



CHANNELS FOR THE NEW SAAS INDUSTRY

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Executive Council on Software as a Service
Channel Committee

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CHANNELS FOR THE NEW SAAS INDUSTRY

Channels accelerate business, broaden market reach and help grow market share and lower cost of sales. How does this apply to the new SaaS industry?

**SIIA SOFTWARE AS A SERVICE
EXECUTIVE COUNCIL
CHANNEL COMMITTEE
WHITE PAPER**

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TABLE OF CONTENTS

INTRODUCTION	3
EXECUTIVE SUMMARY	4
SAAS CHANNELS ARE ENTIRELY DIFFERENT.....	5
SAAS PARTNERS VALUE ADD	8
SAAS CHANNEL EXAMPLES.....	8
INTERVIEWS WITH INDUSTRY LEADERS	9
<i>Interview with Eric Berridge, BlueWolf Group</i>	9
<i>Interview with Matt Holeran, Salesforce.com</i>	9
<i>Interview with Bjorn Espenses, CEO of Infopia</i>	10
TOP 10 ASPECTS FOR DEVELOPING A SUCCESSFUL SAAS CATALYST CHANNEL.....	11
CONCLUSION.....	13

INTRODUCTION

This white paper explores how Software as a Service (SaaS) companies can leverage indirect channels to provide necessary services and market expansion required to maximize revenues and customer satisfaction. It examines the unique role the channel plays in SaaS, as well as challenges and differences from traditional channel modes.

It also provides insight from successful SaaS channel partners and SaaS providers to determine what works and what doesn't -- and what you need to do to develop a successful indirect channel. The content of this white paper was compiled based on interviews with channel thought leaders from early and successful SaaS companies.

SaaS Executive Council Background

The SaaS Executive Council is an initiative of the Software & Information Industry Association (SIIA). The Council is a multi-vendor coalition designed for the formulation of best practices, education and communication to help SIIA members and the industry at large better understand the realities and opportunities presented by the "Software-as-a-Service" model. As SaaS continues to gain traction over traditional premise-based software licensing models, the Council will focus its efforts on delivering primary market research and analysis to help software vendors, channel partners and SaaS consumers get the highest value from SaaS solutions.

The SaaS Executive Council has four working group, known as Committees. These Committees each focus on a specific area of interest to SaaS customers, vendors and partners. This paper was produced by the Channel Committee. More information can be found on the website of the SIIA at www.sia.net.

Contributors

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EXECUTIVE SUMMARY

With an estimated 10 million companies using SaaS worldwide in the next 5-10 years, the SaaS industry will provide business opportunities for more than 200,000 partner companies.

Channels in the SaaS industry are fundamentally different from their counterparts in the enterprise software world. In SaaS, partners don't take title to the product, there is no inventory or logistics, no contractual reselling activity, no repair service and no physical goods to install or connect.

The main focus for partners in the SaaS world is on business process alignment, optimizing the use of the information, solution deployment, application support and integration with existing systems.

While traditional IT products are sold in a "fire and forget" mode, SaaS solutions are sold with an opportunity for ongoing services. Successful SaaS companies not only think in terms of recurring revenue but in a "Recurring Services Model".

As SaaS vendors host the application, they effectively become part of the IT organization of their customers. Hence, tech support is a vendor internal activity. That fact results in a very different channel structure.

Because of the different structure and services in the SaaS model, channels are no longer "resellers" or "Value Added Resellers" they are – CATALYSTS. Catalysts are companies or individuals that understand the various business needs in terms of organizational improvements in areas such as Sales, Marketing, HR, Operations, Logistics etc. and also understand the advantages of SaaS-based applications. They help small, medium and large firms transform their "Information Technology" into "Information Management".

SAAS CHANNELS ARE ENTIRELY DIFFERENT

Before we can build a channel for an industry we need to fully understand the aspects and models of the industry itself.

Why is SaaS so different?

For many, SaaS is software and just a different delivery model. But once one is part of that industry, it quickly becomes apparent that nearly every aspect of a SaaS company is different from the traditional software industry and that, therefore, the channel needs to be different too.

Architecting the Solution

While traditional software runs inside the firewall, SaaS applications run remotely and they are available to all sorts of independent users and entities. No code is installed outside the SaaS provider. There is no traditional installation required by a partner.

Testing the Software

Traditional software follows lengthy development, testing and release cycles of twelve months or more. Conversely, SaaS solutions are iterated continuously and the testing effort is ongoing as well. Many more people can be involved in the testing effort without the negative side effects associated with PC installation and faulty beta versions. Channel partners should become an important group in the test cycle.

Providing the Application

Access to SaaS applications is provided via the web by a simple login. A user can configure it without ever physically installing the software. Nothing gets shipped or installed, nor are there issues of compatibility with existing systems. Channel partners don't have to deliver anything.

Licensing the Application

Licensing is actually easier in SaaS because access to the application can be controlled by the provider. There is no title a reseller can carry.

Protecting IP on the solution

No media, no copying, no copyright infringement and less risk that IP can get stolen. That means fewer legal issues for partners.

Operating the Application

The application is not installed, embedded, integrated, adjusted and setup onsite with the customer; it is operated by the SaaS provider. Tech support is a SaaS provider internal task. That significantly impacts the role of the channel partner. There is often significant configuration, setup and integration work to be done – but even that differs from traditional software.

Updating the Software

Updating the software is also a SaaS provider internal task. There is no technical job for a partner other than the need to provide business alignment support.

Service Level Agreements (SLAs)

The service levels need to be established by the provider (because the SaaS provider runs the software, not the customer) and that is entirely different from the traditional software model where there is no SLA in place. These service levels will

determine the allowable downtime, response times and credits associated with failure to meet these documented standards.

Buying the solution

There is no capital expenditure and therefore often no purchasing department involved. Many times, the buyer is the user rather than the IT department. Partners likely will not sell to a corporation, but service individual groups of users.

Selling the solution

IT departments are still learning about SaaS. The buying decision is most often made at a departmental level. Sales cycles are typically shorter because the initial investment and the perceived risk are far lower than traditional software. Most SaaS companies sell through highly effective inside sales teams, while traditional software companies use more expensive field sales organizations. That said, channel partners will further expand the sales reach and create different ways of selling the services.

Marketing

Most SaaS marketing targets the consuming user rather than an "organization". At the same time, large companies get excited about the cost advantage and simplicity of SaaS and let their employees choose what is right for them. SaaS becomes a consumer product that is sold into business. Therefore, marketing will also be very different. SaaS companies need to invent a business-targeted consumer marketing approach. With that, partners and partner marketing will become a different activity than in B2B marketing.

Servicing the solution

Because the delivery of the product is the responsibility of the SaaS vendor, there is no traditional technical service required. What users *do* need is help maximizing value from the application and provision of support for business process adjustments and business use. This is arguably the biggest opportunity for vendor independent catalysts.

Integrating the solution

Since much of a company's data resides inside its firewall, there is an integration challenge to connect local with remote systems. Integrating a SaaS application with on-premise systems is far different job from integrating two local systems which can both be customized. Companies need to understand new technologies and security aspects. SaaS vendors will not have the capability to provide that service – independent catalysts need to step in.

Compensating sales teams

Creating a compensation plan for solutions that cost \$60 per user per month creates significant differences from traditional software sales compensation models. SaaS companies must develop different methods to compensate sales teams for selling the service compared with traditional software companies. Therefore, channel partners will also need to be on a different model.

Margins to indirect sales

Similar to sales compensation, SaaS providers need to offer catalyst partners a different model from the traditional "margin on product sale." That, in turn, influences how a channel partner compensates their own sales team.

Bundling the solution

Bundling two physical products is pretty easy – bundling services requires a deeper understanding of the user’s needs and the possibilities to connect the respective applications. Bundling in the SaaS space can provide the opportunity to differentiate partners and their respective capabilities.

Returning/Terminating the use

Goods have a tendency to come back. The end customer may want to exchange, return, repair or discontinue use of the service for any other reason. Customers will simply discontinue the service if they fail to continue to extract value from the solution. In SaaS, there is no repair or exchange service opportunity for a reseller – but it may provide an opportunity to offer different/other services.

Reporting financial results

SaaS is built on a recurring revenue model. This requires a company to fully understand revenue recognition, deferred revenue and a cost/cash model that allows the company to build a healthy financial model that is very different from the traditional software industry. Likewise, a partner is required to understand those differences and to build his own financial model that is connected to the respective SaaS vendor.

Personnel

SaaS companies typically have a fundamentally different strategy regarding market penetration: they “Land and Expand”. Servicing the customer and making him successful with the application is the primary focus of a successful SaaS organization. Traditional software companies tend to “sell high – you may not get additional business” and “availability of goods” before a buyer chooses something else because it is available. This wheeler/dealer mentality in a channel partner has no place in a world of ongoing customer service. But, local partners will have an advantage over others as they constantly service their customers.

Others

When examining all the differences in the SaaS model, there are even more differences in operations, production, administration... but the list above shows the most important.

SAAS PARTNERS' VALUE ADD

Given there is nothing to resell, nothing to technically install and no opportunity to provide any kind of logistics, what can a successful SaaS partner contribute?

The most important value a partner can add is to provide business-process-relevant implementation and integration services to the customers. While an application may be generally easy to use, the more important question within an organization is "how are we all going to use it together". SaaS partners are not "resellers" delivering software, but rather catalysts for this new industry, making it work long term. They help customers become quickly productive and ensure the service is fully embedded into organizational processes.

In order to do that successfully, a SaaS Catalyst needs to understand their customer's business processes and have a good understanding of the respective verticals. A CRM, HR, Project Management or Marketing Application can be used in variety of ways, but the partner helps orchestrate the configuration and implementation to shorten the "time to value."

SaaS enables even very small companies who don't have IT departments or capabilities to leverage software to better run their business. SaaS Catalysts will play a very strategic role in the vendors' success in reaching that market and retain customers long term.

SAAS CHANNEL EXAMPLES

There are few companies with a proven and successful channel model in the SaaS industry, but Salesforce.com and Intacct Inc. both have a robust partner network worthy of examination.

Intacct Inc. works closely with various channel partners to provide small and midsize businesses with on-demand financial applications. Two of the most successful indirect channels that Intacct has cultivated are CPA firms offering outsourced accounting services and industry-focused software companies.

Top 50 accounting firm SS&G Financial Services, Inc., for example, uses Intacct to remotely manage the books of major restaurant chains, including Papa John's Pizza. With Intacct's web-based solution, SS&G's accountants in Cincinnati can provide restaurant chains across the country with services ranging from monthly consolidation to financial management consultation. As a result, in the first year with Intacct, SS&G saw its outsourced business grow by more than 75%.

RealPage, Inc., a Carrollton, Texas-based property management software vendor with an installed base of more than 20,000 apartment communities, integrated Intacct's financial applications with its screening, leasing, and facility management software. The combined front-office and back-office solution helped RealPage increase sales 800%.

Salesforce.com provides CRM solutions over the Internet and works extensively with development and implementation partners to broaden their market share. Based on partner feedback, salesforce.com plays a leadership role in channels

focusing on partners with a high degree of self-sufficiency. Today, salesforce.com has over 100 partners who help customers implement the SFDC solution. Rather than having local support people on staff, salesforce.com trusts their competent and trained partners to help customers implement and deploy their CRM solutions.

Even though it looks like everybody can register and be productive in minutes, in fact, it takes a week or more, on average, to internally define rules of engagement, structure customer data and define ways to use the system. Partners not only help with business process consultancy, but many also develop value-added tools and services around the application. A typical salesforce.com partner makes money through implementation and configuration services, business process alignment consultancy and development of additional tools and programs. Unlike a traditional CRM reseller, there is no technical configuration to be sold – the sole focus is on business processes and integration work.

Financially this is a win-win situation. The vendor [salesforce.com] is not required to open local offices all over the world in order to service their customers. More and more partners can participate in SaaS industry growth and leverage salesforce.com's platform to provide services with a reasonable marketing investment.

INTERVIEWS WITH INDUSTRY LEADERS

In order to complete the picture, we interviewed a variety of industry leaders and asked for their advice and key findings. Much of the interview content is presented throughout this white paper, but the following interview extracts reflect specific experience and advice.

INTERVIEW WITH ERIC BERRIDGE, BLUEWOLF GROUP

Bluewolf Group is a new breed of channel for the SaaS industry. With the firm's 175 consultants, they help companies implement and integrate solutions including salesforce.com, Eloqua, Openair, Responsis, as well as providing custom work for SAP, Oracle and others. Bluewolf Group drives on-demand revenue through their consulting practice.

According to Berridge, SaaS channels make money by either providing consulting services around certain solutions or by developing products enhancing existing solutions. He states that salesforce.com does an amazing job for developers by making the product partner friendly.

Eric's advice: Vendors need to ensure that their partners can be self sufficient and that the partner doesn't require resources from the vendor to buy and implement a product.

INTERVIEW WITH MATT HOLERAN, SALESFORCE.COM

Salesforce.com has built a very effective channel that includes both big and small companies. For instance, Vertical Response offers their solutions via the AppExchange to 400-500 customers. The AppExchange model helps developers reduce the burden on integration and also reduces sales and marketing cost. Vertical Response is an example of a company that provides its solutions through AppExchange with a lead closure rate of up to 40%, according to salesforce.com's

Matt Holleran. Interviews with other salesforce partners confirm that they made it easy to integrate partner solutions with SFDC without the need to engage salesforce employees and be dependent on their resource allocation. For instance, salesforce.com provides ways to test drive not only salesforce.com itself, but also their partners' applications. Some of their partners develop exclusively on the salesforce.com platform and that can dramatically reduce the cost of the development environment. The salesforce.com partnerships are highly integrated into the salesforce.com solution architecture which makes the channel a highly efficient group for all kinds of solutions developers.

Matt's advice: Companies need to design the buying process into their product. The easier it is to explore, try and buy a product, the higher the chance to win the customer.

INTERVIEW WITH BJORN ESPENSES, CEO OF INFOPIA

Infopia tried to develop a partner channel early on, but not very successfully. Even though the product is easy to configure, channels were immature. In more complex projects, Infopia actually pulled in VARs who helped to integrate Infopia's e-commerce products into the customer's on-premise IT world.

More recently, Infopia has begun to collaborate with partners with more success. In a large project for Electrolux, Infopia collaborated with a partner and demonstrated great success for all participating parties.

Infopia's sales organization is structured so that all business below \$50,000 goes through inside sales and all business above \$50,000 goes through field sales. If partners are involved in an opportunity, Infopia provides both contract options. The customer can sign on the partner's paper or Infopia's paper.

Bjorn's advice: The SaaS partner model is very different because of the recurring revenue model. The most important advice is to understand the value chain in that business.

CONSIDERATIONS FOR DEVELOPING A SUCCESSFUL SAAS CATALYST CHANNEL

The SaaS industry is new, the way SaaS Catalysts do their business is new and so is the partner engagement for vendors in this new world. Creating a successful catalyst channel is critical if a vendor wants to compete on a global basis.

Partnership Spirit – The most important aspect of a successful partnership is that the spirit of partnering is based on a joint engagement for a win-win situation. If channels are seen merely as an external sales force that has to, in effect, compete with the vendor, there is little chance of success. The most successful channels – across industries – are the ones where channel conflict is alleviated and all the energy is focused on jointly winning more customers and gaining more market share.

Target Market – There may be certain customers, market segments or geographies where a vendor wants or needs to sell directly to the end customer. As long as the vendor communicates these “rules” and sticks to them, there will be few problems. Vendors must let their catalyst partners know what they are going to do. That will develop trust. If there is a breach of trust, there is always another vendor your partner can turn to. It is always helpful to select partners for specific target markets where you as a vendor alone are not likely to succeed or to have resource constraints.

Compensation – Compensating partners for finding new customers is more difficult in the SaaS industry than in the traditional software space. Setting proper expectations and having clear communication is crucial. Many SaaS companies struggle to adequately compensate their internal sales teams – let alone have a compensation plan for partners. Here are some best practices for partner compensation:

- ▶ **Referral Fee** – paying a 15% referral fee for the first year’s recurring revenue, payable in the same intervals the customer has to pay, should be adequate to motivate a catalyst to start actively promoting the solution and to compensate him for his sales engagement. The fee should be similar to, but less than, your internal cost of sales. If you can sell direct at lower cost – sell direct as long as you can.
- ▶ **Renewal Fee** – contract renewals are less difficult than identifying a new customer and so the compensation should be lower. We suggest an 8% renewal compensation if the catalyst is continuing to serve the customer and the customer does not require the vendor to replace the catalyst.
- ▶ **Coop Marketing Funds** – Provide an additional 3% coop marketing fund to help catalysts participate in local events or activities that assist in identifying new customers. That 3% should be matched by the same amount from the catalyst in order to ensure that the money is spent wisely. The 3% should be based on the revenue that the catalyst generated for you as a vendor.

This model may not work with established consulting firms or VARs, but those cases they may not be a good fit anyway.

Training – Don't make the mistakes of the "old world" and charge your partner for training. Provide at least quarterly webcasts and try to train your catalyst team as well and as often as you possibly can. Catalysts will assemble best of breed solutions for their customers and they will recommend what they know best. Focus training on the business process and usability side since the catalysts will focus on that with their customers.

Partner Programs – Well-structured partner programs are an essential component of a partner strategy in general and with catalysts in particular. Rewarding partners for high levels of engagement is a natural behavior and should be applied to catalyst partners the same as to any other partner. One good practice is to reward based on the number of deployments. Gaining initial market share is critical because much of the growth in SaaS business comes from growth of existing customers. This reflects the ability to execute, build repeating processes and grow market share. This reward, blended with a second component, customer satisfaction, gives the reward not only a deeper meaning, but it drives the most important behavior in SaaS – more satisfied customers.

Services Demarcation – We suggest that vendors and partners have a very clear understanding of who provides which services and where those services interface. At least in emerging companies, the vendor is much more concerned about not satisfying a customer than it is about losing a partner. In order to reduce this as a potential conflict, it is important to draw a "Service Map" that shows the service flow and the interfaces between the parties. As an example:

- ▶ **Deployment** – The vendor releases the application to the customer, provides user ID and password and confirms the availability of the service. Any configuration of the system is then done by the catalyst. The catalyst is educated enough to fully understand the application.
- ▶ **Integration** – The vendor helps with integration up to the interface level and data definition. The catalyst acts as a project lead between vendor and customer. Any technical work in integrating two SaaS vendors is done by the vendors, unless the catalyst has acquired the necessary special skills. Helping the customer move data back and forth can be done by the catalyst.
- ▶ **Training** – The catalyst provides all training to the customer. If the vendor prefers to handle the training, that may be the rule of engagement – but it should be clear from the beginning.
- ▶ **Support** – The catalyst is the first line of support. The catalyst should be equipped to verify whether a system is down, a bug is identified or the situation is a usage issue.
- ▶ **Additional Services** – The vendor should maintain a close relationship with the customer and offer them additional features or functionality.
- ▶ **Joint service log** – It is a good practice for vendors and partners to share their experience and activities with their joint customers in order to ensure that both parties know what is going on. If a vendor and partner have to worry about competing with each other, that will poison the relationship.

Joint Marketing & Sales - Once a relationship (and more importantly trust) is established with a catalyst, joint selling and marketing become very important. Providing sales leads to the catalyst partner can offload at least some of the vendor's sales organization and leverage the partner, while the partner can grow their business based on those leads. On the other hand, as the number of catalysts grows

into the hundreds, and even thousands, it will be important to understand on what kind of deals each partner is working, so a central deal registration may be important. Supporting partners with marketing funds is key in the joint engagement for more market share.

Once you go international with your product, partnerships will add not only better reach in sales, but provide better services for your overseas customers.

Channel Conflict – As we stated in the first paragraph, channel conflict is the biggest obstacle in any channel strategy in any industry. Companies in all industries lose more money and efficiency from channel conflict issues than any other corporate issue. If a direct sales team believes in competition, then we suggest you remove all structures and let the internal sales people freely compete against each other. If that is structured properly, you can then put the channel in place. If that it doesn't work, act with the channel accordingly.

Don't "try" indirect business models. Once a partner community is burned, it is very hard -- and costly -- to recover. Do it right the first time. This doesn't mean that you can't change and enhance your partner programs, but it does mean that once you decide to leverage a channel model you need to stick with it and make it work.

Leadership – A channel strategy, like any other go-to-market strategy needs to be endorsed by the CEO of the company. If the leadership team is not behind the channel strategy, our advice to the catalyst is to not engage unless the strategy is clear and public. As part of the strategy, put a C-level member in charge of partner management who can ensure the prevention and resolution of any channel conflicts.

CONCLUSION

In the early days of SaaS, legacy software channel partners were not providing adequate value and some people even argued that "we flip a switch and the application is live, we don't need a middle man". Today, that picture has changed. Even though an application may be simple to use, it is an organizational challenge to agree on ways to use a certain it, to configure it to match the processes of an organization and, most importantly, to integrate those applications into other existing and new applications that satisfy the needs of an organization.

In order to economically provide implementation and integration services, smart vendors leverage partnerships with deep business domain expertise in the respective verticals. Such partners are not "resellers" in the sense of the traditional IT industry, but companies or individuals who are able to catalyze the new industry by providing local services and consultancy.

Today we see that not only is there a place for partners, the SaaS industry may actually provide more partner opportunities than the traditional IT industry ever has. Given the roughly 14 million small and medium businesses in the US alone that may not have purchased any business software because of their size, SaaS will provide the technology for them and hundreds of thousands of potential implementers may provide the consultancy. Vendors will need to work with those kinds of partners in order to address the huge market potential. Partners will need to align with those new SaaS vendors in order to develop a symbiotic relationship of expertise of business processes and application functionality.

About SIIA

The Software & Information Industry Association (SIIA) is the principal trade association for the software and digital content industry. SIIA provides global services in government relations, business development, corporate education and intellectual property protection to more than 750 leading software and information companies. For further information, visit www.siiia.net.

About the Author

Axel Schultze is a serial entrepreneur, visionary and innovator. He is one of the pioneers of large distribution channels and also of the Software as a Service Industry (SaaS). Axel is currently the CEO of Xeequa Corp. and responsible for all aspects of the company management. Xeequa is the result of his experience with alliance channels and Software as a Service on one side and his networking nature on the other side. Within just a few years he became one of the best connected executives in Silicon Valley (See LinkedIn). His vision for Xeequa is to make it the company that made "cross company collaboration" easy and seamless for all kind of business people.

In 1983 he founded Computer 2000 which became the largest European computer distributor, the third largest in the world. In 1996 he founded Infinigate which became one of the largest Internet Solutions providers in Europe. With his experience in indirect channels he moved to Silicon Valley and founded BlueRoads Corp. in 2001. He successfully raised 3 rounds of funding and created the most successful Software as a Service based Channel CRM Company. He invented a new method of lead distribution and was granted a patent by the US Patent Office in 2006. After 5 years experience with Software as a Service, he and his partner Timothy Chou (former president of Oracle on Demand) created Tanooma, the first vendor independent SaaS community to search and find Application and people in the SaaS industry.

Axel is also author of the book "Channel Excellence", which will be published in 2007. Axel has a degree in Electrical Engineering from the University of Stuttgart.

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