indemnitee complies with certain requirements set forth in the contract. In the context of a software license, a licensee frequently will request the licensor to indemnify it for losses or damages arising out of claims that the licensed software infringes a third party's intellectual property rights. A licensee will also request the licensor to indemnify it for claims arising out of failures or errors in the licensor's software that cause a loss of third party data or disrupt a third party's business.

When the licensor's software is bundled with a licensee's hardware or embedded into a licensee's software, the licensee may request that the licensor indemnify it for any claims that arise out of the use of the bundled product or embedded software to the extent that such claims can be attributed to the licensor's software. From the licensor's perspective, the breadth of an indemnification provision requested by the licensee can be potentially limitless. When negotiating this provision, a licensor can narrow the grounds on which it agrees to indemnify the licensee by excluding certain events or circumstances that might otherwise give rise to a claim. Compelling grounds for excluding a licensee's claim for indemnification can include: (1) the use of an obsolete version of the software; (2) the unauthorized modification of the software by the licensee or a third party; or (3) the combination of the licensor's software with the licensee's technology if such claim would not be sustained in the absence of the combined product.

The licensee will also request the licensor to indemnify it for third party claims alleging infringement or misappropriation of trade secrets. A licensor will strongly resist this request because of concerns about innocent infringement or misappropriation of a third party's intellectual property rights. Because of the flow of information throughout the technology community and the constant movement of technologists

from company to company, a licensor cannot be certain that the trade secrets and source code used to develop a software product have not been misappropriated. The licensor will also resist a licensee's request for indemnification because of the cost of defending such suits. Most lawsuits alleging copyright infringement or misappropriation of trade secrets are extremely complex and involve legions of lawyers and expert witnesses. The cost of litigating such claims is prohibitive, particularly for small software companies. It is not surprising, therefore, that licensors generally refuse to indemnify licensees for infringement and misappropriation claims.

If you represent the licensor, and the parties agree that the license should contain an indemnification provision, make sure the provision contains several points. First, the provision should be drafted to ensure that the licensor maintains complete control of the defense and receives from the licensee the assistance necessary to mount a successful defense or settle the case. Second, exclude from the provision's coverage all instances where the licensor's software is not responsible for the event that gives rise to the claim. Third, impose a financial cap on the licensor's duty to indemnify the licensee. This cap should be established at an amount equal to no more than the license fees and royalties, if any, that the licensor has received from the licensee under the license. Fourth, limit the licensee's remedies to (1) modifying the software so that it no longer infringes, (2) replacing the software with non-infringing software, or (3) returning the license fees to the licensee. From the licensee's perspective, the indemnification provision must survive expiration or termination of the license because infringement claims may very well be filed after the license has terminated or expired. The following is an example of an indemnification provision that can be used in a license agreement:

Section 8. *Indemnification*

8.1 *Indemnification*. Licensor will defend any action brought against Licensee by a third party to the extent that it is based on a claim that the Software or Documentation supplied by Licensor under this Agreement, when used by Licensee as authorized under Section 2, infringes any third party copyright or trade secret. Licensor will pay any award against Licensee, or settlement entered into on Licensee's behalf, based on such infringement, only if Licensee: (a) notifies Licensor promptly in writing of the claim; (b) provides reasonable assistance in connection with the defense and/or settlement of the claim; and (c) permits Licensor to control the defense and/or settlement of the claim. In the event of an infringement action against Licensor with respect to the Software, or in the event Licensor believes such a claim is likely, Licensor shall be entitled at its option to (x) appropriately modify the Software, or substitute other software which, in Licensor's opinion, does not infringe any third party Intellectual Property Rights; (y) obtain a license with respect to the applicable third party Intellectual Property Rights; or (z) if neither (x) nor (y) is commercially practicable, terminate this Agreement and refund to Licensee the License Fees received by Licensor under Section 4.

8.2 *Limitations and Exclusive Remedy*. Licensor shall have no liability to Licensee under any provisions of this Section 8 to the extent that any infringement or claim thereof is based on: (a) modifications to the Software or Documentation made by Licensee or a third party other than Licensor; (b) the use of other than the most current release of the Software or Documentation delivered by Licensor to Licensee if such claim would have been prevented by the use of the most current release made available to Licensee by Licensor; or (c) the combination of the Software with other equipment or software not provided by Licensor if such claim would have been prevented but for such use or combination. Licensee agrees that it shall at its own expense defend and hold harmless Licensor from any action instituted against Licensor resulting from infringement claims based on any of the foregoing. NOTWITHSTANDING ANY OTHER PROVISION IN THIS AGREEMENT TO THE CONTRARY, THIS SECTION 8 STATES LICEN-SOR'S ENTIRE LIABILITY FOR ACTUAL OR ALLEGED INFRINGEMENT OF ANY THIRD PARTY INTELLECTUAL PROPERTY RIGHTS AND LI-CENSEE'S SOLE AND EXCLUSIVE REMEDY FOR ANY CLAIMS OF INFRINGEMENT OF SUCH THIRD PARTY INTELLECTUAL PROPERTY RIGHTS.

Term and Termination

The term of a software license can be perpetual or for a period of years. The duration of the license depends on the purposes for which the software will be used and the relationship of the parties. Frequently more important than the term of the license are the conditions under which the license may be terminated. At a minimum, the licensor wants to ensure that it can terminate the license in the event the licensee fails to fulfill its financial obligations under the

license or the licensee's continued use of the software jeopardizes the licensor's intellectual property rights. The licensee, on the other hand, wants to ensure that the licensor cannot arbitrarily terminate the license after the licensee has invested considerable time and money installing and integrating the software into its business operations. A well-drafted termination provision should define the specific conditions that give rise to early termination of the license. These conditions typically include some or all of the following: (1) a material breach of the license by either party; (2) infringement of copyrights; (3) misappropriation of trade secrets; (4) change of control of the licensee; (5) bankruptcy or insolvency of either party; or (6) failure of either party to meet a performance condition (*e.g.*, sales quota, timely preparation of a derivative work). A well-developed termination provision should also set forth the obligations of the parties after the license terminates, and should always include a provision that explicitly states which provisions of the license survive termination of the license. The following is an example of a term and termination provision for a software license:

Section 9. *Term and Termination*

9.1 *Term*. The term of this Agreement shall commence on the Effective Date and end on the Expiration Date set forth in Exhibit A, or if the term as specified in Exhibit A is perpetual, will continue indefinitely, unless in either case this Agreement is earlier terminated pursuant to this Section 9.

9.2 *Termination*. Either party may terminate this Agreement on 30 days' written notice of a material breach of this Agreement if the breaching party has not cured such breach within such 30-day period. The parties acknowledge and agree that Licensee may at any time delay, interrupt, or cease use of the Software or Documentation, but this Agreement shall continue in full force and effect. Licensor shall have the right to terminate this Agreement immediately, without Licensee having an opportunity to cure, on notice that Licensee has used the Software or Documentation outside the scope of uses permitted in Sections 2.1 and 2.2. Licensee shall have the right to terminate this Agreement as provided in Section 4.2, subject to the terms, conditions, and limitations thereof. Licensee expressly agrees that termination of this Agreement shall not discharge any payment obligations accrued as of the date of such termination, even if such obligations are payable after the termination date, or entitle Licensee to a refund of any amount previously paid to Licensor.

9.3 *Insolvency*. On: (a) the institution of any proceedings by or against either party seeking relief, reorganization, or arrangement under any laws relating to insolvency, which proceedings are not dismissed within 60 days; (b) the assignment for the benefit of creditors, or the appointment of a receiver, liquidator, or trustee, of any or either party's property or assets; or (c) the liquidation, dissolution, or winding up or either party's business; then, and in any such event, this Agreement may immediately be terminated by the other party on written notice.

9.4 *Effect of Termination*. On termination of this Agreement, Licensee shall immediately cease using the Software and Documentation and immediately return to Licensor, or certify the destruction of, all copies of the Software and Documentation in Licensee's possession or under its control.

9.5 *Survival of Certain Terms*. The rights and obligations contained in Sections 1, 2.2, 2.3, 2.4, 4.3, 6.2, 7, 8, 9.5, 10, 11, and 12 and all payment obligations incurred prior to the termination of this Agreement shall survive any termination of this Agreement.

When representing either party to a software license, but particularly the licensee, it is important to be aware of the consequences of one party entering bankruptcy. Section 365 of the United States Bankruptcy Code, which applies to executory contracts, allows a trustee or debtor-in-possession to assume or reject any executory contract. 11 USC §365(a). Most software licenses are executory contracts, because one party to the contract typically owes an on-going performance obligation to the other party; this can include maintaining confidential information, paying and reporting royalties, indemnifying the other party or fulfilling any other material obligation owing under the license. In the event a bankruptcy trustee rejects the license, the non-bankrupt licensee maintains a claim for damages for breach of contract, but the value of such a claim is limited because it is a general unsecured claim in bankruptcy. For a licensee that licenses mission-critical software from a bankrupt licensor, termination of the license can have a significant impact on its business. Once the license is terminated, the licensee no longer has a right to use the software, and if it continues to do so may be sued for infringement. Moreover, regaining the right to license the software will likely cost the licensee considerably

more than it originally paid the now-bankrupt licensor.

Section 365(n) of the Bankruptcy Code was enacted specifically to remedy this problem. The section entitles a licensee of intellectual property to elect to reinstate a license that has been rejected by a bankruptcy trustee and maintain the intellectual property rights it possessed immediately before the bankruptcy filing. In exchange for reinstating these intellectual property rights, the licensee must continue to pay all license fees and royalties owing to the licensor. Other than the right to continue to use the software, the licensee is not entitled to performance of any of the other obligations the licensor owed to the licensee under the original license, including technical support and maintenance. While better than losing all rights to use the software, the result of electing to reinstate the license under 11 USC §365(n) can be troublesome for a licensee who entered into an object code software license in which technical support and maintenance constituted an important part of the original agreement. The most cost effective way for the licensee to ensure that it will receive support and maintenance, and at least some of the other services it bargained for, is to enter into a fully paid source code license or fully paid object code license coupled with a source code escrow agreement. Either agreement, if structured properly, will allow the licensee to gain immediate access to the source code in the event of the licensor's bankruptcy, and provide the licensee with an opportunity to get the technical support and maintenance it needs without having to pay additional license fees.

Confidentiality

While confidentiality obligations are typical in object code licenses, they are essential in source code licenses to protect the licensor against disclosure of the source code and duplication and distribution of the software. In the course of negotiating and implementing a license, trade secrets and other confidential information are often communicated and transferred between the parties. It is crucial to protect against the unauthorized disclosure of this information, and thus prudent to include a confidentiality provision that restricts the use and disclosure of the confidential information by the recipient and individuals working for the recipient. First and foremost, a confidentiality provision should define the information and materials to which it applies. Often the term "confidential information" is defined to include all information owned by the disclosing party that relates to the subject matter of the license and for which reasonable measures are taken by each party to protect the confidentiality of the information. A confidentiality provision should be effective for the term of the license and for some period of time thereafter so as to protect against improper use of the information after the license has terminated. The confidentiality provision should always require the recipient to return or destroy all copies of confidential information received during the course of the license once the license is terminated or expires. A confidentiality provision often contains exemptions for certain circumstances under which disclosure of the information by the recipient is permissible. These circumstances can and frequently do include instances in which the information is already in the public domain, disclosed to the recipient by a third party who has authority to do so, or disclosed when compelled by statute, regulation, or administrative or court order. The following confidentiality provision is a good example of the type of provision contained in many software licenses:

Section 10. *Confidentiality*

10.1 *Confidential Information.* "Confidential Information" means any information disclosed by one party to the other party under this Agreement which is in written, graphic, machine readable, or other tangible form, and is marked "Confidential," "Proprietary," or in some other manner to indicate its confidential nature. Confidential Information may also include oral information disclosed by one party to the other party under this Agreement, provided that such information is designated as confidential on or before the time of its disclosure and reduced to writing by the disclosing party within a reasonable time (not to exceed 30 days) after its oral disclosure, and such writing is marked in a manner to indicate its confidential nature and delivered to the receiving party during the term of this Agreement. Notwithstanding any failure to so identify it in a timely manner, all Software and Documentation shall be considered Confidential Information of the Licensor.

10.2 *Confidentiality.* Each party shall treat as confidential all Confidential Information of the other party, shall not use such Confidential Information except as set forth in this Agreement, and shall use reasonable efforts not to disclose such Confidential Information to any third party. Without limiting the foregoing, each of the parties shall use at least the same degree of care which it uses to prevent the disclosure of its own confidential information of like importance to prevent the disclosure of Confidential Information disclosed to it by the other party under this Agreement. Neither Licensor nor Licensee shall dis-

close any Confidential Information of the other party to any person or entity that has not agreed in writing to keep such information confidential. Each party shall promptly notify the other party of any misuse or unauthorized disclosure of the other party's Confidential Information.

10.3 *Exemptions*. The restrictions set forth in Section 10.2 will not apply to information that: (a) is known to the receiving party at the time it receives Confidential Information from the disclosing party; (b) has become publicly known through no wrongful act of the receiving party; (c) has been rightfully received by the receiving party from a third party authorized to make such communication without restriction; (d) has been approved for release by written authorization of the disclosing party; (e) is required by law to be disclosed after written notification by the receiving party; or (f) is independently developed by the receiving party without breaching this Agreement.

10.4 *Injunctive Relief*. The parties agree that any breach of the restrictions set forth in this Section 10 will cause irreparable harm to the non-breaching party, entitling such party to injunctive relief in addition to all other legal remedies.

If the licensed software contains trade secrets, the confidentiality provision in the license should state that such information should be disclosed only to individuals working for the licensee who have a need to know the information to implement the license. Moreover, the license should explicitly require that each individual who has access to the licensed software enter into a confidentiality and nondisclosure agreement with the licensee employer that forbids the individual from disclosing the trade secrets or copyrights or using them for purposes beyond the scope of the grant clause. Ideally, these agreements should be enforceable by the licensor and the licensee should be responsible for damages incurred by the licensor that are caused by the breach of such agreements. Disclosure of trade secrets to individuals not bound by confidentiality agreements, including employees who do not have a need to know the trade secrets, can result in widespread disclosure of the information and its subsequent loss of trade secret status under state law. Those individuals employed by the licensee company who are not contemplated by the contracting parties to have a use for the trade secrets should not have access to such trade secrets.

Assignments and Transfers

Nonexclusive copyright licenses are personal and nontransferable and thus may not be assigned or transferred without the consent of the copyright owner. *Harris v Emus Records Corp.* (9th Cir 1984) 734 F2d 1329, 1333. This rule applies in bankruptcy proceedings as well as mergers and acquisitions. *SQL Solutions, Inc. v Oracle Corp.* (ND Cal, Dec 18, 1991, No C–91–1079–MHP) 1991 US Dist Lexis 21097. Exclusive licenses can be transferred without the consent of the copyright owner. When it comes to transfers or assignments of a license, the licensor and licensee's interests frequently are diametrically opposed to one another's.

For a number of reasons, the licensor does not want the licensee to have the right to unilaterally assign or transfer the license to a third party under any circumstances. From a competitive standpoint, the licensor wants to maintain as much control as possible over the distribution and use of its software. Moreover, the licensor likely does not want one of its competitors to gain access to its software via a merger or asset acquisition. From a legal perspective, the licensor does not want an acquirer who has been infringing its software to purchase a license through a merger or acquisition and consequently be able to cut off what should be on-going claims of infringement. From a financial perspective, the licensor wants to be able to control the amount of royalties it seeks and receives from each of its licensees. While the licensor may have been willing to license its software to a small company at one price, it may not be willing to license the same software to a larger company at the same price, and indeed would choose to charge a higher price to such company.

The licensee, on the other hand, commonly requests the right to transfer the license to an affiliate or third party in a merger or asset purchase transaction. The licensee's primary motivation is that it does not want the licensor to exert excessive influence over how the licensee conducts its business, particularly if the licensee is contemplating a merger or sale of assets to a third party. The licensee fears that once the licensor receives a request to consent to the assignment of a license in a merger or asset acquisition, the licensor will attempt to extract additional payments from the licensee in consideration for consenting to the transfer. The licensee also fears that the licensor may impose a myriad of conditions on the use of the license after the transfer, or may simply delay or stop the transaction in its tracks.

If at all possible, avoid including a provision in the license that states "the licensee may not assign the license without the consent of the licensor which shall not be unreasonably withheld."

Two major consequences typically flow from the unauthorized transfer of copyright licenses in mergers and asset acquisitions. First, if the purchaser acquires a license, and the licensor has not consented to the transfer of the license, the purchaser infringes the copyright and is liable to the licensor for actual damages and profits gained from the infringement. Second, the purported transfer may be a breach of the license and thus provide the licensor with grounds to terminate the license and seek damages for the breach. The following is a form of licensor-friendly assignment provision:

Section 11. *Assignment*. This Agreement shall be binding on and inure to the benefit of the parties hereto and their permitted successors and assigns. The Licensor may assign or transfer this Agreement with prior notice to the Licensee. The Licensee may not assign or transfer, whether by merger, operation of law, or otherwise, any of its rights or delegate any of its obligations hereunder without the prior written consent of Licensor, which may be withheld in the Licensor's sole discretion.

If you represent the licensor, make sure you preserve the licensor's right to consent to assignments and transfers of licenses in its sole discretion. If at all possible, avoid including a provision in the license that states "the licensee may not assign the license without the consent of the licensor which shall not be unreasonably withheld." Under California law, if the proposed assignee can financially perform the contract, it is unreasonable for the licensor to withhold its consent. If the licensor unreasonably withholds its consent, it breaches the license agreement and may be liable for all consequential damages that flow from the breach. If the breach scuttles a merger transaction, those damages can be considerable. If licensee's counsel insists on including the qualification that consent not be unreasonably withheld, licensor's counsel should offer a compromise provision that states something like the following: "Licensee may not assign or transfer the license without the licensor's prior written consent which shall not be unreasonably withheld, provided however it shall not be unreasonable for the licensor to withhold its consent under the following circumstances:" The parties can then negotiate the circumstances under which the licensor may reasonably withhold its consent to transfers of the license.

If you represent the licensee, your goal should be to carve out those exceptions to a blanket prohibition against assignments and transfers of the license that are most important to your client and that are fair to the licensor in the context of the original transaction. For example, the licensee can argue that it should be permitted to transfer the license to an affiliate as long as certain conditions are met, *e.g.*: (1) the parent maintains sufficient control over the affiliate and its use of the license so as to ensure no infringement, (2) the parent remains responsible for paying all fees and royalties and fulfilling all of the licensee's obligations under the license, and (3) appropriate confidentiality provisions are included in the license or in a separate confidentiality agreement entered into by the affiliate. As a second example, the licensee can request the right to transfer the license in a merger or asset purchase transaction if such transfer is not made to (1) a competitor, (2) a third party that currently licenses the same software on different terms or at a higher price, or (3) a third party the licensor determines is infringing on the copyrighted software. In each of these three instances, the licensor should be permitted to withhold its consent to an assignment or transfer of the license. In other instances, the licensee can make a persuasive case for being allowed to transfer the license. Without this right, it may be difficult, if not impossible, to complete a merger or asset acquisition, particularly if the technology subject to the license is extremely valuable or central to the transaction.

Miscellaneous Provisions

The final section of a software license often contains a number of miscellaneous provisions that are important to the administration and enforcement of the license. This section briefly discusses some of the more important provisions found in this section of a software license.

Integration

Under prior California law, whether extrinsic evidence could be considered when interpreting the intent of the parties to a contract depended on whether the agreement constituted the complete expression of the parties. *Spurgeon v Buchter* (1961) 192 CA2d 198, 203, 13 CR 354. Under current law, the terms the parties set out in writing and intend as the final expression of their agreement cannot be contradicted by evidence of a prior or contemporaneous agreement, but may be explained or supplemented by (1) course

of dealing, (2) usage of trade, (3) course of performance, and (4) consistent additional terms, unless the court finds the writing to be a complete and exclusive statement of the terms of the agreement. Com C §2202. Current law, rather than assuming the parties intended a fully integrated document, assumes that a written contract does not express the complete agreement of the parties unless the court expressly makes such a finding. It is extremely important that the license clearly state that it constitutes the final written agreement between the licensor and licensee and supersedes and replaces any prior negotiations or agreements between them. The following is a form of merger clause that should be used in a software license to avoid any confusion with respect to the intent of the parties:

Section 12. *Miscellaneous Provisions*

12.1 *Entire Agreement*; *Amendment*. This Agreement, including all Exhibits hereto, constitutes the final, complete, and entire agreement between the parties with respect to the subject matter hereof, and supersedes any previous proposals, negotiations, agreements, or arrangements, whether verbal or written, made between the parties with respect to such subject matter. This Agreement shall control over any additional or conflicting terms in any of Licensee's purchase orders or other business forms. This Agreement may be amended or modified only by a written agreement signed by authorized representatives of the parties.

In general, a written license can be modified or amended by express, written agreement of the parties. A written license that prohibits modification except by a signed writing cannot be modified orally. Com C §2209(2). An attempt to orally modify a written agreement that requires written modification can operate as a waiver. Com C §2209(4).

Governing Law and Jurisdiction

In general, the licensor prefers to bring claims for infringement or breach of contract in federal court because federal law protects the licensor's copyrights. If the licensee infringes the copyright, the licensor wants to be able to seek an injunction from a federal court to enjoin the continuing infringement. The licensee, on the other hand, wants to arbitrate infringement and breach of contract claims brought against it to reduce its legal costs and minimize the disruption an injunction would impose on its business operations. The following is a governing law and jurisdiction provision that ensures that the licensor will be able to quickly pursue equitable relief in the jurisdiction of its choice upon discovering copyright infringement:

12.2 *Governing Law and Jurisdiction*. This Agreement shall be governed by and construed under the laws of the State of California without giving effect to that state's conflict-of-law principles. The parties hereby submit to the personal jurisdiction of, and agree that any legal proceeding with respect to or arising out of this Agreement shall be brought in the United States District Court for the _ _[*name of district*]_ _ of California or the Superior Court of the State of California for the County of _ _[*name of county*]_ _. The parties agree that the United Nations Convention on Contracts for the International Sale of Goods shall not apply to this Agreement.

Remedies and Attorney Fees

If you represent the licensor, always include an attorney fees clause in the license to ensure that the licensor can recover those fees in the event that it brings an action to enforce the license. In addition, seek to extend such a clause to cover the costs associated with expert witness fees, because these fees can easily exceed attorney fees in intellectual property litigation.

The provision below ensures the parties that, except as otherwise expressly set forth in the license, all remedies are cumulative and not exclusive. Moreover, it provides that the prevailing party in a suit to enforce or interpret the license will be entitled to attorney fees, costs, and expenses.

12.3 *Remedies*. Except as otherwise expressly provided herein, any remedy provided for in this Agreement is deemed cumulative with, and not exclusive of, any other remedy provided for in this Agreement or otherwise available at law or in equity. The exercise by a party of any remedy shall not preclude the exercise by such party of any other remedy. Should suit be brought to enforce or interpret any part of this Agreement, the prevailing party shall be entitled to recover, as an element of the costs of the suit and not as damages, reasonable attorney fees to be fixed by the court, including without limitation, the costs, expenses, and fees of any appeal.

Notice

Most license agreements require that any notices required to be given under the license be set forth in writing. A writing requirement minimizes the risk of

miscommunication between the licensor and licensee. The following is a standard notice provision found in a software license:

12.4 *Notices.* All notices permitted or required under this Agreement shall be in writing and shall be delivered in person or mailed by first class, registered, or certified mail, postage prepaid, to the address of the party specified in this Agreement, or such other address as either party may specify in writing. Such notice shall be deemed to have been given upon receipt.

Waiver

Regardless of whether you represent the licensor or licensee, a waiver of any term, provision, or breach of the license should always be set forth in writing and signed by the waiving party. Moreover, the written waiver of a single event should never be permitted to apply to subsequent events. The following is a standard waiver provision:

12.5 *Waiver.* No term or provision of this Agreement shall be deemed waived and no breach excused, unless such waiver or consent is in writing and signed by the party claimed to have waived or consented. Any consent by any party, or waiver of a breach by the other, whether express or implied, shall not constitute a consent to, waiver of, or excuse for any other different or subsequent breach.

Agency

The licensor and licensee under the terms of the license set forth in this article have entered into an arm's-length transaction under which neither party serves as an agent or representative of the other party. Even though the licensor is licensing software to the licensee to use in its business operations, by doing so the licensor in no way becomes responsible for the licensee's business or operations. The following is a standard agency provision:

12.6 *Independent Contractor.* The parties' relationship shall be solely that of independent contractors, and nothing contained in this Agreement shall be construed to make either party an agent, partner, representative, or principal of the other for any purpose.

Federal Government Licenses

The federal government licenses a considerable amount of intellectual property from private companies for use in conducting government business. In doing so, under certain circumstances, the government seeks to include specific requirements in the license so that it may use the intellectual property in a manner not otherwise provided for by the licensor. Software that meets certain definitions and requirements set forth in the Federal Acquisition Regulations will be licensed by the federal government under the same terms under which it would be licensed by a private company. The following is a provision that should be included in all software licenses to ensure that the federal government will license the product on essentially the same terms as a private licensee:

12.7 *U.S. Government Licenses.* The Software and Documentation are considered a "commercial item" as that term is defined at 48 CFR §2.101, or "commercial computer software" and "commercial computer software documentation" as such terms are used in 48 CFR §12.212 of the Federal Acquisition Regulations and its successors, and 48 CFR §227.7202–1 of the DoD FAR Supplement and its successors.

Severability

The following is a severability provision that helps to ensure that if a provision or term of the license is found by a court of competent jurisdiction to be void or unenforceable, the remaining provisions of the license shall remain effective and enforceable:

12.8 *Severability.* If any provision of this Agreement is held by a court of competent jurisdiction to be void or unenforceable, the other provisions shall remain in full force and effect.

Compliance

The following is a provision under which the licensee agrees to comply with all laws and regulations that apply to the use and operation of the software and to indemnify the licensor for all claims arising out of the licensee's failure to do so:

12.9 *Compliance With Law.* Licensee shall comply with all applicable laws and regulations (including privacy laws and regulations) having application to or governing its use and/or operation of the Software, and agrees to indemnify and hold Licensor harmless from and against any claims, damages, losses, or obligations suffered or incurred by Licensor arising from its failure to so comply.

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

LICENSOR

Name: ____________________
Signature: _________________
Title: _____________________
Date: _____________________

LICENSEE

Name: ____________________
Signature: _________________
Title: _____________________
Date: _____________________

CONCLUSION

When negotiating and preparing a software license, attorneys representing the licensor and licensee should always keep the following issues in mind:

1. Verify that the licensor actually owns the underlying copyrights or trade secrets for the software being licensed.

2. Make sure that the license clearly and concisely sets forth the parties who may use the software, the software being licensed, and the defined terms that govern the agreement.

3. Make sure that the grant clause states precisely what the licensee can do with the software. All copyright rights are reserved to the copyright owner except those expressly granted to the licensee.

4. Immediately after the grant clause, include a covenant that states that the licensee will only use the software in accordance with the scope of the grant clause. If the licensee uses the software beyond the scope of the grant, it has infringed the copyright and breached the contract.

5. The license must state that the licensor retains all ownership interests in the software and user documentation, the licensee receives a mere license to use the software and documentation in accordance with the terms of the license, and no rights are transferred to the licensee by implication, estoppel, or otherwise.

6. If you represent the licensor, offer to warrant the software "AS IS" and disclaim all implied warranties. If you represent the licensee, request a warranty that the software will perform in accordance with the specifications in the user documentation for the term of the license.

7. If you represent the licensor, include a limitation-of-liability provision that limits the licensor's liability to only those direct damages that result from claims arising out of or related to the license, software, or documentation. If you represent the licensee, request that the limitation-of-liability provision be reciprocal.

8. If you represent the licensor, the indemnification provision must: (a) ensure that the licensor will have complete control of the defense and the assistance needed to mount a successful defense or reach settlement; (b) exclude from coverage all instances where the software does not give rise to the claim; (c) impose a financial cap on the indemnification; and (d) limit the licensee's remedies to modifying or replacing the software or returning the license fees. If you represent the licensee, the indemnification provision must survive termination of the license, because infringement claims may be filed after termination.

9. The termination provision must specify all conditions that result in early termination and should include: (a) material breach of the license; (b) infringement of copyrights; (c) misappropriation of trade secrets; (d) change of control of the licensee; (e) bankruptcy or insolvency; and (f) failure to meet a performance condition. The termination provision should set forth the parties' obligations after the license terminates and the provisions that survive termination.

10. In the event that the licensor files for bankruptcy, the most cost-effective way for the licensee to ensure that it continues to receive support, maintenance, and any other services it is entitled to under the license, is to enter into a fully paid source code license or fully paid object code license, coupled with a source code escrow agreement, prior to the bankruptcy.

11. Make sure the confidentiality provision limits the distribution of confidential information to those persons working for the recipient who have a need to know the information to implement the license and have entered into written confidentiality and nondisclosure agreements with the recipient company.

12. If you represent the licensor, make sure you preserve the licensor's right to consent to all assignments and transfers of the license in its sole discretion. If you represent the licensee, carve out those exceptions to a blanket prohibition against assignments and transfers that are most important to your client and fair and reasonable to the licensor.

13. Make sure that the licensor can file suit in the court of its choosing to enjoin the licensee from infringing on intellectual property rights, breaching the license, or otherwise using the software in a manner that jeopardizes its continued commercial value.