Podcast Series - "About Managing Contractors and Vendors"

Episode 9 Transcript: Contracts and Agreements

Welcome to Episode 9 in this Podcast Series – "Managing Contractors and Vendors". This episode gives a quick overview of contracts and agreements for engaging outsourced service providers, or vendors. It is primarily aimed at Vendor Managers in departments within the client.

Even simple contracts require experience to create well. And large global agreements need deep experience and study to be expert in these contracts.

This episode introduces basic points. You will find more depth in the extended PDF article on this subject, which you can request at no cost on the podcast page at think180.com. And in future episodes, we cover negotiations, metrics, partnering, and other elements mentioned here. For now, we will just be looking at agreements in broad context.

Using agreements

Agreements are usually drawn up when engaging vendors under a contract, but may also be used at other times for confidentiality and security, or protection of intellectual property. There can be Master Services Agreements, to which the specific details of deliverables and pricing are added.

Or the general terms and conditions can be an attachment to the overall contract. Some companies require the same Master Services Agreement for all vendors who provide services, and simply add in the Statement of Work, or "SOW" as it is called, setting out the project specifics.

Contracts are one of the most crucial elements of working with external service providers. A good contract is a summary of the process of information gathering, communication, negotiation and agreement of work to be performed, terms and conditions, definition of deliverables, and obligations and rights of all parties.

If there is effective communication, clear agreement and common understanding of all factors, a written contract starts as a formality. Conflicts can arise when things change, something goes wrong, or a party feels terms they agreed to have not been met. Then the contents of the contract come into sharp focus. A good agreement, well prepared, means less chance this will happen. A hastily prepared agreement may be a problem as a project unfolds.

Creating the contract

What gets included in any signed agreement starts when a decision is made to outsource work, and gets rolled in when the Request for Proposal, or RFP, is created (this was covered in Episode 6). The RFP is where the job and the work to be done is first outlined to the prospective vendors. In the response to the RFP, the providers make claims about their capabilities, prior experience and expertise, and commitments to delivery and price if they are chosen.

Once a vendor is selected, they contract to perform the agreed work to a set standard for an agreed fee. The client agrees to pay the provider upon delivery or completion of milestones, or on a regular basis against an agreed set of service levels.

The agreement also sets out the terms and conditions under which both parties will operate in the relationship, how changes will be handled, processes and procedures, reporting, problem resolution and escalation, and handling disputes.

Since a contract must define the work to be delivered, and is the basis for ongoing management, the department or function that will manage a program should help shape the contract.

The contract must also protect the company from exposure through factors beyond the department. Working with Purchasing/Procurement/Sourcing/Legal is key to protect the overall company interests.

Contracts and Negotiations Handled as a Central Function

Larger outsourced contracts are often negotiated by a Sourcing or Legal Department, and sometimes by a special team, then passed to the group or person responsible for implementation and managing the project. A Vendor Manager may be assigned a program or project, or take a new job managing a program or project that is already in place.

A master agreement is typically an open agreement, used where the company requires an ongoing relationship with a vendor who is likely to work on more than one program. The agreement is broad, and sets out prevailing terms and conditions.

In some cases with large projects extending over a long term, for each separate phase of a program, a separate and specific agreement may be drawn up relating to the deliverables for that phase or program. This agreement must include specific milestones or service levels not included in the Master Agreement.

It is critical to review the agreement and identify elements that are key to being effective as a Vendor Manager. These are outlined in detail in the extended article.

Service Level Agreements

A Service Level Agreement (SLA) is a contract that defines such things as the level of technical support, or business standards, that a vendor will provide to its client. The agreement typically spells out measures for performance, consequences for failing to meet these, and incentives for exceeding standards. This is such a critical area, that an entire future episode will be devoted to it.

Intellectual Property

Agreements made between companies and vendors in the US are also open to interpretation by broader laws applying to this, including copyrights, patents, and intellectual property. As a rule of thumb, material developed for a company by a vendor is the property of the engaging company. These are "work for hire" projects where the vendor is engaged specifically to develop a product, service or other deliverable.

Exceptions may be where the provider uses their own templates or design methodologies. Complexities can occur when a vendor uses a proprietary process to create the work for hire and this process is embedded in the work. Careful negotiation and decisions around trust are needed, and unambiguous definitions of acceptable use are set out clearly in the agreement.

Global or cross-cultural agreements

Agreements between businesses in different countries and business cultures need to be drawn up and reviewed by experts in both environments. And it is not just the wording of a cross-national contract that needs to be understood, it is how the agreement will be interpreted, and the processes for enforcing, renegotiating, terminating and changing that must be factored in. Client contract requirements, that are easy to comply with in the US, may be burdensome for a provider in another country, and cause overall delivery to suffer.

Contracts are treated differently around the world. US businesses see a contract as final and binding. But in some regions a written contract is only the beginning of negotiations between parties, or has different values associated with it. For example, in some more traditional Japanese businesses, a spoken agreement may be more binding than a written contract.

Vendor Manager

Once an agreement is signed and the vendor begins work, a Vendor Manager will be managing the ongoing relationship, delivery by the vendor, and ensuring integration with the recipients of the service and other stakeholders. Specifically, the role will include:

- interpreting the emerging requirements as the project moves forward and evolves
- managing by milestones, standards/benchmarks, deliverables, and service levels
- handling change as an adaptation to changing market or economic conditions
- negotiating and renegotiating terms
- handling terminations, as well as transfers and handoffs to other vendors
- ensuring payment according to milestones, service levels, metrics set out in the agreement

If you are a Vendor Manager, and did not negotiate the contract and draw up the agreement, you need to know the following as a very minimum:

- specific roles and responsibilities of different parties
- how disputes and enforcements are handled, especially for global agreements
- how and why terminations and transfers are done

As a Vendor Manager taking over a project, you need to pay careful attention to interpreting existing agreements. In particular:

- Carefully note standards & metrics
- Who has what role, and where responsibilities lie
- Understand the basis for payments

The success of an outsourcing relationship can be affected by how those managing the vendor see the agreement. Here are three mindsets guaranteed to create problems somewhere along the line.

1. Agreements are a procedural "necessary evil" to get out of the way, so work can start. Once they are done they are tossed in a drawer and forgotten until something goes wrong.
2. If it is in the agreement, then it will naturally get done as required. No management needed. The incentives and penalties will keep the vendor on track.
3. Change orders result from a badly done agreement. They are needed because whoever struck the agreement did not plan properly and foresee what was needed.

You will find more about the consequences and risks of these mindsets in the extended article on the think180.com site, as well as a better way of viewing each of these three aspects.

Reality check - a few questions

If the master agreement is one-size-fits-all, it is important to review it carefully against the work to be done, and the suitability for the specific vendor.

1. Does its stringency and breadth, detail and conditions, match the project and the vendor?
2. Can it be changed, and does the vendor know that?
3. Is there a supply chain? Special care and diligence may be required if the primary provider is engaging or acquiring another vendor.
4. Does the contract make provision or allow for changes in scope, scale, deliverables, timeline, inflation, and changes in the cost basis?
5. Is there balance between penalties and bonuses, and not an over-reliance on these alone?
6. Does the agreement serve both parties - ensure best work, best value, best relationship.
7. Have all assumptions been included?

Problems and changes

A large number of change orders can mean several things - the business grew unexpectedly, went through an acquisition, or made a shift in its business model or operations. Maybe the provider bid was not accurate or there was excessive pressure from the client for a low price. But if everything else is business as usual, then change orders may point to an agreement that was done improperly, and is now showing up as a problem.

Terminating or renegotiating a contract

Many things can create the need to terminate a contract or a vendor. It could range from a project being canceled, buyouts, business drying up, change of business models or vendor expertise, or simply poor vendor performance. There may be a closeout involved, or handoff to another vendor.

Where a contract has run well, and there is a good relationship, a contract with an existing provider may simply be renewed. Even so, things change over time, so there is value in revisiting the terms and both parties being open to renegotiating a better agreement that is acceptable to each.

Even if you open a contract to bids by other providers, more strategic existing providers may see an opportunity to showcase their expanded or deeper capabilities, and knowledge of your business.

Conclusion

Hopefully this has given an overview to contracts and agreements as a dynamic and key part of managing an outsourced project. For more detail and depth in this and other topics, visit think180.com and click on the podcast page link.

And there is more material, and resources, on the Think180 website. Just click "Ensure Vendor Effectiveness", then note the resources listed at the right, including a link to these podcasts and the transcripts as PDFs. And you can subscribe to my blog, Managing Vendors.

And if you need our services, Think180 can provide training or experienced consultation. Our workshop "Managing External Resources" is very adaptable to meet your company needs.

As always, we welcome feedback and success stories, as well as questions you may have. Please feel free to share this podcast with your colleagues. Our e-mail address is podcast@think180.com.

Thanks for listening.

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Note: To request a copy of the extended article on Contracts and Agreements (9 pages), with more depth and details, please email Think180, and we will happily share a pdf copy with you.