Software Licensing vs. Software-as-a-Service ("SaaS") : The Importance of the Technology Model to Contract Drafting

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When I am first retained by a software or SaaS company, I inevitably have a conversation with my contact at the company about their technology model: what is your technology model: "SaaS" or "software license"? Nine times out of ten the client either will be unable to answer the question or will say that they are working under one technology model and send you contracts that reflect the exact opposite.

Why do I ask the question? Drafting an appropriate software contract (or even reviewing and providing feedback on a particular software contract is going to be dependent on whether or not the terms reflect the model. If either the client or the drafter are unclear on the model, then the contract is not going to be a high quality contract.

What is the distinction between a "software license" and a "SaaS agreement"?

In software contracts, perhaps the single most common issue that gets confused is the difference between a software license and a SaaS agreement. But the concepts are very different. In a software licensing model, the software company offers a physical piece of software via cd-rom or electronic download from a website to be downloaded, installed, run, and operated on a piece of hardware that is typically physically on site at a particular company or

residential location. There may be one user or multiple users of the software. The software may be installed on a single piece of hardware or multiple pieces of hardware. There may be services associated with the software that are offered to the licensee such as implementation, customization, training, maintenance, and technical support. In some cases, the company may even offer separate hosting services. However, the software itself is made available to the licensee as a tangible product.

How the SaaS Model is Different

What is different about the SaaS model? In the SaaS model, the software company generally makes no tangible software product available to its users, and the product itself is only available "on the cloud" as a hosted platform. As in the licensing model, there may be one user or multiple users of the platform. But the platform itself is only accessible through the cloud. Thus, the quality of the various services provided is critical because the ability to access and use the hosted platform is entirely dependent on the quality of the experience delivered. In the SaaS model, there is no separate maintenance service provided because that is all expected to be included as part of the hosted platform service package, along with the hosting and technical support. You may still have separate implementation, customization, and training services, however, that are made available separately from the hosted platform. The key feature of this model, though, is the very fact that you are offering a "service" model rather than a "tangible product" model.

Key Mistake SaaS Companies Make with their Contracts

What is the primary issue I see contractually? More often than not, companies say they are offering a "SaaS" model but their contract is in fact based on the software licensing model. What alerts me to this fact? Usually it's the

presence of a license grant to the software and the lack of any clauses explaining all the various services provided pursuant to the platform. It's also not uncommon to see a maintenance agreement attached to the agreement, which is not what I typically expect to see in the hosted platform model. Also, there is often a lack of attention to any of the issues or concerns that you would have in a model where you never receive a physical product, and where you have absolutely no control over data security, your ability to save or download the data on the platform, or how well you can access the platform in the first place. Another problem that you may see is a lack of concern over how you are charged for accessing the model when some sort of set up process is involved. Obviously, if you are being charged on a monthly basis for accessing a platform and a set of related services, you don't want to be charged until set-up is complete and you can access the platform and immediately use it. This is less of an issue in a licensing model where the fee is usually billed once and not charged again during the life of the product.

Why it is important to understand the difference between the two technology models?

The bottom line is that these two models are very distinct business and technology models and the contract will absolutely not be correctly set up if the appropriate technology model is not determined and/or understood in advance of drafting. The same is true in contract reviews: it is impossible to provide accurate feedback in reviewing a contract if the technology model is not thoroughly understood before the review is started. Everything starts with the technology model.

Be Prepared to Explain to Your Software Attorney Your Technology Model

So, if you retain an attorney like me to work with your software company on contracts and you are asked about your

technology model, be prepared to answer the question. Thoroughly sorting out the terms as they relate to the model is critical to the proper drafting or proper revision of your contracts, and spending billable time on this issue is time very well spent, as the job cannot be done properly otherwise.

Has your software or SaaS company been using the wrong technology model for your contracts? Schedule a consultation with us today to discuss how to update your contract to the right technology model at this link.

Distinguishing Between the Software License and the SaaS Contract

The Silicon Valley Software Law Blog looked at what the differences are between the software license and the SaaS contract models in a recent blog posting linked below:

http://www.siliconvalleysoftwarelaw.com/software-licensing-vs-software-as-a-service-saas-the-importance-of-the-technology-model-to-contract-drafting

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Good Drafting of SaaS and

Software Licenses Requires Knowledge of Technology

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There seems to be a common universal belief among many companies that there is a single form agreement circulating among software lawyers with the perfect terms that can just be cut and pasted into their agreements if they can just find the right attorney who can furnish that 'perfect' form agreement. I have lost count of the number of times I have been told by clients that they don't need anything from me other to provide said 'perfect' template. A few have even equated my or another attorney's ability to provide them with the 'perfect' form template to the level of expertise of the attorney.

Why Reliance on a Template is the Wrong Way to Draft a Software Agreement

The reality, of course, is that merely cutting and pasting from a form agreement—even a very well-written form agreement—is precisely the wrong way to draft this type of agreement. In fact, I would take this one step further and take the position that it is precisely the wrong way to draft all technology agreements. Furthermore, it is my opinion that an attorney's willingness to provide any document purported to be a 'perfect' software template is likely to be inversely correlated to his or her level of drafting experience in the space. I certainly was far more comfortable with the idea of furnishing a template in response to a client request of that nature as a very junior and inexperienced attorney than I am today, when I know better. I've seen all too well how companies may take the 'perfect' template provided and rely on it for years and years without understanding that the form required many long hours of attorney customizations and revisions before it was ever put

into use for their business.

Knowledge of the Specific Product Described in the Contract is Essential

While there absolutely are standard terms that you will find in all software agreements—whether SaaS or software licenses—which may form the basis of high quality software template for either the software license or SaaS model, a well-drafted contract is more than just an assortment of the "right" terms, it reflects the actual product offering to customers. Thus, the drafter needs to not only know and understand how to draft these contracts but also have a very high level understanding of what the product offering to customers is. Otherwise, the contract will be of a very poor quality, regardless of how good the lawyer was that put the original form agreement together that the contract may be based upon.

For example, in the enterprise license model, a company may purchase a license allowing a set number of user rights. In such a model, a well-drafted license would at least explain what constitutes a user, how users can be added and deleted, what rights the users have to the various license grants made (which should go beyond the simple 'use of the software'), the cost of purchasing new users, and the cost of purchasing the initial set of users. But the decisions on how to structure each of these terms would be entirely dependent on the business model and product offering made available by the specific software company. Thus, if the terms selected are being cut and pasted from an unrelated form agreement, it is almost certain that the terms chosen will be wrong and make no sense.

The same problem occurs with the cutting and pasting of SaaS agreements. In the enterprise model, again, you may similarly have users with different access rights, which are the SaaS equivalent to a license. Your enterprise customer may want to

start with 100 users and anticipate needing to add 100 more in a period of months. Your enterprise customer may also anticipate losing some users and want to get some sort of credit for the users lost. You may have different pricing based on when the timing of the purchase of new users. Given all these different drafting and business model choices that can be made, if the terms selected are simply being cut and pasted from an unrelated form agreement, again, it is almost certain that the resulting agreement simply will make no sense.

The structural choices in how you draft these kinds of agreements do not end with the user rights. For example, there are choices that the drafter has to make based on what type of data is being collected by the product, where the data is being stored, the level of risk to the company if the data is accessed by a third party, and what needs to happen to the data at the end of the relationship. Also, there are choices that need to be made based on whether use of the product depends on importing pre-existing data into the software and effectively reading such data. It is not uncommon for enterprise customers to have much higher requirements with respect to data than a small business client would generally have. Fees, technical support, and training are other common areas of significant variation from product to product.

A Well-Drafted Agreement Will be Structured Around the Unique Features of the Specific Product

The bottom line is that a well-crafted software license or SaaS agreement will be structured around the technology, features, functionality, and business model of the applicable product and will not be based merely on a set of “perfect” terms from any template. As a software company, that means that if you retain an attorney to advise you on your contracts, your attorney should absolutely be pushing you to provide significant details about how the technology, features, functionality, and business model of your product

work, among other issues. If you are not getting those kinds of questions from your lawyer, then it is highly likely that the terms of any contracts that your attorney reviews or drafts for you will reflect a similarly low level of understanding about those same concepts.

If you are concerned that a software license or SaaS agreement your software company is relying on has not been structured around the unique features of the specific product addressed in your contract, I invite you to reach out and schedule a consultation with me today at this link.