Arbitration vs. Litigation: Which is Better for a SaaS or Digital Health Contract?

I was recently asked by a client whether arbitration or litigation in a SaaS contract was better. The issue had been raised by an attorney on the other side of the SaaS contract negotiation, who had not only tried to persuade my client to revise the specific clause in that case, but had also provided my client the unsolicited advice that "he should prefer litigation over arbitration" in all cases.

My client, who had elected to include an arbitration clause in his standard SaaS contract terms, was unsure what to do and how to respond, and so he reached out to me for guidance.

While the debate over whether arbitration or litigation is better for a particular organization is not a dilemma specific to the SaaS industry, it is one that clients often raise with me in frustration, hoping that I can advise them that one option is definitively "better" than the other. The answer, like many things in the law, is not so black and white, and it should not be decided without considering the pros and cons of each option.

What happens when a SaaS or digital health contract includes an arbitration clause?

First of all, let's assume you have no arbitration clause in your contract and a dispute arises, then the only contractually available forum to hear the dispute will be a courtroom. If your company does not have an in-house legal department with litigators on staff, then you will need to hire a litigation support to handle the litigation process, either from the plaintiff side or the defense side. You will incur costs every time a motion is filed or defended, and you

will incur costs for discovery, depositions, mediation, and the trial preparation, all until the case is either settled or a judgment is reached. This process could take years to go through.

On the other hand, let's assume you have an arbitration clause in your contract and a dispute arises, then the contractually available forum to hear the dispute will be a courtroom. However, your opponent may not want to arbitrate the case, and so your opponent may file in court first, in which case you will have to file to compel the case to arbitration. Alternatively, your opponent may be unwilling to participate in the arbitration, so you may have to file a motion to compel your opponent participate in the arbitration. Once you win any motion in court, you will then have to initiate the arbitration with the private organization that will handle the arbitration, which will generally be AAA or JAMS in the US, but there are other organizations that handle commercial arbitration internationally. This will require you to pay the filing fees, which are often far higher than is required to initiate a case in a court. Once the case is initiated an arbitrator will be appointed to hear the case, and the parties will decide on the format for the case, and the case will proceed outside of court within the private dispute resolution process of the organization selected.

What are the advantages of arbitration in a SaaS or digital health contract?

What are the advantages? Well, arbitration is intended to be a commercial process rather than a legal process, so it is much less formal. It also can be faster, as there is no judicial backlog to slow down the process. There are fewer rules governing the process, so it often viewed as less predictable. But fewer rules also means that the process is more easily managed by business-people who are not litigators. The goal of arbitration is generally to get to a rendered decision as quickly as possible, which may be

advantageous.

How is arbitration different than the standard court path to dispute resolution?

In contrast, the court option is very formal. It can be slow, which may be a negative in some situations and a positive in other situations. And it is governed by rules and precedent, which will require knowledge and familiarity with both to proceed through. Most litigated cases settled, so the goal of litigation may not be to get to a judgment. Instead, the goal may actually be to get to a settlement.

Is arbitration cheaper than going to court to resolve the dispute?

Is one option necessarily cheaper than the other? Arbitration is generally perceived in the business world to be cheaper, due to the faster process and the relaxed rules, but because the process is a private commercial process, the fees for the administration of the case can be higher in some situations and it is still possible to incur legal fees during the process. In contrast, discovery, depositions, and motion hearings can drive up the cost of a litigation process, both in terms of legal hours billed but also in terms of other costs.

Is an arbitration award a faster path to enforcement?

It is important to recognize that getting an arbitration award may not actually be better than a mediated settlement to the party owed an award, since a voluntary settlement may be easier to enforce than a decision. On the other hand, the process is private and stays completely confidential and outside of court records, which may be preferred by both parties, and the informality may be less stressful on both sides of the dispute.

How to Decide between Dispute Resolution via Arbitration or

Litigation When Drafting?

In the end, the choice between arbitration vs. litigation is one of personal or commercial preference. You have to expect that a commercial litigator who spends his career in the courtroom is going to prefer to stay as far away from arbitration as possible. In contrast, transactional lawyers are generally going to prefer to stay as far away from litigation as possible.

I generally recommend to clients that they should contemplate the type of dispute that would arise from a particular set of contract terms before deciding how they prefer to resolve that dispute. For example, if a dispute arises, would an informal private solution to resolving the dispute be better than the formality of litigation? Will the other side have significantly more resources to apply towards the dispute? Would the other side benefit from delaying the resolution of the dispute and causing you to invest significant resources in the process? What will be the anticipated filing fees for each side in the dispute?

All in all, arbitration vs. litigation is not a decision that should be made without some careful consideration of the underlying issues and the consequences of each decision. There are valid reasons why parties gravitate to one option or the other. It is up to your business to decide what should be your organization's preferred standard with respect to a particular type of contract, and whether or not you will be willing to concede your position upon request by a particular client. You may realize that your preferred position is going to be the same in every case, or alternatively, that your position may require review on a scenario-by-scenario basis.

If you have questions regarding whether to accept or reject arbitration in a dispute resolution clause in a contract, please schedule a consultation today to discuss at https://calendly.com/prinzlawoffice.

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.