

What to Do When an IT Contract Hits Your Desk – 20 Key Questions

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It almost goes without saying that each IT project is different and requires a different contract. IT projects such as systems integration, outsourcing, and software development each have their own stand alone issues and risks that need to be addressed. The one-size-fits-all approach rarely works. However, there are still some key generic questions that can be asked when an IT contract hits your desk.

The purpose of this note is to provide a “heads up” on some of the initial questions that can be asked when first confronted with an IT contract. The questions are reasonably generic and can provide a starting point before delving into precedents or instructing a lawyer.

At the outset, note that not every IT contract warrants the same level of attention. Sometimes a quick review will be appropriate, sometimes it will not. The dollar value of the project is not always a good indication of the risks involved or how much time should be spent on the review. A “mission critical” project may not necessarily have a large price tag.

At an early stage it’s helpful to scratch below the surface, talk to the delivery people, and find out what this project will mean for the business in practice. That’s the idea behind the first 4 questions. The remaining questions address some of the detail of the agreement.

1. What’s the deal?

Even before diving into the detail of the contract it’s helpful to go back to first principles and consider the core commercial deal between the parties. Issues to think about include:

- What should the core obligations of each party be?
- What is the outcome that each party is looking for?

- Who else is involved?
- What processes need to be followed?
- What needs to happen and when?
- What are the deliverables?
- What are the dependencies?

2. Who are the stakeholders and what risks do they face?

As well as dollar risk, risks to business, property, data, and even life will often need to be addressed. There may also be risks to third party suppliers, end users, the general public and “Dominion Post front page risk” to consider.

3. What’s the technology?

Although the project will essentially be about delivering business benefits to both parties, there will be a technology layer that can have a substantial impact on what should and shouldn’t be included in the contract. For example, if there’s open source software included in the project there will be separate licences to review, and issues with warranties, indemnities, source code and the licence use to be worked through.¹ Generating a list of the different technology components will usually highlight what other contracts are needed and whether there are additional issues and risks that need to be addressed.

4. How will this project affect other projects and our existing systems?

Often one IT project will be part of a larger series of projects and/or will have an impact on existing systems. For example, the installation of new software or hardware may well end up voiding the support on existing

¹ See our paper:
<http://www.wigleylaw.com/OpenSourceSoftware.html>

hardware and software (because of modifications and changes that are made).

5. Where are the core obligations?

Have the core obligations been captured in the agreement? Are they reasonable, achievable and clear? The issues addressed in questions 1 to 4 should reveal some of the key things that each party should be doing as part of the deal. It's not uncommon for some of the key obligations on a party to be lost in the noise of the agreement.

6. What are the standards of performance?

What level of quality is expected from the deliverables supplied by the other side? This issue is normally addressed through the warranties that are included in the agreement. In this respect it's helpful to consider the extent to which any quality or best practice standards should be incorporated. Often the benchmark for performance will include "compliance with the specifications" or "performance in accordance with the documentation". This leads on to the next question.

7. What's in the specifications?

The specifications for a project include the specific detail on what is actually going to be provided (and is often contained in a schedule, or a separate "Work Request" or "Statement of Work").

A lot of the risk in IT contracting lies in the specifications. Often, the terms and conditions of the head agreement get a close review but are undermined by loose wording in the specifications. It is common for there to be ambiguous descriptions and inappropriate use of legal words (such as "guarantee").

The specifications should usually contain a clear description of the deliverables and include requirements around performance, functionality, capacity, response times, etc. It also helps to check whether or not the specifications should take priority over the main terms and conditions of the agreement.

Sometimes the specifications will be developed as the first phase of the project. If that's the case, it's usually appropriate for there to be some "Initial Requirements" that the specifications must be consistent with, and

processes for accepting the specifications and any changes to the pricing for the project.

8. What are the timeframes?

When must each party's obligations be completed? Is a delay serious enough to warrant termination of the agreement? Should there be liquidated damages?

9. Who gets paid and when?

Does the payment schedule make sense? Should the prices be estimated or fixed? Should there be retention amounts? Should a delay in payment result in termination of the contract?

10. What are the remedies if things go wrong?

Consider the remedies that are available to both parties if any of the obligations in the agreement are breached. There are various types of remedies that can be used, ranging from rights to terminate the agreement and sue for damages to service level rebates and step in rights.²

11. What are we liable for?

Closely related to the question above is the extent of each party's liability or exposure under the agreement. It is almost always appropriate for a party's liability to be capped.³ If this is not done the cost of doing business can be prohibitive. For suppliers, the limitations and exclusions of liability in an agreement can be some of the most important clauses.

Also, whenever there's an obligation on a party, it may be appropriate for exclusions and exceptions to be included. For example, it's not usually reasonable for a software supplier to be liable for any problems with its software where those problems have been caused by customer modifications or additions that it hasn't first approved.

² See our paper: <http://www.wigleylaw.com/mainsite/WhatToDoWhenItContractsAreGoingWrong.html> June 2004

³ See our paper: <http://www.wigleylaw.com/LimitationOfLiabilityAndRelatedIssues.html> Feb 2004 Update

12. Who owns the intellectual property?

Does each party own, or have the rights to use, the intellectual property (“IP”) that it needs? The ownership and licensing of IP is almost always one of the big issues in IT contracts. It’s easy for IP to fall between the gaps and for IP clauses to contradict each other.

At the end of the day it is important to consider what each party really needs. Often, through a combination of ownership and licensing each party’s needs can be met.⁴ The analysis should also consider what will be needed in the future if, for example, the business is sold, components are outsourced etc.

A useful first step is to consider what each party (including third parties) will be providing and producing in relation to the project (question 3 should help in this respect). It can also be helpful to think in terms of categories such as pre-existing IP, modifications to pre-existing IP and new IP.

If a party is not going to get ownership of IP it’s usually appropriate for there to be a licence to use that IP (for the purposes of the project, for future business opportunities etc). In general, the scope of any licence needs to be checked (for example, is it non-exclusive and royalty free, is it for internal business purposes only, does it allow use by another services provider, does it restrict use to a single CPU etc). Also, there should normally be some meaningful performance standards around the quality of the IP supplied (including as to the non-infringement of third party IP rights).

On the practical front, consider the format in which any IP should be delivered (e.g. by email, on CDROM etc), whether the source code to any software is to be supplied, and who will own any work in progress.

13. Where’s the IP indemnity?

Recent high profile disputes between SCO and IBM have highlighted the need to address the risk that IP received from the other party may infringe another person’s IP rights.⁵ If a

party is receiving any IP from the other party then it’s almost always appropriate for the supplier of the IP indemnify and defend the other party against any claim that its use of the IP infringes another person’s IP rights. There’s various ways that these IP indemnities can be drafted (whether you’re the party providing or receiving the IP).

14. What happens at the end of the project?

There may be a need for a transition process at the end of the project to help hand over the provision of the services and deliverables to the customer, or its alternative services provider. Similar processes may be required if the agreement is terminated. There will also often be the need for ongoing support and maintenance services at the end of the project.

15. Where are the acceptance tests?

It’s usually appropriate for there to be some kind of acceptance tests to confirm whether the deliverables have met the appropriate standards, when the warranty period should commence, and when payments should be made. Acceptance criteria for these tests should usually be agreed up front so that there is a clear benchmark for the performance of the tests.

16. Do the processes reflect reality?

Do the processes within the agreement reflect what is going to happen in practice? For example, boilerplate provisions around acceptance testing and change control (two important ingredients in an IT project) may require a procedure that’s not in your interests or that won’t work in practice.

Different methodologies and processes in the supply of IT services and technology will also impact on what needs to be in the contract. For example, in the context of software development, the choice between the use of a waterfall or an agile software development methodology will have implications on how the contract is drafted.

17. Do the metrics make sense?

There will often be service levels and performance metrics that need to be checked (particularly in the case of support and maintenance services). In particular, it helps to check the calculations that are used and

⁴ See our paper: <http://www.wigleylaw.com/IntellectualPropertyInITContracts.html>

⁵ See our paper: <http://www.wigleylaw.com/SCOIBMTheLinuxSpat.html> May 2003

whether there's clarity as to what is being measured.

18. Are the definitions OK?

Almost every IT contract contains a definitions section at the start or the end of the agreement. These definitions form the backbone to interpretation of the contract and need to be carefully checked. For example, the definition of "Intellectual Property" may refer to intellectual property that is created both before and after the commencement of the agreement – this may or may not be appropriate in the circumstances. Also, the definitions may not be used consistently in the schedules.

19. What happens if there's a dispute?

It is almost always appropriate for there to be some sort of dispute resolution process in the contract.⁶

20. Finally, what's missing?

A good question to finish on, particularly if dealing with a contract that has been prepared by the other side.

We welcome your feedback on this article and any enquiries in relation to its contents. This article is intended to provide a summary of the material covered and does not constitute legal advice. We can provide specialist legal advice on the full range of matters contained in this article.

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Wigley & Company
Barristers & Solicitors
Level 7, 107 Customhouse Quay
P O Box 10842
Wellington
michael.wigley@wigleylaw.com
Tel: (04) 472 3023
Fax: (04) 471 1833

⁶ See our paper:
<http://www.wigleylaw.com/TyingUpLooseEndsAndDisputeResolution.html> September 2004