

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

Practical guidance for negotiating commercial software licenses in the Department of Defense

Disclaimer: The content of this 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.

This Executive Summary of the Warranties White Paper

addresses topics of interest to government executives and procurement professionals responsible for drafting software license warranties. The following questions and answers provide a framework for the discussion:

1. What are the types, purposes, and elements of commercial product warranties?

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

2. What are the commercial best practices that should be used for government software license warranties?

Commercial best practices based on the four attributes of express warranties are summarized in **TABLE A – Commercial Best Practices**. These guidelines form the basis for a potential Government Standard Software Warranty (GSSW).

3. How will Publishers likely react to the proposed government warranties?

The most controversial aspects of a potential GSSW are attributes #1. (*what is covered*) and #4. (*what constitutes the warranty period*).

Attribute #1. (*what is covered*). A standard commercial software warranty says the product will perform in accordance with the documentation. The GSSW allows a much broader and deeper product performance and capabilities definition. The broader GSSW creates a “non-standard” warranty from the Publisher's perspective.

Attribute #4. (*warranty period*). Standard commercial software warranty periods range from 90 days to 1 year. First productive use of complex software often occurs after warranty expiration, thereby preventing a reasonable opportunity to discover defects or product shortcomings. The GSSW requires longer warranty periods or a delayed start of the period until first productive use. These GSSW alternatives cause the warranty to be “non-standard” from the Publisher's perspective.

The Publisher 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.

4. How do Publishers' warranties differ from the proposed government warranties?

In order to minimize potential liability, licensors typically use the following techniques in software licenses:

- 1) Disclaim all implied warranties of merchantability and fitness for a particular purpose.
- 2) Limit liability through the integration clause in the software license.
- 3) Provide either no express warranty or a very limited express warranty promising the software will “perform in accordance with the documentation.”
- 4) Limit the warranty to a very short period of time after delivery.
- 5) Provide for limited remedies, or sometimes permit a return for a refund.

5. What are the best negotiation strategies and warranty alternatives for the government when the Publisher rejects the government standard software warranty (GSSW)?

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 standard and alternative warranties.

When considering a standard commercial warranty, the licensee must understand its product performance requirements in detail and how those requirements compare to what is promised in the documentation. When defining expanded requirements, the licensee should list in the warranty clause various documents and activities used in the software selection process—including for example the RFP, RFP response, licensor brochures, licensor web sites, licensor software demos, and other product descriptions.

When considering longer warranty periods, the licensee must know the likely date of first productive use. If the timing of productive use is outside the warranty period, then an extended warranty or a start date coincident with product acceptance might be required.

Recognizing the difficulty of negotiating these expanded warranties with large licensors, licensees might want to consider an effective back-up strategy. In the commercial world, many licensees decide to achieve their product performance and warranty period objectives 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 instead of License Agreements.

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

6. What role do the Federal Acquisition Regulations (FAR) play in software warranties?

There are a host of FAR provisions that apply to COTS software warranties. The following excerpt from the DoD Warranty Guide (Version 1.0, September 2009) 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.”

Be wary of a tendency to accept standard commercial software warranties carte blanche to meet perceived FAR exceptions for commercial products. The standard should be to negotiate warranties as required to meet ‘ the best interests of the government’—and to retain the warranty granted in FAR 52.212-4(o).

7. What are the differences between Maintenance and Warranties, and why do those two types of coverage usually begin at the same time?

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:

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

8. What risks are incurred when buying licenses from resellers instead of publishers?

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.

Buyers of software licenses need assurances that the IP owner authorizes the promises that only the IP owner can make, and that the IP owner will stand behind those promises.

TABLE 1 - Commercial Best Practices

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 Publisher 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 Publisher web sites, etc.
Who is Covered:	Best Practices:
<p>Warranty coverage also has two aspects:</p> <ol style="list-style-type: none"> 1. The licensee (the government) must be the beneficiary of the warranty. 2. The warranty must come from the IP owner (e.g. the Publisher) 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 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.e. a delayed start); 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.e. an extended warranty period). 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 Publisher 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 (beginning with delivery but not ending until 90 days after first productive use).
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 Publisher. 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.

Please visit www.esi.mil for more detailed information regarding this topic in the Software Warranty White Paper – Guideline for Negotiating Warranties for Commercial Off-the-Shelf (COTS) Software Products.

References

¹ Department of Defense Warranty Guide, Version 1.0, September 2009

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. www.esi.mil

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