

Be Wary of Warranties for Software Design

IN SHORT

The Situation: Whether warranties accompany software used in other products turns on many factors, including whether the designer is providing a "good" or "service," statements in advertising, representations made in sales pitches, contractual terms, and state law.

The Issue: How can software suppliers balance their interest in promoting and selling their software while protecting themselves from unexpected liability for breach of warranty?

Looking Ahead: Careful planning and scrutiny of projects, promotional materials, sales presentations, and contracts can reduce the risk of liability for software suppliers while not inhibiting product sales.

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Software drives myriad products that can injure people (such as autonomous vehicles), damage property (such as robots), or create new, unpredictable risks (such as artificial intelligence). To avoid or mitigate the risk of liability, the software supplier should plan carefully from the moment it begins to design, promote, and sell its software. We will use California law to explain a number of factors to consider.

"Good" or "Service"

Courts define software as a "good" when a transaction involves pre-packaged software, even if there are service modifications or ancillary services incidental to the transaction. Courts view software as a "service" when a transaction involves designing software from scratch or acquiring a manufacturer's skill or knowledge in software design. The distinction matters.

The California Commercial Code ("Code") governs transactions involving "goods," including how manufacturers can disclaim implied warranties. In addition, California's Song-Beverly Consumer Warranty Act ("Act") supplements the Code and applies to the sale of a "good." The Act prevents a component-part manufacturer from disclaiming implied warranties if it provides an express warranty. However, if the component-part manufacturer does not provide an express warranty, the Code will permit the component-part manufacturer to disclaim implied warranties and to limit remedies for breach of warranty.

Common law contract principles govern a transaction for a "service." Common law principles allow parties to limit or provide warranties and remedies.

The software designer and supplier may be able to shape the transaction to influence the determination of software as a "good" or "service." The supplier should be aware of and plan for the legal consequences, such as through contract terms or insurance.

Express Warranty

An express warranty is an explicit promise that software will perform in a particular way. An express warranty may arise from a representation that software meets an industry standard or a performance standard, an agreement to certain specifications, factual statements of performance in advertising, or the providing of a sample or model. The word of caution is to scrutinize representations before making them.

Readily Identifiable Software

A software supplier may become obligated to indemnify a retail seller or compensate a consumer if the software is readily identifiable and important to the consumer—for example, a name-branded component part with recognized software. Marketing the software as part of selling the product, therefore, has a potential cost to consider.

Participation in the Design of the End Product

The more that the software designer takes part in the design specifications for the end product or the integration of the software into the product, the more risk it assumes.

Implied Warranty of Fitness for a Particular Purpose



Courts define software as a 'good' when a transaction involves pre-packaged software and as a 'service' when a transaction involves designing software from scratch or acquiring a manufacturer's skill or knowledge in software design. The distinction matters.



This implied warranty comes into play when the software supplier knows of the buyer's particular purpose and reliance on the supplier's skill and judgment to provide suitable software. A supplier can disclaim this implied warranty.

Implied Warranty Created by Conduct or Custom

Course of performance, course of dealing, or usage of the trade can create this implied warranty. Repeatedly accepting an obligation to replace defective software or honoring an implied warranty even if disclaimed can amount to course of performance. Usage of trade turns on standard, accepted practices in the field that are deemed to be part of the parties' agreement, such as a permissible level of coding errors. Because express contractual terms often prevail, appropriate terms in a sales agreement can mitigate the risk.

Implied Warranty of Merchantability

This implied warranty promises that the software meets the standards of performance expected by merchants in the trade. Suppliers can disclaim this implied warranty or agree with purchasers to particular terms that will supersede it.

Disclaimer of Implied Warranties

Unless prohibited by the Act, the Code allows sellers to disclaim any express and implied warranty. Software suppliers may decide to provide a limited, exclusive, and express warranty (such as meeting a particular specification or industry standard) and then disclaim all other warranties. Disclaimers must be specific and conspicuous; state law and practice provides the important language and format for disclaimers. If the Act applies to a transaction, for example, the disclaimer must say that the goods are sold "as is" or "with all faults."

Warnings and Instructions

Specific warnings and instructions can help to avoid or reduce liability. To develop appropriate warnings, software suppliers should evaluate the potential misuses or unintended uses of their software, its foreseeable failure modes, foreseeable users, and the limitations on its functions or performance.

An "ounce of prevention" can mitigate the risk of future warranty liability.

THREE KEY TAKEAWAYS

1. Software designers and suppliers need to analyze from a legal perspective their transactions, agreements, advertising, sales pitches, industry standards and practices, course of performance, course of dealing, and other representations to determine their potential liability for express or implied warranties. Management needs to scrutinize all aspects of sales, marketing, and customer service to control the risk of legal liability.
2. Software designers and suppliers can effectively disclaim express and implied warranties if they follow state law requirements.
3. Software designers and suppliers should take special care to protect against liability risks when designing custom software, when working with product manufacturers to develop new software for their particular needs, or when software is promoted as part of the product.

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