<u>Thomas H. Makeig</u>

Thomas H. Makeig, P.C.
500 North Third Street, Suite 213
Fairfield, Iowa 52556
(641) 4722-2235
Fax: (641) 472-6347
Tmakeig@makeiglaw.com

IOWA STATE BAR ASSOCIATION *e*COMMERCE SECTION CLE
SEPTEMBER 14, 2001
<u>FROM BRICKS AND MORTAR TO THE INTERNET</u>
PRACTICALLY SPEAKING:
DRAFTING AND NEGOTIATING WEBSITE AGREEMENTS

<u>OUTLINE</u>

1. <u>Your client's motivation</u>:

    Virtually all business will be Internet-enabled by the end of this decade.

    Those of our business clients who want to stay in business will not abandon their bricks-and-mortar marketing and distribution channels but will be Internet-enabled.

2. To <u>SELL products on the Net</u>, your client needs

    a. A web site (Net marketing presence)

    b. Integration of Net selling with order processing/ inventory/order fulfillment functions.

    c. Payment or billing means

To PURCHASE from vendors on the Net, your client needs integration of vendors with its purchasing/inventory/ A/P functions

3. <u>To get Net-enabled, your client needs to procure the services of a web site developer.</u>

Everything about commerce on the Net is different from other business:

>   Marketing (positioning)
>
>   Advertising (reaching the customer)
>
>   Content design (graphics and text)
>
>   Software design and selection/customization for
>
>> - web site navigation
>> - transacting a sale at the site
>
>   Web site interface with your client's back office systems (order processing/ inventory/order fulfillment)

4. <u>What a web site developer does:</u>

To enable SELLING on the Net:

a. Develop marketing concept

b. Graphic design of web site

c. Copywriting the web site content

d. Software design/selection/customization to enable easy and effective navigation of the site

e. Software design/selection/customization to enable easy and effective purchasing

f. Integration of web selling with your client's order processing/inventory/ fulfillment functions

g. Design and placement of hyperlinks and banners (advertising and dissemination)

h. Creation of meta-tags and positioning of the website with major search engines.

To enable business-to-business PURCHASING on the Net:

> Integration of Net purchasing with your client's purchasing/ inventorying/ A/P functions.

A good web site developer has a team with a flair for Net marketing, Net advertising, graphic design, creation of text and images, programming of sites with human factors in mind so that the site is easy to find on the Net, easy to navigate, and purchasing at the site is easy to consummate.

Few large businesses procure all these services from a single source. Some web site developers offer all these services.

5. <u>Checklist for services agreement(s)</u> with your web site developer(s):

a. Clearly specify terms of service.

> If possible, get a firm quote on a well-defined, goal-oriented statement of work.

> Many web site developers prefer to work on time and materials (T&M). This places the risk of cost overruns on your client. If your client agrees to T&M, make sure it is against a well-defined, goal-oriented statement of work in any case.

b. Testing and acceptance:

> Make sure your client has a reasonable period to test for apparent defects in the web site developer's work product. Put a time limit on the web site developer's response to any rejection. Provide for several iterations of testing-rejection-fixes.

> Your client will test in a lab or (at best) a beta environment. No test can anticipate all the crazy things that actual consumers do when visiting your site. Make sure there is a reasonable period following customer launch to require fixes of latent defects that appear for the first time following launch of the web site.

> Make sure you preserve the client's ultimate sanction of total rejection with a right to refund.

c.   <u>IP considerations</u>.

Web site developers want to preserve the IP rights to their work as a means of (1) preventing their good ideas from being copied by competitors, and (2) obtaining further contracts for web site development.

The Net environment has created a new set of rules regarding the preservation and use of all forms of IP. Unfortunately not all the new rules have been worked out.

In negotiating with a web site developer, you must consider the following:

1.   Non-disclosure and non-use of the client's proprietary information, including its customer/distributor/vendor databases, financial information, products and processes.

2.   Infringement of 3P rights to web site content (images, logos, text): developer must warrant against infringement.

3.   Infringement of business methods. Many of the business methods used in e-commerce are new. The recent decision of the United States Court of Appeals for the Federal Circuit in <u>State Street Bank & Trust Co. v. Signature Financial Group, Inc.</u>, 149 F.3d 1368 (Fed. Cir. 1998) has opened pure business methods (as opposed to processes, devices, computer programs and the like embodying business methods) to patentability. Consequently all business methods used in e-commerce should be regarded as potentially subject to patent protection, either by your client, the web site developer or a third party.

Accordingly,

(1)   your client should reserve its business methods in all fields of application and not license them to the web site developer.

(2)   the web site developer should not reserve its business methods but assign them to the client, or at least license them to the client royalty-free, for use with the client's web site. If the client wants to reproduce or re-brand its web site, it should have the right to sub-license the web site developer's business methods.

(3)   the web site developer should warrant against infringement of third party rights to business methods.

4.   Hyperlinks/ "Deep Linking." Trespassing and infringement of trademark and copyright in connection with hyperlinks is a growing concern. Any hyperlinks from your client's site to a competing site should be written up in plain text without the use of a competitor's mark, unless permission to use such mark is obtained from the holder or "fair use" can be established. The web site developer should warrant against this form of infringement of third party rights by its work product delivered to your client.

5.   Source code. The web site developer should turn over with its work product the complete source code that it creates in connection with your client's site.

6.   Work for hire and assignment of all rights to the work product by the developer to the client. As an independent contractor, the web site developer enjoys a presumption that it reserves the copyright to any work product created for your client. This presumption should be reversed by the terms of the service agreement. Additionally, all rights to the business methods, content and proprietary information should be assigned to the client.

Frequently web site developers make such assignments conditional upon full payment and compliance with the client's obligations under the services agreement. Also, web site developers are loath to give any more than a royalty-free license to the client to use the site, so as to minimize the risk that their work product consisting of original programming, customization of standard software, arrangement of pages and links, and the look and feel of the site do not pass into general use, thereby diluting the developer's ability to distinguish its work product from that of competitors.

If your client wants to aggressively reproduce its site for use by its affiliates, distributors, co-venturers and others, it may angle for the right to re-brand and sublicense the web site. This would deprive the developer of potential additional contracts for web site development and could cause a loss of control of its proprietary methods, programming, look and feel and the like.

Hyperlinks will replace software. It may be best for the client to rely instead on hyperlinks to accomplish what in the pre-Net era was

accomplished by a right to sublicense custom software created by a software developer. It is possible to funnel the customers of your client's affiliates, distributors and co-ventures to your client's site without reproducing any of your client's web site contents or programming. Your client's affiliates, distributors and co-venturers should simply be invited to create hyperlinks from their sites to your client's site, either to its home page or to your client's order processing page. The order processing page can even be sanitized to avoid branding confusion if your client's distributors and co-venturers prefer to brand the products themselves and simply rely on your client for order processing and fulfillment. This leaves open the possibility that your client will be able to lay claim to the customer due to repeat billing or reservation of the right to claim the customers' data as being proprietary to your client.

7.   The web site developer should provide evidence of its right to use and sub-license any and all IP of third parties incorporated by the developer into your client's site.

   d.   Warranties against defamation, obscenity and illegal activities.

   e.   Warranties regarding security of your client's and its customers' information; warranties against vandalism of the web site.

   f.   All the normal commercial terms on governing law, assignment and delegation, entire agreement, dispute resolution and the like.

USEFUL LINKS

1. A thorough description of the web site development process and drafting tips by a law student:

    http://www.digidem.com/legal/wda/wda.html

2. Link to Law.com's index of Internet and Computer Law web sites:

    http://www5.law.com/ia/lawguide/internet.shtml

3. Law.com provides an invaluable free daily newsletter drawn from numerous lawyers' publications and covering developments in every area of the law. Its cyberspace coverage is especially good.

    http://www.law.com/newswire/