

# **To Use, or Can I Use? Now *That* is the Question!**

**By Karen J. O'Connor**

Licensing software is a complex proposition for most health care organizations (HCOs). First an HCO has to define what it needs. Then it has to identify potential vendors and conduct untold hours of due diligence to narrow the field to those vendors that are best positioned to meet its needs. Finally, it has to reach agreement with the finalist vendor on contract terms and conditions, such as pricing and payment terms.

During the course of this entire process, many HCOs typically do not spend a lot of time contemplating the intricacies of the principle asset they are procuring — the software license itself. Yet the scope of the software license is at the heart of the transaction — the price paid and the terms of payment almost certainly will dim in importance if the asset acquired cannot rightfully be used by all intended users, or cannot rightfully be used for all intended purposes.

For these reasons, HCOs must consider a number of issues when negotiating the scope of a software license, including the authorized users definition, license restrictions, terms governing incremental usage, the term of the license and the circumstances under which the vendor can terminate the license.

## **Who Can Use the Software?**

One of the most critical things a software license must do is convey the right to use the software by all intended users. Think of this as identifying the universe of potential users who have the *right* to use the software, even if they never exercise that right, and even if there are restrictions relating to, for example, the number of persons within that universe who simultaneously can exercise that right. In a software licensing agreement, this objective typically is accomplished through an all-encompassing "authorized users" definition.

For most HCOs, the authorized users of the software likely will need to include, for both the HCO and its current and future affiliated entities, employees, non-employed physicians and other clinicians, volunteers and students, and third-party contractors, including temporary workers, consultants and outsourcing services providers, to name a few. Authorized users also may need to include persons or entities to whom or which the HCO or its affiliates provide

clinical health care services (patients or non-affiliated physicians to which the HCO provides laboratory services, for example), even if access and use is limited to inquiry access only, and any governmental or regulatory bodies lawfully requesting access to the software.

### **License Restrictions**

In addition to ensuring that all intended users will have the right to access and use the software, the HCO also will also need to ensure that the software license does not restrict use of the software in a manner that is inconsistent with the HCO's planned uses of the software. Use restrictions are not inherently bad, but it is critical that their impact be clearly understood.

The software vendor may impose licensing restrictions in a number of ways. For example, restrictions may be placed on the identities of the users ("named" users) or number of users ("concurrent" or "seat-based" users); the number or types of servers or work stations on which the software can be installed and used; and the sites, facilities and/or countries in which the software may reside. The HCO must carefully examine these common use restrictions to ensure that they do not conflict with how it intends to use the software. If a restriction conflicts with the HCO's planned uses, then that restriction should be discussed and modified appropriately during contract negotiations.

In addition to the above-described restrictions, the software vendor likely will seek to impose restrictions on the HCO's ability to transfer the software license to another person or entity. This type of restriction generally is acceptable; however, the license minimally should be transferable to a third party whenever, as specified in the assignment section of the agreement, the HCO has the right to assign the entire license agreement to a third party.

### **Incremental Usage**

Whenever a software license has metric-based restrictions — such as number of users, number of work stations, number of sites, and the like — the HCO should negotiate the right to expand use of the software beyond those metric-based restrictions by paying an appropriate incremental license fee. For example, if a license is restricted to ten concurrent users, the HCO should include in the contract pricing (which might be expressed as a specific dollar amount or as a percentage discount from the vendor's then-current list price) for concurrent users in excess of ten.

Historically (and remnants of history still can be found to exist today), software vendors licensing software to HCOs in the acute care setting have restricted use of software to an identified number of acute care facilities. Under this model, the HCO typically is allowed to expand use of the software to additional acute care facilities, subject to the payment of incremental software license fees that are calculated based on the number of licensed beds in that additional facility.

Today, a new metric has evolved — licensing based not on the number of facilities or licensed beds within those facilities, but rather on the annual net patient service revenues of the HCO and all or some portion of its affiliates. Under this approach, annual net patient service revenues are examined on an annual basis, and incremental license fees are owed by the HCO if that number has increased beyond a pre-determined threshold.

As with any metric-based licensing model, the net patient service revenues model is not inherently bad; however, in the absence of appropriate carve outs, or a sufficiently high buffer for growth, it can result in incremental license fees being owed not because the organization has expanded its use of the software, but simply because the organization has experienced organic growth. Most HCOs will not be happy with that result.

### **License Term**

The length of the license term, and the circumstances under which the license can be terminated, is another important issue to consider. Once implemented, HCOs become heavily reliant on their software systems, and any sudden or unexpected unavailability of the software could seriously impair the HCO's operations, including its ability to continue to provide necessary care to its patients.

With the exception of subscription-based models, most licenses are granted for a perpetual term, but are subject to termination under certain circumstances. Not surprisingly, vendors want to be able to terminate the software license if the HCO fails to comply with *any* term of the agreement, irrespective of whether that term bears any direct relationship to the license itself. The HCO, on the other hand, will want to restrict the circumstances under which the vendor can terminate a license to failure to: (1) pay all undisputed license fees for the software; or (2) adhere to the software license restrictions and confidentiality obligations relating to the software. In either case, the HCO should be given an opportunity to cure the failure, or if

a full cure is not possible, to substantially mitigate the effects of its failure, within a reasonable period of time following receipt of notice from the vendor that the failure has occurred. If the HCO's license to use the software is terminated, the agreement should nonetheless allow the HCO to continue using the software for a reasonable transition period to avoid causing irreparable harm to the HCO's operations or patient care.

An emerging trend among some software vendors is to tie the length of the license term to the length of time the HCO purchases support and maintenance services from the vendor. This approach is unfavorable to the HCO and should be avoided if possible.

### **A Word About Divestitures**

As much as, if not more than, any other industry, the health care industry is notorious for the sheer volume of its mergers and acquisitions (M&A) activity. Although the incidence of these activities has slowed in recent years, HCOs that do engage in M&A activity should consider including in their contracts the right to allow a divested entity to continue using the software under the auspices of the HCO's license for a pre-defined period of time, such as 12 months. During that "transition period", the divested affiliate would have the opportunity to engage in an orderly transition to a replacement system and/or to engage in negotiations with the vendor regarding the terms of its own licensing arrangement.

### **Conclusion**

Along with pricing, payment and other necessary contract terms, HCOs should fully understand and, if necessary, negotiate changes to its vendor's standard software licensing terms. Addressing the license scope and all of its related issues up front will help to avoid unpleasant surprises in the years ahead.

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*Note: The information contained in this article is current as of December 1, 2003, and is intended as general guidance only. This article should not be used as a substitute for legal counsel.*

Rick: I suggest including this as a boxed "side-bar" somewhere in the article.

**Sample Software License Grant Language**

Vendor hereby grants to HCO a perpetual and irrevocable (unless terminated as provided in Section X (License Termination) of this Agreement), non-exclusive, transferable (only as permitted under the terms set forth in Section Y (Assignment) of this Agreement), unlimited user (unless the parties specifically agree in writing to user limitations), fully paid (as hereinafter described), enterprise-wide license for: (a) HCO and its Authorized Users to access and use the software and its related documentation; (b) for HCO and/or its Authorized Users to make as many copies of the software and its related documentation as HCO deems necessary for production, testing, backup, training and education, development and archival purposes; and (c) for HCO to incorporate all or any portion of the documentation into any user and/or technical manuals maintained by HCO, provided that Vendor's proprietary notices are reproduced in connection therewith. The license for an item of software shall be fully paid upon HCO's payment of the applicable software license fee for such item of software, and additional software license fees that may be owed as a result of HCO's expansion of the scope of a license will not affect the fully paid nature of a license as its scope existed prior to such expansion.