

Transforming To Digital Licensing

By Ron Machan and Michael Albrecht

Software executives: Are you more focused on selling and distributing CDs than effectively managing the "right to use" your intellectual property? Are your internal systems and processes built to manage inventory, orders and shipments rather than the changing needs of your customers?

The answers to these questions underscore a transformation that is happening now.

Today's software companies are straining to maintain revenue growth, reduce operational costs, and maintain or improve customer satisfaction. Complicating this scenario is the fact that, while software products continue to evolve, many customers have grown dissatisfied with archaic methods for purchasing, receiving, installing, and managing software products. In spite of the innovation promised by the Internet, most software vendors are still stuck in a physical mindset of shipping boxes, CDs and manuals, and leaving it up to customers to figure out how to best meet their needs. Publishers are not focused on how customers want to buy, receive and use, but have instead structured their business around physical manufacturing and delivery rather than a digital model.

Is there an answer that can meet these tough industry challenges while benefiting both software vendors and their customers? There is. It's called digital licensing and it promises to be a major component in transforming the software industry today.

Time of Dramatic Change

Today's software companies face a time of dramatic change driven by a combination of industry trends:

- Customer demands for service and support
- Evolution of how software is used, licensed, and purchased
- Need for streamlined operations to support growth and reduce costs.
- Technology advances that enable new licensing models.

These changes have their roots in the explosive growth that the software industry has experienced in the past 20 years, which has led to a significant number of challenges for the industry and its customers. One of these key challenges includes the industry's continued reliance on physical products. Technology limitations in the 1980's often compelled companies to develop a physical focus for products and their supporting systems. The way vendors reached markets was primarily rooted in the production of physical goods (e.g., tapes, CDs, manuals) and supporting collateral (e.g., literature, boxes). Consequently, software companies were forced to become manufacturing and physical-distribution-based businesses. While a necessary reality of the early industry, companies often focus exclusively on this method for packaging and distributing products. This model also generates significant overhead costs to maintain the facilities necessary for its support. More critically,

companies began to view their products as a collection of functions, features and versions, often with each combination being represented by its own product ID and physical CD.

Emerging Industry Trends

In addition to the physical focus for products and systems, as well as other existing challenges, software vendors are faced with several emerging trends that, while presenting major opportunities, also present increased complexity:

Providing Software as a Service. Advances in technology -- including the emergence of Application Service Providers (ASPs) -- coupled with evolving customer expectations, have given rise to the idea of "software as a service." Historically, customers purchased software on a perpetual basis with unlimited use of the product's features. While the focus of "software as a service" has been on ASPs, traditional publishers are now exploring options including application rental and pay-per-use models. These models now allow customers to purchase software rights for a specific length of time, or on an as-needed basis. In spite of some implementation and adoption concerns, the new models are gaining acceptance.

Enhancing the Customer Experience. Today, customers expect more from software vendors - both in terms of treatment throughout the sales, distribution and support processes, as well as the degree of product flexibility and customization. Recognizing the flexible nature of digital media, customers now expect software vendors to offer products and services that will meet their specific requirements.

Enforcing License Compliance. As the rapid growth - prevalent within the industry for so long - begins to slow due to changing market conditions, vendors must ensure they get paid for what customers use. No more, no less. Existing customers are a center of attention for this activity and represent lost revenue due to usage beyond license-agreement limits (or "honest abuse"). This honest abuse occurs because the software provides no mechanism or tools to help the customer manage or even know about their usage.

Why Digital Licensing?

Recent innovations in the software industry and available technology have created a current business environment that is ready to more broadly adopt digital licensing.

Technology Maturity. Early adopters of the digital licensing model, such as the electronic design automation industry, successfully used licensing technology throughout the 1990s. With the successful emergence of commercial licensing applications, new vendors have identified an opportunity for growth and are actively developing products to address demand and spur innovation.

Maturing of the Internet. The Internet has proven able to deliver information rapidly, securely, and at minimal cost to the provider. While customers may not yet be comfortable conducting large-scale purchases via the Internet, small purchases and information sharing have become a widely adopted business standard.

Growing Acceptance of Intellectual Property (IP) Protection. Both business and consumer customers are beginning to understand the importance of protecting IP. The high-profile struggles of online music service Napster illustrate an increased awareness that value must be protected. Business software customers recognize the importance of honoring their license agreements, if only to avoid the costly fees and expenses to be incurred should they be found in breach of contract.

- Support discrete-feature bundling and promote levels of personalization.

Operational Efficiency

- Streamline engineering processes through management of single binaries for a product suite with right-to-use unlocked by license keys.
- Increase release flexibility by allowing marketing and engineering to easily reconfigure product offerings.
- Establish digital distribution channels.

Leveraging the New Business Model

Many independent software vendors successfully use digital licensing technology to protect revenues, drive operational efficiencies, and enhance the customer experience through expanded self-service capabilities.

In one example, software vendors have used the technology to provide their customers with ultimate flexibility in how they use the software. Rather than being limited to fixed number of copies for the duration of the agreement, the vendor offered an annual subscription of 12 monthly licenses that could be invoked at any time and expire in 30 days. In this case, the software vendor saw a revenue increase of 30%.

Another software vendor has greatly reduce the complexity of its distribution chain by offering customers a single CD with all products and providing a self-service Web site for customers to retrieve licenses that enable each product.

Still another software vendor has focused on reaching new markets by providing "basic" and "advanced" versions of its products at different price points. Once again, the software executable includes both versions, but keys are used to enable the appropriate set.

Recent industry and market developments have led to the innovation of digital licensing and the exciting opportunities it offers. Companies that successfully achieve a transformation to digital licensing will be positioned to finely hone their pricing strategies, make dramatic improvements on their customer's "out-of-the-box" experience, and significantly reduce the operational constraints and cost driven by the old models.

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Traditional Versus Digital-Licensing Business Model	
Traditional Business Model	Digital-Licensing Model
Products sold as a collection of unique CDs, executables and Product IDs	Solutions sold as a single executable file in which functionality and features are enabled via "activation" or "unlocking" keys.
Fulfillment constrained to delivery of physical goods	Online fulfillment enabled through electronic software delivery
Subsequent customer purchases require additional shipment and installation procedures	Subsequent customer purchases fulfilled through keys that unlock additional functionality
Software purchased "perpetually"	Software purchased via any number of options, including subscription and pay-per-use
Responding to market requires extensive software redesign by engineering	Marketing has the ability to rapidly design products without impacting engineering
Disparate systems for management of customer and entitlements	Common view of customer and customer products
Non-integrated legacy systems create disconnected customer experience	Web-enabled 360-degree view of the customer throughout the install base
Non-integrated, point solution-based contacts	Integrated product suites enabled by licensing

Digital Licensing Vision

The following table illustrates several key differences between the current business model for software companies and the digital-licensing vision.

The current and expected future uses for and benefits of digital licensing include:

Compliance

- Systematically monitor usage against license agreements by protection, compliance, and asset management.
- Provide tool for users to manage assets and pay only if they need to use the software.

Flexible Pricing and Marketing Strategies

- Implement new sales strategies such as shifting from enterprise-wide support models to support for individuals who perform a specific function for a limited time.
- Align licensing and pricing to specific market segments.
- Transition to value-driven sourcing and use ("software as a service").

Business Intelligence

- Improve business intelligence regarding customer activity.
- Provide detailed customer usage information.
- Force registration of all customers and users.

Completion of eBusiness Vision

- Link functions across a digital licensing spectrum (software commerce, software distribution, license distribution, license management).
- Allow customer and channel portals to offer ordering of right-to-use (features, functions, and bundled services)