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Moving ERP Systems to the Cloud

Trends, Risks and Strategies for Successful Deals

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Speakers

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Mayer Brown's Technology Transactions Practice

More than 50 lawyers around the world focused on helping clients develop and manage relationships with suppliers of critical services and technology

Experience in 400 critical services sourcing deals with a total contract value exceeding $200 billion, including data, digital, outsourcing and software

World leader in facilities management outsourcing

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"Band 1" ranking
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14 consecutive years (*Chambers* 2004-2017)

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Ranked as one of the top law firms 2009 - 2018 on World's Best Outsourcing Advisors list for The Global Outsourcing 100™

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"They have current cutting-edge knowledge and are savvy about attuning their counsel to the needs of the client to arrive at a satisfactory solution to many sticky issues."

~ Chambers USA 2017

"They are very good at being able to communicate and synthesize information in a useful and easily understandable way."

~ Chambers USA 2016

"They're very practical in terms of trying to identify solutions and giving very good advice on areas where it's reasonable for us to compromise or, alternatively, where to hold our ground."

~ Chambers USA 2015

"Their knowledge in this area is tremendous. They know us so well they blend into our deal teams and become a natural extension to our in-house team."
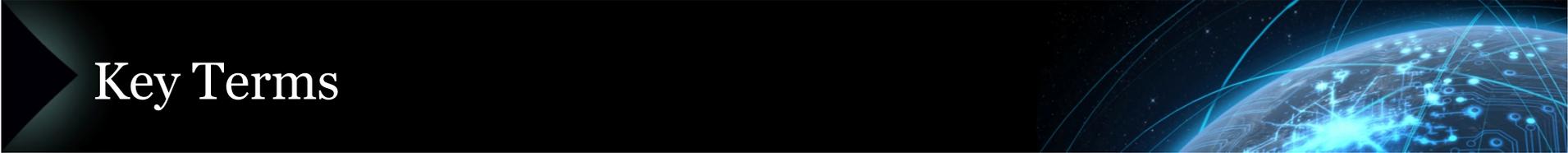
~ Chambers USA 2014
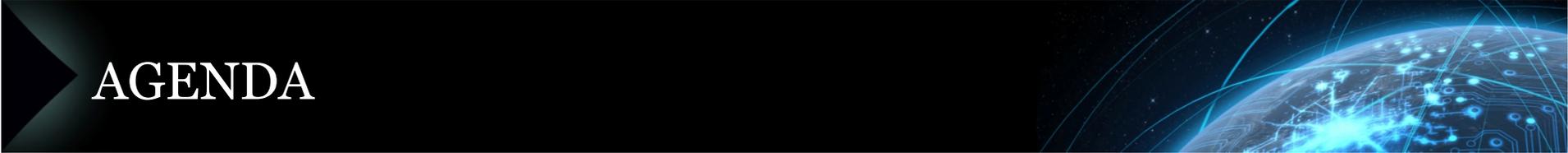
AGENDA

- **TRENDS** in ERP

- **COMPARISON** of on-premise ERP and cloud ERP

- **CLOUD ERP** contracts

- **PREPARING** for cloud ERP adoption

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Part I
TRENDS IN ERP

Key Terms

- **ERP** – Enterprise Resource Planning systems is business process management software that allows an organization to use a system of integrated applications to manage the business and automate functions

- **ON PREMISE** – refers to a business hosting and running ERP software on its own infrastructure or infrastructure managed by a third-party provider for the business – examples include SAP, Oracle, Lawson, JD Edwards

- **CLOUD ERP** – refers to ERP software made available on a "Software as a Service" basis, in which the ERP software provider hosts the software, manages the hosting environment and hosts most of the business's data – examples include SAP, Oracle, Microsoft, and newer SaaS providers, like Salesforce, Workday , NetSuite, Rootstock, IQMS + many others

- **HYBRID ERP** – a structure in which some ERP software modules are On Premise and others are hosted in the Cloud ERP

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Expected Growth in Cloud ERP Adoption

- **2020 OUTLOOK:** 4 of every 10 large organizations will have at least 60% of their ERP applications in the cloud

- **2025 OUTLOOK:** 50% of large enterprises will implement a SaaS strategy to run their core ERP in the cloud

- 38% of organizations are still pursuing a traditional On Premise ERP strategy, but Gartner expects that percentage to fall to 11% by 2019

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How Fast is Your Organization Moving Toward ERP?

LARGE PRODUCT-CENTRIC ORGANIZATIONS	LARGE SERVICE-CENTRIC ORGANIZATIONS
Generally slower adoption of cloud ERP	Generally faster adoption of cloud ERP
2018 Outlook: Only 5% will deploy complex operational ERP capabilities in public cloud SaaS	2018 Outlook: At least 30% will move majority of ERP applications to the cloud
2020 Outlook: At least 35% of new product-centric ERP deployments will be SaaS loosely integrated with on-premises manufacturing execution systems	2020 Outlook: Expected growth in the range of 10% - 15%, bringing the overall adoption rate to around 45% (based on predictions of growth of the cloud ERP market)

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Cloud Adoption Strategies

- Use cloud ERP for smaller divisions or new global deployments

- Significant growth of cloud administrative ERP (e.g., financials, human capital management, and indirect procurement), operational ERP (e.g., demand planning and supply chain procurement), and specialized industry-specific modules and applications (e.g., contract life cycle management)

- Suites from the same vendor may have benefits (e.g., single source, integration), but they may not always represent the best solution for your company's needs

- Approach cloud solutions that provide ERP functionality or that integrate with ERP systems in the same manner as you would approach a larger ERP system

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Part II
ON Premise ERP vs. Cloud ERP

ERP On Premise v. Cloud – Operational Considerations

TOPIC	ON PREMISE	CLOUD
Implementation	Lengthy	Less lengthy, but still requires implementation and integration
Implementation Costs	High upfront costs (infrastructure and license fees)	Lower upfront costs (license fees only)
Customizations	Possible	Very limited, if at all – standardized solution
Ongoing Costs	Investment in expert resources and infrastructure	Less ongoing investment, but beware hidden costs
Change control	Greater control over implementing changes	Less control, or none

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ERP On Premise v. Cloud –Risk Considerations

TOPIC	ON PREMISE	CLOUD
Data Security	Sensitive data in systems controlled by you	Sensitive data in systems controlled by cloud provider
Data Locations	Instances and data locations controlled by you	Instances and data locations controlled by cloud provider
Updates	Ability to control timing of updates and changes	Less or no ability to control timing of updates and changes
Competencies	People with knowledge of systems and operations remain	Less need for people with knowledge of systems
Compliance	Higher ability to manage compliance risks	Loss of some control over managing compliance risks
Performance/Availability	Higher degree of control over availability	Dependent on SLAs from provider

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No One-Size Fits All

- Optimal solution depends on several factors, such as company size, business needs, goals, budget, challenges, and risk appetite

- Migration approach of beginning with particular, limited cloud ERP applications appears to be a common strategy since it allows a company to learn more about, and adjust to, the move to cloud ERP

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Part III

CLOUD ERP Contracts

Contracting Structures & Related Challenges

STRUCTURES:

- Contract for new scope not covered by existing ERP

- Contract to move part of existing ERP scope to cloud with remainder staying on-premises

- Contract to move entire existing ERP scope to cloud

CHALLENGES:

- Cloud contract will be markedly different

- Limited ability to leverage on-premises ERP license terms for cloud contract

- Change of on-premises ERP scope will require renegotiation of on-premises license agreement

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Certain On-Premise and Cloud ERP Issues

DEFINITION OF USE

- Rights to use ERP system for acquired and divested businesses or companies

**DEFINITION OF USERS AND OTHER METRICS THAT SERVE
AS A BASIS FOR CALCULATION OF LICENSE OR SUBSCRIPTION FEES**

- Right to expand permitted users beyond company enterprise (third-party contractor use, use by consultants on behalf of company, use by suppliers, etc.) and license fee calculation by "users"
- Right to withhold disputed fees pending resolution

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Certain On-Premise and Cloud ERP Issues

SAP UK Limited versus Diageo Great Britain Limited (ruling on February 16, 2017)

- **FACTS:**
  - Customer licensed mySAP Business Suite (including mySAP ERP) and   SAP PI engine
  - Customer integrated two Salesforce.com-based systems with mySAP ERP via the SAP PI engine
- **RULING:** Additional license and maintenance fees apply to use of Salesforce.com-based systems. All users of those systems need Named User licenses

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Certain On-Premise and Cloud ERP Issues

- Indemnity protections

- Liability limitations

- Limitation of vendor's right to terminate agreement or services

- Continuation of rights during contested terminations

- Protection against disruptions upon any termination or expiration of ERP use rights (e.g., ramp down rights)

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Cloud ERP Raises New Issues:
Service-Related Issues

- Protections against vendor's right to unilaterally change terms of service ("floating terms")

- Multiple layers of documentation make order of precedence very important

- Vendor service level commitments and penalties for failing to meet those commitments

- Vendor right to suspend delivery of services

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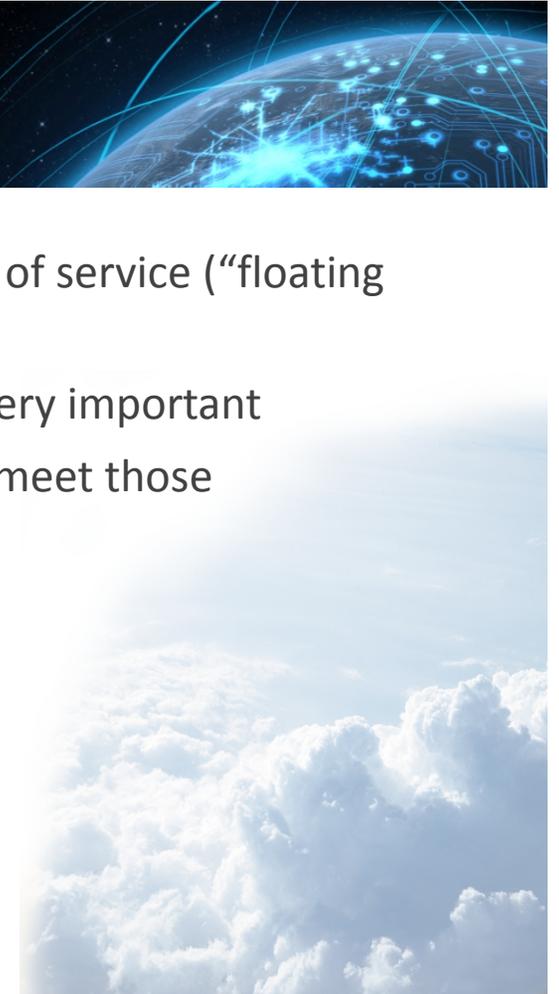
Cloud ERP Raises New Issues:
Service-Related Issues

- Advance notification on changes to services; protection against disruptive changes

- Contractual commitments on the provider regarding maintenance and support tend to be lighter for cloud, and support terms tend to be floating terms

- Cloud providers frequently subcontract obligations (and may disclaim liability for third-party cloud platform providers)

- Cloud agreement warranties tend to be weaker than those in on-premise software licenses

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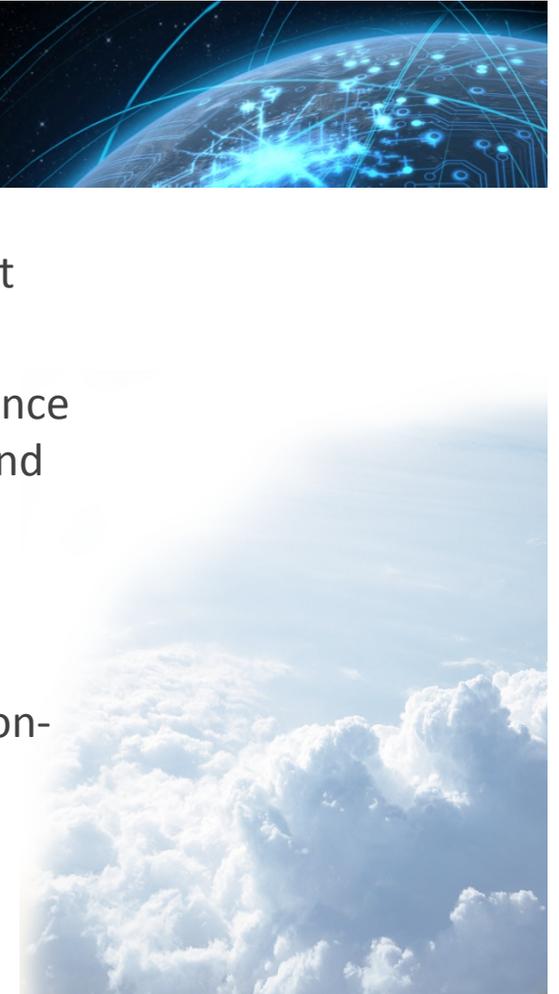
Cloud ERP Raises New Issues: Customer's Flexibility

- Customer right to regular and frequent extraction of ERP data for use in other customer systems

- Customer right to renew services – Vendor's right to not renew services (cloud terms tend to be shorter than on-premise license terms)

- Customer's right to transition assistance from vendor prior to termination of cloud services

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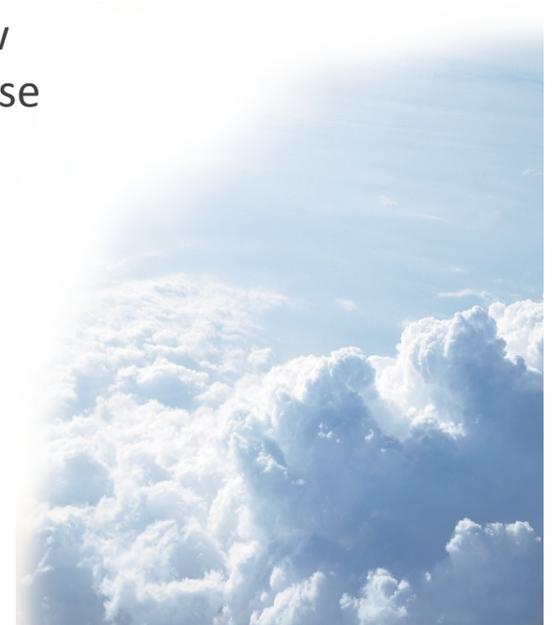
Cloud ERP Raises New Issues:
Data Protection & Compliance

- Vendor commitments for security of company data and liability for data breaches
  - Customer's reliance on vendor's control of audits and ISO certifications
- Vendor obligations to protect confidentiality of company and personal data
- Vendor data use for analytics or anonymously
- Restrictions on vendor locations for data processing and storage of customer data
- Vendor's compliance with law obligations for the cloud services

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Part IV

PREPARING FOR CLOUD ERP ADOPTION

Preparing for Cloud ERP Adoption

IF YOU ARE MOVING FROM ON-PREMISE TO CLOUD WITH THE SAME PROVIDER, CONSIDER THESE STEPS:

- Review your existing on-premise license agreement

- Consider whether you need to update or improve on-premise terms while you have leverage

- Carry forward favorable terms that you negotiated from the on-premise license agreement to the cloud agreement

- Define a "conversion" mechanism in pricing and in the terms that allows for credits and adjustments as you move use licenses from on-premise to cloud

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Preparing for Cloud ERP Adoption

IF YOU ARE MOVING AWAY FROM YOUR ON-PREMISE PROVIDER TO A NEW CLOUD PROVIDER, CONSIDER THESE STEPS:

- Carefully evaluate your existing on-premise agreement to determine any cost or other impacts from winding down your use to move to the cloud (e.g., minimum commitments, payment in advance with no refund, etc.)

- Ensure that you have enough runway time left in your on-premise agreement (and some cushion) to allow for the transition from on-premise to the replacement cloud provider

- Be prepared for a retroactive audit from your on-premise provider

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Preparing for Cloud ERP Adoption

IN ANY EVENT, BEFORE MOVING TO CLOUD, CONSIDER THESE STEPS:

- Develop your own checklist of contractual requirements based on your company's risk, compliance, privacy and security requirements

- Develop standard contractual clauses that address these requirements, and fallback positions

- Use the checklist to evaluate the cloud ERP terms and to educate your business about gaps or shortfalls in a provider's ability to meet your requirements

- Determine an approach for mitigating risks around "floating terms"
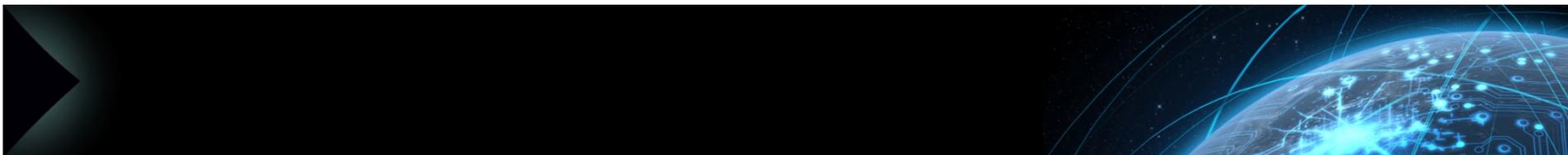
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Questions?

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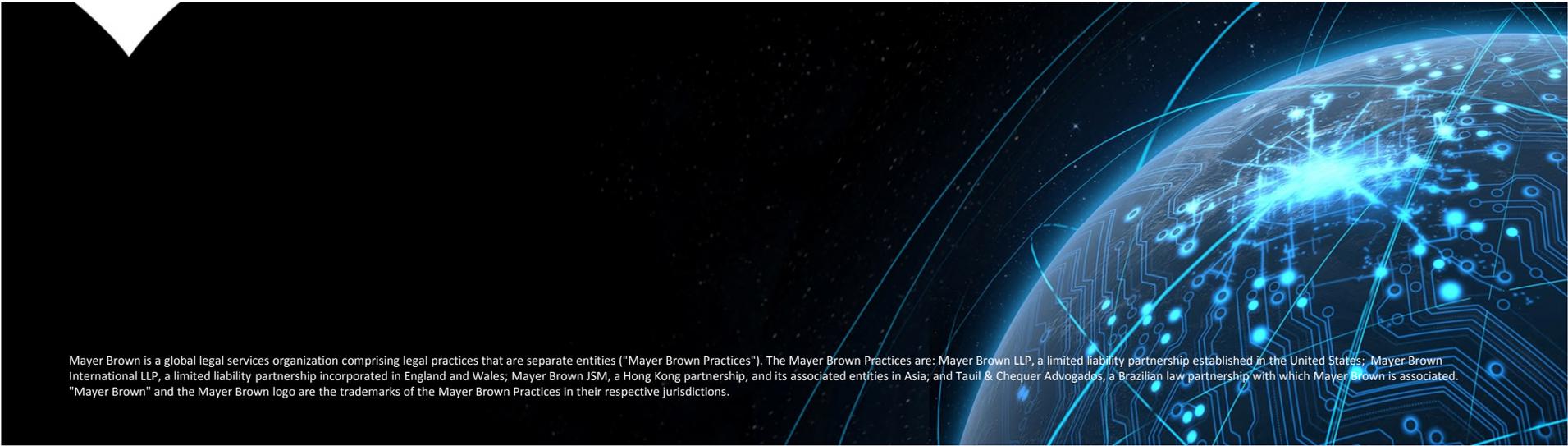
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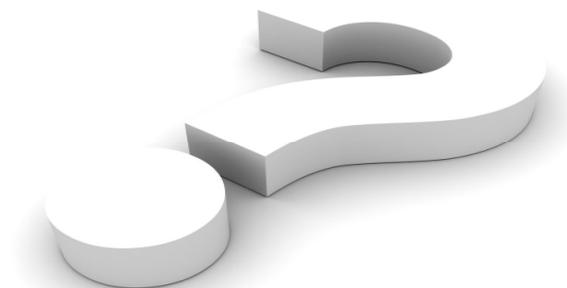
Reminders and Upcoming Webinars

- A recording and link to the materials from this program will be distributed by email to you in the next day or two.

- For those applying for CLE credit, please note that certificates of attendance will be distributed within 30 days of the program date.

- To submit topic ideas for future programs, please email us at TechTransactions@mayerbrown.com.

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