

**The Latest & Greatest:
What are the Latest Business and Legal Developments
Impacting Information Technology License Agreements?**

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Table of Contents

Sarbanes-Oxley Act and Licensing Agreements	1
Stark Law – 2007 Proposed Modifications.....	3
Case Law Developments: Impact on IT Licensing.....	5
Trademark Infringement.....	5
Copyright Law and “Confusion”.....	6
Retroactive Arbitration Provision by Amending Online Terms?	7

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Following the accounting scandals of Fortune 100 companies like Enron, WorldCom and others, Congress reacted by enacting the Sarbanes-Oxley Act. How has this impacted your corporations licensing agreements?

In the healthcare arena, the “Stark Law”, which prohibits physician from referring patients to an entity in which the physician has a financial relationship for certain health services, was amended under the “Medicare Prescription Drug, Improvement, and Modernization Act of 2003”. May your healthcare client’s physicians use the hospital’s IT applications without violating Stark? What are the penalties if your client guesses wrongly?

And finally, a synopsis of the latest case law affecting license agreements: for example, personal jurisdiction due to internet activity; arbitration mandated even without an arbitration provision, and how to ensure “preferential” rights for payments even if the licensee ends up in bankruptcy.

Sarbanes-Oxley Act and Licensing Agreements

The Sarbanes-Oxley Act of 2002 (Pub. L. No. 107-204, 116 Stat. 745) is also known as the Public Company Accounting Reform and Investor Protection Act of 2002 and is codified as 15 USC 7201. The Sarbanes-Oxley Act (“Sarbanes-Oxley”) was enacted, according to the House Report 107-414, “[f]ollowing the bankruptcies of Enron Corporation and Global Crossing LLC, and restatements of earnings by several prominent market participants, regulators, investors and others expressed concern about the adequacy of the current disclosure regime for public companies.” Sarbanes-Oxley contains 11 titles that describe specific mandates for financial reporting:

- Title I – “Public Company Accounting Oversight Board (PCAOB)” (establishes the PCAOB to provide independent oversight of public accounting firms providing audit services to companies. The PCOAB will also draft audit compliance considerations, inspect and monitor quality control, and enforce SOX compliance.)
- Title II – “Auditors Independence” (establishes standards for external auditor independence, to limit conflicts of interest. Section 201 precludes SOX auditors from doing other audit work for the same clients.)
- Title III – “Corporate Responsibility” (requires corporate executives to have individual responsibility for the accuracy and completeness of the corporation’s financial reports. This responsibility, along with the obligations of the board, is to ensure accounting accuracy.)
- Title IV – “Enhanced Financial Disclosures” (requires enhanced reporting for financial transactions, including off-balance sheet transactions, pro-forma figures and stock transactions of corporate officers. Additionally, it establishes controls for ensuring the accuracy of financial reports and disclosures.)
- Title V – “Analyst Conflicts of Interest” (creates measures designed to help restore investor confidence in the reporting of securities analysts, including a code of conduct for securities analysts and requiring disclosure of knowable conflicts of interest.)
- Title VI – “Commission Resources and Authority” (defines the SEC’s authority to censure or bar securities professionals from practice and defines conditions under which a person can be barred from practicing as a broker, adviser or dealer.)
- Title VII – “Studies and Reports” (development of research tools for enforcing actions against violations by the SEC registrants (companies) and auditors, including studies

and reports on the effects of accounting firm consolidations, credit rating agencies effect on the operation of the securities markets, securities violations and enforcement actions, and whether investment banks assisted corporations to manipulate earnings and hide true financial conditions.)

- Title VIII – “Corporate and Criminal Fraud Accountability” (also referred to as the “Corporate and Criminal Fraud Act of 2002”, this section describes specific criminal penalties for fraud by manipulation, destruction or alteration of financial records or other interference with investigations, while providing certain protections for whistle-blowers.)
- Title IX – “White Collar Crime Penalty Enhancement” (also called the “White Collar Crime Penalty Enhancement Act of 2002”, this section increases the criminal penalties associated with white-collar crimes and conspiracies.)
- Title X – “Corporate Tax Returns” (clarifies the Chief Executive Officer should sign the company tax return.)
- Title XI – “Corporate Fraud Accountability” (also called the “Corporate Fraud Accountability Act of 2002”, this section identifies corporate fraud and records tampering as criminal offenses and joins those offenses to specific penalties.)

The requirement and possible criminal penalties for audit reporting has led many software vendors to change certain provisions in their technology licensing agreements. In addition, most publicly trade corporations have had to contract for Sarbanes-Oxley specialists who are capable of both verifying the audit materials are in compliance, as well as hiring Sarbanes-Oxley only auditors.

Information technology providers have become highly sensitized to revenue recognition issues also due to accounting scandals. Conversely, publicly held companies have become highly sensitive to any issues which may affect the company’s reporting obligations under Sarbanes-Oxley. A new type of representation under a master software licensing agreement would include Sarbanes-Oxley compliance. For example:

- (i) to the best of Licensor’s knowledge and belief, the Software complies with all applicable laws and regulations, including Sarbanes-Oxley Act Sections 302 and 404, where not to do so would have a material adverse effect on the Licensor’s ability to perform its obligations under this Agreement.

Companies have also had to contract with Sarbanes-Oxley “specialists” to assist with testing and reviews of management’s compliance obligations for information systems and business process capabilities. A typical definition of the services to be provided under such an agreement might be:

The objective of the IT component of the project is to document, assess and validate the existing internal controls over the IT applications (see definition below) in scope for significant financial accounts and disclosures.

The IT scope statement for the project period: The general computer controls, interface controls, application controls (as needed) and associated validation guidance will be documented, assessed and validated from the point-of-original-entry software application system to the Financial Statements for all Client significant accounts as defined by Client.

Definition of a System

Client considers the following items when identifying systems: A system should have an original data entry point, storage of the data, processing of data, and passage of the information to another location. Under this definition, Microsoft Access Databases and Microsoft Excel Spreadsheets are not considered systems from an IT perspective and are not in the IT scope. However, to the extent they are used in the business process, Client should include Microsoft Access Databases and Microsoft Excel Spreadsheets under the “Manual Control Frameworks” section of the business process for Sarbanes-Oxley purposes.

A Sarbanes-Oxley “specialist” service provider’s agreement might include a provision like the following:

(d) Any Work Product relating to the Sarbanes-Oxley Act of 2002 (“Sarbanes-Oxley”) is intended to assist Client’s management in preparing its assertions and/or documentation of internal control, and cannot constitute Client’s obligations to its external auditors, nor does it fulfill Client’s obligation to design and implement an effective control system and environment. Additionally, the Work Product can be only as complete as the information provided to Company by Client’s management. Company cannot be responsible for any documentation or assessment of those processes or controls Client chooses not to or fails to disclose to Company.

A Sarbanes-Oxley auditor agreement would expressly include a representation by the auditor that it does not and will not perform other auditing services on behalf of client in violation of the Sarbanes-Oxley Act.

Stark Law – 2007 Proposed Modifications

Originally enacted as part of the Omnibus Budget Reconciliation Act of 1989, the Stark Law, as amended,² is actually three separate provisions that generally prohibit a physician from making referrals to a medical facility, with which the physician or an immediate family member has a financial relationship, for the furnishing of specified “designated health services” (“DHS”) under Medicare, unless an exception applies. The Centers for Medicare and Medicaid (“CMS”) is the primary agency tasked with enforcement of the Stark Law. This law has been amended from time to time. Most recently, Stark Law was amended under Pub. L. 108-173. CMS drafted a rule to implement the new amendments in 2006. The amendment made an exception to “financial relationship” for a physician’s right to use electronic prescribing or electronic health records technology.

CMS defines the Stark Law as: “The physician referral law (section 1877 of the Social Security Act) prohibits a physician from referring patients to an entity for a designated health service (DHS), if the physician or a member of his or her immediate family has a financial relationship with the entity, unless an exception applies. (The exceptions are specified in 42 CFR Part 411, Subpart J.) The law also prohibits an entity from presenting a claim to Medicare or to any

² 42 U.S.C.S. §1395nn

person or other entity for DHS provided under a prohibited referral. No Medicare payment may be made for DHS rendered as a result of a prohibited referral, and an entity must timely refund any amounts collected for DHS performed under a prohibited referral. Civil money penalties and other remedies may also apply under some circumstances.”³

Under the 2006 amendment, a physician’s use of a hospital’s information systems will not be considered remuneration – possibly leading to an assessment that a financial relationship exists.⁴ The amendment by Congress (Pub. L. 108-173) only excepted “electronic prescribing”, but the Department of Health and Human Services and CMS used their “separate legal authority under section 1128B(b)(3)(E) of the Social Security Act (the “Act”), [to propose] separate safe harbor protection for certain electronic health records software and directly related training services.”⁵ As specified in the proposed rule,⁶ CMS intends that the new regulation will cover:

- Certified electronic health records software
- Directly-related training services
- Software must include an electronic prescribing component
- Could include billing and scheduling software, provided that the core function of the software is electronic health records

The most recent case under the Stark Law is extremely interesting for in-house counsel as the U.S. Attorney for the Southern District of Florida has brought a suit against the former in-house counsel for Tenet Healthcare Corporation (“Tenet”), Christi R. Sulzbach. The claim was brought under the False Claims Act for filing false claims with the Department of Health and Human Services (“DHS”) relating to known Stark Law violations. In particular, Tenet acquired a multi-physician practice in Florida for which it paid the physicians “salaries” several times higher than the average salary for a comparable doctor in the area. During reviews of the acquisitions, Sulzbach became aware of this issue and outside counsel’s conclusion that this practice was in violation of the Stark Law. Nonetheless, Sulzbach filed compliance letters with DHS yearly thereafter that there were no known Stark Law violations.⁷ This case has already resulted in numerous articles on the charges, possible defenses, and ways to avoid such charges in the future by other in-house counsel.

³ CMS response under FAQ for what does the physician referral law prohibit? Found online at http://questions.cms.hhs.gov/cgi-bin/cmshhs.cfg/php/enduser/std_adp.php?p_faqid=1501.

⁴ See Federal Register, Vol. 71, No. 152, dated Tuesday, August 8, 2006.

⁵ See the Department of Health and Human Services’ proposed rule 42 CFR Part 1001; found online at: <http://www.ehealthinitiative.org/assets/documents/EMBEDDED2.pdf>.

⁶ See fn 3.

⁷ See the Department of Justice’s complaint dated September 18, 2007; found online at: <http://www.usdoj.gov/usao/fls/PressReleases/Attachments/070918-05.Complaint.pdf>.

Case Law Developments: Impact on IT Licensing

Trademark Infringement

In the last year or two, there has been a series of cases debating and establishing conflicting law as to whether or not the purchase of ad words from a search engine and/or the use of such words in metatags constituted “use in commerce” under the Lanham Act for purposes of an infringement claim. One camp says yes, the other says no. Ironically, one of the oft-cited cases for the “yes” camp is an unreported 2006 decision from Minnesota (Edina Realty, Inc. v. TheMLSOnline.com).

“Yes” cases:

- Google, Inc. v. American Blind & Wallpaper Factory, Inc., 2007 WL 1159950 (N.D.Cal. Apr. 18, 2007) (holding that sales of ad words did constitute “use in commerce” for Lanham Act purposes);
- Edina Realty, Inc. v. TheMLSOnline.com, 2006 WL 737064, 80 U.S.P.Q.2d 1039 (D.Minn. 2006) (holding that purchase of keyword is Lanham Act use);
- Buying for the Home, LLC v. Humble Abode, LLC, 459 F.Supp.2d 310, 323 (D.N.J.2006) (holding that purchase of keyword is Lanham Act use);
- Australian Gold, Inc. v. Hatfield, 436 F.3d 1228, 1229 (10th Cir.2006) (affirming denial of judgment as a matter of law on Lanham Act claims based on the use of trademarks in metatags);
- Playboy Enters., Inc. v. Netscape Commc'n Corp., 354 F.3d 1020, 1024 (9th Cir.2004) (held that an infringement claim could be based on defendant's insertion of unidentified banner ads on Internet user's search-results pages);
- Promatek Indus., Ltd. v. Equitrac Corp., 300 F.3d 808, 814 (7th Cir.2002) (affirming district court's grant of a preliminary injunction where plaintiff alleged Lanham Act claim based on defendant's use of the mark in metatags); and
- Brookfield Commc'ns., Inc. v. W. Coast Entm't Corp., 174 F.3d at 1066 (9th Cir.1999) (holding that defendant's use of trademarks in metatags constituted trademark infringement as “use in commerce under the Lanham Act).

“No” cases:

- Fragrancenet.Com, Inc. V.Fragrancex.Com, Inc., 493 F.Supp.2d 545 (E.D.N.Y. Jun. 12, 2007) (holding that mark use in sponsored link on Google and in metatags did not constitute “use in commerce” under the Lanham Act);
- Site Pro-1, Inc. v. Better Metal, LLC, No. 06-CV-6508 (ILG)(RER), 2007 WL 1385730, at *4 (E.D.N.Y. May 9, 2007) (holding that use of a plaintiff's trademark as a metatag and the purchase of plaintiff's trademark for a Yahoo! search algorithm were not “use in commerce” within the meaning of the Lanham Act);
- Merck & Co., 425 F.Supp.2d 402, 408 (S.D.N.Y.2006) (“Google, Yahoo, and others ‘sell advertising linked to search terms, so that when a consumer enters a particular search term, the results page displays not only a list of Websites generated by the search engine program using neutral and objective criteria, but also links to Websites of paid advertisers (listed as ‘Sponsored Links’).” (quoting Gov't Employees Ins. Co. v. Google, Inc., 330 F.Supp.2d 700, 702 (E.D.Va.2004)), motion for

- reconsideration denied by, *Merck & Co. v. Mediplan Health Consulting, Inc.*, 431 F.Supp.2d 425 (S.D.N.Y.2006);
- *1-800 Contacts, Inc. v. WhenU.Com*, 414 F.3d 400 (2d Cir.2005), cert denied, 546 U.S. 1033, 126 S.Ct. 749, 163 L.Ed.2d 573 (2005) (pop-up ad use did not constitute "use in commerce" for purpose of Lanham Act claim);
 - *Savin Corp. v. Savin Group*, 391 F.3d 439, 455 (2d Cir.2004) (claims of dilution claims under the Lanham Act require that a plaintiff show that "the defendant is making commercial use of the mark in commerce.");
 - *Rescuecom Corp. v. Google, Inc.*, 456 F.Supp.2d 393, 404 (N.D.N.Y.2006) (dismissing dilution claim where plaintiff could prove no set of facts showing trademark "use" within the meaning of the Lanham Act); and
 - *U-Haul Intern. Inc. v. WhenU.com, Inc.*, 279 F.Supp.2d 723, 729 (E.D.Va.2003) (entering judgment as a matter of law for the defendant on the plaintiff's claim of trademark dilution because the plaintiff was "unable to show that WhenU was using U-Haul's marks as defined in the Lanham Act").

"Maybe" Cases:

- *J.G. Wentworth, S.S.C. Ltd. P'ship v. Settlement Funding LLC*, 2007 WL 30115, at *6 (E.D.Pa. Jan. 4, 2007) (concluding that use of a mark in Google's AdWord program and in metatags is "use in commerce" under the Lanham Act but no "likelihood of confusion"); and
- *Hamzik v. Zale Corp./Delaware*, 2007 WL 1174863, at *2-3 (N.D.N.Y. Apr. 19, 2007) (the Court agreed with the reasoning in *Rescuecom* and *Merck*, but denied the motion to dismiss, because a search of plaintiff's trademark not only returned defendant's website among the search results, but plaintiff's trademark also appeared next to defendant's name, demonstrating that plaintiff's trademark could be displayed in a way indicating an association with defendant).

Copyright Law and "Confusion"

In the *Perfect 10* case,⁸ the Ninth Circuit described Google's actions in creating thumbnail images as "frames in-line linked images that appear on a user's computer screen."⁹ The Ninth Circuit concluded that Google does not "copy" any image, rather "Google provides HTML instructions that direct a user's browser to a Web site publisher's computer that stores the full-size photographic image."¹⁰ The court continued that "[w]hile in-line linking and framing may cause some computer users to believe they are viewing a single Google webpage, the Copyright Act, unlike the Trademark Act, does not protect a copyright holder against acts that cause consumer confusion."¹¹

⁸ *Perfect 10, Inc. v. Amazon.com, Inc.*, 487 F.3d 701, 82 U.S.P.Q.2d 1609 (9th Cir. 2007).

⁹ *Perfect 10*, 487 F.3d at 717.

¹⁰ *Perfect 10*, 487 F.3d at 717.

¹¹ *Perfect 10*, 487 F.3d at 717.

Retroactive Arbitration Provision by Amending Online Terms?

In the Douglas case, the Ninth Circuit considered whether a service provider may change the terms of its service contract merely by posting a new version on its web site.¹² The district court granted the service provider's motion to compel arbitration under the revised service contract and the plaintiff appealed under a petition for writ of mandamus. The Ninth Circuit follows five factors in assessing whether to grant a writ of mandamus:

1. "The party seeking the writ has no other adequate means, such as a direct appeal, to attain the relief he or she desires."
2. "The petitioner will be damaged or prejudiced in a way not correctable on appeal."
3. "The district court's order is clearly erroneous as a matter of law."
4. "The district court's order is an oft-repeated error, or manifests a persistent disregard of the federal rules."
5. "The district court's order raises new and important problems, or issues of law of first impression."¹³

The Ninth Circuit concluded that the district court had "erred in holding that Douglas was bound by the terms of the revised contract when he was not notified of the changes."¹⁴ The Ninth Circuit in granting the writ of mandamus, and vacating the district court's order to compel arbitration, clearly indicated that effective notice has to be given to a consumer before terms of use (or a service contract) can be amended with an arbitration provision.

The district court had looked at cases where notice was provided either by direct mailing, or by required access to the web site for the service itself. In the Douglas case, the plaintiff claimed that he never went to Talk America's web site as he had authorized automatic deductions for his account.

¹² Douglas v. U.S. Dist. Court for The Central Dist. of CA, --- F.3d ----, 2007 WL 2069542 (9th Cir. 2007).

¹³ Bauman v. U.S. Dist. Court, 557 F.2d 650, 654-55 (9th Cir.1977).

¹⁴ Douglas, 2007 WL 2069542 at *2.