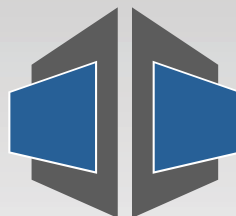


# 5 Steps to Successful ERP Selection



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# Introduction: Don't Jump from Business Pains to an ERP Remedy

Typically, a company approaches ERP when its ailments are causing it to suffer unbearable pain. In most cases, unbearable pain becomes manifest through some combination of business process inefficiency, reporting opacity, and exposure to excessive risk.

Companies generally set themselves up for project failure when they search for an ERP system with a narrow focus on solving acutely painful ailments. Ultimately, they omit consideration of less obvious needs - ones that might not be causing evident pain but are nonetheless critical to business operations.

The first major point to note is that ERP is not a localized solution for a localized problem. It is a broad and far reaching solution that touches all four corners of a business. The purpose of ERP is to unify a company's various business functions in a common transactional and data processing environment. By committing to ERP, a company stands to benefit from the software to the extent that functionality aligns with business needs. However, ERP can be a double-edged sword. When software functionality is incapable of supporting business needs, it can cause inefficiencies, bottlenecks, and the accrual of unanticipated costs.

## A Case Study on the Wrong Approach to ERP

**Business model:** Wholesale distribution to big-box retail

**Current pain:** Repeated penalties of 3% of revenues for late deliveries

**Perceived cause of current pain:** Cumbersome and error prone inventory management processes

As a supplier to big-box retailers, this company is subject to revenue penalties for failing to meet a prescribed four day delivery window. Further, its big-box customers require shipment of complete orders. Partial orders are not accepted. The company's already thin margins are being further eroded by reason of its consistently late deliveries. Further, a customer that accounts for 80% of its order volumes is threatening to revoke the company's preferred vendor status.

The company identified inefficient inventory management processes as the culprit. Currently, inventory receiving and movement data are transcribed on paper, and entered into a standalone inventory management system at the end of each day. However, inventory is oftentimes received the same day it is needed to meet delivery obligations. This delayed recording causes system inventory records – from which order fulfillment is planned - to be out-of-sync with actual inventory statuses.

Ultimately, the company went to market and acquired an ERP system that supported real-time warehouse data collection. During implementation, however, the company learned that the system couldn't support its transportation planning and container loading requirements. After significant investment and business disruption, the company merely shifted a bottleneck from one part of its distribution operations to another.

# Tip #1: Start Your ERP Selection Project...without ERP Selection

Our case study drives home the following point: although particular business pains might trigger a need for ERP software, the focus of ERP evaluations shouldn't be narrowly focused on those pains.

Further, a company shouldn't confuse an identified pain with a requirement that's defined with sufficient particularity for ERP evaluation purposes. For example, a manufacturer might know that it has a problem with cost control. If it were to approach ERP vendors with a general "costing pain", each vendor would probably say that its software supports costing. Although the answer might appear to be satisfactory, relying on it could lead to an ill-advised ERP investment decision.

What would happen if the company is an engineer-to-order manufacturer with a project costing need, and the software it chooses only supports standard costing in a repetitive manufacturing environment? In this case, the company would have emptied its chamber acquiring and implementing a system that couldn't solve its costing pains.

Ultimately, our manufacturing company went wrong by not defining its requirements with a sufficient degree of specificity before going to market.

ERP selection is not rocket science. Relatively speaking, it's mere child's play when compared to the complexity of ERP implementation. Nonetheless, the volume of ERP projects that fail because of poor selection decision-making continues to astound. Picking the right system, the right vendor, and the right service providers are fundamental, baseline, non-negotiable project success factors. If a company can't do these properly, it probably won't realize projected ERP and organizational benefits.

Thus, the starting point for ERP selection is an internal due diligence process designed to discover ERP requirements.

# Tip #2: Internal Due Diligence - Defining Project Feasibility and ERP Requirements

Internal due diligence can take several forms. Two of the most common are described in the following chart:

Internal Due Diligence Form	Description	Sample Critical Elements
<p><b>Feasibility Assessment</b></p>	<p>This form of assessment is intended to justify investment decision-making. In effect, it is used to support a go/no-go project decision.</p>	<ul style="list-style-type: none"> <li>• Ability to support total cost of ownership and cash flow impacts</li> <li>• Determination of whether return on investment and other quantifiable analyses justify an investment</li> <li>• Assessment of non-quantifiable benefits of ERP against associated risks</li> <li>• Assessment of human resource capacity to support Implementation</li> <li>• Determination of organizational support and capacity for change</li> </ul>
<p><b>Business Requirements Assessment</b></p>	<p>This form of assessment is intended to define the collection of business requirements for ERP.</p>	<ul style="list-style-type: none"> <li>• Corporate growth objectives and business models</li> <li>• Reporting requirements</li> <li>• Business process analysis, including:               <ul style="list-style-type: none"> <li>a. Business process maps</li> <li>b. Core, non-negotiable requirements</li> <li>c. Performance improvement requirements (gaps, issues, and opportunities)</li> </ul> </li> <li>• Internal control and risk management requirements</li> <li>• IT and technological requirements</li> </ul>

Although feasibility and business requirements assessments are treated separately above, they're oftentimes undertaken during a common internal due diligence phase. In both cases, an effective assessment requires an understanding of ERP capabilities, and how those capabilities are likely to be translated into benefits, costs, and risks given a company's particular circumstances.<sup>1</sup>

<sup>1</sup> This should not be interpreted to mean that an understanding of any ERP solution in particular is required. In fact, it is generally premature to consider specific ERP solutions, with the exception of assessments that include a performance analysis of legacy ERP software.

## Tip #3: External Due Diligence - Evaluating ERP Alternatives

Once a company has determined project feasibility and defined its requirements, it's ready to go to market. By this juncture, it should have a formally defined and precise set of requirements that it can use as a foundation to evaluate ERP vendor candidates.

By anchoring evaluations in actual business and technology needs, a company can position itself to perform meaningful apples-to-apples comparisons. It also becomes far less susceptible to "sales bias". "Sales bias" is a process by which an astute sales person can influence a sales cycle in a way that may not inure to a buyer's benefit.

The tricky part of external due diligence is devising an approach that drives the following three objectives:

1. Effectively communicating actual business requirements to vendors;
2. Enabling methodological and meaningful evaluations; and
3. Establishing fail-safe processes to guard against false-positive results.

Generally, there are a handful of discrete due diligence components. Each component has strengths and weaknesses, and each creates risks of false positives. For this reason, a company shouldn't restrict its efforts to any single component. Instead, it should undertake as many as possible with a view to performing a full 360-degree assessment that mitigates risks of making a poor decision. The following chart breaks down four typical due diligence components, together with a description of benefits, risks, and best-practices relating to each:

Due Diligence Component	Description and Benefits	Key Risks	Sample Best-Practices
<b>Written Questionnaires</b>	Enables a broad and detailed discovery of capabilities, including: functionality, reporting, pricing, and technology	Written responses are not necessarily indicative of true systems capabilities  Usability is difficult to assess	Provide context through a description of actual business goals and business models  Link the questions to actual process maps to provide a visual representation of requirements, gaps, issues, and opportunities
<b>Software Demonstrations</b>	Enables a deep-dive “test drive” of how a software handles requirements  Provides an opportunity to assess usability	Not all processes and requirements can be tested  Demonstrations do not replicate actual operating conditions, including transaction volumes and system responsiveness	Demonstrate a full order cycle before diving into idiosyncratic requirements  Manage demonstrations according to detailed scripts of non-negotiable and idiosyncratic requirements using actual company data  Involve key departmental users
<b>Referencing Customers</b>	Provides an opportunity to obtain actual use-case feedback relating to system functionality, performance, implementation, and support	The sample might not be representative since vendors typically provide positive references  References are not suitable for deep and broad analyses of functionality	Develop detailed requirements to ensure that referenced companies are substantially similar in business models, processes, and other requirements  Develop detailed reference scripts
<b>Interviewing Implementation and Support Resources</b>	Provides an opportunity to assess expertise and culture fit.	Barring specific contractual obligations, it is often difficult to ensure interviewees will be assigned to a company’s account  Does not cover functionality and technology requirements	Develop detailed interview scripts covering methodological approaches and typical business scenarios

## Tip #4: Contract Negotiations - Don't Get Shackled by the Legal Mumbo-Jumbo

Don't ignore the legalese contained in the ERP agreements. These agreements will ultimately have a material impact on the parties' rights, duties, and obligations over the course of the relationship, which will probably last longer than 10 years.

Companies would be well advised to understand each term and condition, and how each might come to bear in a real-world scenario. In general, there are three substantive agreement categories, as follows:

1. **Software Licensing or Subscription:** The terms and conditions herein define the parties' rights, obligations, and exposures to liability associated with software use.
2. **Maintenance and Support:** The terms and conditions herein define the parties' rights, obligations, and exposures to liability with respect to ongoing product maintenance and support, including: service level obligations, bug fixes, patches, updates, and upgrades.
3. **Services:** The terms and conditions herein define the parties' rights, obligations, and exposures to liability associated with the provision of services, including implementation and related technical services.

When reviewing ERP contracts, companies should consider whether the structure of the deal reflects their interests. In so doing, they should remember that they're the ones accepting the financial obligations and assuming the ERP-related risks. To the extent that they're not comfortable with the terms, they should seek negotiated concessions. In many cases, negotiations can include one or more of the following four subject-matter areas:

- Financial obligations, including short term, long term, and contingent obligations;
- Service-level obligations, including a clear definition of responsibilities and service requirement triggers;
- Performance obligations, including mechanisms to promote successful projects; and
- Legal, including fair and equitable warranty provisions and limitations to liability.



# Organizational Change Management - What it Means and Why It's Important NOW

Organizational change management refers to the process of managing human resource transition from an existing state to a desired future state.

The human capital side of an ERP project is oftentimes the most difficult to manage. Stakeholders at every level –from the top-floor to the shop-floor - are likely to have certain interests that conflict with ERP project success. Many will resist a project for various reasons, including:

- Fear that their jobs will become redundant or replaced by software;
- Fear of losing top company performers to the implementation project teams;
- Fear of learning new job tasks and working with sophisticated technology; and
- Fear that company performance dips<sup>2</sup> may negatively impact compensation or reviews.

Securing project buy-in and managing resistance to change are critical to the success of every ERP project. Companies should initiate organizational change management initiatives at the earliest opportunity. During ERP selection, a company can take the following three proactive steps:

- Obtain senior executive commitment that the project is a leading business priority. By doing so, the executive committee is sending a message that the project takes precedence over other initiatives that compete for limited company resources. To ensure that the commitment is lasting, it is important for the executive committee to fully understand the associated costs and resource obligations.
- Involve key departmental users in the software demonstrations phase. Involving key users in the evaluations process is likely to secure a measure of buy-in, regardless of whether the ultimately selected software accords with any individual preferences.<sup>3</sup>
- Provide basic ERP training with a focus on the benefits. Stakeholders oftentimes resist because they fear technology, the unknown, or a combination of the two. Providing high-level ERP training is an effective way to conquer those fears. It changes the “unknown” into something tangible. The training can be made even more effective if the benefits are related to the day-to-day jobs of affected employees. During implementation, employees will be asked to make sacrifices. They want assurances that there's a payoff for them.

<sup>2</sup>A company should understand that performance is likely to decline both during and immediately after implementation. However, if implementation is successful, performance should improve markedly by the medium-term.

<sup>3</sup>Provided that a decision that runs counter to key user preferences are rational, supported, and well-articulated.



# Conclusion

In the final analysis, companies should treat ERP selection as more than a quest to heal existing business pains. Although pain might be an initial catalyst, they should approach the project as an initiative that has organization-wide benefits – including transaction processing, decision-making, and risk management.

When a company ultimately decides to engage in an ERP selection project, it should strongly consider the following five-step methodology.

1. Don't evaluate ERP vendors before defining requirements
2. Undertake thorough internal due diligence to define business requirements
3. Undertake structured, multi-dimensional external due diligence to evaluate vendors
4. Negotiate contract terms to balance financial and risk obligations
5. Implement change management efforts as early as possible

This methodology will help a company drive ERP project success and, more importantly, the achievement of long-term business objectives.

Good luck with your ERP projects!

# About the Expert

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Pemeco is a leading vendor agnostic consulting firm that specializes in business requirements assessments, ERP selection, ERP implementation, and ERP optimization. Jonathan helps manufacturing and distribution clients leverage enterprise software technologies to optimize their business operations. Jonathan is also a part-time MBA professor of systems analysis and design at the Schulich School of Business at York University, Canada's #1 ranked MBA program according to The Economist Magazine.