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Keeping pace with a changing world: Challenges for contract management and negotiation



TIM CUMMINS, IACCM

The statistics tell the story. For many countries, the swing from products to a services-based economy has been dramatic. And many of those services are in fact “solutions” — an integration of products and services.

Are contracts, the professionals charged with their negotiation, and management keeping pace with

a changing world? That was the question posed to a group of senior executives from commercial, legal and procurement when they met recently at an IACCM roundtable discussion in London.

To start the conversation, the results of IACCM’s latest survey of “The Most Frequently Negotiated Terms”

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were presented. This year's results suggest that many negotiators feel that greater emphasis should be placed on relationship terms and topics such as scope and change procedures.

"In my experience, relationships are generally not sustained when trouble begins," was an observation by an executive from the Aerospace industry. He questioned whether collaboration is ever more than skin-deep. "When I negotiate, I focus on the risk terms and the payment terms," he commented, suggesting that the terms that gain the greatest focus today are in fact the right ones.

However, one of the representatives from legal supported the agenda for change and suggested that litigation is mostly about scope and transition, so more time and expertise in these areas would most likely help to reduce the chances of dispute. He also commented that the world has changed — and perhaps contracts have not kept pace.

"For example, we used to push back on requests for consequential damages by telling clients that we were not their insurer. Contracts today are increasingly about outcomes, policies must be re-examined."

It was agreed that large corporations tend to hard-code their standard terms into policy, and this creates delays and stumbling blocks for negotiators, and these principles are slow to adapt to changing conditions. It results in a lot of avoidable and highly repetitive discussion on issues such as liabilities and indemnities. This is more reflective of the old world of products — whereas today's world is about services.

Contracts have simply not kept pace with the change.

Procurement must align better with the business

Another risk factor that was identified was the challenge of ensuring a match between performance obligations and capabilities. In major projects, this alignment is often broken by the actions of procurement. According to one executive: "Sub-contracts drive savings, but too often result in term commitments that break the back-to-back link. Procurement measurements can be a real problem. For example, we recently had a situation where procurement negotiated price

reductions by guaranteeing a payment schedule — but the contract with the customer had offered a flexible schedule. They had saved money, but endangered cash flow. What is worse, they didn't seem to understand why that might be a problem."

Participants from all functional areas agreed that there are problems with current procurement skills and measurements. They suggested that it is important to operate in integrated teams to ensure procurement is engaged with team objectives. It is also beneficial to have crossover between procurement and commercial/sales contracting, to generate understanding of both buy-side and sell-side perspectives (procurement, in particular, benefits from this). There was also a feeling that procurement's understanding of business priorities is often too narrow — that they need better guidance on what is of value to the company.

"Procurement is mostly driven by short-term goals. Driving down price is easy to measure and is immediate. Longer-term benefits are attractive but often hard to measure, hard to gauge why they arose. So even when there is a desire to apply more value-based weightings to supplier selection, these are often abandoned," observed a partner at a major international law firm.

Functional integration and scope

The group also highlighted that roles and responsibilities in the negotiation process are often confused and inconsistent. But one participant felt they had the answer. He commented that his company — a major player in the defense and aerospace sector — has grasped the importance of flexibility and agility in the contracting and commercial process. "Commercial, procurement and supply chain are all in one place, allowing quick decisions and full integration of policy and practice."

This need for a more holistic commercial competence was endorsed by an executive from a top outsourcing provider. He explained that he is working on expanding the commercial role and his company has already consolidated this with legal. "We understood the need to supplement traditional commercial and legal deal-makers with analysts — covering

areas like service credit regimes, benchmarking provisions, costing and pricing of risk.”

This participant confirmed the challenge of moving from a product to a service culture. “In a product world, activity is based on snapshots, whereas services are output-based and more actuarial. For example, how do you do modeling to understand the real utilization risks?”

Another commercial executive commented on the value of consistent techniques — for example, concepts like “defensive contracting”. He described whiteboarding high risk deals that are likely to end in dispute. By facing this reality, the potential for positive results is increased because the parties plan to avoid the things that could go wrong.

Business discipline

Creating a collaborative and consistent culture was identified as a key success factor for negotiating better deals. One executive observed: “Staff involved in contracting and negotiation have traditionally viewed their experiences as a personal asset. But information is a corporate asset and we had to emphasize that point, as well as facilitating information sharing.” He cited the introduction of blogs as one way that they are now capturing conversations and sharing experiences within the commercial group.

Imprecise roles and responsibilities often lead to a culture of blame, and this is endemic in the world of contracts. As a result, learning is often limited. For many of those at the meeting, this could best be addressed by more consistent practices and methods for contracting and negotiation. “Long-term deals used to be driven by a sequence of bid/monitor/close,” said one delegate. “But today, there is almost endless re-bidding and this puts pressure on skills and process.”

Workload and value delivery

The increase in workload for all groups involved in contracting was

highlighted as a particular challenge, especially when the cost of overheads is also under attack. Participants discussed a variety of methods that they are using to keep costs under control, while maintaining or improving service levels.

“We have to focus on the deals where returns are greatest and our skills of real value. We have to increase returns as well as reduce risks,” said one executive, describing their

increasingly demanded, areas of knowledge for the commercial contracts professional or function.

- Commercial awareness training is a priority. We cannot do it all — we must deliver the message that all employees share in “a duty of care” on commercial issues.
- Commercial and contracting competence will increasingly be about the application of governance — how to do the deal.

Creating a collaborative and consistent culture was identified as a key success factor for negotiating better deals.

approach to segmenting contracts and support. Several participants are working on reducing operational costs through offshoring or outsourcing aspects of their work and re-orienting the skills of existing staff. These programs are accompanied by efforts to ensure greater use of standards and empowering users with more self-sufficiency through better defined processes and support.

Preparing for the future

Our roundtable group concluded the discussion by highlighting some of the key challenges they face as they prepare for the future and equip to respond to the solutions/services world. The following are among the observations.

- External spend now represents 80% of total costs. Open innovation is becoming the key challenge of the future, and this demands new models and attitudes for contracting.
- What constitutes “commercial” or contract management? How broad are the scope and the level of integration? For example, export/import control; estimating; subcontracting — all are key, and

- Metrics are a priority — being able to demonstrate and increase value. We must define “better” deals — for example, fewer disputes, shorter cycle times and fewer errors.

In summary, the participants shared the view that contracts and those charged with their management are often lagging the business practices and models required by today’s market conditions. “For example, agile software development is a dynamic new methodology — but software contracts remain tied to ideas like fixed price and ‘time is of the essence’. They are quite simply incompatible. We end up frustrating the business.” ♦

Tim Cummins,
CEO,
IACCM.

This article is based on a meeting held at the Lloyd’s Underwriting Centre, London on 21 May 2009. This executive roundtable involved 12 senior executives from legal, procurement and commercial roles in various industries, including aerospace, defense, technology, outsourcing, insurance and banking.



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From “servitization” to the service-oriented enterprise, a call for business innovation



DOUG MORSE, Services Transformation and Innovation Group LLC

Key points

- The world economy is driven by services, so you need to have the right skills, process and technology to survive.
- The value of any product is only in its intended use — service creates additional value.
- Everything in the enterprise changes when the enterprise moves towards a service orientation.

Ask any company what they do and they will tell you about what they make or what they sell. Very few will tell you about the value or outcomes that they create for their customers. Creating, or co-creating, value is what the transition to services is all about. “Servitization” is not a word that I like very much, but it has become a popular term in service literature to describe the transition of companies from a manufacturing, or goods-dominate, company to one that is more services-dominate.

Servitization is about adding services to a product base. The service-oriented enterprise is the next step in the service maturity curve and occurs when producers stop focusing on adding value to the products and start to think about how they add value to their customer’s outcomes by creating products that act like service systems. More importantly, they adopt a model where financial rewards are tied to the value created for the customer.

To illustrate by using a simple example, let’s relate this new service-based business model to a manufacturer of jet engines. In the old world, the jet engine manufacturer focused on the

efficient manufacturing of jet engines and sold them to airlines. The emphasis was to build a product that was bigger, faster and cheaper than the one before it. As they moved through a model of servitization, they added product-related services to reduce the total cost of ownership for the customer. Offerings like maintenance outsourcing, specialized leasing arrangements, parts and logistics support, training and technical support are typical. At this point, the jet engine company enjoyed greater revenues and profits over the life of the engine and was able to differentiate themselves in the marketplace for short time. They added value to the base product, and the customers could reduce their cost of ownership and focus resources on the business of moving passengers and freight.

They added value to the base product, and the customers could reduce their cost of ownership and focus resources on the business of moving passengers and freight.

Power by the hour

The “aha” moment came when the engine manufacturer realized that, at the end of the day, what airlines really wanted was reliable thrust to move airplanes as needed and in a safe and economical way. Owning a capital good like an engine meant that the airline had to maximize the value of the asset that it now owned. Since the value of the jet engine (or any other product,

for that matter) is in its intended use, what would be the benefit to the airline if it only had to pay for the value that the jet engine provided to the airline’s business? The jet engine manufacturers re-thought the business model in which they operated. They have now created a next generation of the engines that are fully instrumented. Sensors and controllers on the engine are connected through telematics to an operations center that collects real-time telemetry and prognostic information. The engine manufacturer is also connected into the airline’s operations systems so that it can automatically help manage schedules related to maximizing the safe use of the engines. They sell the whole package as “power by the hour”. The jet engine manufacturer has gone from being an efficient maker of capital goods to a safe and reliable provider of thrust in the mode of a complex service system. The airline no longer needs to purchase or lease a jet engine; they just purchase the use of thrust. This is what the service-oriented enterprise is all about, and it changes everything that

we thought we knew about business models.

Implications of operating as a service system

The implications of operating a business as a service system in a service-based economy change everything in the enterprise.

The organizational structure of the enterprise needs to adapt so that front

office and back office functions become more seamless, and financial metrics and governance become the new frontier.

A goods manufacturer sees product sales as a single transaction. A service provider sees and deals with a valued long-term relationship. Product revenues are counted as the products leave the warehouse or factory, while service revenues are earned, over time; and cyclical revenue streams tied to product releases become more consistent annuity revenue streams with services.

In other words, the enterprises of tomorrow will need to become a large complex service system, interconnected across the enterprise and aligned to maximizing customer outcomes. It is not good enough to just leverage post-sale service infrastructure and knowledge. Companies will need to leverage the entire enterprise to co-create value with their customers in the new service-based economy.

Once a company can start to focus on value co-creation, there is a natural shift from an internal silo-based organization interconnected only at the top by vague business goals to one that is collaboratively driven on mutually beneficial external targets. The lines between front office and back office fade and the goals of design and engineering become aligned to the same goals as sales and support. The traditional models of organizations from the concepts of industrial specialization taught by Adam Smith and others dramatically changes. This change affects how we manage and how we govern in ways not really taught in business schools today.

IBM's shift to provider of IT services

IBM, well regarded for having made a dramatic shift from being a manufacturer of data processing technology to being a provider of information technology services, can illustrate the difficulties that these shifts in business models can bring. I know, because I was a part of the process at the time. There were challenges both big and small during the transition. For instance, from a Wall Street perspective, IBM was classified as a manufacturer of goods. The principle metric for

manufacturers was the return on assets (ROA). How much profit could be returned based on the assets that it held in pursuit of building "stuff"? They were compared with peer groups like GE, GM or other computer makers. When IBM started to leverage their own infrastructure and knowledge to create customer value by outsourcing the IT shops of their customers, it was a lousy ROA metric. However, it was a great ROI business, and one that kept IBM from going into bankruptcy. The definition of service as leveraging resources and "knowledge" to create economic value for the benefit of another was not understood in the traditional business models from manufacturing. An asset is no longer just a machine tool or building, it can also be specialized knowledge, process methodology and other non-tangible

but for the most part knowledge is in the people. You can protect a hard asset like a computer from loss, but how do you do this with people? How do you capture the knowledge of those people so that it can be leveraged and managed as you might with other intellectual property?

The innovation required to make a jet engine into a service had more to do with business innovation than it did with technical innovation. Managing a global fleet of engines is no small feat. The agreements between suppliers, the airlines and the like have to line up and be based on the same objectives. If, for example, you depend on global communications to receive and process jet engine telemetry, the providers of that infrastructure had better have the same goals when it comes to passenger safety or passenger satisfaction. The

Unfortunately, the only school graduating students of higher learning in these service subjects today is the school of hard knocks.

things. IBM had to change the way that they measured success and convince Wall Street that not only is service a good business model, but it requires new thinking in terms of economic impact.

The service evolution is far from complete. Most companies operate along the service evolution continuum from basic warranty support, to value-added services that reduce cost of ownership, to solution providers who bundle products and services together. A few companies have progressed beyond being just a solution provider and integrator of "stuff" to the service-oriented enterprise. Those companies that have shifted from pure product toward pure services orientation have done so in reaction to business cycles and not with a strategic plan on how to change those fundamental operational issues such as supply chain management, contract management, risk management and governance. Just look at risk management as an example. If knowledge is an asset of the enterprise, where does that knowledge reside? It might reside in technology,

supply chain is only as good as its weakest link.

Service development needs to be a company-wide effort

Perhaps the scariest thing today is that service offering development is too often done in the marketing department. The services are not developed with an engineering-type rigor. Service development typically is not done using product life-cycle management principles either. Bringing a product to market usually has a defined set of steps and reviews before launching. Does a service have the same rigor for release in your company? If you are creating a product as a service, like the jet engine example, do your product life-cycle methodologies include all the right checks and balances?

Everything changes when you become service oriented

As I said before, everything changes in the service world. Service requires good cross-domain knowledge. Those most successful at these transitions have ensured that they had cross-

functional teams with the right incentives and alignment to ensure good customer outcomes. Companies had better learn scenario-based planning and know how to deal with complex, interconnected processes. In this world, the services need to be developed in unison with all players at the table, including the customers in many cases. Legal, finance and operations need to be with marketing and engineering as a part of the development process. All of these players need to understand that service is a value outcome, not just something that you add to the product.

Unfortunately, the only school graduating students of higher learning in these service subjects today is the school of hard knocks. Today's practitioners need more than just core skills in contract management or traditional supply chain training. Cross-functional skill sets are required to operate in the services world. The services world will require understanding people, process and technology across the enterprise. Traditional supply chain management now has to extend to the customer if there is to be value co-creation.

People who create the contracts now have to be forward thinking, as the relationships between the parties now last years, rather than ending with the completion of a sale. Firing a supplier has new implications, as the supply chain now has to be retained for the life of the contract.

Concluding remarks

My intent here was to get you thinking about new service models and the complexities they present to a traditional product company and traditional thinking. Becoming more service oriented is not an option, as customers demand that the

relationships with suppliers must be tied more closely with their needs. A service-oriented enterprise has to be more holistic. While the world's economy may be mostly driven by service today, companies have not yet effectively learned how not to manage their enterprise like a manufacturer. Will you be ready to lead in the new service economy? ❖

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Managing supplier integration in new product development



ROBERT B HANDFIELD, North Carolina State University and
TIM MINAHAN, Ariba Corporation

Introduction

Research in new product development (NPD) has shown that a number of factors are important to the creation of successful new products. Two of these more firm-centric factors include *design for quality* and *design for manufacturability*.

Expanding our scope of vision beyond the individual firm, the concept of *design for supply chain* also becomes important.

Although extensive research has focused on integrating customer requirements into new product development, it is only relatively recently that *supplier* integration has received significant attention. Despite the criticality of this subject to managers, mechanisms for successfully coordinating decisions on how products are designed, how they are manufactured and/or delivered, and how the supply base can support the manufacturing/delivery of such a design are still largely undetermined. Moreover, supply chain design is effectively determined during the product development stage — when product, process and information systems decisions are specified and determined.

Early involvement allows procurement and suppliers to suggest new technologies, manufacturing methods and processes that add joint value and competitive advantage — *before product design is locked down*. Involving procurement in design also advances initiatives to meet and beat target cost models and to ensure sufficient supply capacity and quality to support proposed designs at volume production levels.

The nature of relationships between customers, manufacturers and suppliers is also often established early in the

new product development process. It is at this stage that critical decisions are made, with respect to not only the functionality of the product for the customer but, indeed, the packaging, logistical channels, source of materials, and selection of product and process technology that will provide the end user with the desired functionality. In the words of a senior purchasing

“Suppliers are like fish in the ocean. We (the buyers) are the fishermen. The key challenge facing us is how to put out the right bait, so that we can pull up the right suppliers at the right time and get them to help us develop our products.”

executive at a major automotive company interviewed during this research: “unless you can impact the sourcing early in product development, you have almost no impact on the resulting design of the supply chain.”

Indeed, an Aberdeen Group examination of product development approaches found that companies involving suppliers early in new product development process were able to:

- reduce new product material costs by nearly 18%;
- improve access to innovative new products and more stable supply;
- increase the accuracy of product costing;
- improve initial product quality by more than 20%; and
- reduce time-to-market cycles for new products by 10% to 20%, allowing companies to capture greater market share and profit margins for being an early mover.¹

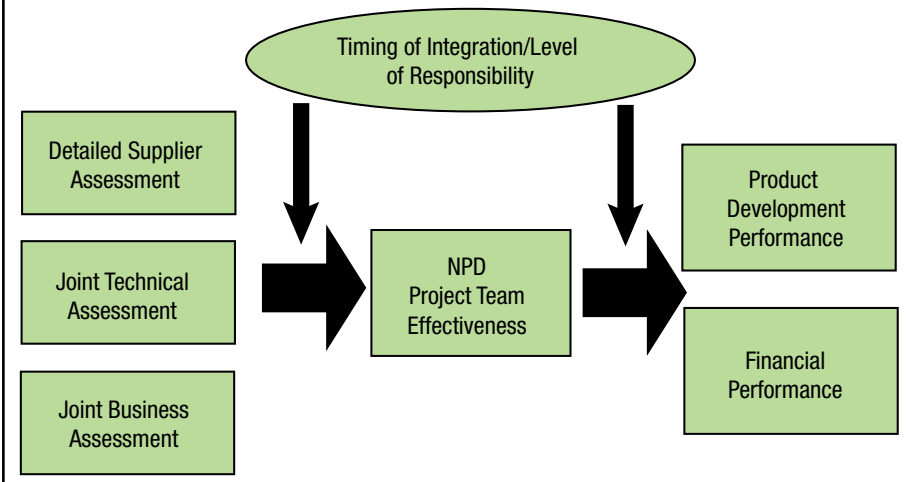
The challenge of supplier integration

More than 60% of manufacturers report initiatives to involve procurement, suppliers and other relevant stakeholders earlier in product development. Despite the importance of the supplier relationship, many managers we spoke with characterized the execution processes for integrating suppliers into NPD projects as a “black box”.² Prior research suggests that the participation of these outside constituents is important, but that many of the processes associated with integration of third parties (suppliers)

into the process are lacking. Our case studies suggest that companies who are successful at supplier integration employ a *systematic process*.³ There are several elements of early supplier integration (ESI) that act as coordinating mechanisms in this context. One area of importance to managers relates to the critical elements required to develop and manage the business relationship with suppliers. A second area of importance is the extent to which such supplier integration efforts have a meaningful financial benefit, as pursuing them is certainly not without a substantial investment of time and resources.

One North American manager we interviewed explained this challenge using an interesting metaphor: “Suppliers are like fish in the ocean. We (the buyers) are the fishermen. The key challenge facing us is how to put out the right bait, so that we can pull up the

Figure 1: Research model showing the importance of various assessment procedures in determining product development team effectiveness and firm performance (including the effect of the timing of supplier integration and level of responsibility awarded)



right suppliers at the right time and get them to help us develop our products. There are several problems associated with fishing: How do we know we're using the right bait? How do we know the right kinds of fish are in the water? Most importantly, when we catch a fish, how do we know whether it's the right fish, and whether we should keep it or throw it back in the water? Finally, how do we know the fish will follow through with its commitments if we decide to keep it?"

There are several key management issues that can enable improved supplier integration into new product development. These are discussed below.

Detailed supplier selection process

The buyer firm must undertake a detailed assessment of the suppliers being considered for involvement, leading to the selection of a supplier with capabilities well-matched to the buying company's needs. In fact, more than a third of the product development process is tied up in assessing the market to understand customer preferences and requirements, and searching for new parts required to create a product concept. Most companies expect that a supplier who is involved in the design process will also supply at least a portion of the volume production requirements for the item, so supplier selection criteria relevant for any

sourcing decision will be relevant here as well (eg, price, quality and delivery). Additional criteria specific to considering a supplier for integration into an NPD effort are also necessary, such as past experience with the supplier, and alignment of culture and technological capabilities. A rigorous supplier selection process, which yields a supplier with capabilities that are a good match with the buying company's needs, will lead to improved project team effectiveness.

Key questions:

- Do we have a systematic supplier selection procedure? If not, one should be developed prior to supplier engagement.
- How familiar are we with the supplier? Has the supplier been involved in NPD efforts with us in the past?
- What level of engineering design capabilities does the supplier possess?
- Can the supplier support or provide future technological development?
- Can the supplier meet its volume obligations once production commences?
- Is there a "fit" or alignment between with the supplier's culture and the organization?

Joint setting of project's technical goals

Supplier input and involvement in the assessment of the technical elements associated with the project (quality, reliability, functionality, and

so on). Given that new technologies are very often closely associated with the inventing firm's (supplier's) core competencies, buying firms must develop and manage cooperative/collaborative relationships with their key strategic suppliers in order to gain access to key emerging technologies. The objective is to maintain a selection of promising and accessible technologies and suppliers on the "bookshelf", ready for use when the company wants to apply them in a new product application.⁴ The company must understand, influence and possibly manage the development time of technologies so that they will be available when needed. A key aspect of these relationships is leveraging the suppliers' knowledge of what is feasible from a technology perspective. One way to do this is to involve the suppliers in performing the technical feasibility assessment and setting the technical targets for the project.

Key questions:

- Was the supplier involved in setting technical performance measures and targets?
- Do we have clearly defined and agreed technical performance targets for both parties prior to project commencement?
- How appropriate to our business strategy is the technology selected, relative to others on the "bookshelf"?

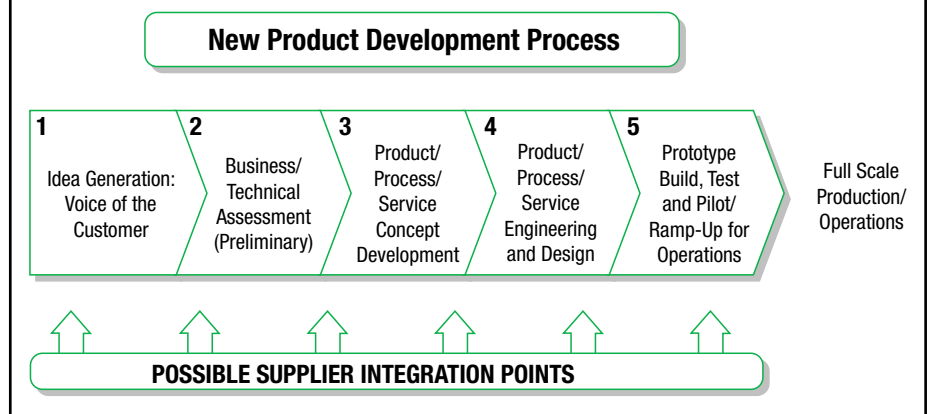
Joint setting of project's business goals

For technology sharing to lead to better supplier solutions, a critical element is the assessment of the business case for supplier integration. All parties on the product development team, as well as key supplier personnel, must understand and agree on the expected benefits associated with the supplier integration effort, in terms of cost, quality, pricing, scheduling, roles and responsibilities. When such elements are openly shared and measured over the life of the project, the outcome is not only a new product, but often lower costs as well.⁵

In other interviews, managers noted that suppliers who had participated early in initial technology sharing discussions later contributed to setting goals regarding project outcomes. Suppliers, because of their product

and process knowledge or expertise, may have more realistic information on the trade-offs involved in achieving particular goals. Such goals are not limited to cost but often include product performance characteristics (such as weight, size, speed, etc) and project performance measures (such as development time). The buying company will have the ultimate authority in goal setting, but the supplier's involvement can help in setting goals that are aggressive but achievable and also help in assuring the supplier's "buy-in" to the goals. For example, a leading Japanese firm visits its key suppliers before the detailed design of a new product begins. These visits help the purchaser decide if the supplier can produce an item at the targeted cost and quality levels. The buyer also assesses the supplier's ability to become part of the product development team. After a general discussion about the technology required for the new product, the supplier submits an initial design

Figure 2: A typical new product development process, with possible points of supplier integration — the earlier key suppliers are involved in the process (stages 1 and 2), the better the project outcomes



Performance outcomes

We also sought to explain the effect of project team effectiveness on the company's financial success and product design performance. Commitments of time, people, funding and effort on the part of buyers and suppliers represent significant investments on the part of both parties. These commitments are deployed with the expectation of

review product development progress, plan new product launches and align technology roadmaps. In some cases, manufacturers have developed gain-sharing opportunities for supplier cost reductions, productivity improvements and other value-added suggestions from suppliers.

The second aim of this study was to assess whether the effectiveness of the managerial practices described in our first goal (joint setting of project's technical goals) was affected by the timing of supplier integration and/or the degree of responsibility awarded to the supplier for the product design. Each of these factors is likely to impact on the success of the supplier integration effort, and is elaborated below.

- **The timing of supplier integration** (ie, earlier or later in the NPD process). We were interested in whether the relationships in the model vary depending on when a supplier becomes involved in the new product development process. As shown in Figure 2,⁶ there are at least five different phases of product development at which suppliers might be involved.

Prior research on ESI maintains that earlier involvement is always better. There is evidence to show that earlier integration is beneficial in cases of higher technology uncertainty; however, the benefits of earlier integration are also countered by the disadvantages of being "locked into" a particular supplier, especially when there are multiple competing technologies vying to become the industry standard.⁷ We compared companies who integrated a supplier in stages 1, 2 or 3 versus those

Leading performers have clearly defined and documented procedures for standardized product development and cost management activities.

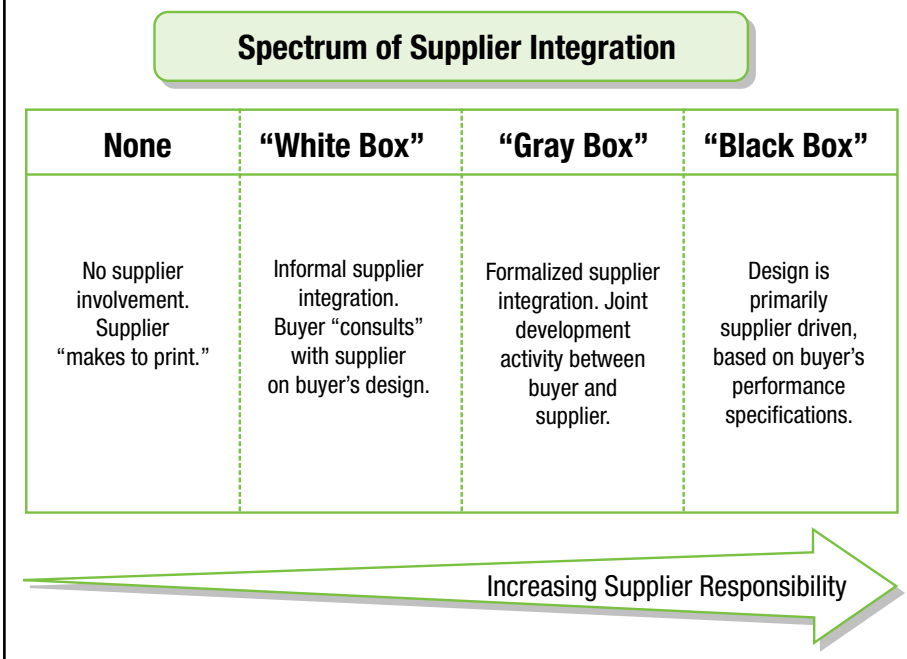
proposal. Starting with a basic frame and shape based only on broad product requirements, the product design evolves, with engineers from both companies working together to evaluate alternative designs that satisfy product requirements.

Key questions:

- Have we adequately specified the terms of the engagement? For example, costs, scheduling and quality levels.
- Does the contract provide for agreement on intellectual property and confidentiality of data?
- What level of input has the supplier had in the process? The higher the supplier involvement, the higher their "buy-in".

an *improved product design* (ie, the degree to which the project resulted in a design that was easier to manufacture at a reduced cost and with a better fit with the finished product), as well as improved *financial performance* (increased sales, increased profit and increased return on investment). Leading performers have clearly defined and documented procedures for standardized product development and cost management activities. These firms have established metrics for measuring product development performance (eg, on-time product launch, quality levels, accuracy of cost targets, deviation from cost targets, and so on.). They also conduct regular meetings with strategic suppliers to

Figure 3: The spectrum of supplier integration, ranging from no involvement through to total supplier responsibility for product design



that integrated suppliers in stages 4 or 5.

- **The level of responsibility assumed by the supplier** (eg, more or less responsibility for product design). Another question that arose from our case studies addresses whether or not the relationships vary depending on the supplier’s level of responsibility for the buyer’s new product development process. We conceptualized “level of responsibility” as the spectrum of supplier integration in Figure 3, including:
 - no involvement;
 - “white box” (the supplier is consulted informally on the project);
 - “gray box” (there is a formalized joint activity that takes place); or
 - “black box” (design is primarily supplier-driven, based on the buyer’s performance specifications).

Table 1 provides further detail on the integration of suppliers in product development. The black box form of involvement constitutes the highest level of integration and customer–supplier information sharing with a great deal of give-and-take during the process. We compared companies who employed gray box integration with those who indicated they employed black box integration.

For example, Harley-Davidson has long made ESI a foundational

component of its product development process. The motorcycle legend has established new product development sourcing groups that co-locate sourcing and commodity managers (most of whom are degreed engineers) with their product engineering groups. Depending upon the design and situation, Harley Davidson will also co-locate key suppliers on-site within its development facility. These commodity experts collaborate with engineers from design concept through to production build to determine the supply mix that provides access to leading innovations, ensures ample capacity to support intended production volumes, and can beat target and should-cost goals.

Table 1: Various integration levels for supplier integration

Integration level	Description
White	Discussions are held with suppliers about specifications/requirements, but the buying company makes all design and specifications decisions.
Gray	The buyer and supplier enter into an informal, or sometimes a formal, joint development effort, which may include information and technology sharing and joint decision making regarding design specifications.
Black	The supplier is informed of customer requirements and then is given almost complete responsibility for the purchased item, with only review and concurrence on the purchased item’s specifications by the buying company.

Lessons for managers

The results of our study led to a number of lessons for managers. These are outlined as follows.

Lesson 1: Conduct a detailed supplier assessment prior to project commencement

Our results support the notion that firms who complete a more careful analysis of the supplier’s capabilities prior to commencing the NPD project will experience enhanced project team effectiveness. This has critical implications for practicing managers as it emphasizes the central importance of making the right decision about which supplier to work with up front. Not only are the supplier’s capabilities important in this decision, but so is finding a supplier who has a compatible culture with the buying firm.

Lesson 2: Involve suppliers in setting technical goals

Our results support the notion that firms who involve the supplier in examining the technical feasibility of the project will experience enhanced project team effectiveness. Involving the supplier helps leverage their knowledge of technical feasibility, resulting in a smoother project with more realistic expectations and targets.

Lesson 3: Joint setting of business goals has no effect on project team effectiveness

Interestingly, the business assessment of the project had no impact on project team effectiveness of supplier involvement. This may suggest that supplier input on technical issues is

more important than on business issues, and that if the technical assessment is done well, the business case will follow.

Lesson 4: Greater NPD team effectiveness improves the quality of product design

This result indicates that as we improve the management of the NPD process, particularly NPD teams, we can expect better quality design outcomes. In addition, leading performers are hiring or developing procurement, commodity and supply chain experts who are degreed engineers, so they can identify technical innovations in the supply base and “speak the language” of the design team. The result includes lower item cost, ease of manufacture, and greater alignment of the supplier component with the overall product architecture.

Lesson 5: Greater NPD team effectiveness improves financial performance

This result is encouraging for the proponents of early, and extensive, supplier involvement. It shows that a firm can expect to achieve real financial benefits from their inter-company product development efforts.

Lesson 6: Timing of supplier involvement

Analysis of the “earlier” versus “later” integration efforts reveals that supplier involvement in *technical* project assessment is important in earlier-stage integration efforts, but not in later-stage integration efforts, while supplier involvement in *business* project assessment is important in later-stage integration efforts, but not in earlier-stage efforts. This may reflect the types of decisions that are being made during the stage at which the supplier is first involved. In the very early stages, the project is less well defined, and there may be significant uncertainty about the feasibility of the project. The focus of interaction with the supplier is likely to be on the question of technical feasibility of the project, with the business case coming later.

For example, at office products manufacturer Steelcase, supply chain managers get involved at the new product concept phase. These supply chain experts develop an early supply chain strategy for the product,

examining locations of potential major customers, how the product will be delivered, what supplies are needed and how they will be delivered to Steelcase manufacturing, and options for product customization. When the product reaches the development phase, suppliers become actively involved. Steelcase has also set target costing goals for new product launches, measurements of supply chain progress and activity related to new product launches.

Lesson 7: Degree of supplier responsibility

Analysis of the “gray box” versus the “black box” integration efforts shows that supplier involvement in technical project assessment is more important in black box efforts than in gray box efforts, while supplier involvement in business project assessment is more important for gray box than for black box efforts. This suggests that suppliers who are assuming greater responsibility in the design effort need to have input into the technical assessment in order to assure effective decision making, and probably need to share more information with the buying company. Suppliers involved at a black box level are assuming broad responsibility for making sure the component/system they design will function properly in the overall product. Suppliers who are taking on less responsibility in the design effort don’t need the same level of interaction with the buying firm regarding technical issues. ♦

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Contractual challenges in moving from products to services and solutions



PROFESSOR SOILI NYSTÉN-HAARALA, University of Joensuu, Finland

Companies operating in a life-cycle business must have contracting capabilities which are compatible with this kind of business. Capabilities developed in earlier business models, such as a product sales business, are no longer sufficient.

Key points

- Contracting capabilities can be found at different levels of the organization and should be harnessed, documented and incorporated into the business processes.
- Each business model requires compatible contracting capabilities.
- Contracting should be a team-driven process, not the domain of one individual.

Transferring to a life-cycle business requires senior management to have a holistic appreciation of the company's contracting processes and contracting capabilities, ensuring that they are aligned with each other and with the company's business.

Contracting capabilities as part of business know-how — a practical example of the processes

Empirical research which we conducted in a number of enterprises in Finland has influenced the construction of this example, which seeks to depict the challenges faced by service and life-cycle corporations.

The company sells machines, equipment and production lines. In addition, it services both the equipment it sells and that of other manufacturers. It decides to concentrate on service business which, in addition to generating continued income, may provide it with more market feedback about its own machines, equipment and production lines, which could then be improved.

The company has a small legal department which has been given the

task of developing contract models for new business operations. The managing director has asked the lawyers to develop new service contracts, at the same time ensuring that the legal risks of the new contracts are manageable.

The first objective is to make clear that the contract is more than just a legal document. The lawyers cannot consider legal risk management unless they understand the company's business and its new service business operations. The core objectives of contracting capabilities in these circumstances are developing service descriptions; renewing the content of the contract templates; ensuring the compatibility of pricing and service levels; and developing warranty and incentive systems. This development work requires cooperation among the company's different groups and departments. This task should be given to a working group including people involved in sales and service; a lawyer; and individuals responsible for customer support and repair services.

The contract processes should be standardized and documented to ensure that the contracts are clearly and continuously under one person's management from the drafting of service descriptions, negotiations and contract execution, to the end of the contract. It is recommended that overall responsibility for the contract process be given to a contract manager. If this is not possible, someone else should be charged with the responsibility of ensuring that the "communications baton" is passed

smoothly from one contract stage to the next.

As not all customers are interested in buying services related to the purchase of equipment, the company should also consider what customer-orientation means in practice. How can the service provider be integrated into the customer's processes, how can the customer be convinced of the need for service, and how can the service-provider's own profit be guaranteed? The tools and opportunities of risk management differ between a service business and a product sales business. Service business contracting capabilities emphasize relational capabilities and flexibility. Mechanisms for managing contingencies can also be incorporated into the contract document, since they are more the rule than the exception in a service business.

Benefits to companies

- Companies learn to apply contracts as tools for implementing business strategies and risk management.
- Companies learn to align contracts, the law and business for their competitive advantage.
- Small-to-medium enterprises learn from large companies what entering the life-cycle and service business requires from them. All participating companies acquire tools which help them update contract content and processes of their whole value chain.
- By developing and documenting the contracting capability and know-how within the company, it can offer flexibility and alternatives to the customer.

Contracting capabilities identified

The research divided contracting capabilities into capabilities connected with:

- **contract content** (documents, default rules, trade customs and practices between enterprises);
- **contract process** (organizing contracting with the company and contract management); and

- **relational capabilities** (in dealing with the clients).

These three types of capabilities often overlap.

Contract content capabilities

The shift from a product sales business to a life-cycle business requires a total change of approach to contracting. While the sale of goods makes the seller think about limiting the liabilities with warranties, life-cycle performance partnering focuses on performance-based obligations, with a clear definition of the outcomes and metrics for evaluating them. Introducing incentives for better performance also affects pricing. The scope of the contract for the sale of goods is determined by specifications, while in service business, service descriptions and the customer's role become important. This change inevitably requires more tailor-made contracts, as using standard contracts or even a company's own templates becomes complicated.

Flexibility is required in service and life-cycle contracts, since the need to adapt to contingencies is more the rule than the exception in this kind of business. Contract law, on the other hand, does not support flexibility, because it aims to define the conditions of the contract and foresee potential changes in circumstances. Incorporating flexibility into the contract documents to respond to changes in circumstances is a huge challenge. Examples of such contractual clauses are scarce. Quite often, companies are satisfied to renegotiate clauses, even though there is no mechanism on who negotiates with whom and how. The absence of adequate standard or model contracts makes it difficult for companies to develop their contracts to meet the challenges of a life-cycle business. However, the need for flexibility does not mean that safeguards should not be included. In fact, the seller's risks increase in a life-cycle business and risk sharing becomes an important issue.

Contract process capabilities

Small companies in which the CEO still can manage the processes do not have standardized contracting processes. When the company grows, the need for standardized contracting processes increases. This should,

however, not lead to a rigid list of "dos and don'ts" from the legal department, which may hinder sales decisions. Additionally, a life-cycle business requires the company to enter into the customer's processes and, further, a collaborative joint mapping and information analysis with the customer from the beginning to the end of the process.

Relational capabilities

The significance of relational capabilities increases in a life-cycle business where joint planning, achieving mutual goals and meeting customer targets are important factors. Differing operational policies, concepts and cultural habits pose challenges for relational capabilities. The quality of the relationship should be taken into account, from customer selection through differing opinions and understandings or handling of disputes during the cooperation process, to a positive termination.

Practicing a customer-oriented approach is challenging and risky, and requires a new way of thinking from both parties. Too often, there is a dichotomy: the sales people sell services as tangible products and the lawyers focus on limiting liabilities. Adopting a customer-orientated approach is more challenging when the customer is not ready for it and prefers a more traditional maintenance contract. Unguarded customer orientation may turn into customer dictation when the seller is not prepared for such a relationship, but when the customer knows what he or she wants. The sharing of both the risks and the benefits is indeed a commendable objective in a relationship, but not easy to achieve in practice.

Lawyers and contracting

One special issue which the group studied was the role of lawyers in contracting. Our research results show that the lawyer is still seen as a legal adviser who safeguards the company against liabilities. If the company's lawyer still works with the contracting models which represent the traditional sale of goods, the lawyer may create a burden for the sales people who want to shift to a life-cycle contracting model. It is

still very seldom that the lawyer is accepted in business processes and is consulted from the beginning to the end of the contracting process. The lawyer is called upon when something goes wrong, or asked for advice when the sales people want to change the templates. In the latter case, the lawyer often takes a strict safeguarding position. In practice, it is difficult to find a proactive business-oriented team with lawyers working as proactive legal advisers. One reason may be found in out-of-date working methods and thinking modes of the organizations — both in companies' decision-making practices as well as in the legal education.

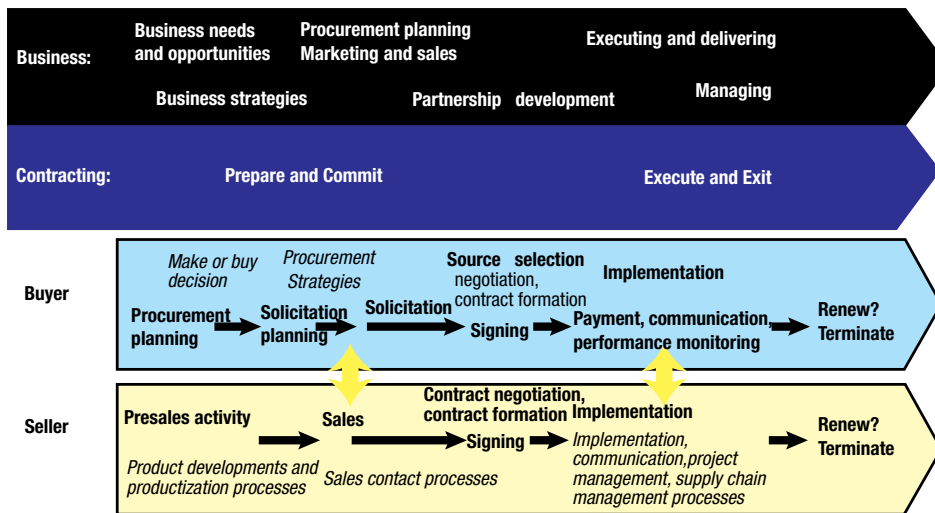
About the research consortium

The research consortium, Corporate Contracting Capabilities (1.1.2006–30.4.2008), conducted multidisciplinary empirical research on the contracting capabilities of eight Finland-based international companies of different sizes and from different industries. The final report focuses on life-cycle business. The financiers of the research were the Finnish Funding Agency for Technology and Innovation (Tekes) and the Academy of Finland.

The research group understands contracting as a process starting from preparatory phases, such as product development and productization of services from the seller's side and procurement and solicitation planning from the buyer's side. The process continues through contract design, commitment and implementation intertwined with business processes. A broader perspective of contracting helps companies in finding and developing their contracting capabilities at different levels and in different departments of the company and helps them to orchestrate the capabilities in creating and capturing value. In practice, however, companies still seem to understand contracting too narrowly as the designing and signing of documents (the dotted line in the figure below).

CCC was a pioneering project. There are still very few empirical studies, and a corresponding contribution to the theory of contracting is missing. Actually, there is no comprehensive theory of contracting, only a collection

Figure 1: Contracting and business processes



Source: CCC project final report 2008

of separate contracting theories. Contracting is, however, studied more and more, and theory will in the future develop in cooperation with different research groups. Before any theoretical breakthrough is possible, many more empirical studies are needed. Such studies require cooperation between business and academia.

In part, the work continues in a new research group, “Intellectual Property in Open Business Models” (2008–11), a joint project with the Technical Research Center of Finland (VTT) in Tampere and Joensuu University, financed by Tekes. The model for contracting in open business models in creating innovations is even more

challenging than life-cycle business contracting. Contracts have to be truly relational, since in the beginning nobody knows what the innovation — if any — will be and how the costs and benefits should be shared.

For more information on the method and theoretical background used in this research project, please contact Professor Soili Nystén-Haarala. ❖

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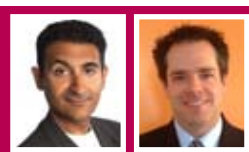
Links

The project web page and the summarized final report of the CCC project in English can be found at <http://yliopisto.joensuu.fi/oikeustieteet/siviili/CCC%20Research%20Report.pdf>.

Tekes Liito program: <http://akseli.tekes.fi/opencms/opencms/OhjelmaPortaali/ohjelmat/Luotsi/en/etusivu.html>.

IPOB project: www.3vtt.fi/proj/ipob/index.jsp.

Why integrating your buy-side and sell-side agreements in one contract management system is advantageous



**ASHIF MAWJI, Upside Software Inc and
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Furthermore, when it comes to the data, one company’s buy-side contract management is another’s sell-side, so there is *no* compelling reason to separate the two.

Benefits from integrating buy-side and sell-side contracts

If you take the approach of integrating all of your enterprise contracts into a single repository within a single contract life-cycle management (CLM) software tool, the benefits you’ll immediately recognize are savings associated with:

- having closely aligned and streamlined processes for both buy-side and sell-side contract management that align with overall corporate strategy;

Key points

- By combining buy-side and sell-side contracts into a single repository, you can provide tremendous value to your executive leadership in the areas of compliance, reporting and savings.
- This article advances 10 compelling reasons why you should integrate both buy-side and sell-side, shows how to structure your project team in the appropriate manner, and advises which type of contract you should go live with first.

Typically, buy-side and sell-side contract departments are separated within organizations and utilize different processes and systems to obtain the same outcome — an executed contract — however, the more important goals include management of the performance, delivery, payment and compliance obligations agreed to. The obligations relating to either buy-side or sell-side agreements are managed in a similar manner, so it makes sense to have them in one centralized system.

- providing executive level visibility into every contract enterprise-wide;
- integrating contract data with customer relationship management (CRM) or financial systems to automatically maintain master supplier and customer profile records, thus ensuring accuracy of data and elimination of duplicate data entry;
- automated event management and other date-driven “action items” that can be driven and managed uniformly within a single CLM software tool;
- business intelligence/streamlined reporting that will provide management with the right operational and strategic data to make better decisions (seeing the whole picture rather than one side of the business);
- a complete book of business in a single CLM software tool for reporting and retrieval purposes to reduce the costs associated with looking disjointed to customers, suppliers and your corporate executives when searching for contracts data real-time;
- complete and accurate data for sales forecasting and expenditure budgeting;
- the value created by linking buy-side and sell-side relationships and transactions when your suppliers’ goods and services are transactionally linked to your customers through contracts:
 - as an example, it would be extremely valuable to know which of your suppliers are also your customers;
 - where a specific part/product/service coming from a supplier is refined by your firm and produced into a deliverable consumed by the same entity (ie, your supplier also becomes your customer); and
 - when there are issues on either side (ie, in a buy or sell relationship), it’s critical to know the full impact;
- the ability to strategically govern and manage adherence to approved standard terms and conditions and templates at an enterprise level for both buy-side and sell-side contracts; and

- having complete and accurate data to identify and monitor business relationships, and sensitive or high-profile relationships and their key metrics, ultimately to renew and capitalize such high-value contracts.

It’s sometimes easier said than done to integrate these two sides of contracting. However, it is important to ensure that from a project structure standpoint, the steering committee is comprised of members from both the buy and sell sides of the organization, but that the chair position is from finance, since this group has a huge stake in both groups’ success.

There’s also the question of which goes live first — buy-side or sell-side? There’s no right answer. Traditionally, buy-side has seen a higher return on investment (ROI) than sell-side — however, more recently, the metrics are similar for both groups. As such, it doesn’t really matter which side goes live first, but perhaps deciding who does could be based on the following.

- Which group is ready (ie, have their processes for integration been thought through or documented)?
- Which group wants to go first?
- Which group has the budget? (Or, if they both have a budget, which group has the bigger budget?)
- Which group’s deployment appears to be simpler? (It’s better for phase 1 to be simple as opposed to complex.)
- Which group has been nicer to you? (Just kidding.)

If it’s a tie, flip a coin (but ensure it’s not a two-headed coin).

Irrespective of which group goes live first, it is strongly recommended that both groups’ requirements are taken into consideration before you select a provider. More importantly, ensure that the full scope of the deployment (ie, all the requirements and objectives) is known up-front, as it will affect the design and deployment, even for the first group. It will be important to know some of the following elements.

- What type of data fields will be captured and reported on?
- What type of reporting is required?
- What are you going to do about the existing contracts from a conversion standpoint?

- What systems will you need to interface with upstream and downstream?
- What are the cross-integration requirements between the buy-side and sell-side?

Case study

In a recent deployment undertaken by Upside Software for a Fortune 100 high-tech organization, the client had several systems used by the various organizations for managing contracts. While each system was either procured or built to suit the needs of the specific group it served, the organization as a whole did not have a consolidated repository, reporting or governance pertaining to contracts. As such, the company embarked on a project to find one contract management system to help fulfill the needs of all the organizations it served. After a comprehensive RFP (request for proposal) process, which comprised all the groups as part of a selection/evaluation process, a commercial software package was selected.

The full deployment took about six months to complete, and initially the full payback was projected to be attained within 10 months from when the system went live. There were indeed many hurdles during the deployment, including getting consensus from the various groups on the configuration and setup; however, using a steering committee with one chairperson with ultimate decision-making authority helped resolve these issues.

As the various groups were going through the deployment process, they found that there were a lot of similarities between them, even though the initial impression was: “We are unique and completely different.” The process also helped the groups learn from each other and ultimately improve their contracting processes. They learned an important lesson, in that sometimes best practices come from within your own organization.

Shortly after they went live on the system, they were reaping the benefits outlined earlier in this article. One example pertained to the formulation of their risk mitigation plans and,

specifically, the case of where a major supplier was also a key customer. So, what happens when you can't pay that supplier on time, if that supplier also owes you money (as a customer)? It's very likely that payment will be held back, which does affect cash flow. There were a number of such supplier/customer relationships, so it helped them to adjust their cash flow projections as part of their risk mitigation strategies. Before having a consolidated system like this, pulling such a report would have been a daunting task. Similarly, other interesting data became available, such as:

- If we sever our relationship with supplier X, what revenue impact will we realize (assuming supplier X is also a customer)?
- Which entities are both our suppliers and customers?
- In cases where strategic sourcing principles are being applied to narrow down suppliers, which providers are also customers?

This particular customer was able to get a full ROI within six months of deploying the system (as opposed to the projected 10 months). Needless to say, they were convinced they made the right decision in picking one solution to manage both their buy-side and sell-side agreements.

Conclusion

We have shown the advantages which can be gained from integrating your buy-side and sell-side contracts into a single repository within a single CLM tool, including achieving enhanced ROI on your contract management process. Many of the best-of-breed providers in the market can cater to both these types of agreements. Be sure to do your homework and pick the one that works best for your particular business. It's important to ensure the provider has ample customers for both types

(buy-side and sell-side) and can provide references of organizations that do in fact manage both types of contracts in the same system. ❖

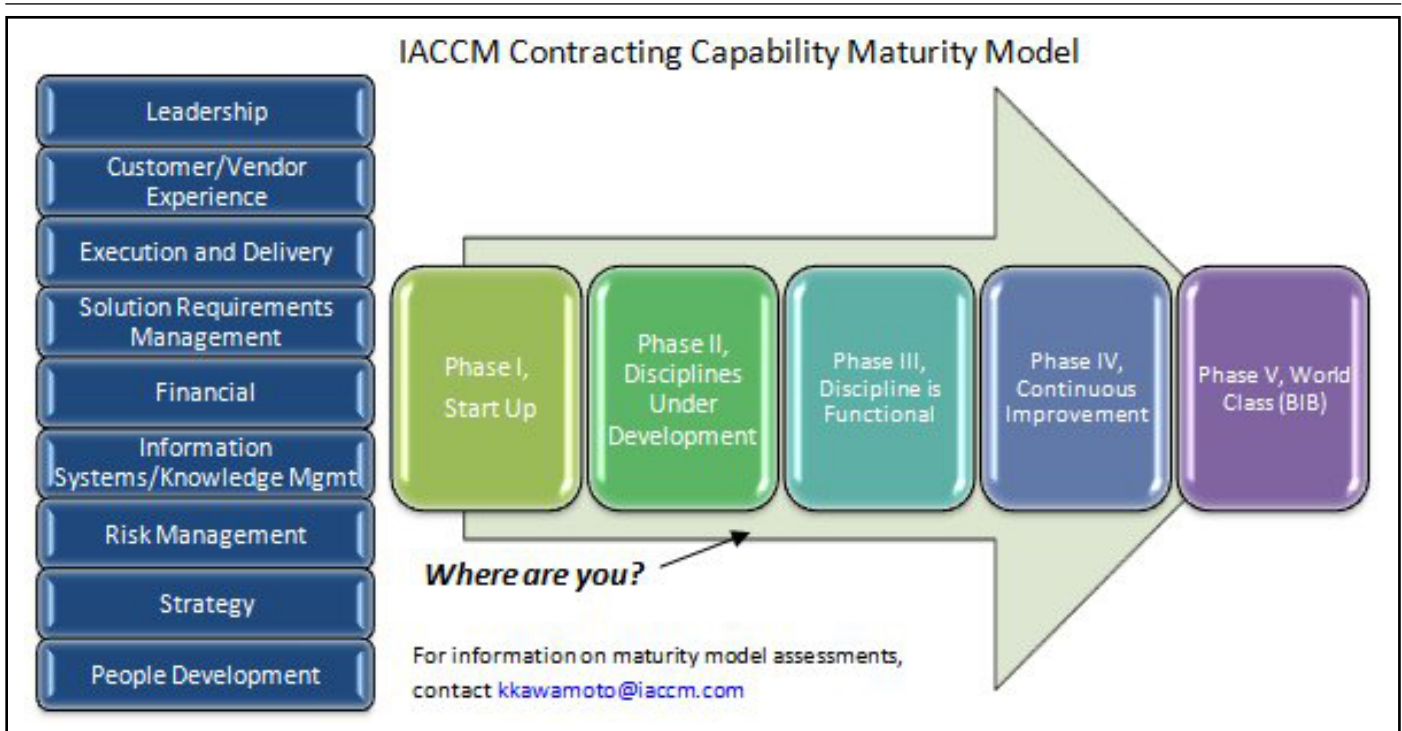
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Rob Rowe has more than 15 years of experience working with legal and contracting organizations on a variety of strategy and organizational issues. Rob has worked within a contract management role in multiple industries including technology, telecom and, presently, the health-care industry. His focus includes the areas of team leadership, cost containment, process improvement and strategic technology utilization. He brings this broad knowledge of different industries, technology tools and contracting experience to his work as a director of contracts administration at OptumHealth.



Better business through proactive productization and visualization of contracts



KATRI REKOLA, Rekola Design and HELENA HAAPIO, Lexpert Ltd

Key points

- Productization (or productification) is used to clarify, simplify and standardize service offerings, and make them concrete and easy to visualize.
- Service productization helps companies to package service modules into service products that are easier to understand, buy, sell, replicate and multiply.
- Contract terms are an important part of service productization — and contracts themselves can be productized to simplify and demystify the contracting process.
- Cross-functional collaboration is essential to the productization process.
- When contracts are appealing and understandable to non-experts as well as contracts professionals and lawyers, they can truly work as a road map for the business relationship and as tools for project, quality and risk management.
- The sooner contractual issues are addressed the better: this is where *proactive contracting* and *service design* come in!

The challenge: achieving true cross-professional collaboration

In the case of most B2B services, the only tangible thing that the customer sees when buying a service is the service contract. Thus, it is not a big leap of imagination to say that a high quality contract is needed for a high quality service, and the sooner contractual issues are addressed the better. While contracts professionals and lawyers can make a valuable contribution to product life-cycle management, few people involved in new product or service design, or development, have contracts or terms high on their agenda.

Contracts mean different things to different people, and some product and service managers regard contracts as a nuisance that gets in the way of doing business. Obviously, not all have such extreme views; however, it is common for some to ignore the importance of contracts as tools for project, quality or risk management.

The challenge is how to promote understanding and acceptance of the views and expertise of different

professional groups and a sense of a mutual goal — successful implementation and satisfied customers — among all professionals, and how to overcome preconceived ideas and attitudes that get in the way of true collaboration.

A productized service can be seen as a package of service modules contained in a contract.

Productization is a way to meet the challenge

In service design and development, the term productization refers to a method that aims to clarify, simplify, standardize and make concrete and easy to visualize service offerings. Productization of services draws on the

principles of modular design — that is, breaking the service process into modules that can be used by several service processes, and bundling a set of those service modules into a package — the “service product”. A productized service can be seen as a package of service modules contained in a contract. The contract describes the roles of the parties and the core content of the offered modules, along with appropriate terms and conditions.

When contracts, too, are regarded as products that can be modularized, simplified, visualized and compared to those offered by other companies, it will be easier for contract professionals and others involved to “sell” contracts internally and externally — and easier for everyone involved to understand and translate contracts into desired action and outcomes.

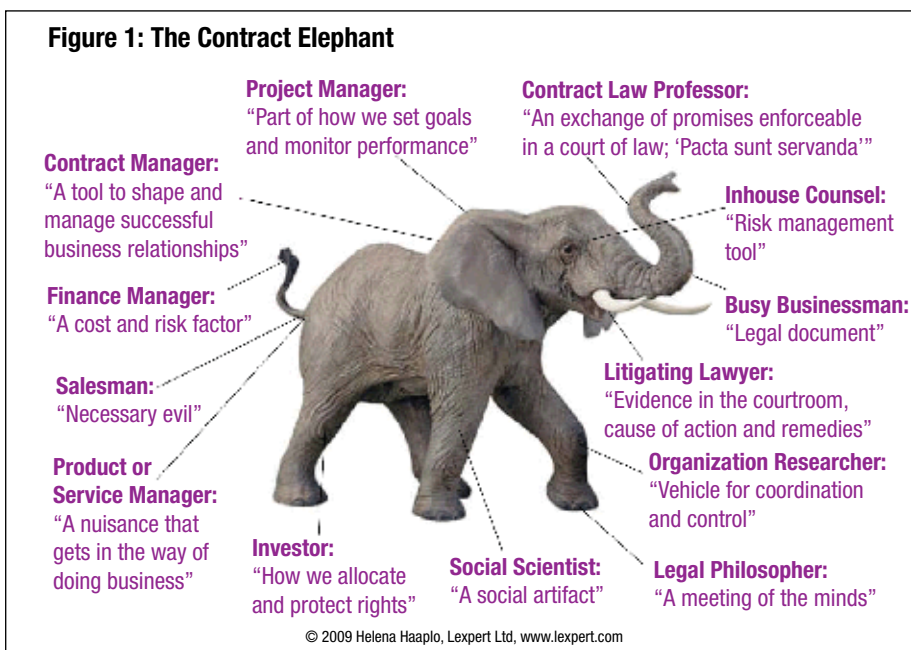
Visualizing contracts

One of the goals of productization is to visualize the invisible. Service development professionals are familiar with flow charts and other visual ways to illustrate just about anything.

Why not extend this same method to contracts and contracting? The Contract Elephant (see Figure 1) is a good starting point.

As we all know, flowcharts and mind maps enable us to quickly see the big picture as well as the details, and can help us to communicate and

Figure 1: The Contract Elephant



evaluate a proposed transaction or relationship (or network of transactions and relationships), assess its risks and opportunities, and co-create tools to control them.

In the context of knowledge visualization, *strategy visualization* has been developed into a fine art, one of its aims being to activate and engage employees.

Visualizing legal information ("Rechtsvisualisierung") has become a research field in its own right, especially in Central Europe, where one of the pioneers, Colette R Brunschwig, wrote her doctoral thesis on "Visualisierung von Rechtsnormen — Legal Design" ("Visualization of Legal Norms") in 2001, focusing on the formation of contracts under the Swiss Code of Obligations. In their article "Doing deals with flowcharts", in *ACCA Docket's* 2001 October issue, Henry W Jones and Michael Oswald discussed the various benefits, with examples, and the technology tools available to help attorneys and others to use flowcharts to add value and improve productivity and efficiency.

New tools have become available since 2001, yet we know very little about their application in contracting. Why not develop the ideas and examples further through both empirical and theoretical research? Why use just text, black on white, when crafting contracts or contemplating their terms? Like the authors of this article, many IACCM members are already involved in such projects. Why

not combine our efforts, collect what we already know, and then take it further?

The advantages of collaboration and productization

For service development, coming up with viable service content is seldom the biggest issue; the real hurdle is bundling it into an entity that is of good quality and is easy to understand, buy, sell, and multiply or replicate, and that sets the service provider apart from its competitors in a positive way. When the barriers to collaboration are overcome, good-quality contracts can provide a valuable tool for project management, a visible script to follow throughout the business relationship, and concrete guidelines to make sure that the measurable elements of the service product stay within the acceptable limits.

Service productization, on one hand, and **contract productization** (including the visualization of its terms and conditions), on the other, should represent two compatible sides of a process that produces successful service contracts that guide the production and delivery of good-quality service products.

Service productization can bring many benefits to contract managers, both on the buy-side and on the sell-side. It can:

- simplify the contracting process;
- provide a well-thought-out basis for a service contract;
- eliminate the need for many different

types of contracts;

- make it easier to truly understand the content and scope of the service; and
- align the terms and conditions with the intentions and promises of the service developers and the marketing and sales people, as well as with the needs and expectations of the customer.

Contract productization, on the other hand, can help make contracts more understandable, and thus easier to accept and adopt as tools or road maps to follow throughout the service relationship.

Ensuring customer satisfaction

Services and contracts should be designed with successful implementation in mind. For the service provider, it is important to bring together:

- the capabilities of the company (its ability to deliver the service);
- the expectations of the customer (what the customer thinks the service is about); and
- the offering of the company (what the company promises to deliver), and to use the contracting process and documents to communicate clearly how the parties aim and agree to work together (see Figure 2).

A discrepancy between these elements inevitably leads to problems. Yet many problems can be prevented when the service is described accurately in the contract. This means having a well-designed service description/specification understood by all parties. A good contract and clear procedures are also needed, so that if problems arise, they can be proactively dealt with before they develop into a business and legal headache.

The learning experiences of Company A — contracts as quality and performance management tools

As we have illustrated, contracts can provide a tangible and enforceable mechanism for ensuring successful service delivery, and a framework and incentives for successful performance. Good-quality contracts establish the basis for control, and clearly outline performance, reporting and administrative obligations and measures. As one global manufacturing company

came to realize (we'll call it Company A), the usefulness of good contracts lies in their ability to provide a mechanism for performance evaluation — and service recovery guidelines in case of a failure to perform.

Performance measurement and monitoring are needed, from the customer's point of view, to make sure that the service provider delivers what they have agreed to, and, from the service provider's point of view, to control and optimize the service delivery process and secure predictable outcomes.

Performance measurement is also essential to improve the quality of future performance. After a couple of false starts, Company A came to learn that this requires precise and measurable indicators specified in the contract and agreed on by all parties. Whatever measures are used, they should be meaningful to both the customer and the service provider. Before realizing this, Company A tended to measure what they could measure, irrespective of its relevance. To come up with a valid evaluation system and key performance indicators (KPIs) that actually work, input from contract professionals, service designers and developers as well as the frontline was needed. Company A also found it was a good idea to use the appropriate standard KPIs provided and defined by a national Standard, instead of devising indicators.

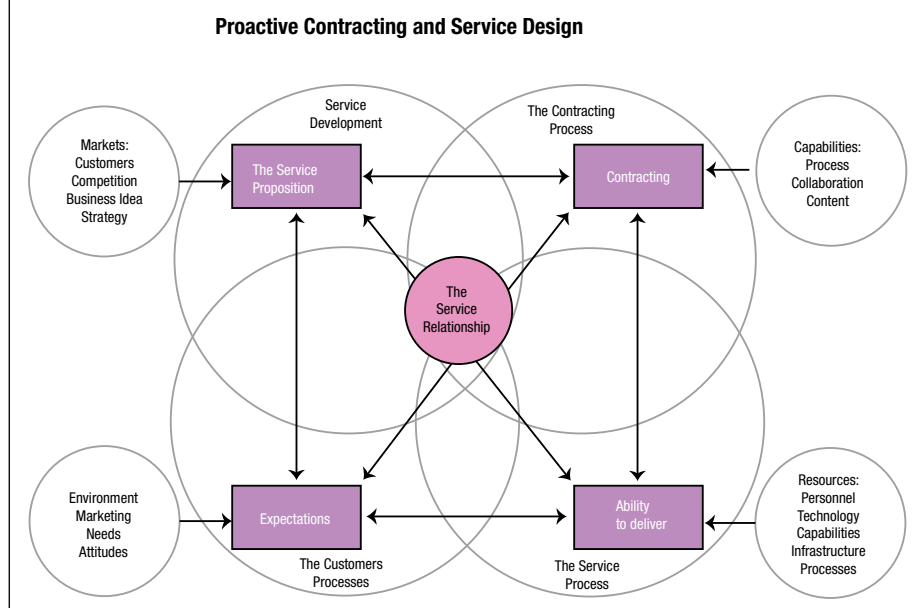
Successful service recovery requires systematic planning and management of recovery procedures. As Company A gained more experience with services, they came to realize this. When these procedures are supported by a clear service description, proactive remedies and well-thought-out governance, complaint handling and dispute control mechanisms in the contract, a sound foundation is set for success, even if problems arise.

Thinking of service recovery and providing clarity as to how to proceed are a natural part of the productization of services — and of *proactive contracting*.

Further information on the proactive approach and ProActive ThinkTank

The authors of this article are active in the development of the proactive

Figure 2: Expectations, intentions, promises and the ability to deliver the agreed service come together in the service relationship, guided by a service contract that serves as a road map



approach and of the ProActive ThinkTank — one of the IACCM Forums (see www.iaccm.com/proactive/ and www.proactivethinktank.com). The ThinkTank is an outgrowth of the Nordic School of Proactive Law (www.proactivelaw.org). The mission of the ThinkTank is to provide "a forum for business leaders, lawyers, academics and educators to discuss, develop and promote the proactive management of relationships, contracts and risks, and the prevention of legal uncertainties and disputes". The website will provide a venue of collecting and sharing such information as best

practice tools and techniques, case studies, articles and reports on ongoing research. If you wish to join the ProActive ThinkTank or obtain additional information, please contact one of the authors. ❖

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Helena Haapio, LL.M, MQ (Master of Laws, Master of Quality), helps her clients become more successful by applying a proactive approach, one that helps them achieve better business results and stay out of legal trouble. Helena is a member of the IACCM Advisory Council and the coordinator of IACCM Finland. Before founding Lexpert, she served for several years as in-house legal counsel. In 2008 she acted as expert to the European Economic and Social Committee (EESC) in preparing its Opinion on the Proactive Law Approach.

Managing risk in SaaS, Cloud Computing and other on demand and Web 2.0 IT contracts



ERIC ESPERNE, James River Consulting LLC

Software-as-a-Service (SaaS) and Cloud Computing are the new generation of business computing. In time (some predict by 2012) these new ways of delivering networked applications will have the same world-changing effect on business that Windows and browsers did.

SaaS and Cloud represent the “commoditization” of computing: replacing systems that are developed and implemented on a customer-by-customer basis with product-like, one-size-fits-all offerings. The business world is slowly embracing SaaS and Cloud, weighing their costs and benefits against the existing software licenses and information technology (IT) infrastructures that are internally maintained. Whether SaaS and Cloud Computing become viable corporate computing forms will depend in large part on the contractual terms on which they are provided. Successfully contracting for SaaS, Cloud Computing or any of the other new “on demand” and “Web 2.0” business computing services depends on commanding knowledge of three things: (1) the technology behind the service; (2) the legal nature of the underlying transaction (good, service, license, lease); and (3) the contractual and product options for mitigating risks.

Before moving directly into a discussion of contracting techniques and strategies, though, it is helpful to step back and take a look at the bigger picture of SaaS and Cloud Computing.

New contracting mindset

Today, the key negotiation issues for IT systems are mostly about license rights, intellectual property and

protecting the large up-front investment in license fees and hardware.

License restrictions on software can be onerous and complicated. For example, a software license may limit deployment to North America. Enterprise license agreements (EULAs) covering hundreds or thousands of copies are subject to audits for unauthorized installations. Proprietary software requires source code escrows, while newer generations of open source raise concerns about prior licensing and patent infringement, eg, Microsoft claims to hold 235 patents used by open source. Software pricing has always been arbitrary. For both hardware and software, separate maintenance agreements are as important to total value as the sales

The key contract negotiation issues ... are service levels, data rights and security, and compliance.

terms. Security patches and bug fixes are often only available at the discretion of the software company. Anyone who has negotiated IT contracts is all too familiar with fighting battles over these issues.

With SaaS and Cloud Computing, the risks presented by IP and total value become much less critical, because customers no longer pay up-front, or take possession of a physical copy of the software, or own or lease hardware. Essentially, SaaS and Cloud Computing are a “point of access” for accessing computer applications, data, hardware and networking. SaaS and Cloud offer

much lower total cost of ownership than current systems and eliminate capital expenditures. Pricing of SaaS and Cloud is for the most part usage based, though due to the nascency of the industry the pricing varies widely and sometimes resembles licenses.

Figure 1 illustrates different SaaS pricing schemes by their potential value to customers.

The commercial secret to SaaS and Cloud Computing is the use of “multi-tenancy” architectures to lower costs by sharing the same software and hardware among multiple customers, combined with the global ubiquity and lower cost of the internet. The trade-off that customers make with SaaS and Cloud Computing is the acceptance of what some call “good enough computing” — using whatever features and services are included in the product — in place of systems custom fit to the business: a loss of

operations control and transparency; greater exposure to risks such as hacking; catastrophic failures; and misappropriation of data.

Figure 2 is an itemized comparison of the features of on-premise software and infrastructure systems and SaaS and Cloud Computing.

Key negotiation points

The key contract negotiation issues for SaaS and Cloud Computing are service levels, data rights and security, and compliance.

Service level agreements (SLAs) are just as critical as pricing and they

can be as difficult and complicated to negotiate as licenses. The industry standard for SLAs is weak: no SLA, or a single application or network availability SLA with credits. Internal corporate SLAs for IT are much more robust. Getting vendors to move beyond stock SLAs can be a challenge. The idea of service guarantees also extends to catastrophic failure, which can bring a customer's business to a halt, raising the question: "At what point do the vendor's responsibilities to keep the IT (and the business) going end?" The technical capabilities for measuring service levels and dealing with catastrophes may or may not be included in a particular SaaS or Cloud Computing offering.

Establishing rights over proprietary and confidential internal and customer data, and keeping it secure, is the next significant risk to be addressed in SaaS and Cloud negotiations. Most, if not all, of SaaS and Cloud Computing takes place outside of the customer's corporate fire wall, meaning the customer cannot implement its own security measures or conduct independent penetration testing or security audits. The global aspect of SaaS and Cloud also raises security and legal concerns, as multiple instances of the products may be replicated in a number of locations worldwide.

Potential vendor rights in customer data generated in SaaS and Cloud systems is a little-discussed and unexplored area of the law. Vendors may see a market in selling the aggregated data of customers in a particular industry or market segment. Also, it is unclear whether vendors have any legal rights to withhold data for non-payment, or a duty to backup and preserve data after termination.

Finally, regardless of who owns and manages computing systems, the corporations supported by SaaS and Cloud are still primarily responsible for complying with laws and regulations. Again, the question of where the vendor's responsibilities end must be considered. For example, if a doctor's office contracts for a SaaS-based medical records management system that is advertised as compliant with the US Health Insurance Portability and Accountability Act of 1996, what is the provider's true compliance

Figure 1: SaaS pricing schemes

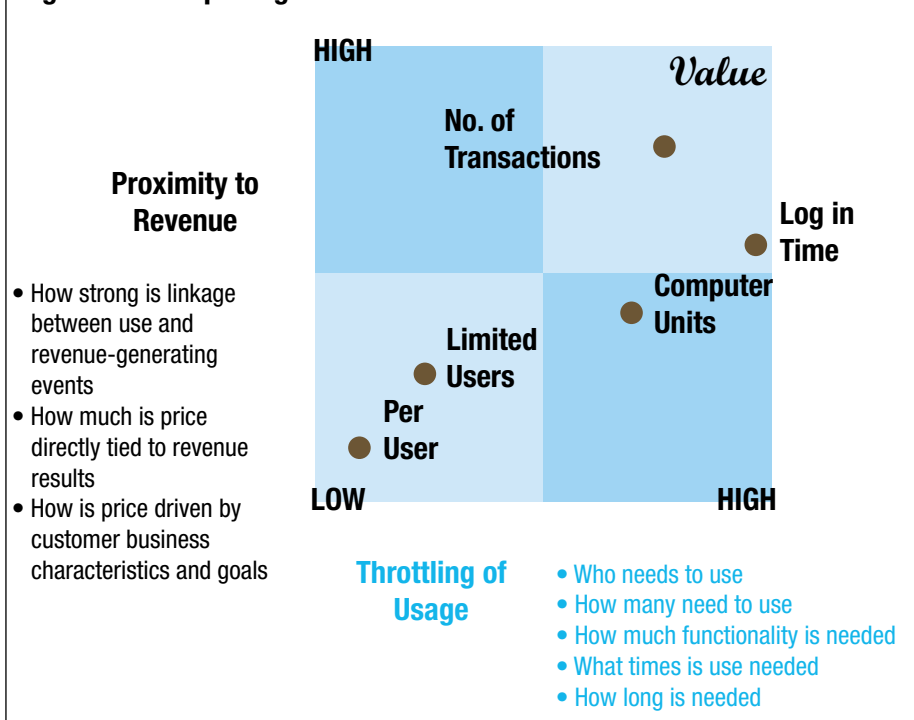


Figure 2: Comparison of software/infrastructure and SaaS/Cloud Computing feature

	Software & infrastructure	SaaS & Cloud Computing	
	Up front investment, 5% of total cost of ownership	Usage based pricing, 80–90% of total cost of ownership	✓
	License restrictions, auditing	Some usage restrictions, easily terminated, changes to terms	
	Enhancements in later versions	"Agile" development, immediate updates	✓
	Potential infringement issues, source code escrows	Data rights & security issues, potential conversion to SW	
✓	Unlimited customization & integration, customer-centric	Limited configuration & mashups, products-centric	
	Unlimited warranties, maintenance 15–20% of license	Limited SLAs & transparency into operations	
✓	Strong risk management & compliance (security, associated providers)	Weak risk management & compliance but efficiencies (e-discovery, SOX)	

responsibility? Further, does the data center hosting the SaaS application have any responsibility?

Three key areas to understand for effective negotiation

As mentioned earlier, contracts professionals should develop their understanding in three areas to be effective negotiators of SaaS and Cloud Computing.

Understand the technology

SaaS is application software especially developed or modified to be accessed over the internet by a web

browser. It is often sold as part of a computing platform that allows clients to configure functionality, administer user identities and integrate or "mash up" with other SaaS applications (eg, Salesforce.com). The applications and the data they process are hosted at third-party data centers rented by the SaaS provider.

Cloud Computing is data center hardware made available over the internet without the SaaS applications and with or without on-demand platforms (eg, Amazon Web Services). Cloud Computing is different from managed hosting services in that there is

no purchase or leasing of hardware and no physical access to the data center.

To understand the risks presented by a SaaS offering, it is also essential to understand the product's technological architecture. There are three basic architectures.

- **On-demand:** Separate application copy per customer and dedicated servers. Resembles ASP model except for web services-based code. Most customizable, updates unavailable, and most expensive.

– features are less customizable.

It quickly becomes evident that SaaS and Cloud product features and the architectures on which they are delivered directly impact their risks and legalities. Knowing how the technologies work is a prerequisite to entering into contract discussions.

Determine the underlying legal transaction

SaaS and Cloud Computing agreements are subscription agreements.

only revocable for specific violations. Some vendors will escrow source code (deposit with a neutral third party), but issues of vendor financial viability, termination rights and data portability are probably more important. Leasing does not come into play unless there will be dedicated hardware and/or the customer wants distinct possession and control rights.

Create options for mitigating risks

Risks can be mitigated both through negotiating technical product features and through detailed establishment of contractual rights and responsibilities.

Customers can require vendors to provide them with transparency into their operations, such as application performance and network uptime, through either online screens or other methods of regular reporting. Even better are service level management (SLM) tools (eg, NimBUS, Oblicore) that tie operational service levels to the impact of the product on the customer business, giving customers the ability to measure value. These methods of looking inside system performance should become part of the product description in the contract or standalone generic contractual duties.

Transparency also applies to maintaining security. Vendors can make the results of their own penetration testing and security audits available (eg, WebTrust) if they don't allow customer-initiated testing. Certifications of vendor operations according to industry standards such as ISO/IEC 27000 are another option. Like services levels, security provisions must be written in the contract.

SaaS and Cloud product features and the architectures on which they are delivered directly impact their risks and legalities. Knowing how the technologies work is a prerequisite to entering into contract discussions.

- **Virtualization:** Single application environment configured to run on shared servers with other applications. Customizable or configurable, fast updates if applicable, and less expensive.
- **Multi-tenancy:** Same application copy for all customers and only on shared servers. Configurable but not customizable, fastest updates, and least expensive. Multi-tenancy relies on "logical" partitions between customers using the same computing facilities, so:
 - data is more vulnerable to breaches;
 - systems are more vulnerable to failures; and

However, some SaaS vendors continue to grant licenses to software accessed through the service and impose license-like restrictions on use. Subscription periods can be monthly or multi-year. Vendors usually reserve the right to cancel or suspend the service for a host of reasons and to change service terms at any time (by posting new terms on their website).

In SaaS negotiations, it is important to first frame the issues by determining whether the vendor intends the offering as an online service, a license or both, and then identify the issues for negotiation. It may be advantageous to characterize the transaction as a term license and argue that the license is

CONTRACTING EXCELLENCE

The next issue — Vol 2.6: Aug/Sept 09 — will be on the theme of *Knowledge Management*

Each issue also carries advertising opportunities, so if these interest you (or you know of others who may be interested) please let us know. <kkawamoto@iaccm.com>.

Rights and responsibilities regarding data must be addressed in the contract precisely and definitively, otherwise it may be very difficult and expensive to sort them out later.

Customers need to establish the legal rights and technical abilities to access their data via application program interfaces (APIs) and to receive exports of their data from databases in a non-proprietary format. Backing up data may be a premium service offered by the vendor and can be negotiated with other commercial terms, or the customer may be able to contract directly with a third-party backup service. The vendor should have a duty to immediately report all events of unauthorized access of data. Vendors should also disclose the geographic locations where customer data resides, and customers should be granted the right to opt-out of those sites. Subpoenas for data by governments or litigants should be immediately relayed to customers and both the responsibilities and the costs of responding to them delineated between the parties.

Other potential issues, such as audits that expose data and any kind of aggregate analyses of data, also should be specifically addressed in the contract. Finally, the data rights at the time of termination must be clearly articulated in the contract. Any power of the vendor to withhold data or place a lien on data for non-payment should be either expressly granted or expressly excluded.

Some existing software original equipment manufacturers (OEMs) who have entered the SaaS market continue to offer their on-premise software, along with the SaaS offering, to protect their existing

sales operations. To rationalize the two offerings, these OEMs give SaaS customers an option to convert from SaaS subscriptions to software licenses. In some cases the conversion acts as a rent-to-buy deal by applying SaaS subscription fees to the price of the software. Negotiating a conversion clause can be an appealing way for customers to hedge against many of the risks of SaaS. ❖

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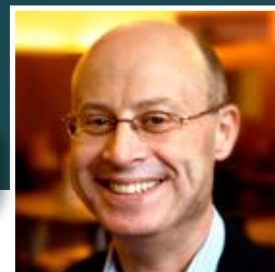
About the author

Eric Esperne is an IT and outsourcing contracts consultant located in Medway, Massachusetts. He worked on some of the very first web hosting and ASP contracts while an in-house counsel at Cable & Wireless during the dot com boom. Presently, Eric works with clients in developing and negotiating SaaS sale and purchase, hosting and channel sales agreements. He has written and presented on the subject of the challenges of contracting for SaaS at the enterprise level.



Outside contracting

Walking the Macmillan Way



Walking 74 miles across Exmoor in the west of England over the first holiday weekend in May seemed like a fine way to support St. Luke's Hospice, a wonderful organization that had done so much for my father over the last months of his life.

After 10 training walks and numerous gym workouts, I arrived in Exmoor and cautiously set out.

The walk from North Petherton to Landkey near Barnstaple was invigorating, challenging and my fellow walkers were great fun. The weather was kind with very little rain, the Exmoor scenery was beautiful, and my feet coped pretty well. As for the spacehopper stress ball in the picture of me at Dunkery Beacon, sufficient to

say that it helped me raise a bit more money for St. Luke's.

So I'm now pondering my next challenge. ❖

Mark David

<http://www.justgiving.com/markdavid>

Outside contracting — contribute to this column

Do you have a special activity or achievement in your life outside of contracting? If so, send photos and a 100-word description to Suzanne Birch at sbirch@iaccmresourcing.com for consideration to publish in this column.



Connective forces — getting back to the bargain



JACQUI CRAWFORD, SwissPort

Richard Susskind provocatively predicts the end of lawyers in his latest bestseller — *The End of Lawyers? Rethinking the Nature of Legal Services* — although his reflections are only intended to provoke his profession to wake up and accept change and carve a new niche in a globally connected world. He argues that the legal profession needs to think not of selling the drill bit, but delivering the hole. He worries that IT can produce standard legal documents and eliminate the need for very expensive bespoke legal help. Legal work could be unbundled, simplified and systematized. Pesky IT genius will create new disruptive technology that could allow the proletariat to Google an agreement, learn their trade secrets and change the face of the legal profession to the extent that the lawyers are on their knees looking up at the curve of change that could leave them behind. What a great idea!

Swiftly from sales never did align well with Liable from legal's objectives. Legal were always trying to muscle in on their business on the pretext of protecting the company from the impending doom of deviance from conditions precedent. It all took ages and got so complicated that customers even paid external counsel to wade through a trough of complicated conditions before they reached agreement. Swiftly would dearly love Liable to clear off and leave sales armed only with a Wi-Fi laptop and some general guidelines on how to set up big deals and a simple template. If the going gets tough, Swiftly can always work with Clever from contracts to negotiate risk transfer in the deal.

Where an entire relationship structure requires complex partnerships, or risk and reward sharing among multiple

parties, to deliver the customer proposition, there is a requirement for legal's expertise to be used to best effect in these discussions.

I would argue that the disruptive technologies Susskind describes are actually positive and connective and will disseminate knowledge. Commercial directors ought to consider that the challenge just shifted from keeping competitors out, to inventing innovative solutions that keep customers in because they feel comfortable connected to you. These connective forces are elastic, intangible, subconscious and instinctive.

In a competition where offer, price and accessibility are equal among

... the challenge just shifted from keeping competitors out, to inventing innovative solutions that keep customers in because they feel comfortable connected to you.

all parties, procurement decisions are more likely to offer the strongest sustainable connection to the buyer's own inherent values. Clustering these predominant forces into themes or principles offers a platform from which to build a competitive value proposition:

- **Conduct** (perspective, ethics, culture, trust, heart, intent)
Expressed vision and intention are in harmony with the actions of all employees
- **Agility** (capability, intellect, potential, flexibility, desire to learn)
Inherent adaptability of the company

to re-shape and re-invent itself in response to market conditions

- **Endurance** (prudence, confidence, daring, thought direction)
Staying power and sustainability of the business model, including organic growth potential

When the connective forces are present and demonstrated in practice, the organization will be attractive to other connections.

Examples of connective forces

An exemplar of connective forces in practice is Le Manoir Aux Quat' Saisons in Oxford (UK), the meticulously executed personal vision of the award-winning Michelin Chef Raymond Blanc.

Conduct

Raymond's magic was a bold vision that he conducted with passion, confidence and an unshakable drive to

first attain the standard of perfection he wanted to achieve and then repeat consistently for the pleasure of his guests and a sustainable profit. The value proposition is completely uncluttered and sets out experiences that customers may choose from a wide but interconnected range.

Agility

This service venture carries its own specific risks — perishable raw materials, inventory risk, fickle customers who could change their loyalties at the emergence of the latest celebrity chef or place du jour — and

is highly susceptible to cost and market pressures. An agile business model drives success and is dynamic enough to predict shifts in the environment and allow the team to respond with seasonal service offerings. Raymond's suppliers are trusted and valued partners, integrated with the enterprise in areas where their mutual success is important.

The website binds the offerings with a brand identity that is direct and personal. Pre-booked and pre-paid experiences deliver the most elegant cash-up-front order book in the service business.

The value proposition is not about food — it is a managed experience. Every encounter with a member of the team is pleasant, subtle and comfortable. Monsieur Blanc, being a high-profile individual, is his own free PR agent. You trust that the experience is good value because he appears to care. It all blends and the overall effect is effortless.

Endurance

The enduring value will be in Raymond's ability to maintain the core standard of service and flex with the requirements of the market. Brasseries Blanc look set to deliver a more economical experience with all the flair.

Not a lawyer in sight, not one barrier between the offer and the decision to buy.

I agree with Susskind that it is overtly simplistic to predict the end of lawyers. However, I do predict the rise of the self-directed negotiator, and this capability does not require the services of a lawyer. There will be situations where specific legal issues will need to be addressed in the negotiation and management of commitments. It will be the maturity of the commercial enterprise and the nature of the relationships it nurtures with customers and partners that will ultimately determine the legal skills and the optimum balance. The measure in these situations need not necessarily be the complexity of the relationship. With a decent set of standardized legally operable terms, the negotiation reverts to a discussion about the bargain itself.

The exciting prospect is the opportunity to re-invent skills and capabilities that were traditionally

the preserve of the legal function and amalgamate them with the business function to create a clear and practical process around our business commitments. If commitments are clear and uncluttered, the value will be evident and downstream management much simpler. That has to be a benefit for any business looking to cut out waste and still deliver great service, and a golden opportunity for the commercial professional to embrace every benefit that disruptive technology offers. Step up and use it to de-clutter our commercial deals and get back to the bargain.

I offer the following process steps as a starter for debate in our commercial community.

1. Test whether you have the capability to achieve your **vision** on your own, or if action or help is needed to close any gaps.
2. Ask your customers to specify their **requirements** and agree who is accountable to make it happen and who will validate delivery of the requirements.
3. Set out your **value proposition** so that the customer knows exactly what you will do for them in consideration for payment. Bear in mind that even though a contractual agreement will supersede the offer, this is where the trust, confidence and connective forces are forged. Discrepancies between offer discussions and final agreement damage connections. Don't forget to address what happens if stuff changes. Understand all the variables that could affect the price and set out these basic assumptions as the benchmark. Both parties want certainty in the bargain to avoid surprises, so be clear about what creates uncertainty and factor it into a change process.
4. Set out the **agreement** and include defined requirements:
 - core and elective services to meet requirements;
 - measures of performance (KPIs);
 - customer commitments;
 - problem rectification;
 - warranty;
 - defaults and recovery provisions; and
 - term and termination.The legal boilerplate and operability

provisions should be standardized and the entire focus should be on forging an uncluttered path to commitment.

5. Become a **lean and learning organization** that organically grows in tune with the market environment and its customers. Innovative and creative, it eliminates waste and keeps changing. People have room to innovate, there is open communication, commitments to staff and customers are honored and learning is valued.

If the beating heart of your business is re-wired to deliver an uncluttered and well-managed reciprocal commitment plan, the value of your proposition will sparkle from every employee and every connection from your business. ♦

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From the front line



If you have any questions to which you need answers, or opinions you would like to share with *Contracting Excellence*, please send them to the editor <ktarrant@iaccm.com> for consideration, entitled 'From the front line'. Don't forget that you can post your questions at <www.iaccm.com/forums.php>. This column will feature a couple of recent members' questions and answers from the forum.

Question 1**Putting together a commercial model**

From Steven Jackson: I have been tasked to put together a set of bullets/topics to drive discussions on creating a commercial model/framework for an upcoming contract. I have a few ideas such as "what are the important issues and how are they weighed? (cost/programme etc)", "How will payments be made? and for what? (monthly - overhead, direct, material etc)".

Does anyone have a list of important issues to address/discuss when putting together a commercial model? I appreciate the actual model may differ from contract to contract but the things to consider should be similar across all models.

Responses:

Charles Rumbaugh: There are different models depending upon the jurisdiction and items(s) being acquired, eg, goods versus services and UCC versus International (CISG)

On my website there is a generic Request for Tender (RFT) outline that I developed for lectures at the Naval Postgrad School for International acquisitions by foreign buyers. It is under "Teaching Experiences," 2006, on my website

Also, a much shorter version (or launching point) would be acceptance criteria, warranty, and liability for latent defects as a minimal starting point for UCC items.

Tim Cummins: In my experience, the key points for any commercial model relate to certainty over the customer's desired outcome — and then the level of responsibility you can

accept in delivering to that outcome. I advocate that you first define the objectives of the relationship (not the solution) and then move to understanding of the capabilities (features and function) that will be required to fulfill these needs.

From there, you can begin a discussion on how these capabilities will get delivered and by whom. The point of a commercial model is that it should seek to maximize the chances of success. So it must enable open discussion between the parties of the risks that will be encountered and how they can best be managed. Once this is determined, you can define the parties (buyer, seller and potential other players); their roles and responsibilities; the way you will measure and motivate success; and the consequences of failure.

Philip Adams I: have listed a few general ideas below in no particular order, but I can probably provide a more detailed list if you need it:

- Establish contract scope of works; design?
- Establish contract deliverables; time, cost, technical, quality etc.
- Set up process to plan, monitor and maintain progress.
- Identify contract risks; develop, monitor and maintain plan (risk register).
- Establish change control procedure; early identification and notification to client; notification requirements specified in contract?
- Cashflow; subcontractor/vendor payments versus main contract payments.
- Payments; applications for payment?, procedures specified in contract?
- Establish periodic (monthly?)

review of costs versus value, project profitability (early warning tool).

- Procurement; procurement plan (what do you need and when do you need it), subcontract/vendor contracts back to back with main contract.
- Establish structured team for commercial management with single point responsibility.
padams@systechgroup.net

Question 2**Cradle-to-grave versus pre/post execution split**

From Ingrid Lehner: Currently, contract management in our business unit is split into two segments: one contract manager handles the contract through negotiation and signature (ITO), while another contract manager handles the execution phase (OTR). In previous jobs that I have had, contracts are handled "cradle to grave". I would like to have some feedback as to the pros and cons for each approach.

Responses:

Charles Rumbaugh: If the contract is the basis for relationship contracting then it may be a little confusing (and upsetting) to the customer, where relationships are important, to see a change after contract award.

Some of the issues are not dissimilar to individual versus team negotiation — and I suggest you revisit the IACCM audio call-in earlier this year on this topic. The training, educational level, etc. of individuals can also impact the calculus in changing where you are now. But some companies have a "hired gun" that does the negotiation and then moves on. Again, not dissimilar with someone getting paid to put the deal together and then, in effect, having no responsibility for performance!

One recent concept in negotiations is to have the opposite negotiating team brief your executives "on what the deal" is and vice versa. This is very

difficult to do if the initial “players” are no longer there.

But, if your new organization has them separate, presumably the current customers and your executives accept the practice — why change if it is working. .. but is it? Did they bring you in for change or status quo?

Mark Hope: I have experienced the same split that you describe and undertaken both the negotiator role, and moving on to the next deal upon signature, and I also headed up a team that inherited and managed all the deals from signature onwards. I undertook both these roles predominantly in the telecoms and IT outsourcing arena ie, £10 million to £1 billion deals.

My take on this is that the vast majority of the knowledge and expertise acquired by the negotiator is of most use in about the first three months of contract management when transition is being implemented, and when any “to be resolved” or quirky issues (where you needed to have been there) require attention, when the first few change controls need to be processed and any initial disputes take place (setting the scene going forward). Thereafter, the tasks become more transactional and business-as-usual, and the knowledge and experience of the negotiator become much less of a factor and, indeed, less resource needs to be expended as the contract is by then hopefully on the straight and narrow. To my mind, doing a good job of contract management by using the negotiator in the first few months saves resource and money in the long term. It also gives the poor soul a bit of a break from negotiating!

It is of course possible to succeed where the job is handed over, but to do so requires robust mandatory procedures and processes to facilitate the handover, along with knowledge and document transfer to the extent of a one or two day event. In this model, I would strongly recommend devoting more resources in the early days using your best and most experienced people from the contract management team.

Another point I would mention, is to bring the negotiators and implementers together every now and then to make sure that implementation

problems are fed back to the negotiators to avoid repeating the same mistakes.

Your dilemma is an old chestnut and one that companies change their minds on regularly. Usually it is the demand for the few specialised negotiators that prevents these negotiators sticking with the deal they’ve just signed, that drives the separation. If demands prevent you ever being able to facilitate the negotiators staying with closed deals, my other recommendation would be, as second best, to send in an old head and/or trouble shooter every now and then to “clean up” in term deals if they have gone wonky due to neglect.

Question 3

Skilled Retention and HR Metrics Post ECM Implementation

From Michael Cram: Wondering if anyone has kept metrics on skilled employee satisfaction and retention or any other quantitative metrics post the implementation of a contract management automation tool.

Responses

Rob Rowe: We have just begun to track key performance indicators using our contract automation tool to measure such things as turn-around times between certain points in the contract lifecycle. Additionally, we have also experienced real value that goes beyond the numbers (ie, employee satisfaction). Let me give you some examples of what we have seen post implementation that aligns with our organization’s directional compass:

- **Collaboration:** Having an automation tool increases the amount of staff collaboration (common discussion threads appear in staff meetings, team breakouts etc), discussions around tips, shortcuts, general experience using the tools fosters collaboration amongst the contracting team.
- **People:** Retaining key staff is essential in building a smooth process and maintaining a "system" for successful contracting in support of sales/procurement. Giving your staff access to the right tools does indeed increase the retainment of

key staff who would otherwise leave under circumstances where they get no support from the organization they work for to do their job in a professional manner

- **Quality:** If your staff know they are contributing to the greater good of your organization by producing quality deliverables (hand-offs), then they ultimately will be more engaged in the process and will buy into the "system".
- **Accountable:** Having an automation tool that management can report on presents their staff with something that formally stamps their name on contracts and their work. This leads to a "system" of accountability which should drive engagement and better performance from those key staff you want to retain.
- **Innovative:** Keeping up with the times is not enough anymore. To really succeed in this world, you need to include innovation in your daily work flow. Having an automation tool for your staff to use for the contract management process will not only fill the gaps needed for your team to support sales/procurement successfully, but will also be a leveraging point that spawns new ideas in your overall contracting process (points of work before and after the actual contracting process reaches), for example integrating contract data with other systems in your organization that adds value and further streamlines other indirect processes.

Tim Cummins: Satisfaction levels and utilization rates tend to go hand-in-hand. One leading ECM supplier has observed that, “in cases where utilization is in the lower quartile, we have found that these organizations view CLM as administrative and are not performing Contract Management as you and I understand it”.

Catherine Uffen, M.A., J.D.: It matters whether the focus is on the recipients of the benefits (executives, sales) or the users of the system (lawyers, paralegals, contract managers). Both should be tracked but may have different interests.

It might be helpful, since no one has tracked skilled worker satisfaction, for

members to propose the text or focus of KPI's. For example, track skilled workers using the system directly through post termination interview:

- Whether employee is leaving for an environment where there is a contract management system up and running, or for the opportunity to do so
- How important is it for your satisfaction with your job role and to your understanding of your role in the organization to be able to offer reports on non-standard terms and attendant risks to finance, audit, and security?
- Has the use of a contract management system reduced the number of superficial questions from beneficiaries?
- Has the use of a contract management system where

executives, sales etc. can see signed contracts improved their (a) focus when asking questions? (b) use of legal terminology to communicate with you better, and (c) awareness of risks of non-standard terms?

Question 4

Career Development and Resourcing Strategies

We are seeking good practice examples regarding the design and implementation of:

1. a comprehensive procurement organization resourcing strategy (global, matrixed; operational & strategic procurement; etc.)
2. career path models — demonstrating relationship b/t various roles at various levels,

the experiences and therefore the competencies they build (the building blocks of a career), and how a Proc/SCM professional creates their own career path in the organization using these building blocks

Response

These were significant topics at the IACCM conference in Orlando in May? You might benefit from looking at some of the presentations and expert podcasts in the IACCM member library. I use them extensively for internal development work. There are many to choose from on the subjects you mention, but a couple that spring to mind from Orlando are those by John Lickvar at Shell and Tom Larkin from Credit Suisse. ❖

Negotiation excellence

The following is from Tim Cummins' blog, *Commitment Matters* of 6 June

Negotiation is one of those elusive topics that everyone sees as important, but few can really pin down. It is something that we believe we are good at or bad at, without being able to specify precisely how we make the judgment.

In the business world, most executives think that skill as a negotiator is an important characteristic (probably true) and surveys suggest they believe they are personally good at it (rather more questionable). Historically, it has been seen as something innate, rather than something that can be easily taught. It has been treated as a skill, rather than a process. But on what criteria?

What are the characteristics of a "successful" negotiated outcome? Is it getting what you want (short-term) or laying the foundations for a successful relationship (long-term)?

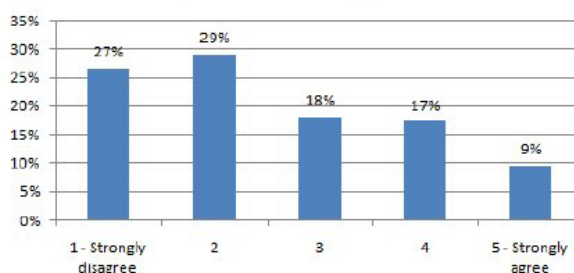
And moving beyond the personal and individual, to what extent do organizations make themselves successful at negotiating? Are there companies or entities that have a consistent record of success and, if so, how have they established that capability and "bred" successful negotiators or negotiation teams?

These are questions that IACCM intends to answer with its exploration of Negotiation Excellence. Last year, it tackled the area of post-award contract management — and not surprisingly, found that the success of many deals depends on what

happened during the negotiation phase. It undertook that work by asking professionals worldwide to nominate companies and organizations that they admired (or respected) for their performance in this area. The results (published in September 2008) were followed up with in-depth interviews with the winning organizations.

A similar process is being followed now and IACCM is inviting people to nominate the companies that they believe represent excellence in negotiation; you can participate at <https://www.etchouches.com/negotiation1>. As with all IACCM surveys, input remains confidential; no one will be in touch to sell you anything; and all participants receive a report with the final results. ❖

Did you know that only 26% of IACCM members agree or strongly agree that their companies have a system to decide when to travel and when to use alternatives!



For information on Research, contact kkawamoto@iaccm.com