

## **PROVIDER USE OF CUSTOMER LICENSED SOFTWARE IN OUTSOURCING ARRANGEMENTS**

By: Shawn C. Helms

---

Companies considering whether or not to outsource critical business functions must take into account numerous and significant operational, legal and business risks. These risks often go to the heart of the company's business; thus outsourcing transactions often receive attention from the highest levels of company management. Because certain outsourcing transactions promise substantial savings and transformational process improvements, there is often tremendous pressure to complete these transactions as soon as possible. Faced with enterprise level risk, pressure from above and an expedited timeframe, outsourcing deal teams often ignore the risks associated with allowing the outsourcing provider to use the company's licensed software. This article discusses why this is a risk that should not be ignored and what factors to evaluate when analyzing whether or not a customer can allow an outsourcing vendor to utilize its third party licensed software.

### **Third Party Use Under Typical Software License Terms**

In a typical software license, the software provider grants a license allowing the licensee to utilize the software in the licensee's business. This license normally has a number of limitations restricting the licensee's ability to transfer or disclose the software to third parties. These limitations can take the form of license restrictions, confidentiality provisions or other contractual limitations. Licensees rarely negotiate the right for contractors, agents or outsourcers to use the software on behalf of the licensee. Therefore, these limitations, read with precision, often restrict a licensee's ability to allow any third party access to, or use of, the software. However, licensees often ignore such restrictions and allow third party contractors providing staff augmentation and other services to use the licensed software. Despite certain agency arguments, such use is often in direct violation of the terms of the software license.

Most licensees believe that because the contractor's use is within the original license number limitations (thus the software providers are not "losing money"), the legal risks associated with such contractor use is low. In most cases, they are right. Historically, software providers have not aggressively enforced license agreements to prevent limited and temporary third party contractor use. But, the risk for possible legal challenges increases dramatically in large information technology and business process outsourcing transactions. In such transactions, the outsourcing provider takes over business functions of the customer, stepping into the shoes of the customer's employees. When doing so, the provider will often use the customer's licensed software. As discussed above, this use might very well be in violation of the license terms. Furthermore, when customer employees transfer to the outsourcing vendor, becoming vendor employees, you get the same result - a violation of the license agreement. Therefore, the same individual, working in the same cube, doing the same job function, using the same software, will be in compliance with the software license one day (when still an employee of the licensee), and will be in violation the next (when an employee of the outsourcing vendor).

From a legal perspective, software use by outsourcing vendors is no different than the use by a temporary contractor. Both are third parties using software not licensed to them. However, the outsourcing scenario carries more risk to licensees because outsourcing relationships are long term, publicly announced and may involve a significant number of licenses and potential compensation for the software provider. Furthermore, software providers perceive use by certain outsourcers as significantly more risky because outsourcers are in the business of leveraging software for multiple customers, a situation that can lead to a loss of revenue for software providers. In addition, software developers often have special "service provider" licenses that contain specialized terms to govern the leveraged use of software for multiple customers. These special licenses are not in place when the outsourcer utilizes software licensed to an

outsourcing customer. The result is that the licensee may incur significant legal liability by allowing outsourcing vendors to utilize its third party licensed software without analyzing if it has the appropriate license rights.

### **Analyzing Software License Terms In Light of an Outsourcing Transaction**

The legal risk associated with allowing an outsourcing vendor to utilize a customer's licensed software can be eliminated (or mitigated) by ensuring that the software license has the appropriate rights. These rights might include terms that allow for the transfer or assignment of licenses or provisions that would otherwise allow the outsourcing vendor to use software on the licensee's behalf.

When negotiating software license agreements, it is always best to include a provision that expressly allows "contractors, outsourcers or other agents" to use the software on behalf of the licensee. In the absence of such an express provision, the analysis becomes clouded. In the typical scenario, a licensee has not negotiated in such a provision and is stuck reviewing its existing software license agreements with an eye toward whether or not such third party use rights can be read into the terms of the licenses.

The "golden rule" of licensing is that the licensor (software provider) retains all rights not expressly granted to the licensee (customer) in the software license agreement. Therefore, the analysis of whether or not the customer has the right to allow a third party outsourcer to use the licensed software begins and ends with the text of license agreement. In determining whether appropriate rights exist in a software license, the license terms need to be viewed in their entirety, with particular focus on the following provisions:

- **License Grant** – The actual license grant will often limit the scope of the license to the named licensee. Sometimes, the license will extend to the licensee's affiliates. This type of limited grant is detrimental to the licensee's position if the goal is to allow a third party outsourcer to use the licensed software. On occasion, the license grant will include language that contemplates use of the software by "consultants," "contractors" or "vendors" providing services to the licensee. If this language is present, the licensee will have an argument that the outsourcing vendor fits within this scope. However, this interpretation must be considered in light of the other uses of the terms elsewhere in the license and the other provisions in the license agreement. In addition, the license grant may state that the license is non-transferable and non-sublicensable. These restrictions are more evidence that the software provider intended to restrict the license to only the licensee.
- **Confidentiality** – Software licenses often contain confidentiality provisions that restrict the disclosure of confidential information. Sometimes the definition of confidential information can include the licensed software, thus prohibiting the disclosure of the software to third parties. However, the confidentiality provision might permit third parties providing services to the licensee to have access to the confidential information on an "as needed basis" for the purpose of providing such services.
- **Competitor Restrictions** – A software license may contain a restriction that prevents the use or disclosure of the software to competitors of the software provider. Such a restriction would likely be violated if the licensee disclosed the software to an outsourcer providing information technology or software development services. It would also prevent disclosure in a business process outsourcing transaction if the provider is a significant software provider like IBM. In both cases, a reasonable interpretation would be that such companies are competitors of the software provider, thus disclosure to such a company would violate this restriction.

- **Assignment Provisions** – A license may also contain a provision limiting the licensee's right to transfer or assign the license to other parties. This would prevent the licensee from simply transferring the entire license, and thus the right to use the software, to the outsourcing provider.

In addition to the use, transfer, disclosure and assignment limitations, a licensee must also consider if other license restrictions would prevent the use by the outsourcing provider. For example, a software license may limit the number of licenses, restrict software use to particular hardware owned by the licensee, restrict the use of software to a certain physical locations or restrict the export of the software outside the United States. All such restrictions need to be taken in to consideration.

While it would be logical for the license grant, confidentiality section and assignment provision to be consistent, it is not unusual to see conflicting terms. These sections are often drafted and negotiated in silos without adequate consideration as to their interaction. For example, a license grant may allow certain third party use, but the confidentiality provision might limit disclosure of the software to only employees of the licensee. This makes it difficult to determine whether or not the license permits the outsourcer to use the software. As with any contractual interpretation, one must resolve such conflict by attempting to determine the intention of the parties, taking the license as a whole.

When considering the operational, financial and legal consequences of allowing an outsourcing vendor to use a company's third-party licensed software, a company would be wise to carefully analyze the applicable software licenses. Such an analysis will allow a company to accurately determine its rights and risks related to such a decision.

**Shawn C. Helms – Attorney, Jones Day - Dallas.** Shawn Helms' practice is focused on information technology outsourcing, business process outsourcing and other complex technology and intellectual property centric transactions. Shawn has broad experience in the areas of telecommunications and information technology. Shawn graduated from Georgetown University Law Center in 2000 and is licensed to practice law in Texas and California. Shawn's full bio and contact information can be found at <http://www.jonesday.com/shelms/>.