

**Contract Strategy and Negotiations  
On Behalf of Cerner Corporation**

**Medical Technology Acquisition and Assessment**

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**Develop a list of 3–5 key criteria your organization needs from the software contract if it is to be a successful deal for your organization. Justify these items and explain why they are the most important to your organization.**

For Cerner Corporation to consider the software contract negotiation with Northwestern Midsize Hospital (NMH) a success, the following five key criteria have been identified as most important to Cerner:

### **1. Property Rights**

Justification: Success in the marketplace depends to a considerable extent on the ability to develop and maintain proprietary software, processes and technologies that distinguish Cerner from other companies. Protecting copyright, patent, trade secret, and all other intellectual property rights is essential. Furthermore, we cannot allow licensees or any third parties to modify our intellectual property or use our product in a manner that is not authorized under the agreement.

### **2. Limitation of Liability**

Justification: Product liability is always a concern for a business. The degree and extent of liability could be disastrous to a company. To that end, Cerner will implement exclusion clauses, limitation of liability clauses or caps on damages. This will allow both parties at the beginning of the business venture to balance risk against potential benefits, procure appropriate insurance coverage, control and predict financial exposure and, ultimately, manage their businesses in a commercially sensible way. Our intent is to use a legally vetted 'tried and tested' template that permits enforceability and successful limitations or exclusions.

### **3. Distribution and Access Modifications**

Justification: Selling license seats are analogous to unit sales in a manufacturing company. It is important that we control the distribution and receive compensation for each unit

of our intellectual property that is used. For example, our software packages usually allow a client to distribute login access to up to 25 of its employees. This means that NMH shall not make available or allow access to all or part of the Software to any third party by assignment, sublicense or any other means. NMH is not allowed to copy, adapt, reverse engineer, decompile, disassemble, or modify, in whole or in part, any of the Software or Documentation for the purpose of selling or distributing it to a third party.

#### **4. Payment Schedule Fees and Payment**

Justification: Cerner has devoted a substantial investment in its intellectual property. We have spent over \$1B dollars in R&D over the past 10 years and expect to spend another \$1B over the next 5 years (Coombs, 2006). Consequently, we need to recoup our investment at the front end of each transaction. License fees are due in 3 installments: 50% upon contract execution, 40% 60 days post contract execution and the final 10% due at Acceptance (Coombs, 2006).

#### **5. Acceptance**

Justification: Cerner Corporation provides software solutions that transform health care via eliminating errors, variance and waste for health care providers and consumers around the world. More than 9,000 facilities worldwide are licensed to use Cerner solutions. Due to the fact that Cerner is a leader in healthcare IT solutions and that our products have been validated in over 9,000 facilities worldwide, **acceptance** of the Software shall occur at NMH first operational use of the Software.

#### **What are you willing to take off the table and not pursue?**

Property rights will be taken off the table for the reasons mentioned in the justification.

### Why were other items less important?

The other items are not less important, but infringement of property rights is nonnegotiable. The other items are important for the reasons described in the justification sections.

### Do you have a BATNA (best alternative to a negotiated agreement)? What is it and why would it work?

**Table 1 - BATNA**

| <b>Criteria</b>                       | <b>BATNA</b>  | <b>Why would it work?</b>                                      |
|---------------------------------------|---|--|
| Property rights                       | Off the table   | Generally acknowledged in the Industry                         |
| Limitation of Liability (LOL)         | Limit the liability to the amount paid to Cerner under the agreement.   | Would move Cerner from the position of accepting no liability. |
| Distribution and Access modifications | Increase from 25 to 30 licensed seats – or lower the price per seat if total quantity of licenses is increased. | Offering discounts to NMH                                      |
| Payment schedule fees and payment     | Change from 50%, 40% and 10% to a modified percentage of 35%, 45% and 20%                                       | Provides NMH more of a holdback                                |
| Acceptance                            | Several points of acceptance  | Moves from automatic acceptance                                |

Table 1 depicts the BATNA and why it would work. Property rights would be taken off the table for the reasons previously discussed; it is generally accepted in the industry that this is non-negotiable unless there is some sort of software co-development agreement. The BATNA for the LOL is limited to the extent of the amount paid to Cerner under this agreement; the reason it would work is that the LOL is generally an accepted clause in software agreements. Furthermore, Cerner's willingness to compromise on liability may create a more favorable climate for the negotiation.

The distribution and access modification BATNA would be an increase from 25 to 30 licensed seats if a larger enterprise wide deal could be negotiated. The payment schedule and fees BATNA could be adjusted to reflect a percentage from 50%, 40% and 10% to a modified percentage of 35%, 45% and 20%. This may work because there is positive movement from Cerner toward a reasonable compromise. The acceptance BATNA could move from automatic acceptance to acceptance at two or more points during the implementation process (such as interface testing or component module testing) instead of one; Cerner would be showing flexibility toward NMH during the negotiation.

**Consider what push back you would get from the other side in a contract negotiation on each of your 3-5 key issues, and outline which negotiating strategy you would employ to manage each of those opposing viewpoints.**

**Table 2 – Push Back**

| <b>Criteria</b>                       | <b>Push Back</b>  | <b>Negotiation Strategy</b>                                       |
|---------------------------------------|---|---|
| Property rights                       | Little to no push back  | Don't escalate: Use power to educate                              |
| Limitation of Liability (LOL)         | Liability – no cap  | Don't escalate: Use power to educate                              |
| Distribution and Access modifications | Increase from 25 to 30 – lower based on overall quantity increase | Don't reject: reframe   |
| Payment schedule fees and payment     | Greater NMH hold back   | Don't push, build them a bridge                                   |
| Acceptance                            | Install, interface, final testing, requirements verification      | Don't react: go to the balcony<br>Don't argue: step to their side |

As shown in Table 2, Cerner would expect little to no push back for property rights. However, if our initial response was rejected, Cerner would use the opportunity to educate NMH. We would mention that Cerner has devoted a substantial investment (billions) in its intellectual property. Cerner's financial viability may become compromised if we operate in an open source fashion.

NMH is likely to react negatively to a capped liability clause. Again, Cerner will employ education to demonstrate that our liabilities contract language is consistent with standard industry practice. NMH will likely either ask for price reduction or more seats for the same price. Cerner would not reject the offer but instead reframe the issue such as offering more seats or a lower price for an enterprise wide sale.

Our payment schedule is front end oriented. NMH would likely insist on greater hold back. Cerner would build a bridge to the payment schedule that reflects an adjustment from 50%, 40% and 10% to a modified percentage of 35%, 45% and 20% if necessary. NMH is unlikely to agree to automatic acceptance and may even react negatively. Cerner would not react in kind or argue but instead collaborate to identify acceptance points that both parties can agree on.

Finally, in a practical sense, Cerner would negotiate in the context of the entire offering and not necessarily only on the criteria points mentioned in the previous sections. Cerner would identify what was most important to NMH, which may or may not be important to Cerner. Acknowledging and understanding NMH's preferences and interests potentially creates more room to offer concessions that may increase the likelihood of a "win-win" situation during the negotiation.

### **Advantages and Disadvantages of the Go to the Balcony Approach**

During service level agreement (SLA) negotiation, it is important for both Cerner and NMH to respond in a manner that will facilitate the process. Going to the balcony (remaining calm in the face of stone walling efforts, personal attacks or misleading tricks), allows individuals to check their emotions and refocus objectively on the purpose of the negotiation (Overly & Kalyvas, 2004). The primary advantage of this approach is that the removal of emotion gives negotiators the opportunity to think more clearly and constructively about the

issue at hand, thus increasing the chances of obtaining a mutually satisfactory agreement. Becoming involved in a cycle of action and reaction only makes the negotiation process more difficult and could also damage reputations as well as professional relationships. From Cerner's perspective, going to the balcony could possibly alter NMH's perception of Cerner (from aggressive and harsh to reasonable) and may lead to more productive dialogue.

However, the go to the balcony approach could have some drawbacks. Exhibiting too much emotional detachment may make the other side believe that there is a lack of interest, boredom or little preparation for the negotiation. Some people like verbal sparring, which could be their communication style and not a way to sow discord. For these individuals, going to the balcony could signal that the other side does not "speak my language" or is not really concerned about the end result, perhaps unintentionally creating psychological road blocks that can make progress more difficult.

### **Alternate Approaches for Negotiating the SLA**

One approach to negotiating the SLA is for Cerner to engage in the process with an open mind and to understand the interests of NMH. Cerner's main concern is protecting the integrity of the software and associated proprietary rights and NMH may want to alter the terms of software distribution. However, this does not mean that Cerner cannot actively listen, acknowledge NMH's competence and ideas and agree where necessary without conceding anything (also known as "stepping to their side") to facilitate the negotiation and minimize resistance (Overly & Kalyvas, 2004).

Another approach is for Cerner to thoroughly prepare for the negotiation and be ready to build a golden bridge for NMH, to draw them in a particular direction to agree, especially if no progress is being made. The golden bridge method (which may be needed during discussions



about product distribution and payment schedules) consists of: actively involving NMH in drafting or modifying specific sections of the agreement, satisfying the other side's unmet interests, finding a way for NMH to present the changes as a victory and guiding NMH across the bridge to accepting terms of the agreement (Overly & Kalyvas, 2004).

### **Operational Alternatives for the Cerner Infection Control Software Application**

The Infection Control system NMH wants to use can be delivered via different IT models. Cloud computing consists of hardware and software resources available on the Internet as managed third-party services and provide access to advanced applications and high-end networks of server computers (Mitchell, 2012). Application service providers (ASP) are third party entities that manage and distribute software based solutions to customers across a wide area network from a central data center (Webopedia, 2012). Software as a Service (SaaS) is software that the SaaS vendor develops, owns and runs on its computers where the end user can access the software over the Internet; SaaS has the following characteristics (Levinson, 2007):

- The client does not own the software but usually rents it for a monthly fee.
- SaaS is a one-size-fits-all solution; all clients use the same software and the code cannot be customized.
- Any functionality the SaaS vendor adds to software based on client feedback is available to all customers.

Although SaaS evolved from the ASP model, SaaS actually generates the economies of scale needed to offer software at a lower price, which makes it easier to upgrade customers to new versions of the software (Levinson, 2007). NMH has indicated that it is interested in a SaaS vendor that can deliver an Infection Control system. This option makes sense given that Cerner's product is delivered via SaaS and the license expressly prohibits NMH from utilizing the

Infection Control software through a third party, as described in the cloud computing and the ASP models.

### **Warranty and the SLA Negotiation**

Cerner's exclusive warranty states that the Infection Control software is provided "as is" and may not meet all of NMH's business requirements. Cerner does not claim the software adheres to state or federal laws regarding record keeping, confidentiality or compliance with hospital acquired infection prevention guidelines. Also of note, Cerner's warranty does not hold Cerner accountable for any software performance failures, errors, bugs, provision of patches, and correction of errors in updates. In addition, Cerner is not liable for the impact of Internet security breaches or Internet disruptions on software functionality, or any potential issues that may arise on NMH's computer systems from utilization of the software. The warranty strongly favors Cerner as there are no specific remedies available for NMH if the software is defective and Cerner is not responsible for any problems that arise from use of the software. NMH may want to identify and include specific software remedies as well as resolution procedures; Cerner should expect to spend some time addressing this issue during the negotiation.

### **Source Code Escrow and the SLA Negotiation**

Source code escrow allows NMH to obtain the Infection Control software code to maintain and modify the software if Cerner fails to provide support and maintenance services due to bankruptcy or terminates support of the licensed product. The Infection Control software will play a major role in NMH's efforts to eliminate and/or reduce the number of adverse events and hospital acquired infections. Software functionality is necessary to minimize the impact on patients, to facilitate provider identification of cases and to enhance provider decision making

regarding timely and effective clinical treatment. Therefore, NMH should have the opportunity to acquire the source code if Cerner goes out of business or discontinues the software product.

The terms outlined in the Cerner license agreement are standard and allow release of the source code either on a permanent or temporary basis, for reasons defined in the agreement.

Cerner narrowly defines what NMH is allowed to do upon receipt of the source code – to maintain, modify or correct the software for use within the scope of the license only. There can be no changes to the source code itself, if released from escrow, and both parties should ensure their understanding of this condition in the agreement.

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