

Sage ERP

Why Implement a Two-Tier ERP Strategy



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Executive Summary

Well-run, global organizations are increasingly adopting a two-tier enterprise resource planning (ERP) strategy. With such a strategy, organizations keep their existing Tier-1 ERP solution to run common processes, such as financials, at the corporate level and give subsidiaries a Tier-2 ERP solution to address their specific requirements with greater flexibility, agility, and improved manageability at a lower cost. This white paper details the benefits of a two-tier strategy, the types of organizations most likely to benefit, and what to look for in an ERP solution to implement this strategy.

The Growing Popularity of the Two-Tier ERP Strategy

Organizations in the market for ERP solutions are increasingly considering a two-tier ERP strategy. A recent study by Constellation Research found that 48% of buyers in 2011 were considering a two-tier strategy, up sharply from 32% in 2010 and 27% in 3Q09.¹ Similarly, Ventana Research from 2010 found that one-third of companies with more than 1,000 employees use an ERP supplied by a single vendor, while two-thirds use software from two or more vendors.²

What Is a Two-Tier Approach?

According to Gartner Research, organizations typically choose from six common global deployment options for ERP when they have a central administrative ERP system, as shown in Figure 1.

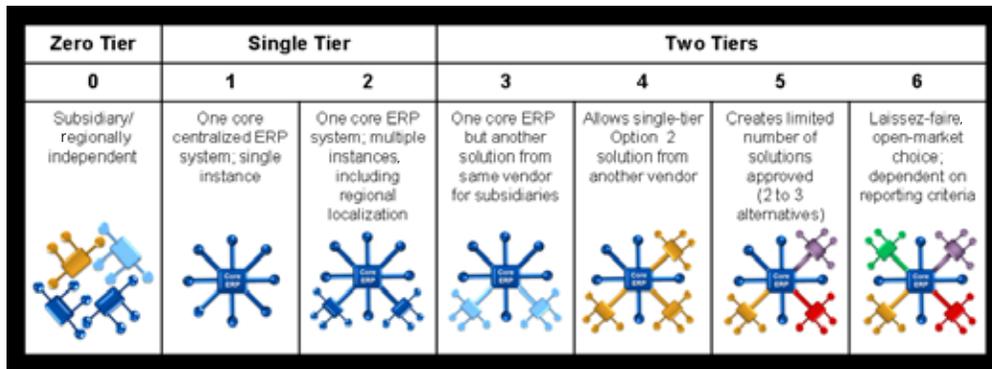


Figure 1. ERP Deployment Options³

In a two-tier ERP deployment approach, organizations keep their existing Tier-1 ERP systems at the corporate level while allowing divisions or business units to select a second ERP system. The Tier-1, corporate ERP system acts as the global standard for running processes that must be standardized across all divisions, such as financials, human resources, and procurement. The secondary, Tier-2 ERP system supports the specific needs of subsidiaries, usually for smaller operational requirements such as sales, marketing, field services, or local manufacturing. As Figure 1 shows,

A recent study by Constellation Research found that 48% of buyers in 2011 were considering a two-tier strategy.

1 R "Ray" Wang, "The Case for Two-Tier ERP Deployments," Constellation Research, March 2011 <http://www.enterpriseiregulars.com/32701/research-summary-best-practices-%E2%80%93-the-case-for-two-tier-erp/>

2 "A Strategic Approach to Establishing Two-Tier ERP," Ventana Research, 2010

3 "Two-Tier ERP Suite Strategy: Considering Your Options," By Nigel Montgomery, Gartner Research, July 28, 2010

the Tier-2 ERP solution can come from the Tier-1 vendor, from a second vendor, or from a list of approved alternatives. Gartner says that the laissez-faire approach is the “predicament” that needs to be resolved with the two-tier ERP approach.

Drivers for Two-Tier Adoption

Two-tier ERP systems began their rise in popularity during the economic recession that began in late 2008. As IT budgets were slashed, IT departments were forced to make do with less. In many cases, large-scale ERP migration plans were delayed or eliminated entirely. Instead of moving to new systems, companies focused on improving existing systems, including legacy ERP applications. As a result, many organizations decided to retain functionality in their existing systems that was still working while migrating to Tier-2 systems where existing solutions were not meeting their requirements.

At the same time, organizations began realizing that big-bang, corporatewide ERP installations are often ineffective. When a system becomes very large, it becomes costly to customize, maintain, and upgrade. Deploying a complex, large-scale ERP solution to a subsidiary is particularly challenging, because smaller divisions may not have the IT infrastructure and experience to customize and support the solution. And because larger vendors have been slow to innovate, there’s a good chance that a Tier-1 system will not offer the capabilities subsidiaries need to improve their competitive advantage. Subsidiaries need a simpler, flexible, yet robust and cost-effective system that delivers the same results while integrating seamlessly with the corporate system.

Today, the economy is recovering, and corporations are once again looking to grow. Nonetheless, two-tier implementations continue to gain momentum. In many cases, subsidiaries are the key to developing new business, especially in emerging markets, such as Asia, Latin America, Africa, and the Middle East. Many companies are therefore creating or acquiring new subsidiaries to move into new product and service areas. This means these operations have power and senior management attention—and need to move quickly. IT needs to accommodate these newfound engines of organizational growth. The simplicity, cost effectiveness, and flexibility of Tier-2 solutions make them ideal for fulfilling these requirements.⁴

Additionally, two-tier ERP is a way to consolidate IT support—and thereby reduce costs—in cases where organizations are unable to adopt a single ERP solution. For example, many organizations have undergone multiple mergers and acquisitions that leave them with multiple ERP solutions—and unacceptable support costs. When such organizations are unable to consolidate to a single ERP system, they are finding an answer to the problem with a two-tier ERP solution.

Who’s Adopting the Two-Tier ERP Strategy?

Many types of organizations can benefit from a two-tier ERP strategy, particularly those with subsidiaries that employ multiple business models, including:

- Subsidiaries with different lines of business. Having one standard ERP makes little sense if one subsidiary delivers services and another manufactures goods.

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⁴ Jim Shepherd, “Two-Tier ERP May Finally Happen,” Gartner, June 14, 2011

- Subsidiaries in different industries. Organizations that make one set of products but sell them to different industries. For example, if the organization makes medical devices, FDA certification can be an onerous task that can be simplified by specialized ERP vendors with validation modules. When selling to the DIY market, however, a subsidiary may prefer an ERP with sophisticated promotion and supply chain capabilities.
- Subsidiaries that provide different functions within the same value chain. One subsidiary may manufacture medication, while another may be responsible for distribution. The ERP processes and localizations would be fundamentally different.
- Subsidiaries in different countries. Global organizations many need smaller, more nimble ERP solutions to meet the needs of local locations, including support for different tax codes, languages, and currencies.
- Acquisitions. Headquarters may acquire businesses to support strategic, inorganic growth initiatives. If converting the acquired company's existing ERP solutions means high costs or timing challenges due to lack of available skills, sticking with the existing ERP solution or putting in a modern, user friendly Tier-2 ERP system that communicates back to the headquarters' Tier-1 ERP system can be a better approach.
- In addition, organizations that want to upgrade and modernize their ERP solutions may wish to keep some legacy systems as they upgrade to more modern systems.

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Benefits of a Dual-Tier Strategy

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Comprehensive Functionality Easily Configurable to Industry and Global Requirements

Tier-2 solutions are available that deliver the same comprehensive functionality available through the Tier-1 vendors. At the same time, the vendors provide industry-specific experience gleaned from the vendor's customer base and the systems easy to customize to meet specific industry or regional workflow requirements.

Reduce costs

Seventy percent of respondents to a recent Software Insider survey remarked that existing, Tier-1 systems are too expensive.⁵ An estimate published by *CIO* magazine in 2009 placed the cost of the average Tier-1 ERP system deployment at between \$13 million and \$17 million.⁶ ROI calculation on Tier-1 ERP systems show that high costs are due to overruns in implementation, customization, maintenance fees, and staff costs. Upgrade costs are also high—45 percent of respondents said that upgrades are too costly.

5 R "Ray" Wang, "Tuesday's Tips: When to go with a Two-Tier ERP Strategy," Enterprise Irregulars, March 2010 <http://www.enterpriseirregulars.com/14224/tuesdays-tip-when-to-go-with-a-two-tier-erp-strategy/>

6 Ron Gill, "The Rise of Two-Tier ERP," Read Periodicals, November 2011 <http://readperiodicals.com/201111/2524027791.html#b>



When all of the implementation, ongoing maintenance fees, upgrades, and modifications are considered, a two-tiered system can offer significant financial savings. For example, Gartner Research found that companies see a 33 percent reduction in implementation costs when a two-tier system is deployed.⁷ As mentioned previously, a two-tiered approach also allows organizations to consolidate IT support resources across the organization, further reducing costs.

Improve Innovation

Companies must continually adapt to new threats and opportunities. Subsidiaries in different corners of the world are often subject to different competitive forces and are compelled to evolve in different directions. Yet 35 percent of Software Insider survey participants found that enterprise-class ERP vendors have not innovated quickly enough. Subsidiaries are finding that they can customize Tier-2 applications more quickly than they can convince corporate to change the global ERP system to meet their local needs.

Greater Agility

Sixteen percent of respondents to the Software Insider survey want more agile systems that can integrate and work with other systems, new channels and emerging stakeholders. Large-scale ERP systems cannot keep pace with a changing environment because they take so long and cost so much to deploy. The unmanaged change results in the need to patch systems, manual processes and chaos.

Tier-2 ERP solutions allow subsidiaries to take more control of their system because those systems are easier to configure. A two-tiered infrastructure can be deployed quickly and cost effectively. The time to implement and modify or upgrade is likely to be shorter, which means that deploying such a system will deliver a shorter time-to-benefit, and these systems can be modified more quickly and easily than a Tier-1 ERP solution.

What to Look for in an ERP Solution for Use in a Tier-Two Strategy

Of course, not every ERP solution is well suited to your organizations requirements for a Tier 2 ERP system. Look for a Tier-2 ERP solution that can deliver comprehensive functionality, flexibility, and low total cost of ownership.

Comprehensive Functionality

Organizations adopting a two-tier strategy need to consider the functionality the tier-two ERP solution delivers. The solution should offer comprehensive, accounting, finance, front-and back-office functionality, and support similar to that found in Tier-1 applications out of the box. For example, it should incorporate business intelligence (BI), rather than requiring organizations to purchase BI separately as an add-on module. Comprehensive functionality makes the solution easily adaptable to a specific organization and allows organizations to avoid heavy customization.

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⁷ <http://www.erpsoftwareblog.com/2012/02/benefits-of-a-two-tier-erp-solution/>

Part of this functionality should include specific support for global subsidiaries, such as multilanguage, multicurrency, multilegislation, and multicompany structure. And the vendor should have expertise in multiple industries and the ability to help the organization configure the solution to the requirements of its industry.

Consolidation of data from subsidiaries or business units into a single folder structure allows organizations to easily roll up data in real-time for rapid reporting. This eliminates the need for time-consuming data reentry, reduces errors, and makes for reliable, coherent data.

Flexibility and Adaptability

Not only should the functionality be comprehensive, functions should be easily configurable so the organization can customize it to meet its specific requirements. The solution should also integrate seamlessly with the organization's existing IT environment, including support for existing databases or operating systems. An adaptable user interface that can be deployed through a Windows® Client or a web browser gives the organization the option to make the system available across the globe without the time, effort and money required to install the system on premise. Users of the browser interface simply log on wherever they may be located. The solution should also be scalable enough to start with ten users and ultimately accommodate thousands of concurrent users.

Low Cost

A Tier-2 solution should be cost-effective and fit into the organization's budget not only initially but over the entire period of ownership. A solution that is robust (so that it doesn't require a lot of support), deployed rapidly, and easy to maintain will reduce overall support costs. An intuitive user interface minimizes training costs. Parameterized configuration simplifies any necessary customization. A system built on a service-oriented architecture will be easy to upgrade and customize while a simple and secure update procedure makes it easy to take advantage of software improvements.

Conclusion

By using a two-tier ERP strategy, global organizations with multiple subsidiaries stand to gain from comprehensive, highly customizable solutions, lower costs, as well as greater innovation and agility than they could achieve using a single, large-scale ERP solution standard throughout their organization. However, they need the right ERP solution. An ERP solution that furnishes comprehensive functionality, is highly flexible and adaptable, and offers robust, easy-to-configure and-maintain functionality that reduces TCO can fully deliver on the promise of a two-tier ERP strategy.

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