WeirFoulds Technology Insights: "Types of IT Arrangements: To Build, Buy or Rent?"

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Types of IT Arrangements: To Build, Buy or Rent?

A variety of arrangements are available to businesses when seeking to leverage software as part of their business operations. While the differences between these types of arrangements may seem small, it is important that organizations understand the type of arrangement they have selected so that they can enter into the correct type of contract and do not face unintended business or financial consequences. This article will discuss the three main types of information technology ("IT") contract arrangements that organizations generally choose from: (1) building a custom product; (2) buying a product license; or (3) "renting" software-as-a-service ("SaaS").

IT Arrangement Options: Build, Buy or Rent

Building a custom product

Given the associated costs and longer timelines, which are discussed in more detail below, building a custom software product is an increasingly rare choice. However, organizations that do wish to develop a custom software product should consider whether they wish to do so internally or whether outsourcing or subcontracting the development work is a better choice.

Outsourcing vs Subcontracting

Though both outsourcing and subcontracting involve using software developers external to a company, the key difference between these arrangements is where the responsibility for the work lies. When projects are outsourced, full responsibility for the outsourced functions is given to a third party. In these cases, the third party is expected to proactively anticipate and solve issues and to make long-term decisions with regards to the outsourced functions. This can be contrasted with subcontracting, where an organization maintains responsibility and decision-making power over a project, but delegates discrete tasks to subcontractors. For example, organizations often choose to subcontract the use of an existing cloud provider to host software instead of building their own cloud, as the latter is often prohibitively expensive.

Buying a license

Instead of building a custom software product, organizations may wish to buy a license for an existing product. A license for a technology product is essentially permission to use the product. For a fee, software owned by a vendor is installed, run and operated on hardware physically located on the organization's premises (or off premises if the hosting functions have been outsourced). A license does not convey a full legal interest in the licensed property to the licensee. While it can grant certain legal interests, the purpose of granting a license is to preserve the vendor's ownership of the intellectual property.Renting SaaS

Another type of arrangement, which is often confused with a license, is SaaS. SaaS is essentially a subscription to software-based services that are hosted by the SaaS provider. Organizations can pay a fee, often monthly, in order to use an existing software product. Unlike licenses, SaaS products are generally only available for use on a cloud as a hosted platform. In fact, many SaaS service agreements do not contain any software licencing terms, and instead speak of a right to use the services provided through the software.

What is the difference between a license and SaaS?

Though licenses and SaaS products do have similarities, it is important to understand which type of product you are seeking so that you do not accidentally use a licensing contract for a SaaS product or vice versa.

When an organization purchases a license for a software product, the product is generally installed and operated on that organization's hardware and updates to the software will need to be installed accordingly. The organization will usually pay the vendor a fee for the use of the software for a specific term (for example, for 3 years). It is also often the case that the licensed software may be installed and operated by the organization on a third party's hosting service or cloud service, but the control of the software stays in the hands of the organization. Unless the organization purchases additional services, the organization will be responsible for maintenance and support services.

SaaS products differ in that the entire "stack" of hardware and software that provide the service are owned and managed by the SaaS provider, and as the customer, the organization simply gains a right to use the resulting service. This is typically achieved by having the SaaS service delivered online via a browser. As such, the product is automatically updated and users simply access the most updated version through a browser. Organizations will pay a recurring fee (often monthly) to use the product. This subscription will include maintenance and support services, though organizations may be able to purchase additional services separately. To the extent that, from a legal perspective, licenses to software or other intellectual property rights are required by the organization to access and use a SaaS service, those rights may reasonably be implied if they are not expressly set out in the agreement with the SaaS provider.

Maintenance and Support Services

Maintenance services involve maintaining the technology product in a state where it continues to function and meet required standards. For example, if an operating system changes, software may need to be updated so that it continues to run properly.

Support services involve services that assist a user in understanding how use or fix a product. For example, a help desk, where users can call to receive assistance with software, is a support service. Maintenance and support services are often bundled together. The cost of these services is generally 10-20% of the product cost per year. When deciding between a licensing or SaaS arrangement, it is important to consider the organization's need for these types of services since SaaS products typically include some or all of them, but licenses generally do not without payment of an extra fee.

Professional Services

Professional services are distinct from maintenance and support services. Professional services are generally additional services an organization may procure by hiring a vendor or a third party to complete with respect to the product. These can include implementation, custom design or development of a technology product. Fees for these types of services may be charged on a fixed-price or time and materials basis. Organizations purchasing licenses or SaaS subscriptions may also wish to purchase professional services to complete various tasks. For example, a company may purchase a subscription for a SaaS product and also hire professional services to integrate the SaaS product into the company's existing software environment.

Which IT Arrangement is Best for You?

When it comes to selecting an IT arrangement companies will want to consider a variety of factors including:

- cost;
- time;
- customization;
- control; and
- maintenance and support.

Building a Custom Product

There are a variety of advantages to building a custom technology product. These include that the product will be extremely customizable and that it can be built to work seamlessly with the company's existing software environment. Moreover, if an organization builds its own product, it will own the intellectual property rights to the product and may market and sell the product for profit. This is key for organizations whose core business involves building and selling software. However, this is not the case for most organizations seeking out software. For those organizations the high expenses and longer timelines associated with building, maintaining and supporting a custom product combined with the significant human resources required – whether internal, outsourced or subcontracted – make this a less attractive option. It is not a surprise that with all the products available today via licenses and SaaS subscriptions, building custom software products is becoming an increasingly rare choice.

Buying a Product License

In contrast to building custom products, purchasing a license to use an existing software product is less expensive up front and allows for faster implementation since the product already exists. This allows organizations to focus their internal resources on other tasks that may add more value to the business. The disadvantages to licensing arrangements include that the product is less customized (though some vendors will offer customization services) and that the vendor retains the intellectual property rights in the product. An organization that purchases a software license will also be responsible for maintenance and support services itself; however, as discussed above, many vendors will offer these services for an extra fee.

"Renting" a SaaS Product

Lastly, like licensing arrangements, SaaS subscriptions are also less expensive up front and allow for faster implementation since the product already exists. However, in addition to these advantages, SaaS arrangements have the added bonus that they include maintenance and support services. It is also easier to switch products as business needs and the market change if an organization is using a SaaS product since it is subscription-based and accessed via a browser and is not installed on an organization's own hardware. As with licensing arrangements, the disadvantages to SaaS products include that the products are less customized and that the vendor will retain the intellectual property rights in the product. Again, some vendors will offer customization services for SaaS products, but the availability depends on the specific product.

Conclusion

If building software is a core part of an organization's business or there are no solutions on the market that address the relevant business challenge, building a custom product may be the way to go. However, this is an increasingly rare choice given the associated costs and longer timelines. More often, where lower costs and faster deployment are a higher priority than a fully customized product, businesses should consider buying a license or "renting" a SaaS product. Moreover, if ongoing maintenance and support and flexibility to switch products are important, SaaS is likely the best option.

While technology contract arrangements can be complex, organizations do not need to navigate this landscape alone. For more

information on the topic discussed in this note, or for legal advice regarding this topic or any other information technology or intellectual property law-related matter, please contact the technology team at WeirFoulds.

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