

## When to buy, when to rent

By [Lauren Gibbons Paul](#)



Midsized businesses have good reasons to rent their software applications from a service provider under the software-as-a-service model rather than buying them outright. However, the renting approach does not necessarily work for all applications.

### In Summary

- Renting a software application from a service provider can help midsize organizations save money on software licenses, hardware and installation.
- The software-as-a-service (SaaS) model also frees up the IT department to concentrate on mission-critical or revenue-generating projects.
- With hosted software, however, you must pay closer attention to security, and you will have fewer options regarding customization and integration.

It is easy to see why midsize business decision makers are drawn to the concept of software as a service (SaaS). Under this notion (sometimes called "software on demand" or "subscription-based software"), a company pays a monthly per-user fee to "rent" a software application from a service provider, which hosts and maintains the application at its site. An evolution of the application service provider (ASP) model from a few years back, SaaS applications are different because they are designed from the ground up to be delivered and used over the Web.

### SaaS at a glance: the good news

- **Costs are predictable and usually lower**, especially in the first two years.
- Most providers will help you **get up and running quickly**.
- **The information technology (IT) department can focus on more strategic projects.**
- Lower costs and shorter timelines translate **into lower risk of project failure**.
- **Upgrades and fixes take place transparently**, so your IT department does not spend countless hours on maintenance and support.
- **You can change applications quickly**. If your company and industry are experiencing rapid growth and transformation, SaaS can give you a faster way to rip-and-replace applications should that become necessary.

### SaaS at a glance: the bad news

- **Less ability to customize the application**. With SaaS, you will have to fit your business processes to the provider's software template.
- **Less ability to integrate with data from other applications**. If you rent your customer relationship management (CRM) application, for example, integrating it with internal data from other business applications, such as enterprise resource planning (ERP), will not be possible absent a large integration effort.

Midsized business executives need to carefully consider the trade-offs before making the decision to rent or not to rent. In more strategic areas related to your niche industry that might require heavy customization, you might opt to purchase a solution or develop it with a vendor, versus renting it. For instance, while supply chain management is not a popular application for SaaS today, payroll, accounting, Web conferencing, intrusion detection, salesforce automation, e-mail and messaging, and human resources are, according to [IDC Research](#).

"This is a paradigm shift in the purchase of software. [The software asset] doesn't depreciate over time, but you can budget it over time," says Robert Bois, research director at [AMR Research Inc.](#), in Boston. A significant portion of the cost savings come from the fact that you do not have to make a major upfront purchase of software licenses, nor will you need to buy hardware on which to run the application.

As for total cost of ownership (TCO), when it comes to CRM, for example, the cost of renting the application from a provider is generally 25 to 30 percent lower than the cost of running it yourself for a year, adds Bois. The longer the company uses the application, however, the more the TCO tends to balance out. After several years, running the application on-premises tends to be less expensive.

Microsoft works with service providers to enable them to offer hosted versions of popular applications such as Microsoft Exchange. In March, the [Microsoft Dynamics](#) business and financial software unit announced a program allowing service providers to offer hosted versions of Microsoft Dynamics CRM, according to Kevin Faulkner, product marketing manager for Microsoft CRM, in Redmond, Washington.

Microsoft also has its own SaaS offerings, [Windows Live](#) and [Microsoft Office Live](#), which offer a rich array of Internet-based business services for an affordable monthly fee.

Over the next five years, the research firm Gartner anticipates that 30 percent of all new software applications will be delivered using the SaaS model. "Our research indicates there are three reasons for its increasing popularity: cost, speed and focus on core competencies," says Ben Pring, vice president of IT services and sources for Gartner, based in Stamford, Connecticut.

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## Understand your unique business processes before deciding what to rent

Midsize businesses stand to benefit greatly by adopting standardized business practices in those areas where it may be difficult to derive competitive advantage, such as financial or account management. As applications like ERP and CRM have matured, the software and related business processes have become more standard—in many respects, perfect for renting.

"The vast majority of back-office applications are not differentiating for an organization, and, consequently, they are ripe for outsourcing," says Pring. There is a caveat, however. Whether or not an application such as CRM is core to the business is a question your company needs to address individually, he notes. A particular back-office function, like how the company delivers a product (think [Netflix](#)), could be a competitive advantage,

Some experts advise running robust business applications like ERP on-premises, regardless. "You lose flexibility when you outsource. And you're usually getting a 'light' version of the application," says Stephen Ibaraki, a longtime industry analyst based in Toronto and the recipient of *Computing Canada's* Lifetime Achievement Award in 2005.

More important to Ibaraki is the limited ability under SaaS to customize the application or integrate it with in-house data sources. Integrating internal data and the data maintained by your vendor is certainly possible, but will require extra work, whether done by an employee, the service provider or a third-party consultant.

Another benefit of SaaS is the ability to try before you buy: rent an application and then have the option to bring it in-house later. Renting an application does not wed you to any vendor, giving your growing company the ultimate flexibility.

When and if your company gives renting a shot, get the most out of the experience by taking advantage of the opportunity to reengineer your processes. For example, one of Bois' customers, a \$150 million manufacturer, recently went through an on-demand software implementation. "They realized they had two different types of salespeople, the hunters and the farmers. They realigned their sales processes to account for that—the renewable part of their business versus the one-time sales opportunities," says Bois. "View this as a catalyst to review how you do business."

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