Case study

Due Diligence of an installation company's new strategy vs its existing ERP solution

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The assignment for Schnitzer & Company

A client company tasked us with reviewing the existing ERP solution in a target acquisition during the due diligence phase. The driving motive was for the client to come to grips with the potential risks of having to replace the existing ERP solution in the acquisition. The evaluation was not only to investigate longevity of the existing ERP solution but also to find out what limitations there might be relative to the strategic initiatives that were intended for the acquisition. A key to exceeding expectations in this investigation was Stefan Schnitzer's in-depth knowledge of core business processes in installation and construction companies.

Our delivery consisted of the following:

- A complete ERP solution map
- An "as-is" process map for the main administrative processes
- Fit gap descriptions for each strategic initiative with detailed development activities needed to close the gaps
- Overall cost estimate of implementing ERP improvements to support the strategic initiatives

The target company

The most important finding in this study was the very centrally administered setup of the target company. Contrary to most large scale companies in the construction and installation sectors this company kept much of the administrative workload centrally managed. The benefits out of an ERP system perspective are two-fold:

- The number of ERP licenses are low
- The number of people to train should you replace the ERP system is limited

However, the negatives are also clear:

- Central admin will grow linearly with the number of projects in the business
- The control of the business diminishes with the size of the business, governance weakens

The company had somewhat less than 200 employees, all salaried. The organization was small enough to only have one layer of managers below the CEO. However, with just a little more growth the management structure would need another layer.

The company was privately held and very lean. It had never made a loss and had impressive margins for its sector. For our client to increase the value further of the company they would need to implement strategies that diversified the focus of the company as the very profitable niche they operated in was expected to soon be exhausted.

Strategic initiative 1 – expand into a neighboring country

The first and most obvious strategy to evaluate the ERP solution against was to copy the existing business model and set it up in the closest neighbor country. What does that really mean when you get down to the nuts and bolts level in an ERP system? Well, it is not all that mysterious, the following properties of the ERP solution needs to be evaluated:

- Can the system handle more than one currency and does currency translation exist?
- Can the system import/export payment files in different currencies?
- Can the system handle more than one e-invoice application for customers and vendors?
- Does the system have generic file transfer language support such as XML?

- Does the system support intercompany transactions?

It turned out that most of the items where not a problem but it would still render an investment in the ERP solution to enter the new market since none of the home market supporting applications (e.g. e-invoices, payroll bank transfer etc.) in the ERP solution where going to work in the new market. Further, in the home market the payroll module was integrated whereas a new payroll application would be needed in the new market.

Strategic initiative 2 – grow in a different contract and delivery model

The existing very successful contracting model was fixed price greenfield and to some extent brownfield projects. All purchases were also done on fixed price.

The strategic initiative was to expand into more of a service type business where contracts were typically T&M. This translates in an ERP sense into checking the following:

- Can purchases be coded on article level into a project?
- Can invoice be done from a project based on purchased number of articles?
- Does the system support setting up pricelists on article level?
- Does the system support setting up rebate letters on article or article group level?
- Is it possible to set up “means price lists” e.g. kilometers driven
- Is time reporting on project numbers supported in an efficient manner?

It turned out that many of the items in the above list were missing in the current ERP solution. Pursuing this strategy would mean either to expect the administration to grow rapidly to handle customer invoicing or the need to replace the current ERP. Our conclusion was that a replacement of ERP was the most logical choice since there exists ERP systems that out of the box supports the processes needed. For the size of the company a new ERP would not be that costly.

Strategic initiative 3 – continue growing in existing business model

The most pressing matter that would arise from growing the business further within the current model was whether it was possible to reorganize the company structure to fit with the expected new layering of the management structure. Instead of two layers of profit centers a third layer was anticipated. In an ERP sense this means to check:

- How many dimensions can each transaction be coded with? A dimension is a label put on each cost and revenue amount and allows a report to be segmented on the dimensions.
- How flexible is the report generator in the ERP?
- How can transactions be exported to for example Excel for further analysis?
- How can relationships between dimensions be structured in the ERP?
- Does the authorization model allow further steps in approval hierarchies?

As it turned out almost none of the above questions could be confirmed which further strengthened us in the recommendation to switch ERP to something more appropriate and supportive of the strategy.

Summary

It is important to point out that businesses functioned long before ERPs ever existed. However, today the cost of administration is too high to ignore and hence to pursue the strategies explained above without proper system support is only viable for shorter periods of time. It is of course possible to implement the strategies without changing the ERP setup but it is not advisable.