

Software License Compliance Management: Optimizing Software Revenue and Customer Satisfaction



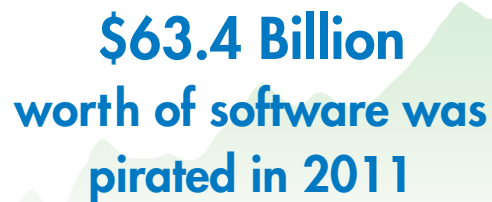
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Why Software License Compliance Management Matters?

Research firm IDC pegs the global packaged software market at \$325 billion in 2011. At the same time, the 2011 BSA Global Software Piracy Study finds well over half of the world's personal computer users—57 percent—admit they pirate software. In fact, the commercial value of pirated software climbed from \$58.8 billion in 2010 to \$63.4 billion in 2011, propelled by shipments to emerging economies where piracy rates are the highest. Clearly application producers have a lot at stake when it comes to software license compliance management.

Successful business relationships depend on trust between buyers and sellers. However, the software industry has historically struggled with trust as it relates to the exchange of fair value. Many companies find themselves with unintentional overuse despite their desires and best intentions to avoid it. Regardless of the reason, piracy or unintentional overuse of software costs application producers billions of dollars annually. It's also a problem for corporate users who need to comply with contract terms as a matter of business ethics and compliance with corporate governance guidelines. Ultimately, any disparity between authorized use and actual use undermines the trust between buyer and seller.

Selling software is not like selling hard goods—especially when it comes to the sale of enterprise applications into large corporate accounts. Application producers provide the customer with an application based on an understanding of how the customer will be entitled to use that product across the organization. Application producers typically enforce how the product will be used with a licensing model that protects and monetizes



\$63.4 Billion
worth of software was
pirated in 2011

their IP. Over time and depending on the markets and segments the producer serves, the producer may adapt a different licensing model based on changing customer needs or they may choose to adopt multiple licensing models. These dynamics make getting compliance management right very difficult. Those companies that get compliance management right are able to optimize revenues while delivering an even better experience to their customers. And those that don't, risk losing revenue and alienating their customers in the process.

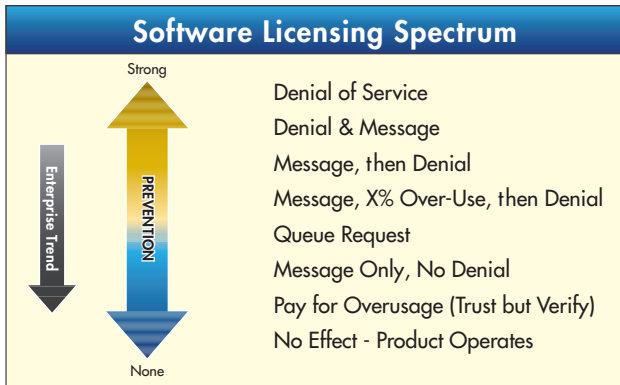
Throughout this whitepaper we will examine the pros and cons of traditional compliance management approaches, the impact technology has on compliance management, the increasing complexity of software licensing models, and the growing trend towards trust—but verify compliance management approaches, including:

- Automating compliance management
- Enabling pay-for-burst and pay-for-use

And lastly the paper looks at revenue, trust and the customer relationship and how Flexera Software addresses the software license compliance management needs of application producers.

Pros and Cons of Traditional Compliance Management Approaches

Compliance management approaches vary greatly from producer to producer and, frequently, from product to product within the same producer. While the industry has gravitated to some common approaches there are diverse options available.



Strict Enforcement – Some companies have implemented a licensing approach of strict enforcement. Under this approach, entitlements are enforced by licensing mechanisms that may either completely disallow access to software when usage exceeds licenses or only allow some limited amount of “overdraft” leeway. This approach provides a high degree of confidence for the producer. It may, however, inconvenience the customer if there is an immediate and legitimate business need for exceeding the license. While strict enforcement will force customers to stay within their license limits, there are situations where it is actually to the producer’s advantage to have them exceed those limits (either temporarily or on an ongoing basis) – so that the producer can realize additional revenue from the additional use.

65%
of organizations
were audited in 2011
- Source Gartner

Software Audit Only – Another common compliance approach is the software audit. The software audit only approach (an approach where producer has chosen not to use any enforcement mechanisms in their products) removes the barriers to software use by making it easy for customers to broadly use the software throughout their business. Under this software audit only approach, the producer undertakes a direct examination of the customer’s use.

This is often accomplished by dispatching either producer or third-party staff to the customer’s site to retrieve usage data captured by some sort of monitoring or usage capture mechanism installed on the customer’s systems and/or to observe usage in real time over a period of time. This approach has the advantage of allowing both producer and customer to discover any use of the software in excess of contract terms, so that fair additional compensation can be paid to the producer, if appropriate. There are many disadvantages to this approach, including:

- Cost of maintaining and dispatching audit teams
- Difficulty auditing the entire organization so producers often audit one location at a time and apply the discovery to the rest of the organization—which is often incorrect
- Audits get settled for pennies on the dollar
- Inability for most producers to audit many of their customers. In fact, most only audit 1-2% of their customers
- Customers perceive an audit as invasive and adversarial

Enterprise (All-You-Can-Eat) License Agreement –

Many large companies have long preferred enterprise (all-you-can-eat) license agreements. Under this approach, the producer provides software to the customer without stipulating specific restrictions on use (may include very limited or no enforced licensing) – although certain limits and conditions may be incorporated into the contract to protect the producer from contingencies such as mergers or acquisitions. The advantage of this approach is that it eliminates the need to monitor specific use parameters and address unanticipated fluctuations in those parameters. The primary disadvantage of this approach is that it may not reflect fair value. For the producer, this may mean loss of potential revenue. For the customer, it may mean investing time in completely a true up and possibly paying for more software than is actually being used – which can result in rapid erosion of the business relationship with the producer.

There are pros and cons to traditional compliance management approaches. Each approach may be appropriate under specific conditions but none of them are perfect for all situations. In some cases, for example, an audit may be too costly and/or intrusive. In other cases – such as when spikes in business activity give customers a legitimate reason for temporarily exceeding software license parameters – rigid enforcement mechanisms may be counter-productive and disruptive. As a result, we are seeing a growing trend to towards compliance management solutions that offer trust but verify approaches.

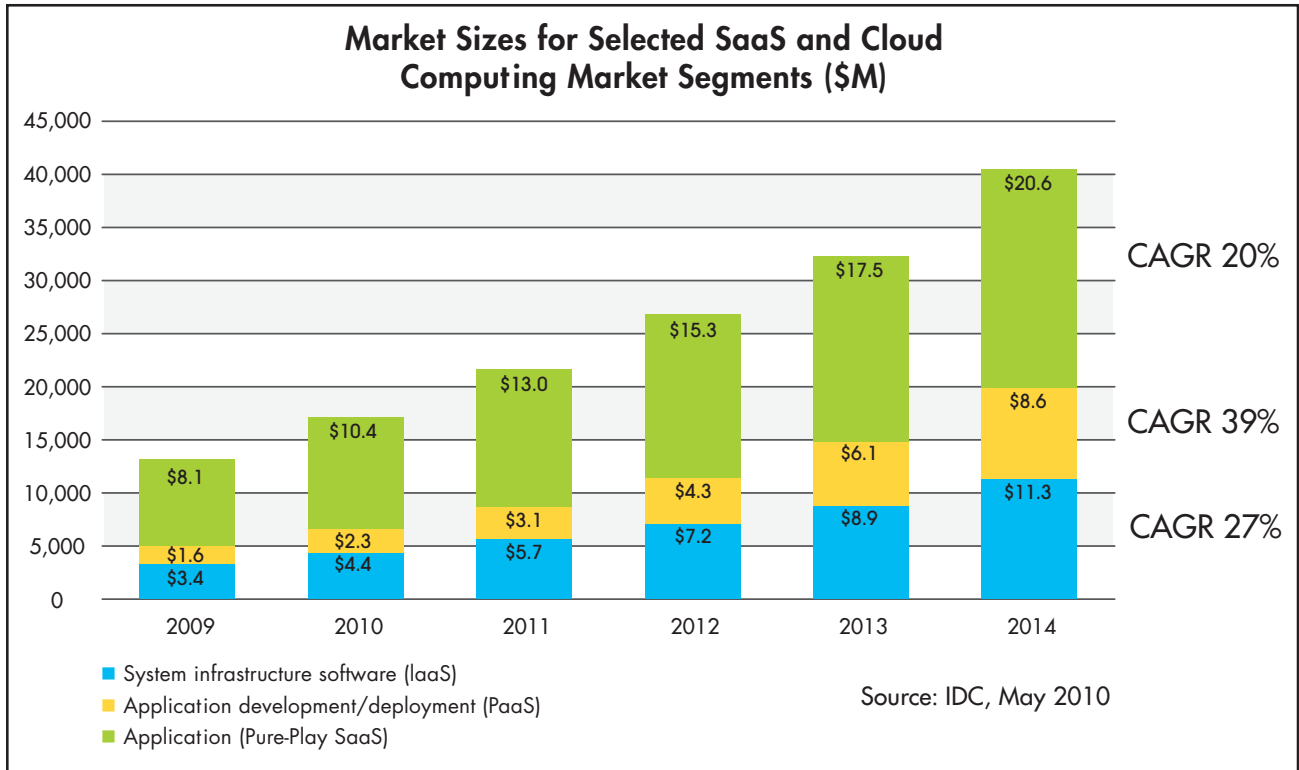
Impact of Technology on Compliance Management

The cloud offers substantial economic and operational advantages to enterprise IT – most notably the ability to quickly add and subtract service capacity as dictated by

changing business needs. These advantages are at least partially offset by the new management challenges that arise when resources can dynamically appear, multiply, migrate and disappear and cause software licensing compliance issues. The nature of entitlements governing application usage rights also change as software residing in public and private clouds is accessed from a broader range of devices that may or may not be owned by IT.

Rapid IT adoption of virtualization technologies has outpaced the business' understanding of software license

compliance implications of virtualizing desktops and the datacenter. Virtualization dramatically increases the likelihood that servers running licensed software will be replicated, regardless of whether or not that replication falls within licensing rights. As IT transfers workloads to managed service providers, questions arise as to who is responsible for which licenses and/or whether IT ought to pay the managed service provider a second time for entitlements that are already covered on its existing license.



And finally, the shift from perpetual to subscription and trust but verify licensing models points to the fact that enterprise IT need and want to:

- Pay for only what they use, reduce shelf-ware
- Stop disruptive software audits
- Stay in compliance
- Ramp departments up and down based on project needs
- Optimize software spend
- Purchase software how they buy in their personal lives
- Simplify the licensing experience

Ultimately, the licensing approach chosen by a producer is a function of corporate philosophy, product price point,

target markets (including geographical issues), nature of the product (i.e., a defense application will inevitably have a different licensing strategy than a user productivity application), competitive pressures, customer expectations and demands and many other factors. The bottom line is that there is no simple or singular answer for any company or product.

The Increasing Complexity of Software Licensing

As producers adapt to embrace new technologies, support new software deployment models and offer their customers new licensing options, they and their customers face growing complexity. For most producers, all of these changes represent additions, not replacements, to the number of licensing models they support as they must continue to support old models for their existing customers.

Application producers and customers enter into contracts in order to ensure that they make an exchange of fair value. During the negotiation process, each party tries to gain any advantages it can. Producers try to get as much money as possible in exchange for goods and services they deliver. Customers try to gain concessions on price while maximizing deliverables and flexibility around usage. But, in the end, both parties must accept the terms and conditions of the contract and agree to fully comply for the entire period of time that the contract is in force.

Software contracts can include a wide range of terms and conditions. Some of them address ancillary services such as

implementation and support. Some of them address access to future upgrades. The core terms and conditions of any software contract, however, are price and use. Customers want to keep the price down and in some cases only pay for what they use. Producers want to keep the price up and ensure that they are getting paid for as much use as actually occurs.

The first challenge in engineering the exchange of fair value in a software sale is, therefore, to define use. This is no small matter. In fact, use of software can be defined in many ways including:

Licensing Model	Definition of Use										
Named users	Entitles the customer to have a given number of specified individual employees who use the software										
Concurrent use	Puts no restrictions on who is entitled to use the software, as long as the customer's total number of simultaneous sessions does not exceed a specified number at any time										
Node-locked	Entitles the customer to only use the software on a specified set of end-user desktops										
Server- and/or CPU-based	Restricts the customer's entitlement to a specific number of physical servers and/or a specific number of CPUs within those servers										
Transaction-based	Entitles the customer the right to execute a specified number of transactions (which must also be appropriately defined) with the software (similar to usage-based)										
Usage-based	Entitles the customer the right to use the application freely then captures usage and shares that usage with the customer. Types of usage data that could be captured include: <table style="width: 100%; border: none;"> <tr> <td style="width: 50%;"><i># of compilations</i></td> <td style="width: 50%;"><i># of pictures sent</i></td> </tr> <tr> <td><i># of characters translated</i></td> <td><i># of campaigns managed</i></td> </tr> <tr> <td><i># of drawings rendered</i></td> <td><i># of email messages sent</i></td> </tr> <tr> <td><i># of CPU minutes</i></td> <td><i># of gigabytes stores</i></td> </tr> <tr> <td><i># of data converted</i></td> <td></td> </tr> </table>	<i># of compilations</i>	<i># of pictures sent</i>	<i># of characters translated</i>	<i># of campaigns managed</i>	<i># of drawings rendered</i>	<i># of email messages sent</i>	<i># of CPU minutes</i>	<i># of gigabytes stores</i>	<i># of data converted</i>	
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Environmental limitations	The producer bases pricing on entitlement for a particular type of use – i.e. in the production environment, in a development environment, or in a disaster recovery environment.										

Application producers may also grant corporate customers an enterprise license, which sets no limits whatsoever on the use of the software within the organization – although the contract may define the bounds of such a license to ensure that changes in the business don't result in use beyond that which is anticipated at the time of the agreement. This type of license may also include some type of a periodic true-up, whereby the customer agrees to pay for actual use according to a pre-defined schedule in exchange for the flexibility of using the software on an as-needed basis.

Each of these approaches may be appropriate based on the products sold, the markets served and corporate culture. For example, a node-locked model may make the most sense in a 24/7 contact center where different users may occupy any seat at any given moment – but where users won't need access to the software from home or on the road. A transaction-based model, on the other hand, may be more appropriate for applications that are exposed to the producer's customers via the web – making it impossible to accurately predict total utilization in advance.

Producers and customers who enter into these types of contracts in good faith must clearly have some means of capturing usage and ensuring compliance with these various complex models of compliance or use. If they don't have such a mechanism in place, there won't be any way to ensure that the terms of the contract are being honored and that a fair exchange of value is actually taking place. The clear definition of customer entitlements, therefore, only has real meaning when it is accompanied by an effective means of managing and capturing use in the context of those entitlements.

Traditionally, application producers have failed to provide customers with an effective means of pro-actively discovering disparities between authorized and actual use. This lack of a compliance management capability greatly increases the likelihood that customers will inadvertently violate their contract terms. It also prevents customers from defending their own integrity by either restricting their use or offering producers fair additional compensation for observed additional use.

The Growing Trend towards a Trust but Verify Compliance Management Approach

Competitive pressures, increasing enterprise interest in subscription models and a desire to improve producer/customer relationships is driving growing interest in a trust but verify compliance approach. Adopting a trust but verify approach is a particularly attractive alternative for application producers seeking to ensure the exchange of fair value in an atmosphere of trust. With this usage-based model, application producers and customers have access to actual customer application usage information that can be reconciled against the customer contracted entitlements. The ability to get to a single source of truth regarding entitlements and actual usage is the foundation of a successful trust but verify approach.

Implementing a trust but verify approach for compliance management automates the entire compliance process. It requires the producer to instrument their products with a usage-based licensing model. Today's sophisticated enterprise applications are typically comprised of a variety of functional components that invoke complex sets of software processes. To capture the use of such applications, it is therefore necessary to instrument these components and processes in a way that accurately measures use according to whichever licensing metric (pay-for-burst, pay-for-use, etc.) is applied.

Producers who adopt a trust but verify approach for compliance management can expect a "single source of truth" that provides visibility and transparency of usage data that is accessible by both the customer and the producer. This "single source of truth" makes it easy for customers and producers to answer the most important compliance-related questions, such as:

- Has use of the software exceeded the terms of the producer agreement? If so, by how much?

- How often has excess use occurred? Is excess use continuous? Is it occurring during specific times of the day, month, or quarter? Has it only occurred during infrequent periods of peak business activity?
- Is excess use restricted to specific modules, locations, departments, or users?
- What do these current utilization trends imply about future needs?

Based on these insights, producers and customers can make informed decisions about compliance. In some cases, they may simply find that the customer is in full compliance with the existing agreement. In other cases, they may find it necessary to restrict use in order to eliminate use that is both excessive and unnecessary. In still others, they may determine that the amount of excessive use is too trivial or transitory to warrant any action at all. And lastly, they may determine that the customer should be billed for the overage based upon the terms of the agreement.

Customers may also find that the application usage information captured helps form insights and help them better predict their license requirements for the future. This can help customers make sure they get the full amount of budget they need to fulfill those projected needs.

A key principle driving interest in any compliance management approach is that corporate IT organizations need greater visibility into their actual use of software relative to the entitlement terms granted by their strategic producers. Without this visibility, customers will invariably have difficulty maintaining compliance with their software license agreements—no matter how well-intentioned they may be.

Revenue, Trust, and the Customer Experience

Application producers that implement an effective software license compliance management approach can expect an increase in revenue. But, they face a variety of challenges as they seek to protect and monetize their intellectual property in order to maximize revenues. Providing their customers with licensing and pricing that is easier, more flexible and adaptable is critical to their success. Application producers that adapt their licensing and pricing strategies to meet their customers' needs will be able to monetize their products in new ways and adapt to changing market needs.

In a competitive marketplace, every advantage counts. That's why application producers are constantly looking for ways to optimize development, marketing, sales, services, partnerships, and pricing. Having the ability to support the full licensing spectrum can provide a similar edge when it comes to both realizing the full potential revenue of every account and establishing stronger long-term relationships with corporate customers.

Application producers and customers seeking to build strong partnerships and relationships need to adopt more flexible software licensing, pricing and compliance strategies and alternatives. To stay competitive application producers need to support the entire software licensing spectrum—from strict enforcement to a more open trust but verify approach. And, they need a solution that can accommodate the changing needs of their customers operating in dynamic and emerging markets.

Application producers that support a trust but verify approach will give their customers full visibility into their actual software use—however they agree to define that use. With this usage data in hand, application producers and customers can engage in fact-based trust but verify conversations to arrive at mutually agreeable decisions about value received and corresponding fair compensation.

The results of these trust but verify conversations include increased revenue for producers, verifiable compliance for customers, and relationships between the two that are strengthened by mutual trust and cooperation. The embrace of trust but verify licensing approaches by the software industry thus offers substantial benefits to producers, customers, and the market as a whole.

Flexera Software's Compliance Management Solution—Enabling Flexible Licensing Models and Monetization

Maximizing software revenues is a function of ensuring customers are compliant with producer license agreements and that producers have mechanisms to capture revenues throughout the software lifecycle. As new technologies and customer preferences increase and the demand for new license models continue to evolve, getting compliance management right enables market leading performance.

As the market leader in software license compliance management solutions, Flexera Software empowers application producers to implement a broad spectrum of licensing models within a single product—from strict enforcement to a more open trust but verify approach—to maximize revenues and ensure compliance. Application producers are able to:

- **Enable flexible monetization and licensing models** – the ability to sense and respond to changing market conditions is a significant competitive advantage. Having keen insight into product use enables you to quickly alter monetization models across products and tailor the models for various market segments, geographies, etc.
- **Offer mature monetization models for SaaS applications** – many application producers are developing SaaS applications and require sophisticated, mature solutions to implement the required monetization models the market demands for such solutions (e.g., pay-for-overage, pay-for-burst, pay-for-use)

- **Ensure that application producers get paid for the value delivered** – prevent anti-piracy and licensing abuse across all geographies with the right licensing model. Automate back-office operations that ensure license compliance to streamline internal operations (i.e., reduces the costs of audits) while ensuring all potential revenue is realized

The software license compliance management solution from Flexera Software automates compliance management by supporting the full licensing spectrum, all licensing models and the back-office automation required to manage a growing software business, enabling application producers to generate more ongoing revenue from customers.

Flexera Software—Industry Leader in Licensing and Entitlement Management

Flexera Software compliance management solutions are used by over 3,000 application producers to protect and monetize over 20,000 software applications.

About Flexera Software

Flexera Software is the leading provider of strategic solutions for Application Usage Management; solutions delivering continuous compliance, optimized usage and maximized value to application producers and their customers. Flexera Software is trusted by more than 80,000 customers that depend on our comprehensive solutions—from installation and licensing, entitlement and compliance management to application readiness and software license optimization - to strategically manage application usage and achieve breakthrough results realized only through the systems-level approach we provide. For more information, please go to: www.flexerasoftware.com



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