



# Evaluating and Contracting for Cloud Financials

*Best Practice Considerations*

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## Seeking a New Model

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For an increasing number of companies, the tremendous cost and resource requirements of owning and operating on-premises software are a burden they are no longer willing to bear. The headache of licensing, installing and deploying core business applications are only the start. Costs multiply with the ongoing expense of operating the system over time. Add in the challenges of upgrading software, patching operating systems, managing licenses and users, monitoring data security and disaster recovery and you begin to get the magnitude of commitment – and expense – required. Just as daunting is securing approval for such major upfront capital investments for projects which normally have a very high failure rate. To make matters worse, none of this is strategic – for the vast majority of companies, there is simply no economic value added in running your own business applications – it just distracts from your core business objectives.

Not surprisingly, more and more organizations are concluding that on-premises software is outdated and misaligned with their operating goals and are increasingly adopting a new, flexible, cost-effective model: cloud computing. With cloud computing, the application provider delivers shared, scalable services that the company accesses over the Internet using Web browsers or mobile devices. There's no need to own, license, operate, manage, or control the underlying hardware, software, or infrastructure that supports the service. Cloud computing is typically delivered on a term-based subscription basis, eliminating the need for upfront software licensing fees or hardware purchases and you only pay for what you use. Because the vendor operates the system on behalf of thousands of companies, they achieve dramatic economies of scale, providing better operations at a lower cost than any individual business could achieve on their own.

Beyond these tactical advantages of cost-effective, anytime/anywhere access to your critical business applications, there's also the strategic perspective. Cloud computing applications are uniquely suited to aggregate and synthesize information from a wide variety of sources. Imagine a dashboard displaying the YouTube video of a recent earnings conference call, key real-time performance indicators from across your business, payables data from geographically dispersed entities, stock charts from external sites and sales data from Salesforce CRM – all visible anytime, anywhere from the comfort of your personal web browser. That's the compelling value that's attracting a growing number of small/medium-sized businesses to move to the cloud.

## What's Different in the Cloud?

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When it comes to selecting a cloud computing solution for your accounting and financial management operations, the basics are the same as you have used to select on-premises software for decades – requirements definition, prioritization of needs, RFI/RFP creation, demos and trials, reference-checking and support quality. But with cloud computing, you also need to assess the vendor's operational track record. Your chosen vendor will not only be developing and delivering software applications to you – they will be running those applications for you as well.

Do they have the right infrastructure to operate and deliver that service and a track record of operational excellence?

On a larger scale, you also want to assess the vendor's ongoing business practices and culture to ensure the company is a good "fit" for your organization. The relationship with a cloud computing provider is different and (ideally) stronger than what you would have with an on-premises software provider. With on-premises software, you bear all the responsibilities – the deployment, use, maintenance and operations of your applications. So, the relationship with the software developer is somewhat arm's-length. By contrast, in the cloud computing world, the vendor provides crucial, strategic services, operating and maintaining your systems on a minute-by-minute, 24/7/365 basis. You're establishing a long-term, ongoing relationship, which makes vetting your vendor a mandatory process.

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#### Evaluation Process:

- Define Requirements
  - Prioritize Business Needs
  - Create RFI / RFP
  - Review Demos / Trial Product
  - Check References
  - Assess Cloud Vendor Performance
  - Assess Cloud Vendor Track Record
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## The Web Shifts Power in Your Favor

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Fortunately, counterbalancing these increased responsibilities in cloud vendor selection is the fact that the Web shifts transaction power from seller to buyer. Think about how consumers purchase automobiles today vs. in 1995, for example. In this day and age, it's unthinkable that a savvy buyer wouldn't look up 3rd party reviews, review commentary from other owners, document pricing and deals other buyers are receiving and understand quality, service and resale value metrics before entering a dealership and speaking with a salesperson.

Quite simply, buyers of business applications have a wealth of powerful, valuable resources at their fingertips that were unimaginable 10-15 years ago. Previously, sellers held most of the power by tightly controlling access to information about products and customers. Sure, you could ask for references – but when references are supplied by your salesperson you can almost be guaranteed they are not unbiased. Today, you can tap into search engines and social networks to access truly unbiased third-party information to help improve your decision making process. Start by simply "Googling" the name of your vendor candidate – then pair it up with "nightmare" or "happy" to review passionate opinions from other companies just like yours who are already using the product or service. Search LinkedIn to find people in your network who are current or former clients of the vendor you're evaluating, or even Tweet to your followers to see what their experiences have been. If you haven't done this, you'll be amazed at how freely the community will share information with you about their experiences. By applying and involving your community in the selection process you get unvarnished opinions and reviews that provide unbiased insights that buyers generally find reliable and trustworthy. Accessing this unbiased information outside of the vendor's control greatly increases your chances of having a successful outcome.

## Service Level Agreements – The Key to a Successful Relationship

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When you engage a cloud computing service provider for your accounting and financial management applications, you're entering into a long-term strategic relationship with the company that will be managing your financial software. They will operate it, maintain it and ensure its proper performance. That's why **service level agreements (SLAs) are essential**. The SLA tracks the shared expectations between you and your vendor for how that system will function. A solid SLA reduces risks, documents goals, defines penalties and prevents surprises that are an integral part of a long-term vendor-client relationship. SLAs have several dimensions that all cloud computing evaluators should consider.

### Control

In cloud computing, there are numerous operational processes that become the sole responsibility of the vendor, duties that were previously assigned to in-house IT. To mitigate the risk of this loss of control, the SLA should tightly define the parameters of three aspects of performance:

- **System Availability** – This metric governs the percentage of time that the service will be up and running for all of your users. At minimum, you want 99.5 percent availability – that's roughly 7 minutes of downtime allowed per day. Certain companies in specific industries may need to specify higher levels.
- **System Response Time** – Being available isn't enough. You need a guarantee that your applications will perform at an appropriate speed – carefully defined and constantly measured/monitored. While many SLAs omit response times, it's a good idea to build in a mechanism to hold your cloud computing vendor accountable. You should mandate that the vendor maintains sub-second response time to ensure that the system feels quick and productive.
- **Disaster Recovery** – In the case of a catastrophic failure of the vendor's infrastructure, such as a major earthquake or hurricane, how soon will your service be available again? How much data will you lose? Your vendor should have a complete disaster recovery plan which minimizes your disruption of service and data loss. Demand no more than 24 hours of downtime coupled with no more than a few hours of data loss in the very unlikely event a catastrophe occurs.

While many SLAs have traditionally penalized vendors for not making pre-defined performance goals, many SLAs are now also creatively incorporating incentive bonuses for vendors that achieve greater-than-expected performance milestones. If it's very important to you that the vendor achieves 99.8% uptime, but they normally guarantee only 99.5%, consider paying them a bonus when they achieve your desired level of performance.

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### Service Level Agreements: Performance

- Define Appropriate System Availability for Your Business
  - Determine System Response Time
  - Review and Understand Disaster Recovery Plans
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Naturally, cloud computing firms have an inherent advantage in their ability to cost-effectively deploy gold-plated infrastructure and operations vs. what you could do yourself. They are amortizing their costs over thousands of clients. As a result, cloud computing vendors can provide an unbeatable computing foundation encompassing world-class, SAS 70 Type II-audited data centers with 24x365 operations on multiple continents; dedicated disaster-recovery facilities conforming to and exceeding industry-standard best practices; redundant hardware and networking for complete failover; continuous off-site backups; and more. Because the cloud computing vendor amortizes costs across so many other organizations, it's likely that their technical infrastructure is far richer than anything an individual small or mid-sized company could afford to deploy, staff, or maintain on their own.

### **Operational Risk**

When you're using a cloud computing solution, your data is stored remotely and accessed through the Internet. Assuming your vendor has addressed the potential risks surrounding security, privacy and data ownership, remote storage should not be a great concern. The fact is, given the number of clients they serve and the potential fallout, a security breach of any sort for a cloud computing vendor is viewed as catastrophic. Virtually all established vendors are far more capable of managing these risks than small or mid-sized organizations and should be very willing to include parameters governing these issues within their SLAs. Some key points to consider:

- **Ensure Data Ownership** – Make certain that it is unambiguously clear that you own your data and that you can get it back if you ever decide to leave. This is a pitfall with less-reputable vendors, who can de facto hold your data hostage during separation disagreements.
- **Ensure Migration Assistance** – In many cases, merely getting a copy of your data is insufficient. If you decide to leave, the vendor must help you get your data back in a workable form/format. A modest professional services fee is appropriate in such cases.
- **Ensure Passive Storage Availability** – Build into your SLA the option to retain your data on the vendor's system for an appropriate fee. This gives you flexibility to retain access to read-only data even if you're no longer actively using the service in production.

Operational risk also encompasses concerns relating to all aspects of the security of the service. As with infrastructure, the security capabilities of commercial cloud computing vendors far surpass those of what virtually all small or mid-sized companies can feasibly deploy by themselves. From a facilities perspective, cloud data centers employ sophisticated measures including biometrics and "man-traps" to prevent unauthorized access. From a service perspective, strong encryption of network traffic, hardened servers, redundant firewalls and antivirus measures, perimeter monitoring, strong password policies and IP restrictions – all backed by complete audit trails and third-party security audits – are some of the important measures that cloud computing vendors should be able to offer their clients.

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#### **Service Level Agreements: Mitigating Operational Risks**

- Determine Data Ownership Policies
  - Ensure Migration Assistance
  - Ensure Passive Storage Availability
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## Business Risk

Another important element of a quality SLA are the business guarantees the cloud computing vendor rationally and plausibly offers based on their track record of implementations. Compared to on-premises implementations, cloud computing vendors can more easily implement new customers because they have far greater control and far fewer variables to contend with – they're working in an environment they own, control and manage, as opposed to unique data centers and operating environments owned and managed by customers. Make sure your SLA takes advantage of this dynamic by demanding more from your vendor.

Establish criteria for the quality and timeliness of professional services engagements. Be willing to pay bonuses for implementations that proceed better than planned and, of course, structure penalties for failures or breaches. One commonly overlooked area of the SLA is proactive communication. Ask for monthly product/feature updates and quarterly product roadmaps so that you're aware of the vendor's forthcoming product directions. What's more, be sure you understand how your requests for new features and other product feedback/input will be prioritized.

**One crucial area that few companies think of requesting: a money-back guarantee.** Cloud vendors may be willing to offer you a money-back guarantee (perhaps with some sort of sliding scale or schedule) – particularly if you are willing to commit to a pre-defined scope of work and criteria for success. Confident vendors will agree to these arrangements because they have a strong track record of successful implementations – effectively they know ahead of time that they can successfully implement your applications.

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### Service Level Agreements: Mitigating Business Risk

- Understand SLA Credit Process
  - Review Contract Cancellation Policies
  - Review Proactive Notification Processes
  - Review Published SLAs
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## Penalties, Rewards and Transparency

An internal IT department has a built-in level of accountability because it must perform and report their activities and progress to the rest of the internal organization. With a cloud computing vendor, there's a degree of separation that clients should address through their SLA. Savvy companies structure their SLA to ensure that the vendor documents its methodology for measuring performance, calculating penalties and rewards and offering full transparency into its operations. Some of the specifics include:

- **SLA Credit Process** – How does the vendor handle SLA lapses? Do you have to proactively monitor and report the lapse and request the credit? Is the process cumbersome? How long does it take to process credits? Does the vendor automatically issue credits if a failure occurs that impacts your service?
- **Contract Cancellation** – Can you get out of your contract if the vendor continually and materially fails to comply with your SLA? What are the milestones/metrics that define these systemic, long-term failures?

- **Proactive Notification** – Make sure your vendor has formal mechanisms in place to proactively alert you regarding system availability, planned downtime, production issues and pending updates.
- **Public Disclosures of Status** – Review your proposed vendor’s public real-time status Website that transparently shows their operational performance statistics, availability status and other metrics. What are the longer-term trends and track record? If there are incidents, what were the outcomes? If the vendor doesn’t have such a publicly available Website, it’s a red-flag that merits further investigation. Remember, you won’t be dealing with an internal IT department from whom you can demand this information.
- **Published SLAs** – Review published SLAs and understand how they apply to you. Be sure to scrutinize privacy policies as well.

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#### Service Level Agreements: Penalties, Rewards and Transparency

- SLA Credit Process
  - Contract Cancellation
  - Proactive Notification
  - Public Disclosures of Status
  - Published SLAs
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## Contracting and Negotiating Strategies

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In today’s business environment, more power is accumulated in the hands of buyers. You have unprecedented opportunity to control the pace and direction of contracts and negotiations. This is especially true in cloud computing, where business models are predicated on radically different economics. Vendors typically are measured by their stakeholders on monthly recurring revenue (MRR) and they don’t make a profit until 12-36 months into a client relationship. That forces them to focus on lifetime value and helps keep customer and vendor goals and activities well-aligned. Their overarching goal has to be getting customers deployed and keeping them happy over the long term.

Under this business model, cloud vendors can experience significant pressure to generate sales, leading some to offer steep initial subscription discounts. If you don’t protect yourself, a steep discount in year one can lead you to a large price increase in year two. If you’re a careful buyer, this should lead you to pause. If you’re engaging with a cloud computing vendor offering large up-front discounts, be sure to demand a cap on price increases in subsequent year – 5% to 10% price increase caps are the standard. Also forbid changes to module definitions – unscrupulous vendors sometimes change their entire pricing model after one year, believing that the customer is “trapped” and leading to unfortunate surprises and ugly discussions in year two.

Cost of sales is another metric that matters greatly to cloud vendors that operate under very tight margins. Without large six-or-seven-figure upfront contracts, cloud companies can’t afford lengthy sales cycles. Offering to be a reference or providing a testimonial/ROI analysis in exchange for a pricing discount is a good buying strategy that will often be accepted by the vendor. What’s more, the more prepared you are when you enter your purchase cycle – through a well-structured RFP and a responsive evaluation team – the faster the sales cycle is for the vendor, which is likely to increase the vendor’s willingness to entertain discount discussions.



Cloud computing is synonymous with monthly pay-as-you-go models. But annual contracts – offering modest discounts in exchange for lengthier terms – are not uncommon. If you opt for an annual contract, make sure you understand what happens with overages. If you need to provision 15 users instead of the 10 you anticipated, you don't want to encounter pricing surprises. Make sure you negotiate prices for overages in advance – so you know exactly how much it will cost you if you need to consume more of the service than you thought you would.

Finally, be sure that all necessary support, training and maintenance services are included with your subscription. Check carefully to avoid unexpected costs or other unwelcome issues.

## Understanding Total Cost of Ownership

Given the fundamentally different economic models between cloud computing and on-premises software, it can be difficult to perform a true apples to apples Total Cost of Ownership (TCO) comparison. It is a tempting – but fundamental – error to compare the on-premises license fee with the monthly costs of cloud computing subscriptions. In cloud computing, vendors include many services as part of the monthly fee that aren't incurred until after the initial on-premises license fee. Yankee Group estimates that, of the total, fully loaded cost of on-premises software deployments, only 9 percent of the cost is reflected in the actual software license. Customization and implementation comprise 43 percent, hardware is 26 percent, IT personnel consume 14 percent of the cost and training and maintenance take the other 8 percent. These ongoing costs reflect everything from applying patches and fixes to full-blown upgrades as well as performance tuning, custom integrations and upgrading the infrastructure to accommodate the application, including network capacity and security.

By contrast, 68 percent of the cost of cloud computing applications is captured in the monthly subscription fee, with the balance devoted to implementation, customization and training. When one considers that most organizations typically deploy financials for 7 to 10 years – necessitating several software upgrades and wholesale hardware replacements – the long-term cost advantage clearly swings to cloud computing.

ON PREMISE		Pro forma cost estimate for on premise						
In this section enter the anticipated costs for the initial deployment and ongoing management and support of an on-premise solution.		Initial	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6
Total software costs	Estimate 0	0						
Software maintenance cost as a percentage	20%	0	0	0	0	0	0	0
Total hardware costs	0	0						
Hardware maintenance cost as a percentage	20%	0	0	0	0	0	0	0
Initial deployment consulting	0	0						
Ongoing staff cost:								
Number of IT employees to support the system	0.0 Employees							
Annual fully loaded cost of an IT person	0		0	0	0	0	0	0
Upgrade frequency / new version cost:								
How much will an upgrade cost to deploy?	0							
How frequently do you expect to upgrade?	Every 7 years		0	0	0	0	0	0
Other costs associated with the on-premise solution								
Additional initial costs	0	0						
Additional ongoing costs	0	0	0	0	0	0	0	0
<b>ANNUAL COST FOR ON PREMISE</b>		0	0	0	0	0	0	0

  

ON DEMAND		Pro forma cost estimate for on demand						
Enter the anticipated costs for the initial consulting and ongoing fees associated with an on-demand solution.		Initial	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6
Annual application license fee	Estimate 0	0						
Initial deployment consulting	0	0						
Ongoing staff cost:								
Number of IT employees to support the system	0.0 Employees							
Annual fully loaded cost of an IT person	0		0	0	0	0	0	0
Other costs associated with the on-demand solution								
Additional initial costs	0	0						
Additional ongoing costs	0	0	0	0	0	0	0	0
<b>ANNUAL COST FOR ON DEMAND</b>		0	0	0	0	0	0	0

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You can use a simple ROI tool to evaluate the impact of various cost components.

## Hosting Traditional Software

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One strategy that some companies find attractive is to host on-premises software in a remote, managed data center and access that application through a Web client or Citrix-type tool. This strategy is a good start, providing you with anywhere/anytime Web accessibility to your business applications. Unfortunately, however, the hosted model presents several critical drawbacks. You are still responsible for managing versions and upgrades as well as maintenance and you retain the responsibility to configure, integrate and extend the software. You also bear the costs of both software licenses and hosting. Finally, these types of deployments can violate the terms of many software license agreements. So while hosting is a good first step, it offers just a few of the benefits of cloud computing.

## The World is Flat

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With cloud computing's ability to provide real-time access to far-flung entities and to integrate with other systems, the constraints of time and distance go away. By aggregating more content and more data with broader communities of engaged users, cloud computing helps global companies manage their financials faster and more easily.

Cloud computing levels the playing field by delivering the same services Fortune 100 companies enjoy to smaller companies. And companies that adopt cloud computing find that their IT professionals can focus on value-added, differentiating tasks. Through its radical simplification of IT infrastructure, and its inherent shifting of costs and risks from client to vendor, cloud computing transforms how companies access and use computing services.

The Return on Investment of moving your business applications to the cloud is tremendous, with thousands of companies having made the leap successfully. **Expect to achieve 100% to 500% or greater ROI when adopting cloud financials.** Using the techniques described in this white paper, you can greatly enhance your chances of achieving this level of return while at the same time minimizing your risks when making your move to the cloud.

To request a copy of the ROI calculator spreadsheet, contact [info@intacct.com](mailto:info@intacct.com). For more information on cloud computing and financial software, visit [www.intacct.com](http://www.intacct.com).



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