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Attorney Best Practices for Minimizing Risk for Technology Licensees and Licensors

May 27, 2008

Presented by
ACC Law Department
Management Committee

Sponsor

Presenters

- **Jason Anderman,** Vice Chair of ACC's Law Department Management Committee & Counsel of Becton, Dickinson and Company
- **Tim Cummins**, President and Executive Director, International Association for Contract and Commercial Management
- **John Boruvka**, Vice President, IPM, Iron Mountain Digital

Part I: Technology Escrow Basics

Part II: Advanced Technology Escrow

Part I: Technology Escrow Basics

- Why today's information society is exposed to risk
- What is technology escrow?
- Why do licensees (buyers/users) need it?
- Why does a licensor (vendor/developer) need it?

Information Society's Risk Exposure

- Why today's information society is exposed to risk
  - Networked world creating rapid change & uncertainty
  - Diversifying into new markets
  - Assets more diverse
  - Much innovation from small companies
- Trust at a premium

Part I: What is Technology Escrow?

The practice of securing conditional access to software source code and other proprietary materials for the benefit of all parties to a technology transfer license agreement.

- A "safety net" for investment in software, technology and other forms of intellectual property
- Provide controlled access to a licensor's proprietary code under specific release conditions with defined use rights
- Used to engender trust between two parties partnering in business.
- A "pre-nup agreement" for a software licensee's mission critical technology investments

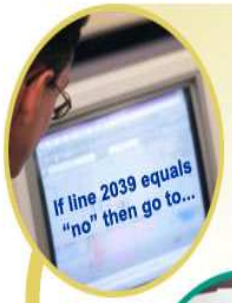
Parties include:

the technology developer, also referred to as the *licensor* or *depositor (a.k.a. "seller")*

the technology customer/partner/investor, also referred to as the *licensee* or *beneficiary (a.k.a. "buyer"*

the escrow agent (Iron Mountain), trusted neutral party

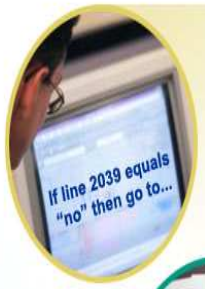
Why is source code so critical?



Developer enters human readable **source code**

Compiler translates from source into computer readable language, **object code**

System reads the object code to run **program**



Most developers **do not provide** the source code

Since the compiler cannot convert object code back to **source code...**

…the licensee is unable to **support** the program

Access to key development data is essential to support, upgrade or maintain the technology. Source Code is the key to a vendor maintaining a sustainable revenue stream.

Identifying Technology Risk

Operational Dependencies
- Number of users
- Customer impact
- Lost productivity
- Lost revenue
- Public safety

Costs
- Initial investment
- License fee
- Installation
- Retraining
- Customization
- Reprogramming
- Hardware

Investment of Time
- Time to identify new product
- Availability of substitute products
- Time to negotiate new license
- Time to recode

Vendor Assessment
- Vendor stability
- Subcontractor partnerships
- Breadth of product lines
- Commitment of staff

RISK FACTOR

Determine what level of software escrow protection is needed

Beneficiary's Pain Overview

New technologies that may not be around in a few years

Small software vendors where long-term viability is a concern

Not protecting business applications that can affect internal financial reporting/controls

Acquiring Intellectual Property

Access to proprietary data in a SaaS environment

Large vendors that provide a great deal of software customization

Why is Escrow necessary for:

Developers

- Establishes Credibility with the Marketplace
- Shortens the Sales Cycle
- Levels the Playing Field
- Satisfies a Client Requirement
- Protects Your Intellectual Property Rights
- Reduce workload

Beneficiaries

- Leverage After the License has been Signed
- Timely Access to Current Source Code and Maintenance Materials
- Have an Option to Control the Future
- Satisfies Legal Compliance
- Minimize Risk of Loss
- Avoid Litigation and the Courts

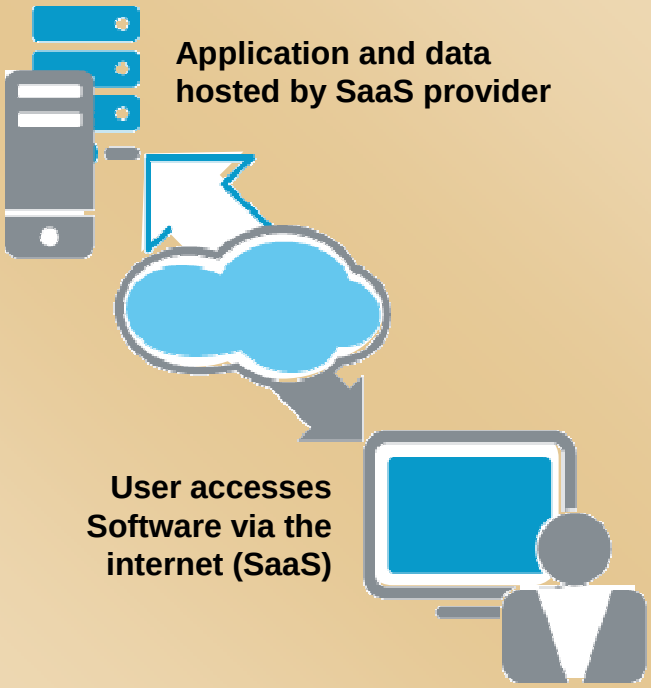
Part II:
Advanced Technology Escrow

Part II: Advanced Technology Escrow

- What are the key issues that I can address to minimize client risk when licensing Software-as-a-Service (SaaS) applications?
- What are the challenges or risks surrounding off-shore development and licensing?
- What are the challenges or risks surrounding exclusive supply agreements?
- Why and when should I recommend verification of the content of an escrow deposit?

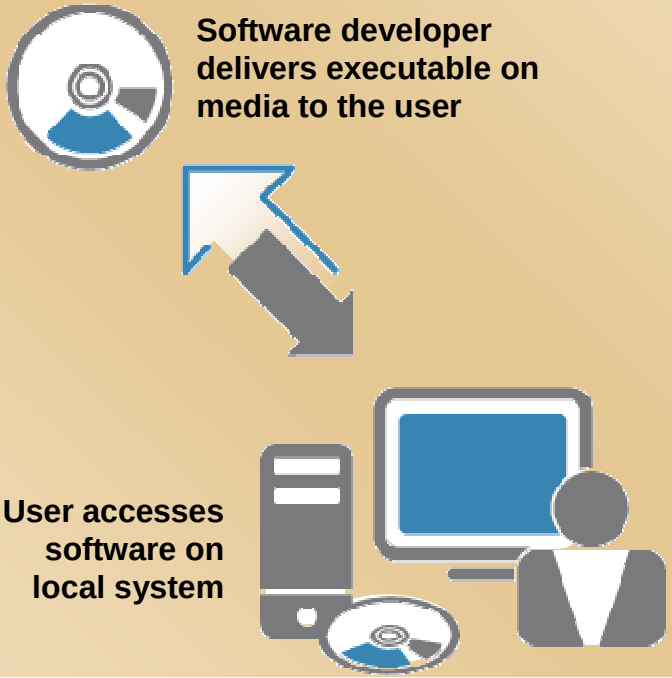
Changing Licensing Models

SaaS



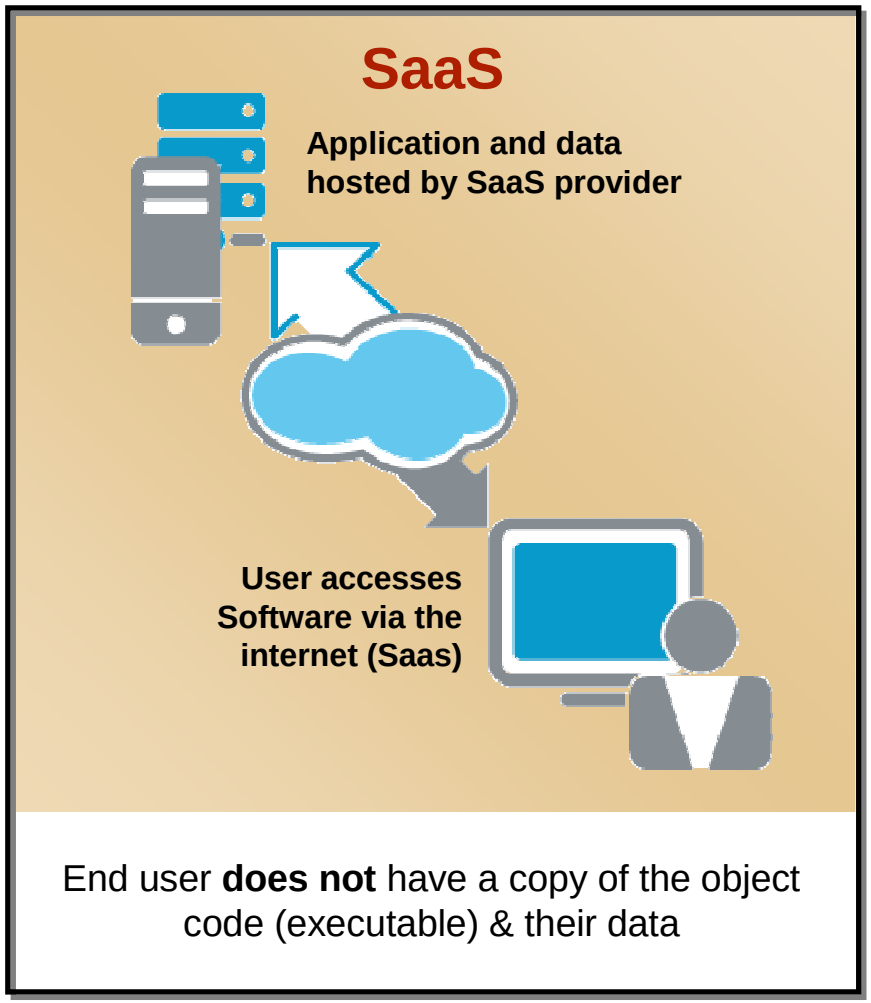
End user **does not** have a copy of the object code (executable) & their data

On Premise



End user has a copy of the object code (executable) & their data

Risk with SaaS Licensing Model



NO SOURCE CODE ACCESS

Plus

- **No copy of the executable code readily available to reload and run in a live production environment**
- **Generally, no access to usable data**
- **Often hosted through a third party, introducing additional risks**
- **DR/BC contingencies?**

Actionable Guidance: SaaS Providers & Subscribers

- Think Governance, Risk & Compliance (GRC)
- Review DR plan and ask what are the contingencies?
- Identify a failover back-up host to restore application
- Can they assume rights of SaaS provider in the event that they default on their obligations to the DR supplier
- Mandate a SaaS Protection strategy beyond traditional escrow to ensure long-term viability of the relationship and verify it!
  1. Compile the source code, validate build instructions
  2. DR test on the object code, restore data & validate procedures
- Establish a repeatable process to ensure consistency with each new enterprise-wide subscription plan.
- Craft a DR plan that is easily verifiable by prospective clients, which also includes succession planning. Think of it like a "living will"
- The SaaS escrow and verification testing is a part of the DR plan. The app is a responsibility that someone will inherit when something goes wrong
- Entrust a neutral 3rd party escrow agent to vault the deposit materials and to verify the RTO & RPO
- Leverage the exercise to gain credibility and to create competitive advantage
- Embrace the marketing value by publishing verification reports on your website, issuing press releases, etc.
- Offer SaaS protection escrow services as a valued added premium service to offset the cost of implementing an escrow plan.

Case in Point: The Common Application

Background	**The Common Application online, a non-profit site, lets students apply to** nearly **300 colleges and universities using one common application over the web.**
Challenge	**It uses a 3rd party technology partner to deliver the application online. As such, it needed some level of protection and security to ensure best user experience.**
Solution	**The Common Application online acquired Iron Mountain's SaaSProtect Escrow Service ™ and Verification testing.**
Benefits	**The Common Application now has the confidence that its systems will be kept up and running, in case of problems with the 3rd party technology partner provider.**

"The primary benefit is the security that we get. We know that if catastrophe strikes - either catastrophe in terms of a business relationship going bad or a natural or personal catastrophe - there is a 'plan B' that we can avail ourselves of quickly and securely with Iron Mountain, and that's something we haven't had before."

– Rob Killion, Executive Director of The Common Application

Risks & Challenges

- Offshore / Outsourced Development
- What are the challenges or risks surrounding such development and licensing?
  - Ownership rights
  - Preventing IP theft
  - Ensuring access to methods, work in progress, records and data ….. (recovery, transition)

Risks & Challenges

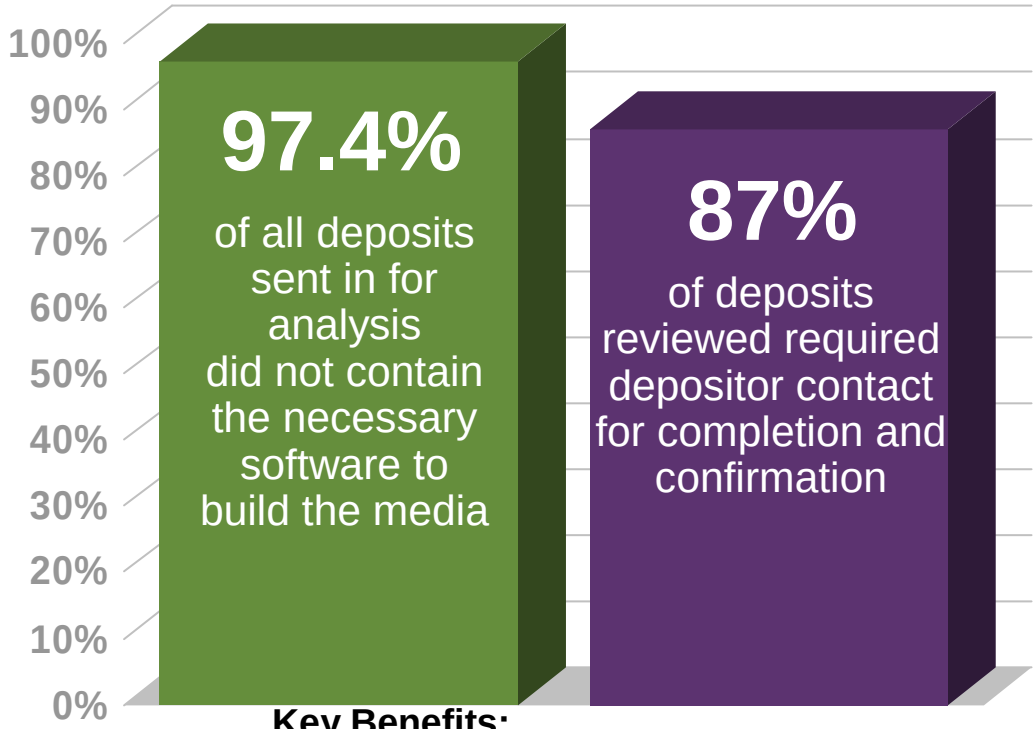
- Exclusive Supply Arrangements (exclusivity usually because of financial or intellectual property reasons)
- Risk of Supply Interruptions (particularly bad for a reseller or an essential raw material)
- Need for Alternative Manufacturer (usually a third party)
- Escrowed Specifications, Manufacturing Process and Know-How, Properly Validated, Protects Against Supply Interruption

What are Verification Services?

Verification is the process of regularly auditing the materials deposited in an escrow account to provide assurance that, in the event of a deposit release, a licensee would be able to quickly and effectively read, recreate and maintain the developer's technology in-house.

- Ensure deposited technology assets are complete and in working order
- Duplicate the original development environment with information on utilities, compilers, operating systems
- Strengthen escrow value by enabling a fast, successful deployment of deposit materials

Your Escrow Deposit – Trust, but Verify!



An escrow arrangement is only as good as the quality of the deposit materials.

VERIFICATION of materials provides assurance that, in the event of a deposit release, a licensee would be able to more quickly and effectively read, recreate and maintain the developer's technology in-house

Key Benefits:

- **Confirms that the technology can be successfully recreated and maintained**
- **Minimizes the risk of incomplete or corrupt deposit materials**
- **Strengthens the value of the escrow by ensuring a functional deposit**
- **Resolve deposit issues with the developer's assistance before crises arises**

Expected Industry Verification Levels

File Listing	**What does the deposit contain?** Verify that all media is readable, virus free and contains a complete file listing
Level 1 – Inventory	**Is the necessary information present?** Verify that information required to recreate the Depositor's development environment has been stored in escrow
Level 2 – Compile Test	**Do those deposit materials compile?** Verify the ability to compile the Deposit Materials and build executable code
Level 3 – Binary Comparison	**Do those deposit materials compile?** Verify that the compiled files on deposit compare identically in your actual, on-premise licensed technology
Level 4 – Usability Test	**Does the software work properly?** Verify and confirm that the built application work properly when installed

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Case in Point: Trans World Entertainment (TWE)

Background	Operates 900 specialty music and video retail stores, such as FYE, Coconuts, Strawberries, Wherehouse Music, CD World, Spec's and Planet Music
Challenge	Needed to protect a competitive-edge software. TWE worked with a software developer partner to create a proprietary listening viewing station (LVS) that allows customers in its stores to sample a CD or DVD by just swiping the bar code at the LVS.
Solution	Established an escrow agreement that included Verification services
Benefits	TWE competitive-edge software is protected and it now has the assurance the software could be accurately recreated, should the circumstances occur that required it to be so.

"I would definitely use technology escrow and verification services from Iron Mountain again. Considering our investment in the software, the cost to protect these assets is trivial."

– Trans World Entertainment

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Regulatory Compliance

- Corporate compliance regulations, such as Sarbanes-Oxley, mandate that companies implement near real-time ability to report on all events that "materially affect" their business.
- Technology escrow protects applications that enable companies to meet compliance regulations
- Technology escrow tools provide real-time, secure access to critical vendor and strategic application data

"As part of the Sarbanes Oxley Act, organizations must establish a plan of action in the event a software vendor fails and discontinues the support and maintenance of its systems.**"**

— **LENNY SMITH**, *Director of Division Operations*
Fidelity National Information Services

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Q & A

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Conclusion

- In information society, protecting knowledge assets is key
- Legal recourse not enough
- Escrow a core element of a 'best practice' strategy

White Papers:
Email ipm-info@ironmountain.com

- "Technology Escrow: Who's Using It and Why"
- "Verification Services: Fulfilling the Promise of Technology Escrow Agreements"

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