



# CIO's Guide

## to Software-as-a-Service:

*A Primer for Understanding and Maximizing  
the Value of SaaS Solutions*



## What is Software-as-a-Service (SaaS)?

SaaS is a software deployment model in which an enterprise application is delivered and managed as a service by the vendor to meet the needs of multiple customers simultaneously. A widely used example is the service model used by ADP to provide payroll and other business services to multiple organizations.

SaaS solutions are delivered via a network, most often the Web. They are priced on a subscription service basis, often based on the number of users or seats.

This SaaS model shifts the burden of getting and keeping an enterprise application up and running from the customer to the vendor. It permits users to leverage the software functionality without the burden of deploying and managing the software themselves. It also eliminates the added costs and complexities of deploying additional hardware and software, or dedicating additional staff resources to support the enterprise application on an ongoing basis.

The SaaS model also enables every customer to benefit from the vendor's latest technological features without the disruptions and costs associated with software updates and upgrades.

## What business trends are fueling the growth of SaaS?

A combination of macro-trends are driving companies of all sizes to consider SaaS alternatives to traditional, on-premise software applications to better achieve their corporate objectives. These market trends include,

- Changing competitive forces
- Changing workplace requirements
- Changing economic and ecological conditions

### Changing Competitive Forces

Globalization and eCommerce have fundamentally changed the competitive landscape, leveling the playing field while lowering the barriers to entry in nearly every industry. While these trends have created new market opportunities, they have also opened the door to more competition and undercut customer loyalty.

### Changing Workplace Requirements

Mobile technology and broadband networking have also fundamentally changed the workplace, and created new technical challenges for businesses. Not only are today's employees more comfortable leveraging technology to do their work, but the next generation of employees who have grown up in an on-demand culture will expect their employers to offer an even wider array of web-based services to enable them to perform their jobs effectively.

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### Changing Economic and Ecological Conditions

Deepening recession and escalating fuel costs are significantly affecting corporate operating budgets, forcing businesses to re-evaluate where they make their capital investments and how they can allocate their limited resources to have the greatest impact on their financial performance with the lowest environmental impact.

## What is wrong with legacy, on-premise applications?

In many cases, legacy enterprise applications have proven to be too expensive to acquire, deploy, update and maintain. They also lack many of the features and functional capabilities which are essential in today's rapidly changing business environment.

According to industry research, 31.1% of software projects are cancelled before they are completed. Of those software projects which have been completed, over half (52.7%) have taken twice as long or have cost twice as much as originally expected.

When on-premise software applications are fully deployed, the maintenance and management costs can be ten times the original license fee, according to AMR Research. AMR has also found that many organizations over-provision their software license in anticipation of future software usage that never materializes.

In addition, legacy enterprise applications were designed to sit within a highly centralized and static corporate environment. These applications were not structured to be easily accessed in a secure way by a highly dispersed and variable workforce.

## How widely adopted are SaaS applications?

In many cases, on-premise applications often fail to produce the return on investment (ROI) that organizations expect, and they typically require a higher total cost of ownership (TCO) to keep them up and running. As a result, many companies are adopting SaaS applications as a way to avoid the up-front capital investments and risks, along with the ongoing costs and limited returns of legacy on-premise applications.

In an increasingly challenging competitive and economic environment, corporate end-users and executives are becoming more receptive to a widening array of SaaS solutions to address their business needs.

Over the past three years, THINKstrategies has seen a steady increase in customer interest and adoption of on-demand SaaS solutions. Our most recent survey of over 100 companies conducted in October 2008, in conjunction with Cutter Consortium, found 63% of the companies had adopted a SaaS solution, nearly double the percentage in 2007! (Figure 1.)

Our survey also found over 90% of those already using a SaaS solution are satisfied with the quality of the solution, plan to expand their use of SaaS and would recommend a SaaS solution to their peers.

## What are the most important benefits of SaaS?

The key benefits of SaaS are:

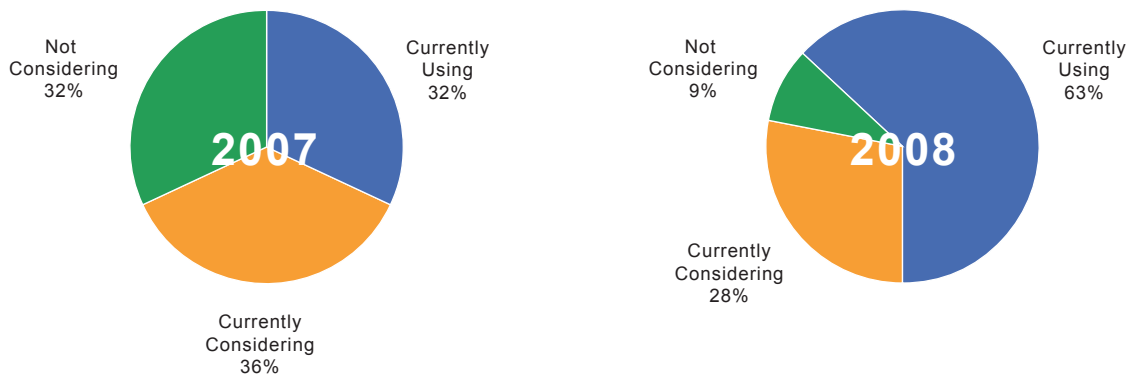
- Accelerated software deployment with less risk.
- Lower up-front costs.
- No additional hardware and lower internal staffing requirements.
- Greater reliability, security and privacy.
- Higher productivity/ROI, at a lower total cost of ownership (TCO).
- Greater agility to scale software to meet changing business requirements.
- Quicker time to value.

As a result of these benefits, Gartner predicts the SaaS market will grow at a compound annual growth rate (CAGR) of 22.1% through 2011, twice the rate of the overall enterprise software market<sup>1</sup>.

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<sup>1</sup>Gartner/Dataquest Insight: "SaaS Demand Set to Outpace Enterprise Application Software Market Growth", 08/03/07.

Figure 1: Percent of Companies Using or Considering SaaS



Source: THINKstrategies/Cutter Consortium 2008

## How does SaaS differ from the previous generation of Application Service Providers (ASPs)?

ASPs differ significantly from SaaS. Under the ASP model—also referred to as “managed application services” or “hosted applications”—the service provider is simply reselling and housing a traditional, on-premise application in its facilities to relieve the customer of the ongoing operational requirements.

Although the ASP model relieves the customer of the operating responsibility, it doesn’t eliminate the up-front costs, extended deployment cycles and remote accessibility issues related to legacy applications. The customer still must acquire an up-front perpetual license for the software, pay for the additional servers and systems to support the application, and acquire an appropriate maintenance agreement. The ASP managed application is still unable to accommodate the remote access needs of a dispersed workforce or fully leverage the other important attributes of the Web.

In addition, the ASP has to manage multiple versions of various software packages, each of which has been customized to meet the needs of individual corporate customers. This creates tremendous operational challenges for the ASP which can result in significant support issues for customers.

It is for these reasons that most of the ASPs founded during the dot.com era failed and disappeared, and those traditional enterprise software vendors offering an ASP model are having difficulty. This old model simply doesn’t satisfy the business needs of corporate customers.

By contrast, the SaaS model enables the application vendor to develop, deliver and manage its solutions in a more economical and scalable fashion to meet the needs of its customers. Although there is a tradeoff in the amount of customization which is permitted, the SaaS model enables the vendor to achieve greater service reliability and security levels by supporting a standard software version in a more efficient and dependable manner.

SaaS solutions enable customers to quickly and easily acquire essential business applications without a significant up-front capital investment in perpetual software licenses and additional hardware systems. They also avoid extended deployment cycles and added consulting and support costs. SaaS solutions have also been specifically designed to be more flexible and accessible for a highly dispersed and variable workforce than legacy applications.

Figure 2 lists the key differences between the old ASP and new SaaS models

THINKstrategies’ survey research has found that over 90% of those organizations already using a SaaS solution are satisfied with the quality of the solution, plan to expand their use of SaaS and would recommend a SaaS solution to their peers.

In response to this track record of success, 76% of companies using SaaS applications plan to expand their use of SaaS, according to Burton Group and Ziff Davis Enterprise Research (Source: “Software as a Service”, Baseline, July 2008).

Figure 2: ASPs vs. SaaS

ASP Attributes	SaaS Attributes
Resold legacy applications	New net-native applications
Retained perpetual licenses	Subscription model
Difficult to Upgrade	New functionality delivered regularly
Customized	Configurable

## Is there a minimum subscription term?

While certain SaaS products, typically those used for a limited population or focused on a narrow application, permit users to subscribe on a 'pay-as-you-go' basis, every SaaS solution provider delivering an application designed for broad deployment across a large enterprise requires a minimum subscription commitment. Depending on the application, this minimum commitment is typically three to five years, which is paid one year at a time in advance. This is required because of the high level of up-front investment which the SaaS vendor must make in facilities and service delivery capabilities to properly support enterprise customers.

THINKstrategies has found, in fact, an increasing number of enterprise business decision-makers and procurement officers prefer to make a commitment longer than the minimum required term in order to simplify the contracting process and gain the price advantage of a multi-year agreement.

## When do I begin payment—upon activation of my service or usage?

Unlike traditional on-premise software applications which require extended deployment cycles and considerable end-user testing, SaaS solutions have already been tested by a broad cross-section of customers to ensure that they work well and can satisfy a wide range of corporate requirements. The SaaS solution provider has already made a significant up-front investment to ensure that an application is ready for activation. As a result, most SaaS applications require payment upon activation.

As a result of this standard practice, enterprise customers typically set a timetable for rolling out the solution to their employees fairly rapidly after signing SaaS agreements. This allows them to quickly gain the business benefits of utilizing the SaaS solution. Though this model of paying upon activation is new to corporations that are accustomed to long rollout cycles with traditional, on-premise applications, research indicates that customers are pleasantly surprised by the rapid deployment capabilities of SaaS solutions.

## How does a SaaS provider assure the reliability, security and privacy of its services?

Unlike the traditional, on-premise software product business which put the burden of success on the customer, the SaaS subscription service model places the onus on SaaS vendors to deliver reliable and secure services which meet the needs of their customers.

*Leading SaaS vendors invest in state-of-the-industry service delivery and security technologies and certifications programs.*

SaaS vendors' business depends on delivering quality services and safeguarding their customers' valuable data. As a result, leading SaaS vendors invest in state-of-the-industry service delivery and security technologies and certifications programs.

The certification programs include SAS 70, ISO standards, and Payment Card Identification (PCI) which require the SaaS providers to implement extensive and well-documented security practices that govern their data center operations and personnel. These facilities and staff are routinely tested on a regular basis.

Despite common concerns about privacy issues, there are no documented cases of data encroachment within a SaaS environment even as the number of identity theft and other security infractions within traditional software operations continues to skyrocket.

Many businesses also view the off-site hosting of their data by SaaS vendors as an added disaster recovery/ business continuity benefit.

## Who owns my data?

Under standard SaaS agreements, the customer retains ownership of its corporate data in a SaaS solution and is able to recover this data when the service agreement comes to an end. The specific terms and conditions for the safeguarding and recovery of the data should be clearly described in the SaaS agreement.

## Can I customize my SaaS solutions or request a modified Service Level Agreement (SLAs)?

All of the leading SaaS vendors have crafted their solutions, SLAs and hosting policies to meet the needs of the vast majority of their customers at a reasonable price. These customers have come to the realization that many of their enterprise applications, such as CRM, expense management or talent management, are driven by a set of business requirements which are common to most companies.

THINKstrategies' research and consulting work has found that over 90% of SaaS customers have been satisfied with their SaaS solutions and have renewed and/or expanded their service agreements, and are willing to serve as reference accounts. These figures far exceed satisfaction, renewal and referral rates for traditional, on-premise software products.

However, many SaaS vendors also recognize that their standard solutions can't satisfy every corporate requirement. Therefore, leading SaaS vendors are increasingly designing their solutions so they can be configured to meet a growing number of specific business needs within the boundaries of their standard solution architecture.

Many SaaS vendors are also willing to make certain exceptions to their standard terms. For example, they might accommodate the needs of government contractors or financial services firms to limit the transfer of data to offshore locations. Of course, these special arrangements will come at a premium price because it imposes additional operating costs on the SaaS vendor.

## Under what circumstances can I terminate my subscription?

Because the SaaS vendor must commit significant technical and staff resources when a new agreement is signed to meet the needs of each customer, most SaaS agreements place significant limitations on the right of customers to terminate their agreements simply for convenience.

However, the customer can terminate for cause. Grounds for termination can exist if the SaaS vendor fails to deliver the solution as agreed in the contract. In addition, SaaS vendors may have a responsibility to pay penalties or to allow termination for failure to meet the service reliability, security or privacy requirements stipulated in their SLAs.

Under standard SaaS agreements, in the unlikely event that a SaaS vendor fails to meet their contractual obligations, the customer often has the right to seek penalties or terminate the service and reclaim their corporate data within the parameters established in their SLAs.

## Can I modify my subscription level if my employee base changes?

A key advantage of the SaaS model over traditional, legacy, on-premise applications is the scalability and flexibility of these services to meet customers' changing business requirements.

However, most SaaS providers delivering enterprise applications require that the number of end-users supported in a customer agreement remain at a fixed minimum level for the initial term of the contract. This allows the SaaS provider to commit the right level of resources to meet the agreed upon customer needs.

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Nonetheless, most SaaS agreements also include specific notification procedures and timelines to ensure that customers can modify their usage levels at the end of each subscription term. This gives their SaaS vendor adequate time to augment their service delivery capabilities to accommodate more end-users and higher usage levels, or scale back its operations to respond to customer requests for service reductions.

## Summary and Conclusions

SaaS is gaining widespread corporate acceptance and adoption because it overcomes many of the inadequacies of traditional, legacy, on-premise software products and “hosted” or “managed” applications.

SaaS shifts the burden of successful deployment and management from the customer to the vendor. It eliminates the need for additional hardware and staff. It accelerates the time to value and increases user productivity by increasing application reliability and security.

Although adopting SaaS solutions may mean that some corporate users have to curtail the level of customization they can demand, THINKstrategies has found that the vast majority of companies have gained business benefits which far out-weigh this limitation. These benefits include:

- Quicker time to value
- Lower cost of ownership
- Higher return on investment
- Greater scalability and agility

In an era when competitive, customer and compliance pressures are escalating, a growing number of enterprises are recognizing that SaaS represents a more economical and effective approach to obtaining and leveraging state-of-the-industry business applications.

### About THINKstrategies, Inc.

THINKstrategies is a strategic consulting services company formed specifically to address the unprecedented business challenges facing IT managers, solutions providers, and investors today as the technology industry shifts toward a services orientation. The company’s mission is to help our clients re-THINK their corporate strategies, and refocus their limited resources to achieve their business objectives. THINKstrategies has also founded the Software-as-a-Service Showplace ([www.saas-showplace.com](http://www.saas-showplace.com)), an easy-to-use, online directory and resource center of over 3000 SaaS solutions from over 700 companies worldwide, organized into over 80 Application, Industry and Enabling Technology categories. The Showplace also includes information and insights regarding industry best practices. For more information regarding our unique services, visit [www.thinkstrategies.com](http://www.thinkstrategies.com), or contact us at [info@thinkstrategies.com](mailto:info@thinkstrategies.com).