

COST JUSTIFICATION FOR PEOPLESOFT HOSTING

Not all reasons for outsourcing application support are cost-based; nonetheless an analysis must still show economic justification. Traditional ROI analyses measure the impact of an investment on cash flow, and typically use either Net Present Value (NPV) or Internal-Rate-of-Return (IRR) calculations. These methods attempt to place a value on the cash flows that will be generated in the future, with investments that are made today.

One problem with this approach is that it requires correlating technology investments to the business bottom line. This is extraordinarily difficult for basic infrastructure components that serve to enable many, if not most, processes, procedures and tasks that span the enterprise. Consider technology staples such as the PBX telephone system, the local area network, or printers and fax machines. These are investments that support numerous underlying and multi-threaded business processes. A similar argument can be made for Financials, HR, CRM and other back office systems.

Other problems exist with technology-based ROIs, such as predicting useful life and accurately estimating support and maintenance costs. Thus, while the cost reduction impacts are fairly easy to isolate and quantify, the direct correlation between the increased opportunity and bottom-line cash and revenue impacts often remain fuzzy.

Justification Factors

We understand the difficulty that IT organizations face in documenting an economic justification for any initiative. The contribution of IT assets and services to the business bottom line is simply not clear-cut. However, we find that analyzing outsourcing arrangements, such as PeopleSoft hosting, can be easier to address when the following four categories of savings and benefits are specifically quantified:

- Cost Reduction
- Cost Elimination
- Strategic Opportunities
- Other Benefits and Intangibles



Cost Reduction

Cost reductions can arise from eliminating or reducing internal resource expenditures as a result of such an outsourcing arrangement wherein the outsourcer pays these as a part of your monthly hosting fees. These can include such cost line items as:

- Database licensing and/or maintenance fees
- Hardware (server) maintenance fees
- System software maintenance fees (e.g., OS, compilers, etc.)
- Other third party software maintenance fees (e.g., nVision, Crystal)
- Training and conference fees
- Reductions in support staff headcount (e.g., DBA, System Administration, PeopleSoft level 2/3 technical support, security administration, etc.)

Cost Elimination

Cost elimination can arise from removing the need for future resource expenditures that would otherwise be required if you were to continue "internal self-hosting" of the PeopleSoft applications. These can include such cost line items as:

- Upgrades to existing infrastructure (Database Servers, Web, and Application Servers) to accommodate the increased system demands of Release 8.9, Release 9.0, or even Fusion
- Upgrades to workstations for core support personnel
- Training of resources to support the application
- Installation services for PeopleSoft databases and components
- Technology spending to implement high-availability and/or Disaster Recovery capabilities
- Additions to IT staff to handle increased workloads that result from new initiatives and projects

Strategic Opportunities

Strategic Opportunities develop from the fact that resources currently assigned to the maintenance and support of the PeopleSoft applications and infrastructure can now be redirected towards more value-added initiatives and activities. Of course, the economics of this particular factor can vary greatly among organizations, and must take into account the projected value of such new efforts:

- Value derived from staffing the new business initiatives
- The competitive advantage in the market place derived from such business initiatives
- Sale of capital assets no longer required under an outsourcing arrangement



Other Benefits and Intangibles

Other less tangible benefits often result from an outsourcing arrangement simply because your organization is no longer responsible for the day-to-day support of your back office business applications. As a result there are certain benefits that can have a larger impact that pure financial justification. Such items can include:

- Higher application availability and reliability due to system redundancies, failover, and monitoring
- Better round-the-clock support
- Tighter security controls that reduce exposure and increase compliance (Sarbanes Oxley, SAS70)
- Better Work/Life balance of internal associates who don't have to support the systems after hours, and on weekends
- More predictability in year-to-year support budgets
- Immediate availability of world-class PeopleSoft expertise

While the required "payback" metrics can vary greatly among organizations, we recommend that justification calculations be addressed for the term of the initial outsourcing contract (3 to 5 years.)

As an example: Assume that a client's PeopleSoft hosting solution has an initial setup fee of \$10,000, and an annual hosting fee of \$196,000, which over a three year contract represents a total investment of \$598,000. Over that three year period, the client would need to identify:

- Cost Reduction
- Cost Elimination
- Strategic Opportunities
- Other Benefits and Intangibles

The four categories mentioned above would need to total \$598,000 to achieve a "break even" economic justification. A total of \$687,700 would achieve a 15 percent return on the outsourcing arrangement.

Economic Justification Calculator

Businesses need a tool to enable them to perform their own economic analyses on outsourcing options. We've developed such a tool where all of the factors described above are itemized, totaled and then compared to the hosting costs, distributed over a three to five year contract period. An "equivalent ROI" is automatically calculated to allow a quick determination if the hosting arrangement is economically justified based on the conditions unique to your business.

To arrange immediate assistance in developing your economic justification simply contact Core BTG by calling [317.426.7483](tel:317.426.7483) or sending an email to Info@CoreBTG.com

