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BUSINESS LAW

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Surviving a computer system contract

LET'S ASSUME that you are at the stage of upgrading or renewing your business' computer system which probably means that you are also purchasing software, hardware and services. Software contracts usually include provision for consultants to continue the customisation of the software and fine-tune the system in the months following the purchase.

You want to go ahead and the supplier gives you a draft contract for you to review and sign. What do you do with that draft contract? You read it and give it to a lawyer who specialises in reviewing software contracts. Only kidding – you hate lawyers. You sign it and put your copy in a draw.

Without or preferably with a solicitor there are seven points that you should be looking for in a computer contract:

1. The exclusion clause

Somewhere in the contract you will find the exclusion clause. This limits the liability of the supplier. Software suppliers tend to exclude liability for as much as they can. A common limitation is to cap the amount of any claim that you may make in court to be no more than the price that you paid for the software. This can leave you very much out of pocket.

2. Damages

What is the amount of damages (compensation) you will get if the contract goes wrong i.e. the supplier makes a mess of it?

- 'Direct' losses. These are losses which directly flow from the breach of contract. They are the price paid, cost of putting it right, any reasonably incurred emergency short-term fixes and directly lost profits.
- 'Consequential' losses. These are indirect losses which do not directly flow from the breach of contract. But there is a limit on what you can claim, damages cannot be too remote.

This is a complicated area of law and what you need to know is – don't allow the supplier to exclude direct losses but expect the supplier to exclude consequential loss.

3. Can you transfer it?

Can you let another company use the software? Can you sell your rights in it to another company? The supplier should give a licence that allows you to act as freely as your business requires in using the software.

4. Who is going to use the software?

Make sure the contract contains the correct company/employee name/s and that the licence is appropriate for the requirements of your business. A licence to use the software at one office will cost you a further payment if you open a branch office. If you put it in the name of one company but in fact another company also owned by you uses it you can be charged extra. However it does not need to be like this if you insist upon the right type of licence for your business – there are about 12 different types.

5. Escrow agreement

What happens if the software vendor becomes insolvent, or is unable or unwilling to keep up with commitments? Then the buyer will need to get access to the software to remedy errors and keep the system up to date. This is usually achieved by an escrow agreement. Here the source code is held by a third party and released to the buyer on specified events such as insolvency or failure to support. The terms are fairly standard. Companies in the computer industry go bust, or the people behind them lose interest with great frequency.

6. Termination

If things are going wrong then you will be reluctant to continue paying the supplier

until they put things right. The contract may provide that if you do not hand over the money when due, the supplier will tell you not to use the system until the installment is paid. If you cannot use the software your business could suffer. It is best not to leave a consideration of these issues until the problem arises. The contract will deal with what happens on termination or if the matter is going badly wrong.

7. Selling your business

When a company buys your business they want to know what they are getting. This check of the business assets is called due diligence. Part of the assets to be checked is the ownership of software.

The buyer relies on warranties. These are personal promises usually by the directors that they own the software. A problem for the seller company is that directors are personally liable.

The problem for the buyer company is that suing on the warranty costs money – it is better to get it right in the first place.

So am I exaggerating about the extent of trouble you can get into when dealing with computer contracts? Well, no. The computer industry has a word for users being ripped off. It is called 'stiffing'. An example is a company which purchased an existing business including expensive essential software. After the purchase they were contacted by the software publisher (a US multi-national) as their use of the software was inconsistent with the licence. The bill was substantial – equal to a new software system. They learnt about stiffing the hard way. So be warned. ●

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