Gartner

Research

Publication Date: 31 August 2009 ID Number: G00170207

How Flexible IBM, Microsoft, Oracle and SAP Have Been With Software Customers During the Economic Downturn

Alexa Bona, Jane B. Disbrow, Peter Wesche, Mike Chuba, William R. Snyder

Due to the economic downturn, many CIOs, application leaders, procurement professionals and asset managers have been anxious to reduce costs and have been looking to their strategic software vendors to assist in some way. We assess how flexible four software vendors (IBM, Microsoft, Oracle and SAP), commonly deemed strategic by clients, have been with customers during these times, and what customers may achieve in attempting to renegotiate current agreements.

Key Findings

- Most organizations have seen little commercial flexibility from their strategic software vendors during the economic downturn.
- Maintenance and support are very profitable for software vendors, and they are reluctant to reduce such costs even when their customers' own businesses have become less profitable.
- Microsoft and IBM have shown a bit more commercial flexibility to their customers in the downturn than Oracle and SAP.
- The clients that have been most effective in reducing costs with Microsoft, IBM, Oracle and SAP in the downturn are those with effective strategic vendor management programs (when those vendors are strategic) or those with potential new business to offer in the near future.

Recommendations

- Even if your software vendor is noted as not being flexible with maintenance and support payments, continue to push back against payments for shelfware and software payments that approach full list price. Without this continued emphasis, vendors continue to believe that the customer is satisfied with the amount that is being paid.
- Whenever you have an opportunity, negotiate license exchange clauses that allow you to trade in existing license spending on unused licenses for new licenses you do need. If possible, also try to negotiate the ability to temporarily suspend maintenance on unused licenses without incurring prohibitive penalties if reinstated.
- If you have the potential to be seen as a strategic customer, leverage strategic vendor management programs to improve benefits and potentially reduce costs during the downturn.

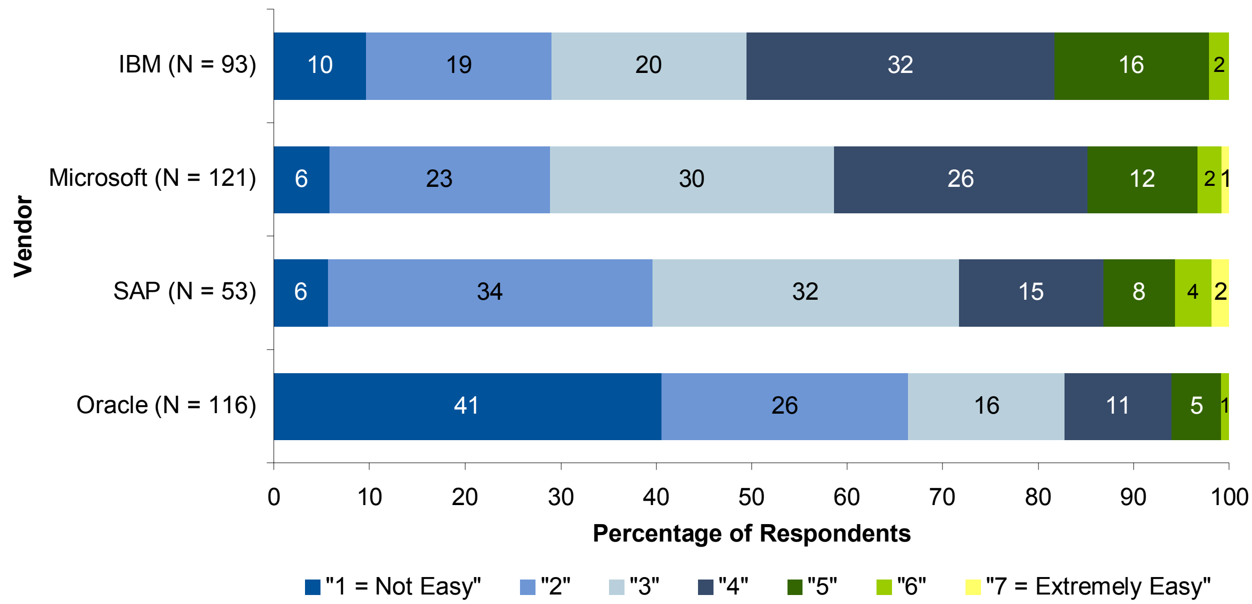
ANALYSIS

During the economic downturn, we have had a dramatic increase in the numbers of client inquiries related to reducing software and maintenance costs, especially with strategic vendors such as IBM, Microsoft, Oracle and SAP, where the spending is generally significant. In general, it is not easy to reduce cost with these vendors due to the high degree of dependency on these vendors' products, and the very high switching costs. However, given that some of these are usually strategic vendors, clients have been asking how they can leverage the strategic relationship to reduce costs in these particular circumstances, and what each vendor is prepared to do.

We have also been informally surveying a number of our clients in conference calls, webinars and conference surveys asking how many software vendors were offering any licensing flexibilities (see Note 1) to reduce fees as a result of the economic downturn. In a series of six Gartner webinars on software licensing and cost savings between February and April 2009, attended by Gartner clients and prospects, 552 attendees were asked this question (see Note 2). Sixty-two percent said none of their vendors had been flexible, 19% stated one or two vendors had shown flexibility, and 13% said between two and four. At one of the webinars (in April) attended by 228 participants, we specifically asked the respondents about their perceptions of the flexibility of four vendors (IBM, Microsoft, Oracle and SAP), provided they had specific recent experience with them. A total of 95 participants provided the following results: 34 respondents said they thought Microsoft was flexible, and 33 said IBM was. In addition, 23 considered Oracle flexible, and 5 considered SAP flexible (see Note 3).

We also conducted an informal post-event survey at four Gartner licensing briefings that took place from May through July 2009 in Europe (see Note 4), asking respondents to rate the vendors they had negotiations with in the past 12 months on a scale of 1 to 7, where 1 was very difficult to negotiate with, and 7 was very easy. The results are shown in Figure 1. Relative to the number of respondents, Oracle was perceived to be the most difficult to negotiate with, followed by SAP, then Microsoft; IBM was deemed to be the easiest. While the results from the two informal surveys are not exactly the same (licensing flexibility versus ease of negotiation), they do indicate that, in general, IBM and Microsoft garnered more favorable responses in this economic environment than Oracle and SAP did.

Figure 1. Rate the Vendors Your Organization Has Had Negotiations With in the Past 12 Months in Terms of Ease of Negotiation



Total number of survey respondents: 230

Source: Gartner (August 2009)

While the figure above only represents surveys conducted in Europe, we have analyzed general licensing practices and the results of detailed Gartner client inquiries to stack-rank the vendors from most to least commercially flexible during the downturn. We were specifically looking at what these vendors were prepared to do to help customers reduce costs, even temporarily, to manage through this period of reduced budgets and often reduced head count. Given that there are not often significant amounts of new money available for new licenses, we concentrated on what flexibilities these vendors offered to reduce cost on existing licenses, rather than flexibilities that would more naturally accompany big new spending.

Microsoft

Based on extensive client reports of their experiences with Microsoft, together with survey results, Microsoft is perceived as being relatively flexible with its customers related to the downturn. First, for those with Enterprise Agreements (EAs) who are locked into paying a certain fee for each Qualified Desktop (see Note 5) each year, and have seen a decrease in the number of desktops year over year because of the downturn, there is a clause in the standard EA contract that says, if the number of Qualified Desktops or Qualified Users changes by more than 10% as a result of a merger, acquisition or divestiture, Microsoft will work with you in good faith to accommodate your changed situation. Although it does not explicitly cater to downturn reductions, in practice, clients have reported Microsoft has been similarly accommodating. In most cases, it will require the client to terminate the EA early and re-sign another three-year EA with the lower volumes. This way, although this means the customer does not have to pay for unused devices, Microsoft also gains the benefit of another three years of guaranteed annuity maintenance revenue in the form of Software Assurance (SA), which is part of the EA payments. For the smaller number of clients with Enterprise Subscription Agreements (ESAs), this agreement programmatically allows for true-downs (see "Microsoft Enterprise Subscription Agreement Promotions Pique Client Interest").

In addition, in more limited cases, usually for customers in particularly volatile industries, we have seen Microsoft willing to negotiate true-down clauses in EAs (not just the standard true-up) that would allow a true-down of at least 10% to 15% of the original volume in a downturn, without having to rewrite the agreement.

The fact that Microsoft programmatically separates out the right to new versions of the software from technical support entitlements, and provides bug fixes and security fixes for 10 years (five years mainstream, five years extended) whether or not you buy maintenance, has also given many clients scope to reduce costs. Clients with severe budget challenges are able to cancel SA or not renew their EA without compromising their ability to purchase a Premier Support contract and call in technical support incidents. Of course, they would have to be willing to forsake the right to new versions of the software, and other SA benefits (see "Toolkit: Analyzing the Benefits of Windows Client Software Assurance and Desktop Optimization Pack"), but they would not have to go without support entirely. Since SA is usually 25% to 29% of the license fee annually, clients who are able to do without this offering for four to five years have been able to make significant immediate savings, and even if they have to rebuy the license in four to five years, they would save over what they would have paid on SA in the same time frame. With the other vendors highlighted here, this approach would be impossible, as canceling maintenance would result in a complete inability to raise technical support incidents with the vendors or get security fixes.

For those customers who do not have an EA, the Select Agreement is by nature a forecast agreement, so if the downturn has led to purchasing fewer licenses than anticipated, the worst that would occur is an annual releveling of the pricing tier, meaning slightly higher prices per unit, but no requirement to pay for licenses not needed. However, like other vendors, Microsoft will not give credit for surplus licenses.

Microsoft has been offering pricing promotions during recent quarters and financing, but these are for new buys rather than for existing licenses. We have also seen high levels of compliance checks throughout the downturn, resulting in unexpected invoices for some.

IBM

IBM has demonstrated somewhat lower reductions and flexibilities than Microsoft, and continued reported high levels of audits throughout the downturn have resulted in unexpected invoices for some (see "Gartner Polls and Surveys Show an Increase in Software License Audits"). However, this is tempered by more positive survey ratings and findings from clients in inquiries on ease of negotiating with IBM. IBM generated high profit levels during the downturn, unlike the other vendors on this list, and thus seems less pressured to discount prices to maintain adequate business levels. It is in more strategic long-term activities where it is likely to offer flexibilities.

IBM has evolved its Open Infrastructure Offerings (which encompass software, hardware and services), allowing for greater flexibility (better product substitution, greater ability to improve or defer installation, greater ability to include business partner spending, wider range of contract term). These flexibilities have improved customer satisfaction, but these agreements do require greater commitment and often competitive product displacement to get IBM's best deal. Although these flexibilities are a short-term win, customers must bear in mind that the long-term costs should be analyzed, including post-ELA time frames, to make sure that the savings are not oversold. IBM has also come up with package deals for customers looking to deploy Linux on the mainframe — which can include the Novell SUSE and Red Hat components. It has announced a series of System z solution packages that expand upon the initial offering for SAP workloads —

again, these deals encompass more than just software. IBM has also instituted subcapacity licensing models that license software based on a utilization model, expanding its use beyond System z to other IBM platforms. IBM states that about 50% of mainframe servers are now using subcapacity; however, based on our own discussions with clients, the percentage of customers is less. The distributed side is also seeing greater interest in, and some usage of, subcapacity licensing, as the increasing adoption of virtualization technologies spurs the benefit. Subcapacity is particularly beneficial for those organizations running disparate workloads in a consolidated environment. Organizations should re-evaluate at least once a year whether they are using the optimal IBM pricing models.

SAP

SAP has been fairly uncompromising on reducing maintenance and support, even when there have been significant head count reductions at the client, resulting in unused licenses. In addition, SAP's replacement of Standard Support with Enterprise Support as well as the increase of maintenance to 22% for existing licenses over several years coming into effect during the downturn left installed base customers highly concerned. Although SAP has ameliorated the situation by capping the increases and working with the SAP user groups to link price increases to benefits achieved by new support services, some customers are still skeptical (see "Navigating the SAP and SUGEN Enterprise Support Arrangements").

We have received many calls from clients who are looking to reduce SAP costs, even temporarily in the downturn. In a number of cases, customers have discovered they have shelfware (licenses bought but never used) from SAP. While customers recognize they will not get money back for licenses purchased in error or as part of big bundle, many are hoping for a temporary reduction in the maintenance and support fees, since no new versions of the undeployed package are being used, and few or no technical support questions are being logged. Customers with Business Suite or ERP licenses can of course reallocate user licenses within that portfolio, if they discover they have too many HR users and not enough finance users, for example. We have also seen some limited instances of SAP allowing broader license swaps/exchanges. Take, for example, customers that licensed Environmental Health and Safety, but never deployed these licenses; if they know how much they paid for those licenses, SAP may allow them to trade them in for something else (such as MDM licenses) that is required. These license exchanges, if offered, are often done on a net-to-net basis, and usually, they would have had to be negotiated prior to the downturn. Customers have reported only limited evidence of SAP applying this policy without contractual clauses, mostly in those cases when SAP sees significant future upside business potential.

If the customer has no new license requirements, the standard SAP contract terms are not helpful, stipulating that maintenance is an "all or nothing" scenario, and even if it is terminated on a temporary basis, customers would have to pay all the back-years in fees, plus often an undefined penalty amount, if they were to subsequently reinstate. However, we have seen some limited examples of SAP allowing customers to temporarily suspend or "park" maintenance, for a period of one to two years — again, usually only if SAP sees future upside business potential. In these cases, the customers would not pay maintenance on the unused modules, and after the one to two years, rather than paying all the back-years in maintenance, they would usually just pay an administration fee that is negotiated, but sometimes 2% to 10% of the maintenance fee for the year the software maintenance is reactivated.

Oracle

Unless customers have significant new license revenue to offer, clients have reported that Oracle has been inflexible. Survey results also validate the difficulty clients face negotiating with Oracle. For more than any other strategic software vendor, we have received calls from Oracle customers looking to reduce maintenance costs, particularly related to shelfware, who have been unsuccessful. As with the customers of other vendors, Oracle customers recognize they will not get money back for unused licenses, but many are hoping for a temporary reduction in the maintenance and support fees. However, in contrast to its relative flexibility in pricing for new licenses, Oracle has been uncompromising in regard to maintenance. Oracle's current maintenance and support policy states that, if a subset of licenses on a single order form, or under a price hold, is terminated or support is reduced, then support on the remaining licenses on that same order form will be repriced using Oracle's standard e-business discount, usually significantly lower than the initial discount offered. Customers have therefore found it very difficult to achieve any savings and mostly have to continue to pay support on unused software (see "Understand Oracle's Repricing Policy Before Combining Invoices for Prior Purchased Products"). The only concessions we have seen Oracle offer on maintenance and support are that, in some cases where the customer has proven financial distress, it has allowed customers to eliminate the annual cost-of-living increase (usually 3% to 5%) on maintenance with the justification that in the downturn the cost of living has not increased. It has also offered some customers financing options on maintenance — usually at 8% interest (see Note 6).

In addition, during the downturn, we have seen an increase in the number of Oracle audits (see "Gartner Polls and Surveys Show an Increase in Software License Audits"), which have often resulted in customers receiving unexpected invoices because they were out of compliance.

In our experience, those clients who are actively managing these vendors within strategic vendor management programs have been most effective in reducing costs during the downturn. They are able to do better demand management, and highlight future business that may be negatively impacted, if some short-term concessions are not made. They are usually better able to work the relationship at more senior levels, resulting in short-term concessions being offered to improve the relationship in the longer term (see "Aligning IT Procurement Best Practices With Vendor Relationship Management," "Q&A: Best Practices for Vendor Management," "First 100 Days: Head of IT Vendor Management").

Additional research contribution and review: Bob Igou.

RECOMMENDED READING

"Gartner Polls and Surveys Show an Increase in Software License Audits"

"Findings: Polls and Inquiries Indicate That Clients Should Be Prepared for an Oracle Audit"

"How to Make the Right Decisions About Oracle Unlimited License Agreements"

"Negotiate Oracle's Software License Agreements to Reduce Unexpected Cost"

"Understand Oracle's Virtualization Policy to Avoid Unexpected Costs"

"Dealing With IBM Software Licensing Requires Increased Effort"

"Control IT Spending for Microsoft Licensing"

"Issues to Consider When Deciding Whether to Renew a Microsoft Enterprise Agreement, 2009 Update"

"Overview: Issues to Consider When Deciding Whether to Renew a Microsoft Enterprise Agreement, 2009 Update"

"Microsoft Enterprise Subscription Agreement Promotions Pique Client Interest"

"Evaluate Microsoft Promotions on Products Licensed With Software Assurance"

"Navigating the SAP and SUGEN Enterprise Support Arrangements"

"New Benchmarking to Guide SAP Enterprise Support Fees"

"Findings From the Gartner Survey on SAP Enterprise Support"

"Regional Compromise Is SAP's Response to Customer Objections"

"German Perspective: Guidelines for Responding to SAP's Increased Maintenance Fees"

"Aligning IT Procurement Best Practices With Vendor Relationship Management"

"Q&A: Best Practices for Vendor Management"

"First 100 Days: Head of IT Vendor Management"

Note 1
Definition of "Flexible"

The Encarta English Dictionary for North America defines "flexible" as follows: "able to adapt to new situations: able to change or be changed according to circumstances" and "able to be persuaded or influenced."

Note 2
Profile of Webinar Attendees

The six webinars were offered globally at different times of the day, attracting attendees from around the world. They were all either existing Gartner clients or Gartner prospects. The informal surveys did not collect demographic data such as job title, geographic location, industry or size, nor did they ask whether respondents were specifically involved in decisions related to these vendors.

Note 3
Webinar Poll Numbers

In the webinar poll, we did not capture how many respondents actually had negotiated with each vendor in the downturn, so some of the lower numbers could account for a relatively low number of respondents negotiating with that vendor.

Note 4
Profile of European Survey Participants

The European cities where attendees were informally surveyed were Basel, Helsinki, London and Stockholm. The 230 respondents were predominantly in the job function of IT management (35%), IT procurement (31%), asset management (15%) or strategic vendor management (11%). Other roles included CIO, legal and compliance management. The majority of respondents (49%) worked in companies with more than 10,000 desktops or laptops; 19% had 5,000 to 9,999; 21% had 2,000 to 4,999; and 11% had less than 2,000. Specifically related to this question, respondents were given a list of 14 vendors and were asked to rate them in terms of ease of negotiation. They were under no obligation to rate all of them and were asked to choose those vendors with whom they had interacted on a software contract negotiation basis in the last 12 months. IBM, Microsoft, Oracle and SAP were the most commonly rated vendors, with IBM getting rated by 93 respondents, Microsoft by 121, Oracle by 116 and SAP by 53. The surveys did not collect additional demographic data such as industry or size.

Note 5
Microsoft Definition of "Qualified Desktop"

"Qualified Desktop" means any personal desktop computer, portable computer, workstation, or similar device that is used by or for the benefit of an Enrolled Affiliate or any Affiliate included in its Enterprise and that meets the minimum requirements for running any of the Enterprise Products. Qualified Desktops do not include: (1) any computer that is designated as a server and not used as a personal computer; (2) any device dedicated to run ONLY line-of-business software (e.g., an accounting or bookkeeping program used by an accountant or a computer-aided design program used by an engineer or architect); or (3) any device running an embedded operating system (e.g., Windows Vista embedded, Windows XP embedded).

Note 6
Oracle Financing on New Deals

On new deals, further financing terms were possible, such as elimination of interest for the first 90 days, followed by eight quarterly payments. In addition, for midmarket customers, Oracle offered a 0% lease for 36 months, with Oracle paying the first month.

This research is part of a set of related research pieces. See "Delivering Optimal IT Costs Is the Focus of the Upcoming IT Finance, Procurement and Asset Management Summit" for an overview.

REGIONAL HEADQUARTERS

Corporate Headquarters
56 Top Gallant Road
Stamford, CT 06902-7700
U.S.A.
+1 203 964 0096

European Headquarters
Tamesis
The Glanty
Egham
Surrey, TW20 9AW
UNITED KINGDOM
+44 1784 431611

Asia/Pacific Headquarters
Gartner Australasia Pty. Ltd.
Level 9, 141 Walker Street
North Sydney
New South Wales 2060
AUSTRALIA
+61 2 9459 4600

Japan Headquarters
Gartner Japan Ltd.
Aobadai Hills, 6F
7-7, Aobadai, 4-chome
Meguro-ku, Tokyo 153-0042
JAPAN
+81 3 3481 3670

Latin America Headquarters
Gartner do Brazil
Av. das Nações Unidas, 12551
9° andar—World Trade Center
04578-903—São Paulo SP
BRAZIL
+55 11 3443 1509