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Cloud for the German Market – Are we getting there?

A Rough Line Legal Comparison

The IT group (in Germany) enjoys a strong market reputation, advising an impressive array of clients and frequently acting alongside international colleagues on multi-jurisdictional projects. Sources say: "A top-class outfit with exceptional advisers."

Chambers Europe 2012

Introduction

Cloud Computing raises a lot of questions as to the contractual requirements under German law. The issues around licensing usage rights, warranties and liability, data protection and exit management are core to any cloud services, be it IaaS, PaaS, SaaS, Process as a Service or any other cloud offering.

How do some of the large providers handle these issues? Do they meet the expectations of German statutory law? Are B2B users reasonably well protected?

As part of the "Trusted Cloud" event of the Federal Ministry of Economic Affaires and Technology on 9 November 2012[1], we have compared some of the prominent offerings addressing the German market[2]:

Interestingly, a number of providers have opted to use terms subject to foreign law, leaving behind the stringent judicial control of German courts on standard terms and conditions ("t&c" and "t&c law"). The downside of this approach is, however, a significantly lower degree of B2B user acceptance (which is by far not limited to the SME segment).

We do not claim to have made a full review. But our rough line analysis shows: Cloud providers are struggling to meet proper expectations against the background of German law. And those who are contracting under German law keep a considerable number of important, but unenforceable provisions in their t&c. At the same time, our rough line comparison might help B2B users as a high-level orientation what to ask for from their providers, if and when there is room for negotiation, whereas **we wish to emphasise that our comparison cannot replace taking proper legal advice on the individual agreements concerned**.

Cloud Standard Agreements

- Amazon Web Services: "AWS Customer Agreement" (as of 15 March 2012), governed by the laws of the State of Washington, and "AWS Service Terms" (as of 26 September 2012)
- HP: "Customer Agreement" for HP Cloud Services (as of 3 July 2012), governed by the laws of the State of New York
- IBM: "Smart Cloud Vereinbarung" (as of 31 August 2012), governed by German law
- Microsoft: "Online-Abonnement-Vertrag" and "Nutzungsrechte für Onlinedienste" (as of October 2012), governed by Irish law
- Oracle: "RightNow Master Cloud Services Agreement" (as of 13 April 2012), governed by German law
- Salesforce: "Rahmen Abonnementvertrag" (as of 15 September 2009), governed by German law
- SAP: "General Terms and Conditions for SAP Cloud Services" (as of August 2012, updated as of January 2013), governed by German law.

Licensing

While in many instances the user of IaaS, PaaS and SaaS does not copy any software,[3] all agreements do provide for some form of a licensing clause. In several cases the license clause contains further restrictions on the scope of permitted usage, including limitations on classes of CPU, named user concepts, etc. Also, most agreements expressly or implicitly resonate the concept of a "software rental", which is the legal basis for effectively imposing non-transfer restrictions under German law.[4]

Licensing							
	Amazon*	HP*	IBM	Microsoft*	Oracle	Salesforce	SAP
License provisions?	✓	✓	✓ (in part for referenced software)	✓	✓	(✓)	✓
Non-transfer restrictions? (in part for referenced software)	✓	✓	✓ (in part for referenced software)	✓	✓	X	✓
Usage limitations by users, CPU classes, etc.?	✓ (in part for referenced software)	X	X	X	X (under usage matrix?)	✓ (user subcriptions)	✓ (named users)
Typical lease of software T&C?	✓	✓	(X)	✓	✓	(X)	✓

*not subject to German law

Warranties

Each agreement contains warranty clauses and/or provisions on contractual remedies for the user with regard to material defects as well as defects in title (IP infringement). Two general comments upfront: (a) Assuming that cloud agreements will essentially be deemed as rental agreements for the purposes of German law (see above), the contractual remedies will follow accordingly. (b) German law of contracts general treats material defects (i.e. malfunctioning of software) and defects in title (IP infringement) largely in parallel.

Remedies for material defects

Under statutory law, the provider of rented software is under a continuous obligation to keep it in proper function throughout the entire term of the agreement, without raising additional cost to the user beyond the rental charge.

Interestingly, a number of providers have set out (a) limited warranty periods, often restricted to one year (even where contracting under German law), and/or (b) warranty disclaimers, claiming that the services are provided "as is", arguing with the nature of software never being free of defects. Both is clearly incompatible with German statutory law.

Where Cloud providers are asking additional charges for varying levels of support services these are justified under German law, if and where the services exceed the mere statutory repair obligations (e.g. premium support including hotline services, supply of upgrades, etc.).

Material defects							
	Amazon*	HP*	IBM	Microsoft*	Oracle	Salesforce	SAP
Short warranty periods?	✗	✗	✗	✓	✓	✗	✗
Costs for support?	✓	✗	✓	✓	✗	✗	✓
Compliance with German T&C laws?	✗ ("as is" usage)	✗ ("as is" usage)	✓	✗	✗	✓	(✓)

Rights regarding defects in title

Despite all agreements defining rights of use, only half of them contain express IP indemnity provisions to defend the user against any third party claims. Where the agreements are subject to foreign law, this is of particular concern with regard to users potentially infringing software patents. Where the agreement is subject to German law, the user can rely on a statutory indemnity (in parallel to material defects, see above). Interestingly, one provider has limited the IP indemnity to patent infringements arising in the US - which would be an unenforceable limitation if and when the provider is contracting under German law.

Defects in title							
	Amazon*	HP*	IBM	Microsoft*	Oracle	Salesforce	SAP
IP Indemnity?	✗	✗	✗	✓	✓	✓	✓
Geographic limitations?	✗	✗	✗	✗	✓ (only US patents)	✗	✗
Compliance with T&C laws?	✗	✗	✗	✗	✗	✓	✓

Liability

All the agreements include liability clauses, which to a large extent would be held unenforceable by German courts (if ruling on standard terms subject to German law). As a result, providers are – more or less consciously – at risk of falling back on the position of German statutory liability. That effectively includes unlimited liability for any kind of wilfulness and negligence, including for any kind of indirect and consequential damages. That may be one of the key reasons for some providers to contract under foreign law, in order to maintain their business model because of its standardisation, scalability and the absence of negotiation. Where or not this latter approach helps to increase the acceptance remains to be seen, however (see above).

Where providers limit their liability to the "typically foreseeable damage" in case of breaching a material contractual obligation (a "cardinal obligation"), their exclusion of liability for other cases of negligence is enforceable. Notwithstanding, some agreements have implemented this materiality threshold even in regard to gross negligence, which renders the clause unenforceable.

All agreements contain monetary or percentage liability caps, which as such are unlikely to be enforced by German courts, if and when the specific damage incurred exceeds the "typically foreseeable damage". The only way out of this provider dilemma would be to individually negotiate a suitable limitation – which may or may not stand in direct conflict with the provider's business model.

Liability (pursuant to T&C law)

	Amazon*	HP*	IBM	Microsoft*	Oracle	Salesforce	SAP
Unlimited liability for intent, gross negligence, etc.?	✗	✗	✓	✗	✓	✓	✗
Typically foreseeable damage (in connection with cardinal obligations)?	✗	✗	✗	✗	✓	✓	✗
Liability for consequential damages?	✗	✗	✗	✗	✗	✗	✓
No liability caps?	✗	✗	✗	✗	✗	(✓)	✗
Compliance with T&C laws?	✗	✗	✗	✗	✗	(✓)	✗

Data protection

Surprisingly, not all agreements stipulate a regular controller-processor relationship (by way of a "commissioned data processing agreement" (CDPA", or "Section 11 Agreement") - which is essential whenever the user puts into the Cloud personal data that he controls. There are significant challenges on how to properly implement the statutory requirements of Section 11 of the German Data Protection Act (GDPA) for Cloud services.[5] Nevertheless, the lack of sufficiently documented technical and organisational measures ("TOM"), as required under the Section 9 of the GDPA, is unsatisfactory.

Additional data protection problems arise if the provider back-ends his infrastructure outside the EU/EEA, either directly or through sub-processors. Proper contractual agreements and sufficient safeguards to ensure adequacy of along the lines of the EU Model Clauses[6] or under the Safe Harbor regime[7] need to be warranted. Users should be aware that German data protection authorities have set sharpened requirements on the controllers to effect such international data transfers, including a "two-step test" (looking at the legal justification for the transfer plus the adequacy requirements) and putting under recurrent scrutiny pre-existing Safe Harbor registrations. In addition, the authorities have made it clear that certain data, such as health data, will not be eligible to such international transfers. All agreements address the issue of international transfers at least in general terms. But we have noted a lack of transparency on locations regarding back-end processing. The user (controller) needs to be aware that it is his sole responsibility to ensure that all legal requirements of compliant processing are met in regard to the data he controls.

A further, highly relevant flaw in most agreements is the lack of information duties by the providers in the case of data leakages. As statutory law requires the user / controller to take immediate action (including informing authorities and data subjects), it is deeply worrying to see that providers could potentially leave their customers uninformed about data leakages for significant time. Users have a vested interest that the provider's t&c stipulate such an obligation. At the same time, users should also be protected from the provider making notifications to the authorities without having consulted the controller. Otherwise, this could impact on the "principle of responsible disclosure" which governs the user's notification to the individual data subjects.

All in all, there is significant room for providers to improve their efforts in documenting data protection compliance. We believe this is the key for achieving greater user acceptance of Cloud offerings

Data protection

	Amazon*	HP*	IBM	Microsoft*	Oracle	Salesforce	SAP
CDPA?	✗	✓	✓	✓	✗	✓	✓
TOM Sec. 9 German Data Protection Act?	✗	✗	(not fully checked)	✗	✓	✓	✓
Intl. data transfer/Safe Harbor?	✓	✓	✓	✓	(not fully checked)	✓	✓
Provider's obligations in connection with data leakages?	✗	✗	✗	✗	✗	✓	✓

Exit management – think about the end!

Depending on the nature of the Cloud service provided, users are ultimately dependent on the provider to retrieve the data stored in the Cloud in a usable and migratable format. As part of a "clean exit" providers need to ensure proper deletion of existing data from the Cloud. It is equally important, however, that providers enable a smooth and efficient migration to another provider or back to the user's own systems. The proper definition of data formats and sufficient time periods for the transition are pivotal to prevent the "vendor lock-in" that many users raise as a concern – or might have overlooked when entering into their Cloud agreement.

In general terms, providers need to demonstrate more clearly their efforts in supporting efficient exit and data migration when defining easy exit scenarios ("plug & pull"). It is highly questionable whether such support should actually trigger extra charges, as suggested by some providers. A common industry standard with more user friendly exit terms is yet to develop. Whether that should include certain know how transfer (such as proper documentation of the database configuration) is up to debate.

A further point of vital importance is hardly or not at all considered: The rights of the database maker under (EU and) German copyright law. Where a user uploads database, he will need to grant a license to the provider to use the data; some t&c address this point implicitly by defining a generic content license granted by the user. More importantly, however: Where the provider takes raw data or reconfigures pre-existing database, it may well be that, by operation of law, he is the holder of database rights with regard to such newly created database. The test comes at the exit: Does the provider have proper rights in the database, which he needs to waive? Users are well advised to pay attention to this particular aspect, and request clarity and contractual safeguards that they can exit without a claw-back or rights retention on side of the provider.

Exit management

	Amazon*	HP*	IBM	Microsoft*	Oracle	Salesforce	SAP
Exit support?	✓ (extra costs)	✗	✗	✗	✓	✓	✗
Data migration (format compatibility)?	✗	✗	✗	✗	✓	✓	✗
Database maker's rights (Sec. 87b German Copyright Act)?	✗	✗	✗	✗	(✓)	(✓)	✗
Know-how transfer?	✗	✗	✗	✗	✗	✗	✗

Conclusion

Some of the German rules on t&c, in particular around warranties and liability, are challenging for providers that need to rely on standardisation and scalability within their Cloud offerings. In general terms, however, providers are yet far away from offering best practice against the background of German law - which is influential on user expectations not only in the SME segment, even where the provider is contracting under foreign law.

Particular concern regards the lack of adequate documentation and transparency regarding data protection compliance - which is further accelerated where back-end operations are located outside the EU/EEA. Additional significant concerns regard the exit and the lack of transparent contractual provisions working against a “vendor lock-in”. Users are well advised to consider carefully the consequences of insufficient contractual documentation in this regard in particular.

All in all, Cloud offerings are still finding their way to the German market from a legal perspective. Providers may want to consider stepping up to a common best practice, whereas users need to pay particular attention to the pitfalls around data protection as well as regarding the exit.

Conclusion

- Licensing clauses in part not very explicit
- Warranties and liability widely incompliant with t&c law
- Conformity with t&c law poses challenges to the business model
- Data protection documentation considerably underdeveloped
- Exit terms largely underdeveloped and worrying for user’s perspective
- T&c generally to be improved - best practice yet to come

Information Technology

Bird & Bird's expertise in the field of information technology is driven by its deep industrial knowledge of business processes and innovation. Universally recognised as market leaders in the information technology sector, the Chambers Global legal directory currently ranks Bird & Bird as the leading technology law firm in Europe and Asia and amongst an elite group of four globally.

We provide the full range of legal services required by IT businesses and for IT users. Our in-depth knowledge of the IT marketplace built up through our dedication to these areas over many years means that our legal advice enhances the business and technology objectives of our customers. We are a trusted advisor to many of the most valuable tech companies in the world.

With our team of over 150 specialist IT lawyers based across our 23 international offices we advise international corporations, local businesses and public sector entities who seek consistent and high quality legal advice across Europe, Asia, and the Middle East. We are also increasingly working in emerging territories including Africa, Russia and South America.

Our highly flexible and individualised approach to providing legal solutions is driven by an in-depth understanding of our clients' strategic goals and objectives. Key areas of our IT practice include the support of strategic outsourcing and systems implementation, global and local software distribution, the support of fast growing and innovative tech companies, technology disputes, data centre developments and rationalisations.

We have a range of focus areas where we provide thought-leadership on IT-related legal developments. These include cloud services, agile development methodologies, big data, cyber and IT security, open source and open data, and software patentability.

Our clients confide in us to take advantage of pioneering, highly complex technology, in order to stay ahead against their competitors - we stand at their side by assessing the legal risks and helping to safeguard their interests.

[1] See http://www.trusted-cloud.de/de/1152.php; Note: the title of this rough line comparison has been adjusted for the purposes of this White Paper.

[2] **Amazon Web Services:** available at: http://aws.amazon.com/de/agreement/ (last downloaded 28 November 2012);
HP: available at: https://www.hpcloud.com/customer_agreement (last downloaded 28 November 2012);
IBM: available at: http://www-05.ibm.com/services/europe/de/cloud-development/contracts/Z125-8499-12_SmartCloud_Agreement_International_31Aug2012_(sign)_de.pdf (last downloaded 28 November 2012);
Microsoft: available at: http://www.microsoft.com/global/en-us/office365/RenderingAssets/mosa/MOSA2011Agr-EMEA-GER.htm and http://www.microsoftvolumelicensing.com/DocumentSearch.aspx?Mode=3&DocumentTypeId=31 (last downloaded 28 November 2012);
Oracle: available at: http://www.oracle.com/us/corporate/contracts/rightnow-csa-germany-1715203.pdf (last downloaded 28 November 2012);
SAP: available at: http://www.sap.com/corporate-en/our-company/agreements/western-europe/agreements.epx?SearchText=&SortBy=&SortOrder=ASC&Filter1=DE&Filter2=&Filter3=AGMT011&Filter4=TYP0083&page=1&pageSize=20 (last downloaded 28 November 2012).

[3] Using a computing functionality without even copying software into the user's RAM on a temporary basis remains irrelevant under copyright law; whereas any kind of copying or download of an application, client or other element of software obviously requires providing a license.

[4] Going back to a judgement of 2004 by the Federal Court of Justice on ASP contracts (case ref. XII ZR 120/04 -ASP)), the online provisioning of software for a limited period of time qualifies as a rental agreement under German law. Whereas non-transfer restrictions are enforceable within a rental context, they are not under German law of contracts, whenever a software is sold. Building on this concept, the European Court of Justice has ruled in its recent *UsedSoft* decision that the copyright-based principle of exhaustion *also* applies to selling software which is made available *via download* for an indefinite period of time (case ref. C-128/11).

[5] In regard to the current legal discussion, see the White Paper of the "Trusted Cloud": *"Datenschutzrechtliche Lösungen für Cloud Computing"* (German language version only available under http://www.trusted-cloud.de/documents/Thesenpapier_Datenschutz.pdf).

[6] Available at: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:039:0005:01:EN:HTML (last downloaded 4 December 2012).

[7] See the criticism verbalised by the working group of the German data protection authorities ("Düsseldorfer Kreis") in regard to the Safe Harbor principles: http://www.bfdi.bund.de/SharedDocs/Publikationen/Entschliessungssammlung/DuesseldorferKreis/290410_SafeHarbor.pdf;jsessionid=11EC0007B572CC0FA0CA324161B9F8C4.1_cid344?__blob=publicationFilen (last downloaded 29 November 2012).

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