

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

Updated 6.11.24

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](#).