

View Point



Is your contract process helping or hurting?

Abstract

The time is right for contract and legal teams position themselves as business enablers. The only way to earn the respect of stakeholders is to become partners with clients in closing business transactions on a timely basis while at the same time negotiating and mitigating the risks assumed in the contract. The right balance must be struck.

In order to have this kind of impact, contracting groups must build the right foundation--efficient processes, adaptable staff, and the right tools and services.

All of this will require time and money which is worth the investment as 60-80% of business transactions are governed by contractual agreements and a typical Fortune 1000 Company maintains 20,000 to 40,000 active contracts at any given point of time. Therefore, it is the contract and legal team leader's job to sell to the internal stakeholders the importance of contracting in managing business and to build strong peer relationships so that management is willing to support the team.

Introduction

How will you know whether your contracting processes are helping?

This question can best be answered by your clients and internal stakeholders. Some of the indicators that your processes are not helping your business are:

- Extended contract cycle times
- Perception by internal stakeholders that the contracts and legal team acts as a “policeman” which slows contract closure
- Concern among management that they do not have visibility to contractual risks
- Perception that contract and legal department head-count is too high
- Internal groups (audit, finance, business divisions) do not have ready access to contracts without intervention by the contract staff

When it’s hurting:

Generally, characteristics of a process which is not helping fall into three categories—a disjointed contract process, a lack of understanding of the business goals, and inefficiency.

The beauty of a process is that it produces a consistent result; however, it requires that the manager invest time and resources to define the process and associated roles. Characteristics of a disjointed contracting process include absence of a single owner for the contract output, ill defined interface to internal groups, lack of clarity around the sub-process owners and approval authorities, inconsistent and deviant contractual terms and time consuming review and approval process.

Managers and legal counsel may lack knowledge of the business; value propositions, competitive pressures, product portfolio, financial models, and drivers for their internal clientele. This leads to a narrow mindset that limits the group’s role to what they do best—drafting and reviewing contracts with little focus on the transactions that are of strategic importance to their businesses. This renders the negotiation mentality a zero sum game that consists of shifting as much risk to the other party as possible and driving the price to your advantage. There is little invested in building long term relationships with the client.

Inefficiency is one of the by-products of an ill-defined process. Contracts that are in the pipeline are worked on a first come-first serve basis, without any regard for the size or strategic importance of the business opportunity. Typically, 80% of a company’s spend or revenue is derived from 20% of its suppliers/customers. Granted, the ratio will vary to some extent by industry, but generally the idea is the same.

Contract negotiators are burdened with smaller and less strategic work preventing them from investing the time necessary to close larger contracts, focus on higher value work and strategic and proactive advice. In addition, they are expected to handle a number of lower level administrative functions such as RFP reviews, NDAs, and contract abstractions, just to name a few.

Strategy and Solutions

The starting point is to spend a substantial amount of time talking with your internal and external clients to understand their expectations of the contracting function. Ask if you can touch base with them periodically to gauge the performance of your team. Based on that feedback, create a mission statement for the group. In my role as a former head of contracting, our mission statement was to “close contracts on a timely basis while at the same time managing our risk”. This mission statement served to reshape the culture of the group from merely reacting to work requests to proactively anticipating upcoming business opportunities requiring a contribution from the team.

The next step is to document the end-to-end contracting process, starting with the RFP all the way through to supplier selection (contract administration, change control is the subject of another paper). Process improvements can lead to cost savings in the range of 20-30%, so it’s well worth the investment in time.

Here is a sampling of some of the other key elements of a “best in breed” contract function.

Defined Roles

Since contracting involves different areas throughout the company, it is particularly important to identify and define the roles of all the participants at every stage of the process. Generally, a Contract Manager or Business Division representative will take the lead role coupled with designates from each stakeholder group (Finance, Legal, Sales or internal clients in the case of Sourcing). It is highly desirable that this becomes the core working group for every negotiation involving that particular business division. This teaming arrangement builds knowledge of the process, becomes familiar with the acceptable and standard positions to be adopted in negotiations and understands each other's priorities and requirements. Clearly defined roles will reduce contract cycle times and risks can be minimized if all of the stakeholders provide their input on a timely basis.

Pairing contract managers and lawyers

Associating the two parties to specific sales/user groups fosters long term relationships, minimizes the need to bring the group up to speed on subsequent transactions and higher negotiation leverage. The other advantage is that stakeholders can provide their input based on the order in which the contracts should be worked.

Executive Business Review

Establishing a regularly scheduled executive business review is an effective way of improving management's visibility to business opportunities that are either in the pipeline or are at the negotiation stage. The purpose of this meeting is to review and approve business cases for new opportunities (over a certain dollar limit) and to set guidelines for the RFP response and subsequent negotiations. Again, for significant contracts this executive group would be briefed at critical stages of the negotiation. The role of the line manager should not be diminished as a result of these reviews.

Measurement against Metrics

In order to measure team performance and efficiency, metrics should be put into place. The first category is measuring team performance. There are a variety of metrics in this area, but as a starting point, I recommend quantifying contract cycle times. In my opinion, this is a good "acid test" for how well the process is working. The second category is efficiency. Calculating the revenue/spend per contract manager and associated lawyer is a good way of balancing workload and gauging productivity. In some cases, this ratio will be rather low due to a high volume of smaller contracts.

How to resolve the scarce resource challenge

In addition to improving the process, consideration should be given to other ways of improving the efficient use of contracting and legal resources. The two most effective tools are: Legal Process Outsourcing (LPO) and Contract Database Management

Legal Process Outsourcing

LPO is becoming a popular way of unburdening contract and legal staff from lower value and high volume work. Outsourcing is a cost effective way of augmenting your staff, particularly for repetitive work and at times of peak workload. Contracting work that fits in this category includes:

- First pass review, red-lining, and drafting of smaller contracts, RFPs, NDAs, etc.
- Creation of contract clause libraries and negotiation playbooks.
- Abstraction and contract summaries.
- Risk assessment and Contract Health reporting.
- Obligation tracking.
- Contract review related to M&A, corporate restructuring, litigation, and client/supplier disputes.

It is important to note that outsourcing services can be implemented in a short period of time once the requirements have been defined and the project plan is approved.

Contract Database Management

Adding a state-of-the-art contract database is a requirement for every contracting group. A well designed database provides secure and ready access to all contracts without contract management or legal involvement. Other basic capabilities that are a “must” include structured contract folders, searches, alerts, and reporting.

Databases which are designed specifically for contract management are recommended. The alternative is document storage systems, which are not optimized for the contracting function.

The implementation of a Contract Management System (CMS) for user work flow is not recommended since the user adoption rates are low. Other drawbacks include the length of time to implement and the cost of ownership.

Summary:

The time is right for contract and legal teams to position themselves as business enablers. The only way to earn the respect of stakeholders is to become partners with clients in closing business on a timely basis while at the same time caring for the risks assumed in the contract. The right balance must be struck.

In order to have this kind of impact contracting groups must build the right foundation--efficient processes, adaptable staff, and the right tools and services. All of this will require time and money. It is the team leader's job to sell the importance of contracting and to build strong peer relationships so that management is willing to support the team. How will you know whether your processes are helping? Your stakeholders will insist on your involvement with their deals.

About the Author

The author, Bob Henry, is currently a Practice Engagement Manager with Infosys where he is responsible for their LPO offering in the North America. Prior to joining Infosys, Bob was the Vice President, Contract Management with two large telecom companies. Earlier in his career he served as a Vice President, Sales and Marketing in venture backed technology start-ups. As a practitioner, he has an in depth experience in the contract and legal services space.



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