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# Herzog Tech Division Presents: What's Market in SaaS?

The results of a survey covering several standard legal terms used in SaaS contracts during 2023.

While companies must protect their legal rights, such as IP ownership, they also need to onboard more customers and not deter them through overly one-sided contracts. Standardization provides great advantages for the parties, mitigating negotiation back-and-forth and friction and facilitating the closing of the deal.

In our exploration of the legal landscape shaping SaaS providers and their customers, we delved into the "master services agreement", also known as "terms of use" or "terms of service" (ToS), a pivotal document outlining the legal engagements between the parties. This study scrutinizes the ToS from numerous small and medium enterprises offering SaaS, predominantly incorporated in Delaware or Israel, serving key markets in North America, the EU, and Israel. These companies span a diverse range of sectors such as cybersecurity, generative AI, business intelligen ce, and productivity solutions. Our analysis was limited to publicly-available ToS (as opposed to customer-specific purchase orders), to highlight the foundational or standard legal stipulations. Throughout this survey, we aimed to shed light on the most frequently discussed or negotiated legal terms, establishing a benchmark for what was considered standard in the SaaS industry during 2023.

**Based on our survey, our key takeaways were:**

- **Limitation of Liability.** Most SaaS ToS include a limitation of liability provision limiting the SaaS provider's liability to fees paid by the customer in the preceding 12 months before the claim.
- **Indemnification.** A significant number of companies indemnify their customers for third party claims due to IP infringement arising out of the SaaS services, while a majority of ToS include a similar obligation by the customer to indemnify the company for IP infringement claims arising out of the customer's data. In addition, most ToS we covered include indemnification obligations by customers for other matters such as breach of agreement or law.
- **Warranties and Disclaimers.** Almost all companies we covered included standard disclaimers in the ToS, such as lack of promises regarding product quality, absence of defects or issues arising from improper use of the software, and disclaimers on the warranties of merchantability or fitness for purpose.
- **Modifications.** Most vendors may modify their ToS unilaterally, and for most it is sufficient to post notice of such change on their website to make it effective.
- **Output Ownership.** Almost all generative AI companies we covered provide ownership in their output to the customer, to the least as between the SaaS provider and the customer.

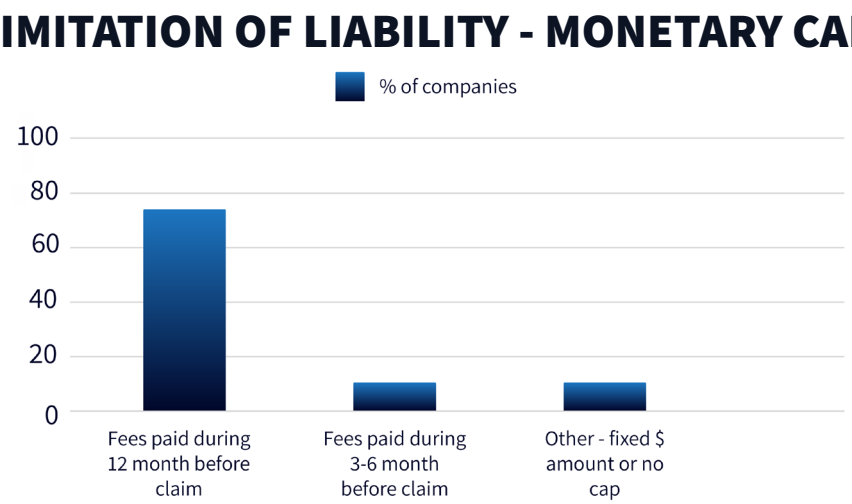
The full results of our survey are available below.

In summary, our survey identified several standard or common terms for SaaS ToS. We should note, however, that these standards or trends only represent those specific ToS we reviewed and may vary on a case-by-case basis, especially for larger, multinational SaaS providers or in case of large enterprise customers with negotiation leverage. If you have any questions on SaaS and other forms of cloud contracts, feel free to reach out to us at the emails set forth at the bottom of the survey.

# OUR FULL SURVEY

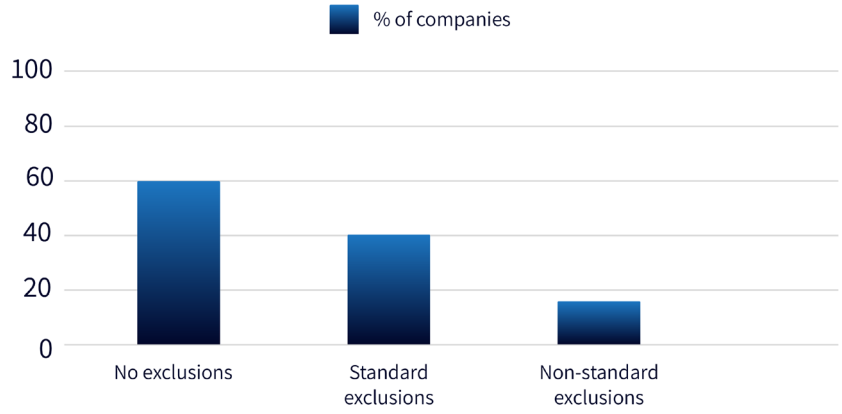
## LIMITATION LIABILITY AND EXCLUSIONS

With more deals, comes more potential exposure. To limit their legal exposure for claims, SaaS providers nearly always outright exclude certain categories of damages in the ToS (such as indirect damages, loss of data/ profits and system errors), for both parties, and set a monetary cap on the SaaS provider's own liability. According to our survey, the most common (around 75%) monetary cap on the SaaS provider's liability were the total fees paid by the customer in the 12 months preceding the claim, with the rest being evenly divided between a 3-6 months' cap, a fixed $ amount (often in the case of freemiums) or, much more rarely, no cap at all.




There are, however, certain causes for damages which are sometimes excluded from the SaaS provider's monetary liability cap, in some cases being subject to an increased "super-cap" of 3-5 times the fees paid by the customer in the 12 months preceding the claim. The standard limitation of liability exclusions are damages due to fraud, willful breach, gross negligence, third party IP claims (which might have their own indemnification provisions – see below) and breach of confidentiality. Other, less-standard exclusions, sometimes requested by large enterprise customers during negotiation, include death and bodily injury (which are generally irrelevant for SaaS), breach of law, breach of platform use restrictions (in cases where the liability limitation also applies to customers) and breach of the SaaS provider's data security or privacy obligations. Per our survey, around 60% of companies had no limitation of liability exclusions at all in the standard ToS, while 40% had all or some of the standard exclusions. Around 16% of companies also had non-standard exclusions in the ToS in addition to the standard ones.

# LIMITATION OF LIABILITY - MONETARY CAP

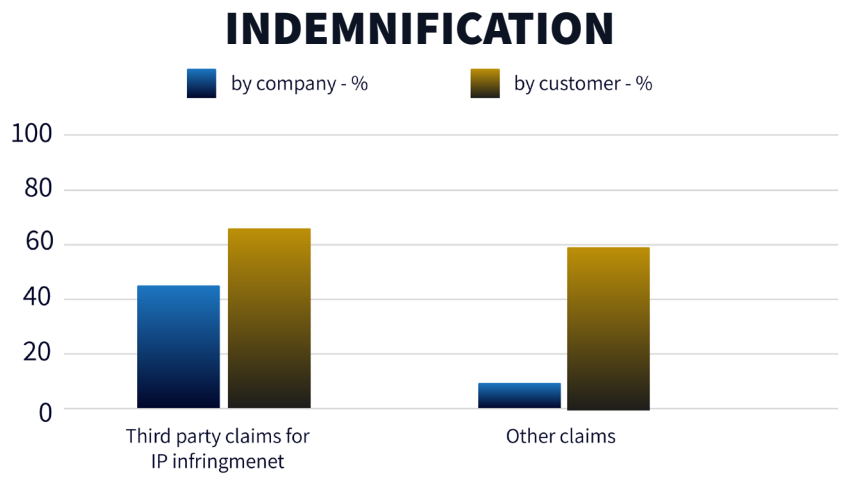




# INDEMNIFICATION

Similar to the limitation of liability, indemnification is another heavily negotiated provision in SaaS ToS. While liability deals with the legal responsibility for damages, indemnification is an obligation – regardless of the legal "fault" – to cover the losses and expenses arising from certain circumstances, often due to claims by third parties which are not parties to the ToS. The indemnification can be from the SaaS provider to the customer – or the other way around - with the most common cause being losses, fees and expenses arising from third party claiming customer had infringed their intellectual property rights due to its use of the SaaS provider's SaaS platform. The indemnification amount is most often uncapped, although sometimes – depending on negotiation power - it is subject either to the limitation of liability or to its own "super-cap" amount.

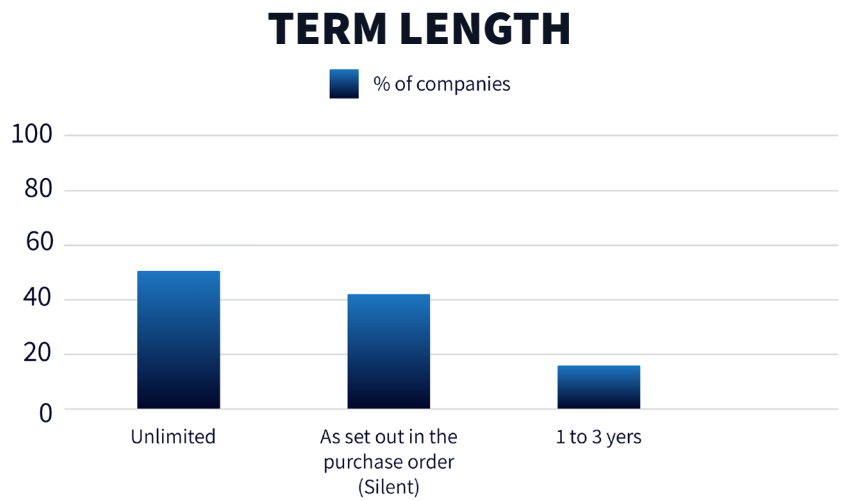
From our survey, around 44% of companies obligate to indemnify their customers for intellectual property-related claims by third parties, while 63% of the ToS include indemnification by the customers towards the SaaS providers if the customer content uploaded or processed through the platform infringes third parties' intellectual property. In addition, 9% of the ToS include indemnification by the SaaS provider for other claims such as those arising out of the SaaS provider's fraud or negligence or violation of law, and 59% include indemnification by the customer for claims arising due to customer's use of the services, breach of use restrictions, unauthorized use or breaches of law.





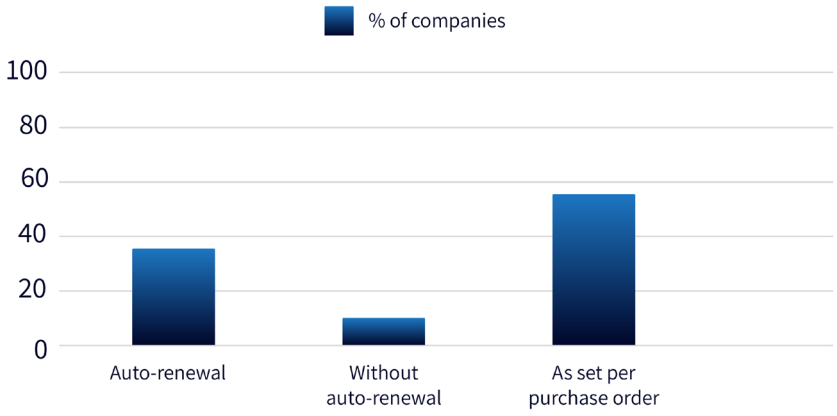
# TERM AND TERMINATION

The term and termination provisions of the ToS specify the duration of the contract, including any provisions for automatic renewal. In the context of the conducted survey, it was observed that 50% of the companies opt to determine the duration of contractual agreements through specific purchase orders or choose not to address this aspect explicitly. Meanwhile, approximately 41% of the companies favor an open-ended agreement structure, accompanied by provisions that allow for termination rights. Contrastingly, a smaller proportion, around 16%, explicitly restrict the agreement term to a period ranging between one to three years.




As for automatic renewal, according to our survey, a majority of 56% of companies incorporate automatic renewal clauses for contract terms in customer-specific purchase orders outside the standard ToS. In contrast, approximately 44% of the companies include provisions for automatic renewal of the contract term within the ToS. Notably, a smaller segment, constituting of around 9%, does not offer the option for automatic renewal at all as a standard.

## AUTO-RENEWAL

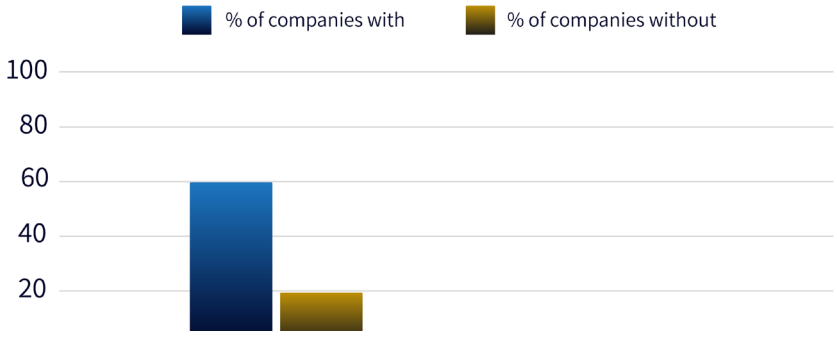



The termination provision outlines the circumstances under which the engagement under the ToS can be terminated by either party. It also describes the obligations and rights of both parties upon termination, such as data return or destruction, settlement of outstanding payments, and the treatment of confidential information, ensuring clarity and predictability and helping both parties understand their commitments and the consequences of ending the agreement.

One key term is termination for convenience, where either party can end the agreement for any or without reason, as opposed to termination for cause or due to breach of contract. Per our survey, around 59% of the companies grant a mutual right for both parties to terminate the agreement for convenience. On the other hand, about 19% of companies we covered do not extend this right within the ToS, while others are silent.

We should note that while termination for convenience may be included in ToS, whether this also entitles a refund if done by the customer is often heavily negotiated and usually appears in different ToS sections or in documents such as the purchase order, not covered by this survey.

## TERMINATION FOR CONVENIENCE

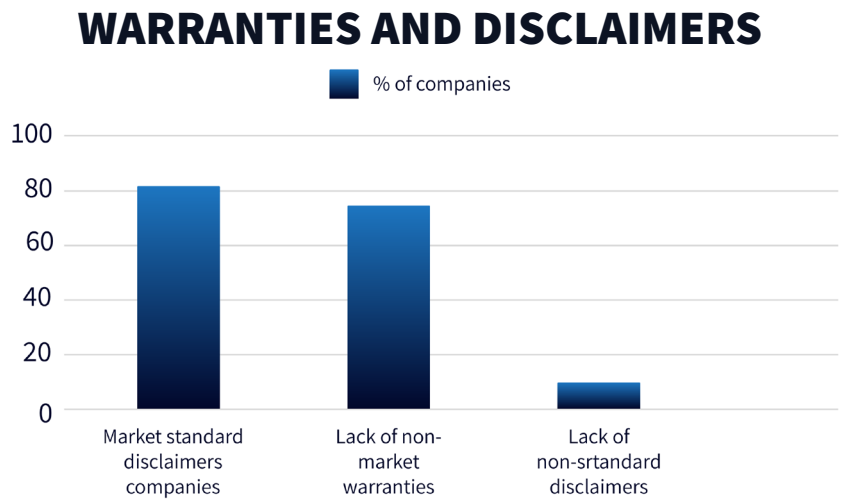




# WARRANTIES AND DISCLAIMERS

In SaaS ToS, the disclaimers and warranties section is essential to outline the SaaS provider's assurances and limitations regarding the software. This section typically either disclaims all warranties or includes minimal warranties affirming the software's conformity to product specifications (if any). Concurrently, it incorporates disclaimers to limit the SaaS provider's responsibility and not make promises regarding the product quality, absence of defects or issues arising from improper use of the software. Such standard disclaimers include, for example, a disclaimer on the warranty of merchantability or fitness for a particular purpose (and sometimes non-infringement) and a specific disclaimer stating the platform use won't be error-free or without interruption. For generative AI, it is also common to see disclaimers regarding output accuracy, completeness or non-infringement. This dual approach seeks to establish a balance between guaranteeing a basic level of service quality and protecting the SaaS provider from extensive liability or reliance by the customer. It's a critical component in managing expectations and defining the scope of responsibility for both parties involved.

Our survey results indicate a unanimous 100% of companies incorporating market standard disclaimers in their ToS. Furthermore, a significant majority, approximately 81%, refrain from including any warranties that are considered unusual or non-standard in the market (which may include a warranty of legal compliance, non-infringement or maintenance of privacy and data security). Additionally, 75% of the companies do not incorporate any unusual disclaimers beyond the standard warranty exclusions.

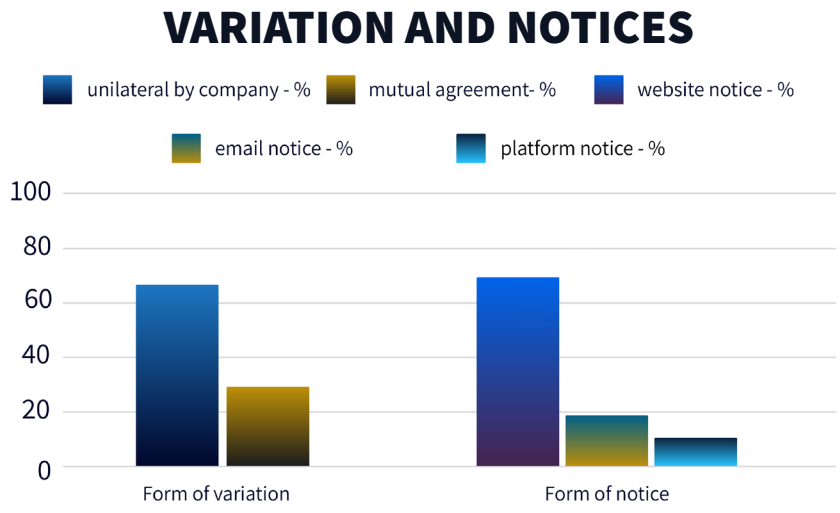




# VARIATION AND NOTICES

A variation or modification clause allows a SaaS provider to unilaterally modify the ToS, with the customer consenting to these modified terms through its continued use of the platform or terminating its use. The customer is typically notified of the changes via an upload of the updated ToS to the SaaS provider's website or an in-platform notification, placing the burden of checking for ToS updates on the customer. The ability to unilaterally modify the ToS is important for SaaS providers with a large number of customers (especially if B2C), because it will be impracticable to negotiate changes with each customer separately. However, for SaaS providers with enterprise clients who engage them via purchase orders, changes – or at least material ones - are often subject to both parties' consent.

Per our survey, where the ToS were not silent, 62.5% of ToS could be modified unilaterally by the SaaS provider, while 25% required both parties' written consent. Re: form of notice, 66% of the ToS stated that a notice on the website (and continued use) are sufficient for modification, while 19% and 9% of the ToS (respectively, including some companies providing both) also provided for an email or in-platform notification (often where the change was to fees or was otherwise adverse).



# SERVICE LEVEL AGREEMENT (SLA)

A Service Level Agreement (SLA) is a contract between the SaaS provider and the customer that clearly defines the performance and quality standards expected from the product, through metrics such as uptime guarantees and response time for support requests, graded by severity level. While product performance is often excluded under the limitation of liability and disclaimer of warranties, the SLA provides a framework for product accountability and includes specific remedies, with the most common being service credits.

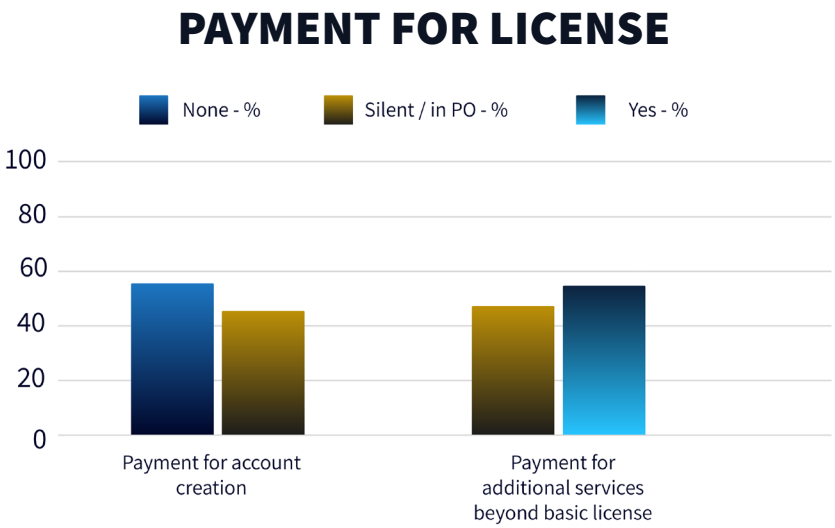
Per our survey, we found that 32% of the ToS referred to the SaaS provider's SLA. Note that this doesn't mean that other SaaS providers don't have an SLA – in some cases, it is only offered to paying/enterprise customers, while for others, the typical metrics of uptime/response time are unfit due to the type of software provided.



# SCOPE OF SERVICE

The service scope section is crucial as it outlines the rights and limitations of the platform's usage. This includes detailing user access rights, specifying the included service features, and distinguishing them from advanced features available at additional costs. It also addresses the extent of allowable software modification, customization, and sub-lease rights, alongside stipulating compliance obligations and auditing rights of the SaaS provider. This section essentially sets the boundaries for software usage, ensuring clear understanding of the service scope and safeguarding the SaaS provider's intellectual property.

According to the insights obtained from our survey, around 56% of companies do not require a payment at the time of account creation on the platform. Conversely, about 44% of the companies either do not address this issue explicitly or specify the payment terms within a customer-specific purchase order. In addition, roughly 53% of companies request payment for additional services provided by the SaaS provider. Meanwhile, about 44% of companies either do not explicitly mention this aspect or delineate the terms for such payments within specific purchase orders.




# OUTPUT OWNERSHIP (GENERATIVE AI)

In the ToS of generative AI companies, the Output Ownership section is crucial to define who owns the content created by the AI model. This part of the ToS needs to address the complex intellectual property issues unique to AI-generated outputs. It should clearly state whether the user, the SaaS provider, or both have ownership rights over the AI-generated output. This includes stipulations on usage, distribution, and potential commercial rights. Given the innovative nature of generative AI, this section is key in preemptively addressing potential legal complexities and ensuring both parties have a mutual understanding of their rights regarding AI-created content.

Based on the findings of our survey, nearly all companies operating in the generative AI sector include clauses regarding output ownership in their agreements. Predominantly, these clauses stipulate that the customer has ownership of the generated output, to the least between it and the SaaS provider (given that machine-generated output may not be protected under IP laws).

**If you have any questions, feel free to reach out to us:**

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