

DoD ESI White Paper

Guidelines for Negotiating Warranties for Commercial Off-the-Shelf (COTS) Software Products

Best practices to consider, and strategies to explore,
before finalizing COTS software warranties.



About DoD ESI

The DoD ESI was formed in 1998 by Chief Information Officers at the DoD. To save time and money on commercial software, a joint team of experts was formed to consolidate requirements and negotiate with commercial software companies, resulting in a unified contracting and vendor management strategy across the entire department. Today, DoD ESI's mission extends across the entire commercial IT life-cycle to include IT hardware products and services. DoD ESI has established DoD-wide agreements for thousands of products and services.

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Disclaimer

The content of this white paper is not provided as legal advice, but rather as general information designed to point out some of the issues and considerations involving commercial software warranties. Readers should not rely on the content of this paper to make contract or other legal decisions. Drafting and negotiating final acquisition documents and software license agreements, including warranty provisions, should be supported by legal counsel.

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I. Commercial Product Warranties in the U.S.

Commercial product warranties allow buyers to know that products they buy will meet a certain standard of performance, and describe the seller's obligations when products don't meet those standards. In the U.S., these common law principles have been codified in the Uniform Commercial Code (UCC), the Magnuson-Moss Warranty Act, and the Federal Acquisition Regulations (FAR), among others. While the UCC and Magnuson-Moss Act have applicability to warranty law, the FAR is the key source of federal law applicable to software licenses acquired by the government.

In general, there are two types of warranties—implied and express.

Implied warranties occur by operation of law and do not require verbal or written expression. There are two types of implied warranties.

- A. The implied warranty of merchantability, meaning the product will perform the basic functions expected for products of that type (*e.g., an oven will bake food at controlled temperatures; a washer will wash clothes, etc.*).
- B. The implied warranty of fitness for a particular purpose, meaning the product will meet certain specific capabilities based on the buyer's needs or the seller's advice.

Express warranties are derived from verbal or written promises about basic attributes, as follows:

- A. what is covered;
- B. who is covered;
- C. when the warranty begins and when it ends, and
- D. what happens when a defect is discovered and reported.

II. Key Elements of a Commercial Software License Warranty

One way to approach best practices for commercial software warranties is to construct a framework around the four attributes of express warranties mentioned above. These concepts are summarized in the table below, with guidelines for each attribute.

What is Covered:	Best Practices:
<p>There are two primary aspects:</p> <ol style="list-style-type: none"> 1. Product defects and bugs. 2. Product capabilities. 	<ol style="list-style-type: none"> 1. The warranty should cover all defects and bugs. 2. The warranty should also cover all required product capabilities. Those requirements must be stated precisely and completely to avoid confusion. In addition to Licensor product documentation, the government should consider including all relevant documents to describe its requirements—such as RFQ/RFP responses, records from product demonstrations, product brochures, product capability descriptions found on Licensor web sites, etc.
Who is Covered & Who Issues the Warranty:	Best Practices:
<p>Warranty coverage also has two aspects:</p> <ol style="list-style-type: none"> 1. The Licensee (<i>the government</i>) must be the beneficiary of the warranty. 2. The warranty must come from the IP owner (<i>e.g. the Publisher</i>) to be effective. 	<ol style="list-style-type: none"> 1. The government should ensure the warranty covers the government as the Licensee. 2. The government should ensure the IP owner (e.g. the Software Publisher) issues the warranty.
Warranty Period:	Best Practices:
<p>There are two key points in time:</p> <ol style="list-style-type: none"> 1. When does the warranty period start? 2. When does the warranty period end? 	<ol style="list-style-type: none"> 1. The warranty should not start until the government has had an opportunity to discover defects, or to discover missing or inadequate capabilities. Usually this opportunity to discover begins with the first use of the software in a production environment. 2. There are two approaches to dealing with this issue: <ol style="list-style-type: none"> a) establish the warranty start date to coincide with first productive use, whenever that might occur (<i>i.e. a delayed start</i>); or b) require the warranty to begin with delivery but to extend for a period ending 90 days after first productive use of the software (<i>i.e. an extended warranty period</i>). 3. For simple software, or market-tested shrink-wrap products such as Microsoft Office, the issue is minimal. The warranty start date can be coincident with product delivery, since it is also probably coincident with productive use. 4. For more complex products, however, where extensive implementation activities are required, first productive use might not occur until many months after delivery—perhaps even many months after the standard Licensor warranty would have expired. In those cases, the government warranty should require either a delayed warranty start date (beginning only with first productive use and ending 90 days after the delayed start) or an extended warranty period (<i>beginning with delivery but not ending until 90 days after first productive use</i>).
Potential Remedies:	Best Practices:
<p>There are important remedies for each aspect of coverage:</p> <ol style="list-style-type: none"> 1. What happens when defects or bugs are reported? 2. What happens when product capabilities are missing or inadequate? 	<ol style="list-style-type: none"> 1. Ensure Service Level Agreements (SLAs) define responsibilities for responding to reports of defects, bugs and capability issues. 2. Ensure the SLAs also define how fast the government will receive fixes from the Licensor. 3. Be clear that defects, bugs, and capability issues under warranty will be remedied at no charge to the government. 4. Specify the conditions under which the government can return the defective or incomplete product for a full refund, and how much additional compensation the government should receive for its time and expense waiting for non-defective software that complies with all documented requirements.

III. Government Standard Software Warranty (GSSW) Clause

The guidelines above form the basis for a Government Standard Software Warranty (GSSW), provided below. Typically, it is most important to secure the GSSW when licensing software that requires configuration, integration, customization, or other implementation services. Software that can be used immediately upon download or delivery, without any additional services, can be warranted using a standard commercial warranty.

- A. Licensor warrants for one (1) year from the date on which the Software is Accepted by Licensee, [or is first used in production by Licensee]*, that the Software will perform in all material respects the functions at the specified performance standards described in the Documentation and Standards of Performance, when operated on a Supported Platform. Documentation and Standards of Performance are defined as the Licensor's standard product documentation, the Licensee's RFP form with Licensor's RFP responses attached hereto, Licensee's Functional and Technical Requirements and Gap Analysis report attached hereto, Licensee's Features and Benefits document attached hereto, all said attachments being made a part hereof. ****[NOTE: Contracting Officer should select Acceptance or Productive Use as the start date of Warranty.]***
- B. Notwithstanding Licensor's disclaimers or attempts to disclaim certain warranties, the provisions of FAR 52.212-4 (Contract Terms and Conditions – Commercial Items) apply to this Agreement, including FAR 52.212-4(o) pertaining to warranties as follows: "The Contractor warrants and implies that the items delivered hereunder are merchantable and fit for use for the particular purpose described in this contract."
- C. In the event Licensee determines that the Product is a Non-complying Product during the one-year period specified above, Licensee will notify Licensor and Licensor will have ___ business days thereafter to begin remedying the non-conformance. If Licensor is unable to remedy such non-conformance within a reasonable time, Licensor agrees that Licensee may return the Product and Licensor shall promptly refund any moneys paid for such Non-complying Product.
- D. Licensee must report to Licensor, in writing, any breach of the warranties during the relevant warranty period. Licensor shall use commercially reasonable efforts to correct or provide a workaround for reproducible Software errors that cause a breach of this warranty, or, if Licensor is unable to make the Software operate as warranted within a reasonable time considering the severity of the error and its impact on Licensee, Licensee shall be entitled to return the Software to Licensor and recover the fees paid by Licensee to Licensor for the license to the non-conforming Software.

Sample Acceptance Definitions

To help Licensees determine when a warranty period should commence, sample definitions of "acceptance" are provided below:

"Acceptance" shall mean that the Software has passed its Acceptance Testing and shall be formalized in a written notice from Purchaser to Vendor; or, if there is no Acceptance Testing, Acceptance shall occur when the Products are delivered.

"Acceptance Date" shall mean the date upon which Purchaser Accepts the Software as provided in the section titled **Warranty Standard of Performance and Acceptance**; or, if there is no Acceptance Testing, Acceptance Date shall mean the date Vendor delivers the Products.

"Acceptance Testing" shall mean the process for ascertaining that the Software meets the standards set forth in the section titled **Standard of Performance and Acceptance**, prior to Acceptance by the Purchaser.

"Standard of Performance" shall mean the criteria that must be met before Software Acceptance, as set forth in the section titled **Standard of Performance and Acceptance**. The Standard of Performance also applies to all additional, replacement or substitute Software and Software that is modified by or with the written approval of Vendor after having been accepted.

IV. Applying FAR to Commercial Software Warranties

A host of FAR provisions apply to COTS software warranties. The following excerpt from the DoD Warranty Guide (Version 1.0, September 2009 –<http://www.acq.osd.mil/dpap/pdi/uid/docs/departmentofdefensewarrantyguide%5b1%5d.doc>) provides a concise summary of how key FAR provisions deal with commercial software warranties.

“The Federal Acquisition Streamlining Act of 1994 requires COs to take advantage of commercial warranties. To the maximum extent practicable, solicitations for commercial items shall require offerors to offer the Government at least the same warranty terms, including offers of extended warranties, offered to the general public in customary commercial practice. The standard practice is to accept the manufacturer’s commercial warranty that is typically some form of materials and workmanship guarantee.

Commercial warranties should be given equal weight to the other key discussion topics of pricing, delivery, and financing—warranties should be viewed as a negotiable item and tailorable. Effective negotiations will require market research to determine (a) what is the “normal” warranty practice for the industry in question and (b) the leverage you may have based on size of the procurement.”¹

The spirit of these provisions is to make it easier for the government to buy—and for sellers to sell—commercial off-the-shelf (COTS) products, by allowing standard commercial warranties. In the author’s opinion, however, there is a limit to the applicability of those standard warranties for commercial software—especially for more complex software requiring implementation projects. For example, is it reasonable for such warranties to limit performance standards to the system documentation for just 90 days after delivery?

FAR 12.212 says that commercial software should be procured...“under licenses customarily provided to the public, to the extent such licenses are consistent with Federal law and otherwise satisfy the Government’s needs.”

Many Licensors will rely on FAR 12.212 to avoid the implied warranties in FAR 52.212-4 (o). The government should not accept attempts by the Licensor to disclaim implied warranties. This position is strengthened by the fact that many commercial customers—especially those whose size and financial power are comparable to the government’s—successfully negotiate stronger warranty terms than Licensors offer as standard warranty terms.

The requirements of FAR 52.212-4 (o), provide for implied warranties of merchantability and fitness for a particular purpose, and should be referenced and included as part of the GSSW.

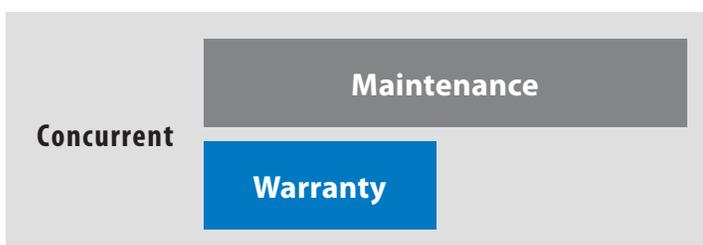
V. Comparing Software Maintenance and Warranties

COTS software warranties typically provide for repair of defects and bugs, replacement of defective media, and in some cases return of faulty software for a refund.

In addition to warranty protections, Licensors also might offer software Support & Maintenance contracts for an annual fee (*usually a percentage of the license fee*). One of the primary purposes of Support & Maintenance is to enable Licensees to submit software issues (*bugs and defects*) to the Licensor for resolution, and to receive fixes, patches, and updates.

To many, it sounds as if warranties and maintenance agreements are designed to cover the same thing (*i.e. to fix software defects*). There are several important differences:

- A. Warranties are part of the license price, so repairs of defects are at no (*additional*) charge, while maintenance is a separately charged element of the license agreement.
- B. Warranties often permit returns and refunds for defective software while maintenance does not. Warranties can include software capability and performance standards, while maintenance usually is restricted to fixing defective code.
- C. Maintenance often begins when warranties end, although sometimes it runs concurrently with the warranty, and continues after the warranty ends.



VI. License Agreements with Resellers, and the Lack of Privity

Privity is a principal in the law of contracts that says that promises in an agreement are enforceable only between the parties to the agreement.

As an example, let us assume the government acquires a license from a reseller of commercial software. There might be a separate agreement between the Publisher (the Intellectual Property (IP) owner) and the reseller defining the terms under which the reseller can sell licenses. Any promises made by the Publisher to the reseller are unenforceable by the government, because the government was not a party to that agreement (*i.e. has no privity*), unless the government acts specifically to incorporate the Publisher's promises in the license agreement.

Buyers of software licenses need assurances that the Publisher authorizes the promises that only the Publisher can make, and that the Publisher will stand behind those promises. This can be accomplished in several ways—by including the Publisher as a party to the license agreement, by dealing directly with the Publisher for the license and specifying the reseller can fulfill the order, or by incorporating agreements between the Publisher and reseller into the license agreement between the government and the reseller.

Privity is important because the Publisher owns the IP embodied in the software. That means only the Publisher can, for example, indemnify Licensees against IP infringement, promise software updates, agree to deposit the software into a source code escrow account, or warrant the product's performance. Absent additional steps, any such promises made by the reseller to the government are unenforceable against the Publisher, due to a lack of privity.

VII. Licensors' Positions on Commercial Software Warranties

A. Sample Warranty Clauses Proposed by Licensors

Licensors prefer to offer their standard warranty clause to limit their financial and business risk. Two sample Warranty clauses proposed by Licensors are provided below:

LICENSOR ONE SAMPLE: LIMITED WARRANTY

1. **LIMITED WARRANTY.** If you follow the instructions, the software will perform substantially as described in the Licensor materials that you receive in or with the software.
2. **TERM OF WARRANTY; WARRANTY RECIPIENT; LENGTH OF ANY IMPLIED WARRANTIES.** The limited warranty covers the software for one year after it is acquired by the first user. If you receive supplements, updates, or replacement software during that year, they will be covered for the remainder of the warranty or 30 days, whichever is longer. If the first user transfers the software, the remainder of the warranty will apply to the recipient.
3. **To the extent permitted by law, any implied warranties, guarantees or conditions last only during the term of the limited warranty.** Some states do not allow limitations on how long an implied warranty lasts, so these limitations may not apply to you. They also might not apply to you because some countries may not allow limitations on how long an implied warranty, guarantee or condition lasts.
4. **EXCLUSIONS FROM WARRANTY.** This warranty does not cover problems caused by your acts (or failures to act), the acts of others, or events beyond Licensor's reasonable control.

5. **REMEDY FOR BREACH OF WARRANTY.** Licensor will repair or replace the software at no charge. If Licensor cannot repair or replace it, Licensor will refund the amount shown on your receipt for the software. It will also repair or replace supplements, updates, and replacement software at no charge. If Licensor cannot repair or replace them, it will refund the amount you paid for them, if any. You must uninstall the software and return any media and other associated materials to Licensor with proof of purchase to obtain a refund. These are your only remedies for breach of the limited warranty.

NO OTHER WARRANTIES. The limited warranty is the only direct warranty from Licensor. Licensor gives no other express warranties, guarantees, or conditions. Where allowed by your local laws, Licensor excludes implied warranties of merchantability, fitness for a particular purpose and non-infringement. If your local laws give you any implied warranties, guarantees or conditions, despite this exclusion, your remedies are described in the Remedy for Breach of Warranty clause above, to the extent permitted by your local laws.

LICENSOR TWO SAMPLE: WARRANTIES, DISCLAIMERS AND EXCLUSIVE REMEDIES

Licensor warrants that a Program licensed to the State shall operate in all material respects as described in the applicable Program documentation for one year after delivery (i.e. via physical shipment or electronic download). The State must notify Licensor of any Program warranty deficiency within one (1) year after delivery. Licensor also warrants that Services shall be provided in a professional manner consistent with industry standards. The State must notify Licensor of any Services warranty deficiencies within ninety (90) days from performance of the defective Services.

LICENSOR DOES NOT GUARANTEE THAT THE PROGRAMS SHALL PERFORM ERROR-FREE OR UNINTERRUPTED OR THAT LICENSOR SHALL CORRECT ALL PROGRAM ERRORS. FOR ANY BREACH OF THE ABOVE WARRANTIES, THE STATE'S EXCLUSIVE REMEDY, AND LICENSOR'S ENTIRE LIABILITY, SHALL BE: (A) THE CORRECTION OF PROGRAM ERRORS THAT CAUSE BREACH OF THE WARRANTY, OR IF LICENSOR CANNOT SUBSTANTIALLY CORRECT SUCH BREACH IN A COMMERCIALY REASONABLE MANNER, THE STATE MAY END ITS PROGRAM LICENSE AND RECOVER THE FEES PAID TO LICENSOR FOR THE PROGRAM LICENSE AND ANY UNUSED, PREPAID TECHNICAL SUPPORT FEES THE STATE HAS PAID FOR THE PROGRAM LICENSE; OR (B) THE REPERFORMANCE OF THE DEFICIENT SERVICES, OR IF LICENSOR CANNOT SUBSTANTIALLY CORRECT A BREACH IN A COMMERCIALY REASONABLE MANNER, THE STATE MAY END THE RELEVANT SERVICES AND RECOVER THE FEES PAID TO LICENSOR FOR THE DEFICIENT SERVICES. TO THE EXTENT PERMITTED BY LAW, THESE WARRANTIES ARE EXCLUSIVE AND THERE ARE NO OTHER EXPRESS OR IMPLIED WARRANTIES OR CONDITIONS, INCLUDING WARRANTIES OR CONDITIONS OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE

B. Common Warranty Strategies and Techniques Used by Licensors

The tension between Licensors and Licensees regarding performance warranties is twofold:

1. Licensees want assurances the software will be free from bugs and defects and they want assurance that it will meet their requirements regarding functionality and performance.
2. Licensors seek to limit their potential liability to a relatively short period of time, to avoid liability for unreasonable or unattainable performance standards (*or those outside their control*), and to avoid warranties that could jeopardize timely revenue recognition.

In order to minimize their liability, Licensors typically use the following techniques in software licenses:

1. **Disclaim all implied warranties of merchantability and fitness for a particular purpose.** Almost all typical COTS software licenses adhere to the legal standards for conspicuously disclaiming these warranties. This disclaimer means the Licensee loses significant warranty protections which otherwise would ensure, to some extent, that the software performs as expected. Without these important implied warranties, the Licensee can rely upon only the express warranties in the license. This places a significant burden on Licensees to ensure those express warranties adequately describe the necessary product performance protections.

Many Licensors will rely on FAR 12.212 to avoid the implied warranties in FAR 52.212-4 (o). The government should not accept attempts by the Licensor to disclaim implied warranties. This position is strengthened by the fact that many commercial customers—especially those whose size and financial power are comparable to the government's—successfully negotiate stronger warranty terms than Licensors offer as standard warranty terms.

2. **Limit liability through the integration clause in the software license.** The integration clause says the written agreement containing it represents the entire understanding of the parties and explicitly excludes any prior or contemporaneous statements or writings made by either party. This clause also says that any future statements need to be in writing and signed by both parties to become part of the agreement. This dramatically limits the scope of warranty protection for Licensees by excluding verbal or written promises made in RFP responses, sales demos, brochures, web sites, etc., unless those or other similar promises are specifically included in the agreement as part of the warranty.

3. **Provide either no express warranty or a very limited express warranty promising the software will “perform in accordance with the documentation.”** The standard of performing in accordance with system documentation can be a very limited and dangerous standard for Licensees. First and foremost, it requires the Licensee to understand thoroughly what that documentation says (*and doesn’t say*), and then to compare it to Licensee requirements (*that are equally important to understand thoroughly*) in order to identify potential gaps. As discussed in the negotiating strategy section below, this can be the starting point for negotiating an expanded scope of product performance covered by the warranty.

4. **Limit the warranty to a very short period of time after delivery.** Many standard software warranties are limited in time—often 90 days. Some Licensors, even some of the major ones, may extend warranties for as long as a year. There are two primary reasons for limiting the time:

- a) the shorter the time, the less potential liability for free repairs of defects, or return for a refund; and
- b) consistency in warranty periods avoids revenue recognition issues for the Licensor.

Usually Licensors set aside a portion of the revenue to account for warranty costs or the risk of return for a refund. The amount reserved or deferred is based on a Licensor’s history of actual warranty expenses. If extraordinary warranties are extended, the entire license revenue might need to be recognized ratably over the term of the warranty or at the end of the warranty, instead of just deferring or reserving a portion of the revenue at the time of delivery.

5. **Provide for limited remedies, or sometimes permit a return for a refund.** Most warranties provide for repair or replacement of defective products. In the COTS software world, that usually means fixing software bugs or defects, or replacing defective media. When defects are prevalent or go unrepaired for some time, or if performance specifications listed in the license are not substantially met, Licensees may seek to return the software for a full refund.

C. Evaluating and Negotiating Licensor Standard Warranties vs. GSSW

As described earlier, the optimal position for the Licensee is to require the Licensor and its reseller to abide by the terms of a GSSW. In the event a GSSW cannot be secured, Licensees should carefully evaluate the Licensor’s standard warranty utilizing the following guidelines and criteria.

1. **Be aware of overarching risk allocation and cost benefit analysis.** Evaluating warranties and negotiating stronger terms more favorable to the government is mostly about allocating risk. The government needs to know the potential cost of accepting warranties that are limited in scope of performance and time, versus the potential cost and associated benefits of negotiating stronger terms. See the DoD Warranty Guide, Version 1.0, September 2009, Section 1.5 (Cost Benefit Analysis), to get an idea of the factors recommended for evaluating the alternatives. Keep in mind that the DoD Warranty Guide is not specific to software. The cost-benefit analysis for software warranties should include an assessment of the potential costs of funding any effort to fill software gaps or to correct defects not covered by the warranty or maintenance. Experience in large ERP projects has shown that those costs can be substantial.

2. **Determine if the warranty adequately describes the Licensee's performance requirements.**

Both the GSSW and the Licensor's standard warranty language cover product defects, but the Licensor product performance standard is limited to a promise that the product will perform in accordance with documentation that the Licensor has written to describe its product performance commitments. This can pose a significant risk to the Licensee since the Licensor is the author of the product specification documentation, which will be written to minimize the Licensor's risk, exposure, and liabilities.

When evaluating the Licensor's standard warranty for product requirements, the Licensee must thoroughly compare the Licensee's product requirements to the specifications and features described in the Licensor's documentation.

a) The warranty and associated documentation should provide the requisite level of assurance that the software will meet the Licensee's expectations about functionality, business process capabilities, standards for system response time (*i.e. how fast the software executes*), numbers of users it can handle, the amount of data it can process, etc.

b) If the Licensor's documentation is inadequate with regard to any of the elements above, the Licensee should define the product capabilities necessary to meet its requirements and make them part of the Licensor's warranty. Sources for key definitions include documents and activities used in the software selection process, the RFP, RFP response, Licensor brochures, Licensor web sites, Licensor software demos, and other product descriptions.

c) Anticipate and be prepared to counter the Licensor's perspective when negotiating. Agreeing to a warranty that is not their commercial standard exposes the Licensor to potential liabilities. While revenue recognition can be a significant factor, the larger liability might be the possibility of the Licensor spending substantial cost and time to redesign or recode the software to meet the performance specifications. There is a big difference, for example, between promising the software can create a purchase order and promising it can create—right out of the box—a delivery order or IDIQ in accordance with all FAR requirements. Licensors might be willing to warrant the former, but few, if any, will warrant the latter. Unfortunately, such disconnects regarding system capabilities are often at the heart of project overruns and dissatisfaction expressed by Licensees.

3. **Clearly identify the date of first productive use and ensure the warranty period is adequate**

a) When evaluating the Licensor's standard warranty for adequacy of the warranty period, the Licensee must consider when first productive use will occur.

i) Licensees need to ensure that the timing of productive use is adequate to provide the Licensee with reasonable opportunity to discover noncompliance with the agreed-upon product capabilities, as well as standard bugs and defects.

ii) If the timing of first productive use provides a reasonable opportunity to discover non-compliance, then the Licensor's standard software license warranty period would generally be acceptable.

iii) If the timing of first productive use does not provide reasonable opportunity to discover non-compliance, or is outside the warranty period altogether, then an extended warranty period or a warranty start date coincident with first productive use should be substituted for the Licensor's standard warranty period.

b) The GSSW would require that the warranty period provide the government a reasonable opportunity to discover defects or shortcomings in product performance. In order to ensure the opportunity to discover is real, the warranty period needs to include a reasonable timeframe after first productive use of the software by the government. This can be accomplished by:

- i)** delaying the start of the warranty until first productive use by the government and ending within a reasonable time thereafter (e.g., 90 days, one year, etc.), or
- ii)** starting the warranty at delivery and extending it for a reasonable period after first productive use. In either case (*delayed start* or *extended period*), the Licensor will typically consider the GSSW as non-standard.

4. Take into account “Shrink Wrap” Licensors perspective vs. “Enterprise Software” Licensor’s perspectives. Most Licensors of shrink-wrap software products (*those products generally useable immediately out of the box*) should not have an issue with the GSSW for two reasons:

- a)** The government does not need to gather and document extensive requirements for word processing or spreadsheets or other similar products. The capabilities are so well known and so extensively tested in the marketplace that there is no mystery or uncertainty about them.
- b)** Productive use can easily occur at the time of delivery. Extensive implementation activities are not required, so the government has a reasonable opportunity to discover product defects and shortcomings beginning with delivery.

Licensors of software requiring extensive implementation activities will react differently to a GSSW. For their products, extensive requirement definitions and specifications are very important to the government, since the fit between government requirements and product capabilities is either uncertain or is known to be less than required. Performance in accordance with product documentation is insufficient. The resulting GSSW product performance requirements will create a “non-standard” warranty from the Licensor’s perspective.

Also, the timing of the warranty period is an issue for Licensors. First productive use might not occur for months (in some cases more than a year) after delivery. The GSSW alternatives of a delayed start or an extended period will cause the warranty to be “non-standard” from the Licensor’s perspective.

The Licensor will be reluctant to agree to the “non-standard” GSSW primarily because it will cause revenue recognition issues, possibly delaying full revenue recognition until the end of the implementation project. In those cases, it is important to consider the negotiation alternatives presented elsewhere in this paper.

5. Consider a Services Warranty as an alternative solution Recognizing the difficulty of negotiating these expanded warranties with large Licensors, Licensees might want to consider a fallback position. In the commercial world, many Licensees—even those with significant leverage—decide to achieve their objectives of getting software that meets Licensee performance specs, and of having adequate time to discover issues, by placing such requirements in the services warranty. Licensors are much more willing to entertain detailed performance specs and extensive acceptance criteria in Services Agreements.

There are two important issues to consider before choosing this alternative.

a) First, the right to return the software for a full refund might not be part of the services warranty because it would still impact revenue recognition of the license (*although some Licensors might offer a refund if serious non-compliance issues are discovered during the project—even if the warranty doesn't require it*).

b) Second, the services warranty needs to be backed fully by the Publisher. (*Remember, without privity, services agreements with Systems Integrators (SIs) or resellers are not binding on the Publisher.*) If the non-compliance would require the Publisher's development organization to write code, the SI would not be able to perform that function or force the Publisher to do it. There are also potential support issues subsequent to development that the Publisher would probably view as custom code, which might not be covered under the Publisher's warranty.

VIII. Summary

In summation, the key elements of a successful software warranty strategy include the following:

- A. Require the Government Standard Software Warranty (GSSW) clause to the greatest extent possible.
- B. Where the GSSW cannot be fully applied, know the reasons for seeking a stronger warranty than the warranty offered by the Vendor. Is it an issue of needing performance standards more robust than the documentation reveals? Is it an issue of needing more time to have an opportunity to discover defects? Or is it both?
- C. If more specific performance standards are required, be sure to define them as clearly as possible and make sure they are measurable.

- D. Licensors will not readily agree to non-standard warranties. Take advantage of the size and timing of orders when negotiating all important license elements—including warranties. The federal government is probably the largest purchaser of software in the world. It should use this buying power on an aggregated basis to negotiate favorable terms selectively.
- E. Know the costs and benefits of expanded warranties. Be prepared to offer something in return (e.g. a long-term partnership with the Licensor instead of doing business on a transactional basis). Most Licensors already know their cost of warranty (remember they generally defer a portion of license revenue to account for warranty), so you might be able to find out the cost of a longer or expanded warranty from the Licensor's perspective.
- F. Do your homework and know where the Licensor has made exceptions to warranty clauses in the past. (*Read "How a European Bank Got Oracle to Surrender Key Software Licensing Points", at CIO.com. http://www.cio.com/article/198000/How_a_European_Bank_Got_Oracle_to_Surrender_Key_Software_Licensing_Points.)²*
- G. Establish the importance of the provisions in the GSSW at the outset of negotiations and stick to that position.

About the Author

Tom Crawford is a seasoned executive and consultant who has been leading and advising technology businesses for the past 20+ years. After successful senior management roles with leading software companies— including SAP, PeopleSoft, Oracle, and BMC— Tom started his own technology consulting business, lending his expertise to several clients in various industries. Tom currently serves as a software contract and procurement subject matter expert for the BuySide Partners team supporting DoD ESI. Tom’s experience leading business units and sales teams that have negotiated and closed scores of software and services contracts ranging up to \$65 million provides the foundation for his expertise and advice relating to software industry sales practices, contract negotiation strategies and commercial best practices for software license terms and conditions. Tom is a graduate of the U.S. Naval Academy, a former U.S. Navy officer, and holds an MBA from Wharton and a Juris Doctor from the University of Pittsburgh. His work with DoD ESI draws upon his diverse experience helping clients save significant dollars in software and services procurement.

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DoD ESI is an official
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