

4 Key Cost Driver Categories for Evaluating ERP Vendor Proposals

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ERP implementation costs can vary based upon scope, project team structure, implementation strategy and commercial model. Sourcing, procurement and vendor management leaders must review their vendor proposals against the attributes under the four key cost drivers to optimize their spend.

Overview

Key Findings

- Many organizations struggle with developing a clear scope, budget, service and solution requirements, and commercial expectations, resulting in poor vendor response on RFP and lack of details, which contribute to scope creep and higher costs.
- Most ERP implementation statements of work (SOWs) in vendor proposals lack accountability of tasks (using a responsible, accountable, supporting, consulted and informed [RASCI] framework) and omit critical roles and workstreams such as program management, design authority and organizational change management (OCM). This makes it difficult to understand and validate the costs included in a fixed price implementation bid.
- Unclear implementation expectations in the client's RFP allow vendors to make assumptions about the deployment strategy to make the bid attractive so the client selects the lowest bid. Subsequently, this creates additional scope changes postcontract, impacting budgets and delivery timelines.
- Many clients use incorrect contracting models lacking clear deliverables and acceptance requirements aligned to KPIs and holdbacks, which moves the risk of delivery quality and timeliness to the client while the vendor continues to be paid for poor performance.

Recommendations

Sourcing, procurement and vendor management (SPVM) leaders who source IT services and solutions for ERP implementations should assess supplier proposals in these four cost-driving categories:

- **Service and solution requirements:** Target standardization by ensuring that the defined architecture principles and standardized out-of-the-box (OOTB) functionalities for the ERP solution are offered. Certify that any complementary enhancements and integration needed for the solution are clearly defined and meet the associated business case.
- **Project team structure:** Ensure accountability by validating that the workload split between client versus system integrator (SI) is adequate for the complexity of the project and the staffing mix is appropriate for the type of implementation (e.g., upgrade versus business transformation).
- **Implementation strategy:** Validate that the implementation cost follows the recommended cost split per project phase. Avoid incurring additional costs by ensuring that the rollout strategy takes into consideration the impact and dependencies with other projects and that the deployment assumptions are aligned across business functions.
- **Pricing and commercial components:** Mitigate risks by utilizing the appropriate contracting model, and align quality and the delivery timeline through holdbacks and bonus structures to incentivize delivery.

Strategic Planning Assumption

By 2024, 80% of ERP implementations without full cost estimates will fail to achieve business value, up from 59% in 2020. ¹

Introduction

Organizations are embarking on digital transformation programs that require them to upgrade their on-premises ERP solutions and move to cloud-based solutions and composable application architectures to meet business outcomes. Clients do not have a good understanding of the cloud ERP solutions and the functionalities offered, so they leave the solution design and deployment to the SIs, resulting in fixed price proposals that lack details and build many assumptions. This leads to scope changes, delayed project delivery, and ultimately, higher costs.

If unable to understand the underpinnings of a fixed price proposal, SPVM leaders risk selecting the wrong partner or tend to select the lowest price bid. They may compare bids with different deployment strategies and project team structures that are not aligned, with many key cost components missing. Nearly 60% of Gartner’s application implementation proposal reviews are ERP implementations where clients ask analysts to benchmark the proposed fixed price and timeline with insufficient details. ² Gartner also gets many requests to provide budget-planning numbers for ERP implementation. As every implementation is unique and depends on clients’ current and future desired outcomes, Gartner analysts cannot validate fixed price costs without understanding all the cost category details.

This research note and attached slides provide the key attributes in the four key categories which drive cost in an ERP implementation (see Figure 1). This knowledge will allow you to ensure that the RFP requires vendors to provide these details, so each vendor’s proposals are transparent enough to be assessed for cost and timelines for your specific requirements. Using these attributes across the four key categories can also allow you to develop a reasonable budget for your ERP implementation, mitigate major risks in the program delivery and unearth assumptions made in the RFP.

4 Key Cost Driver Categories for Evaluating ERP Vendor Proposals

Figure 1. Four Categories of Cost Drivers

Four Categories of Cost Drivers



Source: Gartner
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Analysis

Service and Solution Requirements: Define Principles and Functionalities

Solution gaps are not usually detailed enough in the beginning of each ERP release, nor is there a good baseline in terms of the number and complexity of all reports, interfaces, conversions, enhancements, forms and workflows (RICEFW). Interfacing multiple applications is one of the highest risks, and frequently, API integration standards, conversions and enhancements are responsible for considerable cost increases if not addressed upfront.

Ensure Business and Functional Scope Are Aligned to Best Practices

One of the main drivers for ERP customizations is to enable differentiation in your business, which underscores the importance of defining the architecture principles for the overall ERP implementation. Some examples include:

- Using standardized functionalities and best practices
- Using standard processes that will be used by all business units and entities versus line of business (LOB) or affiliate-specific configuration templates
- Looking for potential “fit-for-purpose” application components in focused areas where ERP is not a good fit
- Reducing impact versus driving transformation for the business, cost containment versus driving a competitive advantage

Recommendations:

- Confirm that deliverables and project assumptions are clearly defined in the SOW and aligned to business requirements.
- Verify that enhancements needed for the solution and add-ons to cover specific business or legal requirements are aligned to the complexity split (see Slides 7 to 9 in the accompanying PowerPoint attachment).
- Validate that ERP implementation assumptions are within the range presented in Slides 3 and 4. In case there is a need for customization, you should perform a cost-benefit analysis to determine if the planned customization is aligned to the target operating model and providing your company a competitive edge.

Project Team Structure: Identify Clear and Effective Team Structure

The team structure enables the project to define roles and responsibilities of the SI, client teams and other third parties within each workstream, and also helps manage the impacts and dependencies with other projects.

SOWs provided in the vendor proposals don't usually clarify the ownership of deliverables and overall program management, which moves the project quality and delivery risks to the client. SIs do not take this responsibility by default, unless clearly documented and sufficiently incentivized in the contract. Therefore, it is essential to have a well-designed program to work efficiently. A clear and effective team structure with defined roles and responsibilities should always include steering entities, decision-making entities and the relative contribution of IT, business and the program management office (PMO).

Recommendations:

- Use workstreams in the scope of the project, and verify that the sponsorship and delivery roles are according to the core team structure of typical implementation programs and have a lead for each workstream (see Slides 12 to 14). Typically, a standard project management structure represents 14% to 18% of the overall program cost. If your vendor's proposal has less than this for project management, they must be expecting that you will do a lot of these activities, not them.
- Confirm that the service provider is responsible for the overall program management or any other additional activities such as change impact, readiness assessment, organizational impact and design, process reengineering, master data governance, infrastructure, and security. These activities require additional external implementation leads and teams in the program and usually represent an increase of 7% to 25% of the total cost.
- Ensure that the lead roles from different delivery locations and the governance between onshore and offshore are defined in the contract (along with defined processes) to efficiently manage the interactions. If the project is delivering transformational benefits dependent on full adoption, you will likely need to set up specific workstreams for organization change management and other technical activities such as data analytics and reporting. This needs to be included in the overall cost of the proposal (see Slides 13 and 14).

Evaluate Client Versus SI Responsibilities for Both the Interfaces and Data Migration

Data migration and integration are usually in the critical path of an ERP implementation program and could represent up to 40% of the total implementation cost.

Recommendations:

- Agree on a RASCI table with the service provider to clearly define the tasks, roles and accountabilities for the client and provider and/or third parties in each phase. Sometimes the responsibilities in the RASCI are presented at a high level and could be misleading for data migration and integration activities. In this case, there is a risk of poor data quality, scope creep and project delay. For example, data migration typically requires different parties responsible for different tasks, such as data quality audits, data extraction from legacy systems, data cleansing, data mapping and transformation, and loading the data into the new system.
- Agree on a RASCI table to define the tasks, roles and accountabilities for integration, i.e., the implementation of all required interfaces between the new ERP system and persisting legacy applications (e.g., CRM, human capital management, supply chain management, e-commerce, finance and digital business applications). The number of integrations to achieve end-to-end results is a key cost driver and is often overlooked as SIs will not assume responsibility unless you point out the full ecosystem that the new ERP needs to coexist with.
- Ensure project assumptions and dependencies are aligned to the cost drivers and type of project (see Slides 7, 8 and 19). In addition, a most cost-effective integration architecture can help control integration costs (both implementation and ongoing support). If there are gaps, they must be negotiated and resourced prior to signature.

Implementation Strategy: Establish a Strategy That Is Driven by Business Cases

The risk of incurring additional costs to complete performance of the project should fall on the service provider. If completing the scope of work and producing the deliverables takes more effort or cost than your service provider budgeted, you shouldn't pay any more, except through mutually agreed change orders. However, in reality, the service provider may cut corners by switching to lower cost resources, planning less effort in some areas, or other similar tactics. This can result in quality deficiencies and additional project risks, or even inadequate roles in the project. To avoid the risk of scope creep, it is critical to ensure the proposal clearly states the volumetrics, deliverables and release strategy that the estimation and timeline are based on.

Recommendation:

- Ensure you have identified the type of ERP implementation you are pursuing as that approach will directly impact the implementation cost. For example:
 1. A new implementation should be planned when a company wants to eliminate custom developments built in its legacy solution. This deployment approach typically involves a higher degree of organization change management, data rationalization, migration and integration.
 2. A system conversion upgrade is when business stakeholders prefer to have minimal changes for how they use ERP transactions, resulting in the retention of most existing customizations.

A new implementation could cost twice as much as a technical migration, and just organizational change management (OCM) could represent 30% of the overall cost of the ERP implementation (see Slides 13 to 14 and 18 to 19).³

Identify the Go-Live and Rollout Approach

Go live approaches offered in vendor proposals must be reviewed carefully as they may increase costs. Deployment approach significantly impacts cost (e.g., deployment by country, business unit, etc.). The number of rollout phases and waves impacts testing, cutover activities and the overall duration of the program, which is a significant cost driver for ERP proposals. You must clearly articulate the SI role across phases and waves/releases. We see a huge variation in SI ERP implementation pricing because of different assumptions competing SIs are making. A technical migration typically has one to three waves, while a new implementation usually has more waves (five on average).

Recommendations:

- Conduct an assessment of the implementation strategies to minimize business and IT architecture risk and cost; and maximize speed to benefit. This assessment should be performed in the planning and scoping phase of the ERP program through a series of business and technical workshops where the following topics are tested and validated with stakeholders:
 - What are the key components of the new ERP solution, and how close is the fit to business requirements?
 - What are the key gaps and how are they resolved?
 - How should the ERP modules and business processes be implemented (e.g., a three- to five-year roadmap addressing key business priorities and drivers)?
- Confirm whether or not the service provider is planning any go-live contingencies. The rollout approach should take into consideration the number of countries, application modules, operating companies and business units. Assumptions about regression testing, acceptance criteria and go/no-go KPIs for future releases should also be agreed on as the basis for the overall implementation effort and timeline (see Slides 7 and 16 to 19).

Commercial Components: Link Pricing and Effort to Deliverables

Incorrect SI selection or misrepresented client effort and participation can lead to inadequate client resources and effort to perform all activities that the SI assumed in their proposal (e.g., requirement analysis, functional specifications, user acceptance testing, data cleansing, integration on the legacy side, etc.). As a result, assumptions that certain activities will be completed by the client might be in the critical path of the program. This leads to project delays, misalignment in terms of roles and responsibilities with SI, and the need to contract extra consultants to the ERP program. Thus, defining clearly the implementation cost and effort by deliverable, as well as who is accountable, is critical to success.

Recommendations:

- Validate that the SI staffing pyramid and planned localization split of SI resources across project phases are aligned to the complexity of the ERP implementation (see Slides 21 and 24 to 26). The main risks of the program should also be considered, and contingencies should be factored into the overall cost to mitigate key risks (Slide 27).

- Always require effort hours and fixed price in the proposal be broken down by deliverables per phase within a workstream, and ensure that the proposal clearly identifies which party is accountable for the delivery. This allows you to connect these deliverables to holdbacks and incentives in the contract.
- When contracting for such complex implementations, consider a managed service contracting model where the SI has the control and accountability to deliver. Staff augmentation models leave all the risk to the clients as the vendor has only committed to delivering the qualified “bodies” requested and assumes it’s the client’s responsibility to manage them and the tasks they are assigned.

Organizations seeking budgetary information for their ERP implementations should use these four key categories to review the potential implementation costs. Most of this process will take place after the ERP software has been selected. This analysis does not attempt to include costs for application software, hardware, system software, networking technology, third-party development software, or PCs and peripherals.

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Evidence

¹ [Ahead of the Curve: Forging a Future-Focused Culture](#), Project Management Institute.

² Of the total number of Gartner application services inquiries related to proposal reviews between 2019 and 2021, 60% were for ERP implementations. Analysts are often asked to explain the difference in implementation proposals costs and how to identify what is driving the costs.

³ Data based on Gartner interactions with clients, specifically in the context of ERP implementation.

Recommended by the Authors

Some documents may not be available as part of your current Gartner subscription.

[Tool: 10-Step Checklist to Review Implementation Services Proposals](#)

[Validate Oracle Cloud Implementation Service Proposals](#)

[Strategic Sourcing Guide for SAP S/4HANA](#)

[Tool: IT Services Labor Rate Calculator](#)

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