

## **Drafting Technology Services Statements of Work: Structuring Terms, Minimizing Disputes, Streamlining Negotiations**

THURSDAY, JUNE 29, 2017

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

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# Drafting Technology Services Statements of Work: Avoiding Contracting Pitfalls



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*Special thanks to Jeff Maleska for his assistance in helping prepare these materials.*



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## Overview

- What is a Statement of Work (“SOW”)?
- Key Issues of SOWs
  - Drafting considerations
  - Understanding common commercial terms
  - Defining terms
- Drafting tips



# Learning Objectives

- Helpful tools in the contracting process
- Recent trends
- Avoid common pitfalls
- Explore negotiation techniques



# What is a Statement of Work?





## Definitions

- Master Services Agreement (“MSA”)
  - Framework for future engagements
  - Legal terms and conditions (representation, warranty, indemnification, and limitation of liability)
- Statement of Work
  - Specifics for a particular engagement
  - Business terms

# What is a Statement of Work?

- Exhibit/Schedule to MSA
- Describes service to be performed or goods to be delivered
- Often contains significant detail
- Covers projects:
  - At time of master agreement; or
  - Future projects during the term of master agreement

# What is a Statement of Work?

- Examples of SOW content:
  - Description of supplier's work product
  - Metrics to determine if work is complete
  - Conditions for acceptance of work product
  - How scope of work may change
  - Price and delivery terms

## SOW Pitfalls

- Often negotiated by the business people
- SOW may not be reviewed by all necessary parties
- Ensure MSA is still valid
- Subjective vs. objective terms
- Terms may conflict with MSA

## SOW Pitfalls

- SOWs can:
  - Undermine the MSA's beneficial protections
  - Cause ambiguity and disagreement
  - Impose unforeseen obligations
  - Enhance the risk of breach (e.g., hyper-technical standards)
  - Lead to litigation/financial losses

## Example Structure

- Overview
  - Introduction
  - Order of Precedence
  - Scope/Objective
  - Project Assumptions
  - Contract Type of This SOW
- Definitions/Acronyms
- Staffing Plan and Project Schedule
- Supplier Responsibilities, Deliverables, and Milestones

## Example Structure (Cont.)

- Personnel
  - Key [Supplier] Personnel
- Customer Responsibilities
- Mutual Tasks and Responsibilities
  - Project Management
  - Progress Meetings
  - Project Managers and Procurement Contacts

## Example Structure (Cont.)

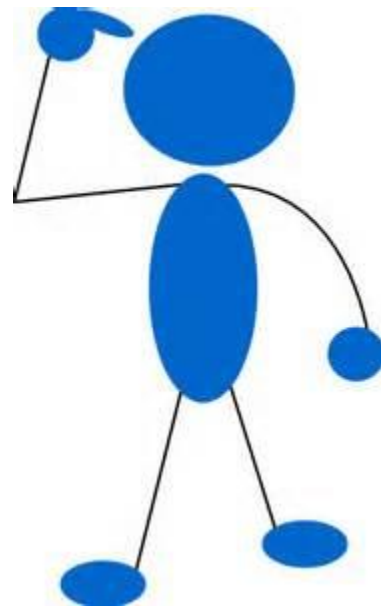
- Change Management Process
  - How to initiate a change
  - Who gives approval for a change
  - Cost estimate preparation
  - How to confirm the change was made
  - Logistics for making the change



## Example Structure (Cont.)

- Completion Criteria
  - When is the project over?
  - Objective vs. subjective standards
  - Acceptance and rejection process
- Payment Terms
  - Expense reimbursement (e.g., travel)
  - Holdback provisions
  - Time and material with not-to-exceed price

# Issues to Consider Before Drafting the SOW



## Before You Start: Planning Analysis

- Negotiate MSA and/or review MSA
- Identify your business objectives
- Confirm your budget
- Evaluate cost of alternatives
- Understand your negotiating leverage
- Determine timeline/deadlines
- Assign personnel/decision-makers

# Tools

- Who is producing the initial draft?
- Checklists and/or sample SOW
  - Update frequently to:
    - Keep current
    - Reflect industry standards and industry trends



## Form Selection

- Choose an appropriate format
  - MSA may include required form
  - Tailored to the engagement
    - Fixed-price contracts = more technical and detailed; whereas
    - Time and materials contracts = less detail
- Review to ensure MSA and SOW do not conflict
- Party drafting the SOW may not have drafted MSA

## Form Selection (Cont.)

- If using the other party's SOW, review it carefully
  - Is it one-sided?
  - Does it contain legal terms?
  - Do terms conflict with MSA?
  - How does the SOW impact the MSA?
    - Compliment or conflict?

# Marketing and Sales Content

- Avoid unintended consequences from pre-execution behavior
  - Parties negotiating should have authority to bind their companies
  - Consider if NDA is needed
  - Marketing puffery = (mis)representation?
  - MSA may specify how SOW must be created

# Understand and Define Key Commercial Terms and Conditions





## Commercial Terms and Conditions

- SOW should contains commercial terms and conditions, not legal.
- Legal terms should be in MSA
- Legal terms only in SOW when appropriate in light of the project-specific needs. For example:
  - Product sale in an otherwise services engagement
  - Unique security protocol
  - “Off the shelf” products
  - Ownership and/or licensing of IP rights
- Amendment to MSA may be appropriate

# Conflicting Terms

- If SOW contains legal terms:
  - Ensure the terms are applicable for the specific engagement
  - Determine whether MSA terms are amended, superseded
- Why legal terms may appear in SOW
  - Unable to renegotiate MSA
  - Terms are unique to specific engagement
- Safety measures
  - Order of precedence in event of conflict
  - Requirements that any SOW terms that conflict with MSA are only binding if signed off by owner/counsel

# Conflicting Terms Example

*StratMar Retail Servs. v. FirstEnergy Serv. Co.*, 2015  
U.S. Dist. LEXIS 128479 (N.D. Ohio, Sept. 24,  
2015).

## Facts

- StratMar contracts with FES
- MSA: FES can terminate with 30-day notice
- StratMar & FES negotiate new SOW
- StratMar emails new SOW; FES never signs

## Conflicting Terms Example (Cont.)

### Facts Cont.

- StratMar begins to work under new SOW
- FES compensates StratMar under new SOW
- New SOW: 60-day notice to terminate
- FES sends StratMar 30-day notice to terminate
- StratMar alleges 60-day notice required

## Conflicting Terms Example (Cont.)

### Holding

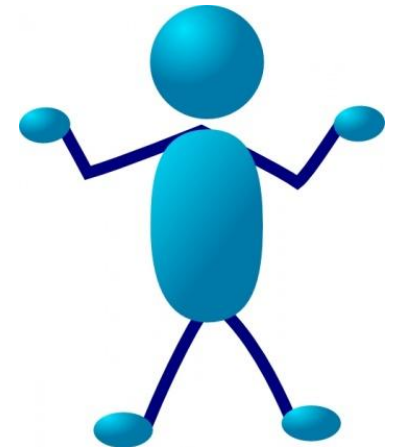
- FES wins; no breach
- Express Contract:
  - New SOW never signed
  - 60-day notice never approved
- Implied Contract:
  - FES payment under new SOW immaterial
  - SOW was “exhibit” to MSA; MSA governs

# Identification

- Identify and define requirements
  - How many resources are required?
    - Resources on or off-site?
    - Resources require system/network access?
    - Subcontractors required?
  - What products are being provided?
  - What's the timeline?

## Personnel

- Identify vendor's key personnel
  - Engagement Director, Project Managers, Key Personnel, Additional Personnel
- Limits on vendor's ability to replace / Consistency of staff over project term
- No additional fees (ramp-up costs) if vendor must replace staff
- Trend: Background and security checks



## Personnel (Cont.)

- Pre-qualification – if so, how?
- Right to review and approve staff, particularly onsite personnel
- Right to replace
- English proficiency
- Training
- Skilled in the type of services at issue, minimum experience requirements
- Workstations
- Responsibility for work negligently performed



## Additional Parties

- Is the engagement for the benefit of the named entity or affiliates, subsidiaries, customers, etc?
- Is the performance by the named entity, or its affiliates, subsidiaries, subcontractors?
- Consider geographic issues
- Diligence on other parties / Know your parties
- Primary responsibility for performance
- Critical v. generic services
- Responsibility
- Assignment

## Define

- Deliverables / Work Product / Reports
- Services
- Schedules
- Specifications
- Information / Data
- Assumptions
- Responsibilities
- Requirements / Dependencies
- Excluded Work
- Acceptance Process
- How and where performance will occur

# Shipping Defined

- Scheduling, Shipping and Delivery Terms
  - Project start / effective date
  - Key (all) milestones
  - Schedule / Deliverable / Performance dates
  - Project completion date
  - Project termination rights
- Delivery Terms
  - How shipped
  - Who bears the cost for shipping
  - Who bears the risk of loss
  - When does the risk of loss transfer (not necessarily tied to payment)



# Acceptance

- Specify objective completion criteria for each party's deliverables, dependencies and responsibilities
- Objective measures for reviewing Deliverables, Work Product, and Services
- Define applicable testing and acceptance criteria and processes
  - Pre-live testing
  - Post-live testing
  - Who reviews
  - Time for review
  - Level of adherence to acceptance criteria / specifications
  - Deemed acceptance
  - Opportunity to correct deficiencies
  - Termination

## Acceptance (Cont.)

- Versus verification?
- What types of tests:
  - Unit tests
  - System tests
  - Stress tests
- Failure to accept
- Remedies
- Payment tied to milestones & acceptance



## Acceptance Example

*SEC v. Morriss*, 2016 U.S. Dist. LEXIS 50194 (E.D. Mo., Apr. 14, 2016).

### Facts

- SOW: 50% project costs required to accept
- Defendant signs SOW; does not pay deposit
- Plaintiff still starts Defendant's work
- Plaintiff never receives deposit; sues

# Acceptance Example (Cont.)

## Holding

- Plaintiff wins; Defendant must pay deposit
- Signing and returning contract bound Defendant
- Defendant knew Plaintiff started work at signing
- Starting work without deposit did not invalidate contract

## Fees

- Schedule for Payment
- Timing of payments
  - Date based
  - Performance based
- Fixed price vs. time and materials
  - Renewal / adjustment in fees over time
  - Consumer Price Index (CPI)
  - Employment Cost Index (ECI)
  - Estimated





## Fees (Cont.)

- Holdbacks and true-ups
- Travel and out-of-pocket expenses (cap)
- Lower interest on late payments
- All fees
- Performance Credits
- Cap
  - Not to Exceed
  - Donut / Shared responsibility for overage
- Third Party Fees (pass through / managed)

## Fees (Cont.)

- Should be structured to:
  - Motivate performance
  - Assist project management
  - Protect against requirement for significant payments despite dissatisfaction with vendor performance
- Determine if a Fixed Fee, Time and Materials, or Hybrid payment method best promotes your goals

## Fees (Cont.)

- Include performance incentives/penalties:
  - Payment withholding pending key milestone completion
  - Project cost overrun protections
- Right to withhold payments in the event of non-performance, dispute

## Fees Example

*Blueshift, Inc. v. Advanced Computing Techs., Inc.*,  
616 S.E.2d 816 (Ga. Ct. App. 2005).

### Facts

- Blueshift contracts with E-Panacea
- Blueshift hires ACT (subcontractor) for E-Panacea contract
- E-Panacea stops paying Blueshift
- Blueshift stops paying ACT

## Fees Example (Cont.)

### Facts, Cont.

- MSA:
  - Invoice every 15 days;
  - Clause 12.2 shall not be altered by any SOW
    - Blueshift not obligated to pay subcontractor if client refuses to pay
- SOW: Invoice every calendar month
- ACT alleges Clause 12 invalid because conflicting terms

## Fees Example (Cont.)

### Holding

- Court upholds Clause 12.2
- Per 12.2 – Blueshift not required to pay ACT
  - \* Only if E-Panacea does not pay Blueshift
- SOW only altered MSA payment schedule
- SOW cannot alter Clause 12.2 terms

# Intellectual Property

- Will vendor be rendering development or customization services resulting in IP company wants to own?
- Will the vendor have access to any highly sensitive company IP?
- Vendor's materials
  - Clearly describe in Statement of Work or other exhibit
  - Use of pre-existing IP

## Intellectual Property (Cont.)

- Work product
  - Who owns
  - Restrictions on use
- Customer data
  - Clearly define
  - Include in what customer owns
- Third Party IP





## Service Levels

- Commitments and Reports
  - Describe the service levels
  - Make sure they are measurable
  - Report frequency
- Root Cause Analysis
- Problem Resolution Commitment
- Service Level Adjustments

## Termination of SOW

- Termination rights:
  - What constitutes a "material breach"?
  - Bankruptcy
  - Assignment
  - Convenience
- Effects of termination
  - Disentanglement
  - Termination assistance
  - Return/destruction of software
- No termination of support services
- Transition Assistance
- How does termination affect the MSA?



## Termination of SOW (Cont.)

- Customer and Vendor position not symmetrical when faced with non-performance
- Customer should strive to obtain commitment that:
  - Vendor will not suspend services except in the most limited circumstances
- A "no suspension of services" clause may not prevent all ills
  - A vendor bleeding money may still walk away from contract, notwithstanding clause
  - Courts seldom enforce personal services contracts. More likely to award damages (subject to liability cap)
- Negotiate an exception to the typical limit of liability clause for damages caused by a vendor's suspension of services

# Termination Example

*Alpha Telecomms., Inc. v. IBM*, 194 Fed. App'x 385  
(6th Cir. 2006).

## Facts

- IBM contracts with Alpha
- MSA outlines general terms
- SOW specifies time period – Dec. 1, 2001 to Dec. 1, 2003
- Feb. 25, 2004 – IBM does not renew SOW
- Alpha alleges IBM terminated without cause

# Termination Example (Cont.)

## Holding

- IBM wins; no breach
- SOW was unambiguous
- SOW terminated on Dec. 1, 2003
- SOW simply expired
- IBM chose not to renew

## Dispute Resolution Provision Example

*Caradigm USA LLC v. PruittHealth, Inc.*, 2017 U.S. Dist. LEXIS 85869 (N.D. Ga. May 30, 2017).

### Facts

- Pruitt (customer) contracts with Caradigm (vendor)
- SOW outlines dispute resolution process
- Pruitt unsatisfied with Caradigm's performance
- Pruitt abandons contract
- Caradigm sued for breach

## Dispute Resolution Provision Example

### Holding

- Pruitt's performance was not conditioned on satisfaction
- SOW allowed unilateral termination only after notice and 90 day cure period
- Pruitt did not abide by cure period—abandoned K
- Liability established: Pruitt liable for entire value of agreement
- Value of damages TBD

# Customer Satisfaction Survey

- Satisfaction surveys to evaluate the quality of vendor's products and services
  - Require vendor participation in process, but be careful...
  - If results of survey demonstrate dissatisfaction of vendor's products or services:
    - Meeting with high-level officials of vendor and customer to discuss and resolve the issue
    - Tie performance credit to result of customer satisfaction surveys



# Drafting Tips



## Is the SOW Covered by the MSA

- Ensure that the legal and commercial terms are appropriate for the envisioned engagement
  - Procedures in event of Breach
  - Remedies
  - Limitation of Liability
- Ensure consistency of defined terms (in MSA and SOW)



## What are my obligations?

- Only undertakings the SOW explicitly address
- Nothing beyond the SOW's express scope
- External understandings are inconsequential
  - *See Bus. Sys. Eng'g, Inc. v. IBM*, 547 F.3d 882, 890 (7th Cir. 2008).

## Details, Details, Details

- If services are not expressly identified in a SOW, vendor is under no obligation to perform them
- Take time to create a SOW that clearly identifies each party's tasks and obligations, deliverables, milestones, schedules, and fees
- Refrain from over-reliance on the vendor to create the SOW. Vendors normally use their proposal, which generally reads like a marketing brochure, with no specifics

## SOW Drafting Tips

- SOWs should generally include no legal terms
- MSA should take precedence over the SOW
- Remove or limit extensive lists of contingencies or assumptions on the vendor's performance
- Consider applicability of references to proposals or other generic marketing documents
- Avoid language that would waive acceptance or result in services or deliverables being "deemed accepted"

## Terms to Watch Out For

- Consider implications of the following terms:
  - "best efforts" or "all reasonable efforts"
  - "partner" or "agent"
  - "including" and "including but not limited to"
  - "world class," "best in class," "defect free," "highest standards" or "industry standards"
  - "guaranty," "warranty," "ensure" and "insure"
  - "time is of the essence"
  - "as directed"
  - "subject to approval"

## Terms to Watch Out For (Cont.)

- "detailed" detailed list"
- "as required"
- "average" or "adequate"
- "to the extent necessary"
- "solely"
- "estimate"
- "shall" versus "may"
- "would," "could," "would reasonably be expected to"

# Formulas

- Make sure they work
- Written algebraically
- Consult an expert
  - Internal business person
  - Caution: be weary of relying on vendor as the expert

$$\begin{aligned}
 S^2 &= \frac{a+b(d^2-c^2)}{4+32} = \frac{a+b(d^2-c^2)}{36} \quad 4 \cdot \frac{\pi}{C+C} \\
 \Rightarrow U^2 &= \sqrt{\frac{(s-s')^2}{12} + \frac{(a+b+c)^2}{36}} \quad 7(a-c) \\
 b+a^2 &= \sqrt{?} \quad S'' = V^2 + \frac{v^2-v}{a} \\
 \alpha &= \infty \quad c+a \\
 2 &= a-b^2 \quad 1=0+0 \quad \frac{\sqrt{a+b}}{a} \\
 + &= cb' \quad S^2 - V^2 = a - C + a \\
 \Rightarrow \frac{\sqrt{a+b}}{a} &? \quad b+a^2 \quad \int = \frac{a+b(d^2-c^2)}{4+32}
 \end{aligned}$$



## Levels of Effort

- Reasonable efforts
- Diligent efforts
- Good faith efforts
- Commercially reasonable efforts
- Best efforts
- Best commercially reasonable efforts
- Tier one efforts

# Material Breach

- Typical contract allows a party to terminate for the other's "material breach"
- May be difficult to determine whether a set of facts amounts to material breach
  - Solution:
    - Identify key scenarios and provide in contract that such scenarios constitute a material breach
- Repeated small breaches

# Cooperation

- At all times during the term, Vendor shall fully cooperate, and shall work in a timely manner, with the other service-providers of Customer as necessary to facilitate the performance of their respective contractual obligations to Customer and the timely resolution of all problems that may arise and impact the Services or the provision thereof, or otherwise adversely affect Customer or its Affiliates (or their respective end-users or patients) in connection with the Services, regardless of the actual or suspected root-cause of such problems or whether discovered through a Root Cause Analysis. The level of cooperation and effort provided by Vendor pursuant to the immediately preceding sentence shall in no event be less than that used by Vendor when dealing with its own subcontractors and service-providers. In the event of any dispute as to whether a particular problem was caused by Vendor (or its subcontractors or third-party service-providers) or by Customer or any of its third-party service-providers, Vendor shall promptly perform and share the results of a Root Cause Analysis with the Customer and the involved third parties in an effort to resolve such dispute in an expedited manner. If the dispute is not so resolved, then it shall be addressed in accordance with the dispute resolution process set forth in Section 14 of this Agreement. Vendor shall at all times treat each of Customer's third-party service providers in a fair and nondiscriminatory manner and refrain from interfering with any such service-provider or Customer's relationship therewith.

## Other Services

- When statement of work isn't enough
  - “The Parties have attempted to delineate in this Agreement, and in its Attachments, schedules and exhibits, the specific tasks, activities, and Services that shall be performed by Vendor hereunder. Nevertheless, and notwithstanding anything to the contrary herein, the Parties acknowledge and agree that no such delineation may possibly be entirely exhaustive or complete and that all such delineations shall be interpreted as illustrations of the general types and natures of services that are to be provided by Vendor, rather than as complete and exhaustive lists of such Services. Accordingly, Vendor shall in all events perform as reasonable to fulfill both the content and the intent of this Agreement, the Attachments (or any subsequent or additional statements of work mutually agreed upon by the Parties in writing), and all other schedules and exhibits hereto.”



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