

BEST-IN-CLASS PERFORMANCE IN CONTRACT MANAGEMENT

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→ **Bryan Ball**, Vice President and Group Director,
Supply Chain and Global Supply Management Practices



Report Highlights

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Contract management improves cost management by providing the visibility into performance against contract terms.

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The Best-in-Class are nearly three times as likely to have transactions compliant against contracts as compared to All Others.

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The Best-in-Class have more than 75% of their contracts in a searchable repository, compared to All Others who have about a third.

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The percentage of contracts renegotiated is more than twice the percentage for the Best-in-Class compared to All Others.

This paper reviews contract management from the perspective of Best-in-Class organizations, the performance advantage they enjoy, and the capabilities that they have in place to enable that level of achievement.

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The majority of organizations use contracts in some way, shape, or form in their business. They are the language of business, and govern the formal relationships between an organization and its vendors, service providers, and trading partners. The reason for contracts is often for the legal documentation and protection of the rights and obligations specified in the relationship, whether they are on the buy or sell side.

Historically perceived as a paper-intensive function by most, and a necessary evil by some, the face of contract management is changing rapidly as the advent of electronic documents, workflow, and electronic signatures continues to grow. Anyone accustomed to working with contracts can cite the perils of paper. In paper mode, all search, retrieval, comparisons, and reviews are manual and time-intensive, which makes compliance and audit tedious, costly and inefficient at best. The result of these issues from managing paper contracts is the perception that contracts are necessary, but not always user-friendly for managing the business. In addition to the cumbersome manual process, another important consideration is that some of the most expensive resources in a company are often engaged in the review, management, and approval of the contract management process. This may include the executive team, legal counsel and even the suppliers, service providers, and trading partners themselves, who get pulled into the often highly inefficient paper process.

However, consider the situation when there are electronic versions of the contracts and supporting documents. The time savings alone can improve overall efficiency by putting valuable time back in the hands of the procurement, sourcing, sales, legal teams, and/or anyone else that might be involved in the process of contract creation, review, and approval.

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This paper reviews contract management from the perspective of Best-in-Class organizations, the performance advantage they enjoy, and the capabilities that they have in place to enable their superior performance. We begin with a review of the business pressures that organizations are facing and how they affect the contract management process.

Business Pressures on Sourcing and Procurement

To understand the value of an efficient contract management process, it's important to understand the environment that sourcing and procurement organizations are dealing with. Figure 1 frames this environment with a view of the business pressures that companies are facing within this space. The first pressure, to reduce cost and improve savings, is to be expected since that is the main mission for sourcing and procurement organizations. As discussed in our recent report, [The Best-In-Class Lead the Way on eSourcing, July 2015](#), it's also the emphasis or priority that companies place on these pressures that drives behavior. For the Best-in-Class, there is no question that they see savings and cost reduction as their primary mission.

The Best-in-Class place a significant priority on stakeholder pressures to perform. This points to their level of engagement and alignment with the overall business goals, in addition to their primary mission of saving money.

Best-in-Class Definition

Best-in-Class – top 20%

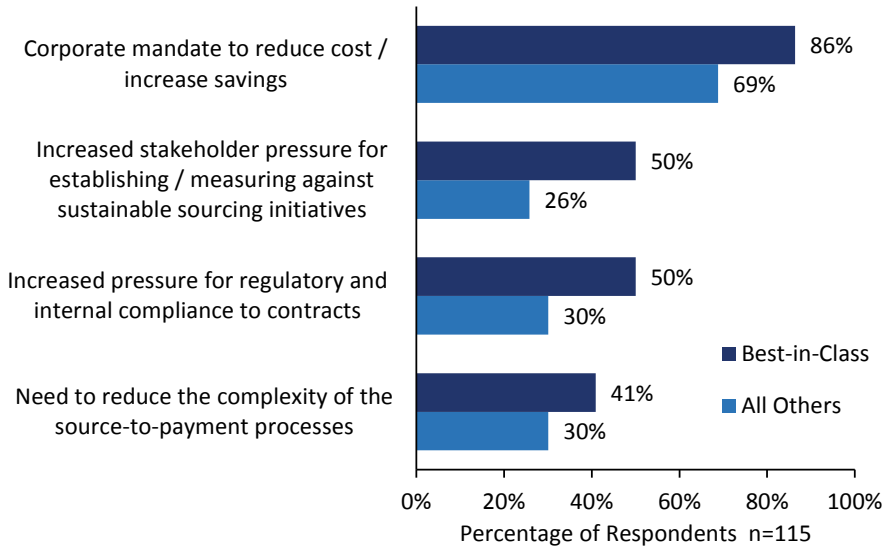
Industry Average – middle 50%

Laggards – bottom 30%

All Others – the sum of the Industry Average and Laggards – 80%

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Figure 1: Business Pressures Felt by Sourcing & Procurement



Source: Aberdeen Group, July 2015

However, even though savings and cost reduction are clearly the overwhelming priorities of the Best-in-Class, they also place a significant emphasis on stakeholder pressures to perform. This points to their level of engagement and alignment with the overall business goals, in addition to their primary mission of saving money.

Of equal importance is the realization that regulatory and compliance issues are key factors to be dealt with as the Best-in-Class pursue their cost reduction efforts. They recognize that these can influence their decisions on vendors and that there may be hidden costs tied to regulatory reporting and documentation.

Other factors include the priority of the Best-in-Class to streamline the complexity of the source-to-pay process. There is a realization that improving their processes and increasing their efficiencies also frees up resources to focus on their primary goal: saving money.

Best-in-Class Performance

Spend under management
Best-in-Class – 89%
All Others – 51%

Average “Realized” yearly savings
Best-in-Class – 12.8%
All Others – 5.6%

Average cycle time for contract approval
Best-in-Class – 40 Days
All Others – 49 Days

On time delivery (required date)
Best-in-Class – 82%
All Others – 59%

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Best-in-Class Performance Metrics

Our sidebars on pages 3 and 4 provide the definition for Best-in-Class companies as well as their superior performance against business metrics compared to All Others. The level of performance for the Best-in-Class is also part of the framework for the environment in which Best-in-Class companies operate. Their results speak for themselves in the areas of spend under management, savings realization, contract approval cycle time, and on-time delivery. The Best-in-Class performance advantage also demonstrates why it is important to understand the capabilities and technologies they have in place that help them achieve those results.

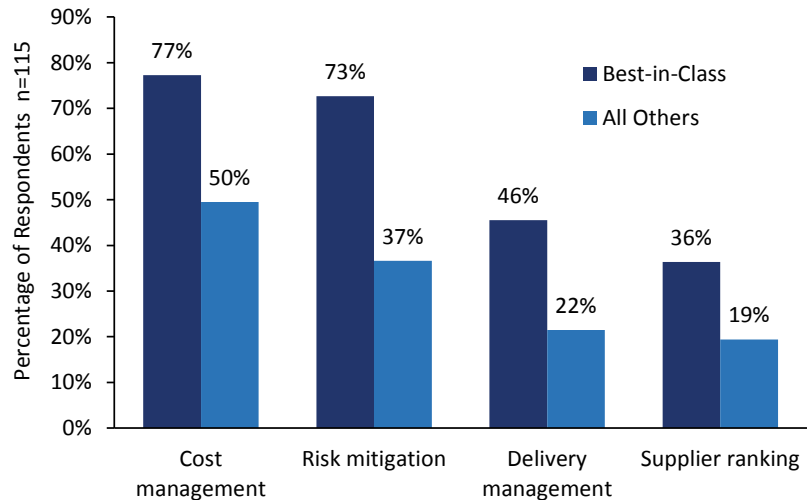
Contract Management: Points of Influence for Sourcing and Procurement

Having established the context for the sourcing and procurement environment, we now consider the areas of impact and degree of influence that contract management has on them. Figure 2 shows the degree of impact identified by the Best-in-Class compared to All Others on core elements of contract lifecycle management processes. The Best-in-Class indicate a much higher level of impact in every area.

- [Read the full report, “The Best-In-Class Lead the Way on eSourcing”](#)
- [Related Research “Contract Management: Key Attributes and Best-in-Class Results”](#)

The Best-in-Class are nearly three times the rate of transactions compliant against contracts compared to All Others. The point is that if transactions do not leverage the contracts in place, then the efforts of the sourcing and procurement teams are rendered useless.

Figure 2: Points of Influence for Contract Management



Source: Aberdeen Group, July 2015

Contract management improves cost management by providing the visibility into performance against contract terms, so that any shortfall can be recognized quickly and addressed with corrective action. In manual operations there may be some tracking as well, but not to the degree that a robust contract management solution can provide.

Contract management improves risk mitigation by creating visibility into an organization's exposure to geographic, product-specific, or vendor-specific issues. Manually creating these views and effectively monitoring them in a paper-based environment is just not feasible. With a searchable repository, the scope and impact of any compliance, regulatory, or event-driven issue can be reviewed quickly and the exposure determined, so that actions can be taken to mitigate the potential risk.

Performance monitoring against contract milestones and dates is a key factor in keeping any project or relationship on track. Alerts of upcoming contract deadlines or milestones can be used to track those events and measure the percentage on time. This

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capability can be leveraged for customer contracts as well to improve the organization's delivery and supplier performance. Contract expiration alerts might trigger action to take steps that leverage contract terms, such as making an extra purchase to achieve a discount. Again, just having the visibility creates the advantage over paper-based systems.

Organizations can establish the searchable data supplier ranking by leveraging the searchable data across all contracts that enables supplier analytics to be performed. In a manual paper-based operation, some of these tasks can be accomplished in a project-style approach, but the advantage of a robust contract management solution is to provide this information on a repeatable and regular basis so it is part of the management process, rather than a one-off project.

Core Capabilities and Performance – Where the Best-in-Class Excel in Contract Management

Figure 3 provides the performance metrics for the Best-in-Class companies related specifically to contract management, and it is clear from just a visual review that the Best-in-Class are far ahead of All Others. A review of each performance measure continues to highlight the efficiency, effectiveness and overall contract process.

The Best-in-Class are nearly three times as likely compared to All Others to have transactions compliant against contracts. The point is that if transactions do not leverage the contracts in place, then the efforts of the sourcing and procurement teams are rendered useless. This can be a function of discipline, visibility, or some other reason, but it also explains why the Best-in-Class are so far ahead in their performance on savings realization and spend under management percentage. There are other issues that also come into play as a result of non-

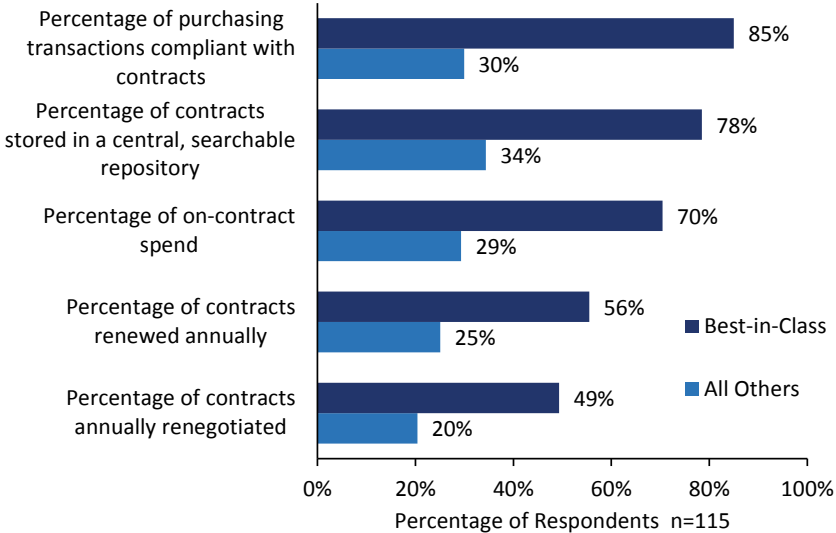
Best-in-Class have more than 75% of their contracts in a searchable repository compared to All Others who have about a third of their information in a searchable repository.

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The accessibility and visibility created by the searchable repository pays dividends and directly impacts the cost, delivery, risk mitigation, etc.

compliant transactions that can be a risk issue due to regulatory, legal, and audit requirements.

Figure 3: Contract Management Performance



Source: Aberdeen Group, July 2015

Next, the Best-in-Class have more than 75% of their contracts in a searchable repository compared to All Others who have about a third of their information in a searchable repository. The accessibility and visibility created by the searchable repository pays dividends and directly impacts the cost, delivery, risk mitigation etc., as discussed in our previous section. The other clear advantage is the efficiency improvement, due to the time saved and the speed of accessing the information. Those time savings translate into more bandwidth for value-added activities, such as analysis or focusing on additional spend categories.

“On-Contract” spend is an indicator of the efficiency of an organization's procurement and vendor management functions. As seen from the Best-in-Class performance metrics, the Best-in-Class indicate “89% spend under management.” 70% of the

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spend is managed by contracts for the Best-in-Class compared to 29% for All Others, which means they (the Best-in-Class) are not spending time reinventing the wheel on sourcing decisions and vendor selections that have already been determined. As an indicator of overall efficiency, the Best-in-Class are more than twice as effective in managing their spend.

Contract renewal is another indicator of efficiency in managing the supplier and contract lifecycle, as well as managing customer contracts. Every time a new supplier is brought on board or a new contract is created, there is time involved to put those things in place. Renewal of contracts indicates that the sourcing process yielded good decisions up front and those steps do not have to be repeated. The Best-in-Class renew 56% of contracts annually, more than twice the percentage of renewals compared to All Others. For All Others this becomes a “catch 22” type of situation. They need to spend more time on the value added activities to move them closer to the Best-in-Class performance, but they also have to repeat the decision process for finding new sources and developing new contracts, which must replace the non-renewable contracts, but kills their time. Similarly, for sales, renewals mean that they can go after new business rather than spending their time trying to “win back” lost business, which often means giving up concessions in terms of price or services.

Finally, the percentage of contracts renegotiated by the Best-in-Class is more than twice the amount compared to All Others. Similar to renewals, this is an indicator of effectiveness and efficiency. If a contract is renegotiated, it means that resourcing or choosing a new vendor is not required. Renegotiation is also likely to occur about as a result of volume changes, performance monitoring, or new options that might now be available. The initiation of the negotiation could come from either party, so

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The theme of greater efficiency and putting valuable time back in the hands of critical resources cannot be overstressed. This is “the why” behind the Best-in-Class efficiency and performance.

renewal should be considered as an adjustment process with the right supplier or customer. Again, this does not require a new relationship to be established; renegotiations leverage the decisions made previously.

Automation and Technology Capabilities: Why the Best-in-Class Perform Better!

How do the Best-in-Class get there? What are they doing differently in their processes, and what kinds of tools are they are using, to achieve superior performance levels for contract management? Table 1 shows the capabilities that Best-in-Class companies have in place for contract management that support both efficiency and visibility.

To appreciate the enabling capabilities, it is important to identify and understand the contract management process from beginning to end. Table 1 is organized by the sequence of steps that typically define the process for creating a contract, plus the supporting contract management capabilities. There can certainly be some variations and iterations that might exist, but all contracts have these five basic steps: proposal phase, contract creation/authoring, negotiations, approval, and electronic signature/execution. Capabilities that support these steps include a searchable repository and supporting reporting functionality.

In addition to the sequence of steps and supporting capabilities that constitute the contract management function, the degree of automation and adoption of electronic document management is also shown in Table 1 for the Best-in-Class compared to All Others. The comparisons tell the story behind the Best-in-Class contract management performance. In each one of the five contracting steps shown in Table 1, from the Proposal phase

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through the Electronic signature, the Best-in-Class are more than twice as likely to have automation in place.

Table 1: Contract Management – Process Capabilities

Contracting Process and Automation Capabilities	Best-in-Class	All Others
Proposal phase	68%	38%
Contract creation / authoring	77%	27%
Negotiations	59%	18%
Approval Workflow	77%	37%
Electronic Signatures	73%	34%
Contract Repository	77%	44%
Reporting and analytics (e.g., KPIs, performance management)	91%	40%

Source: Aberdeen Group, July 2015

The theme of greater efficiency and putting valuable time back into the hands of critical resources cannot be overstressed. This is “the why” behind the Best-in-Class performance. The old adage of “time = money” in sourcing and procurement scenarios is demonstrated by these capabilities and performance numbers.

Capabilities Review

Many contract management solutions provide reusable forms or templates that can be easily created/developed to facilitate the automation of an electronic contract. This greatly simplifies the creation and authoring step by automating the repetitive steps. Accessing standard language that may be applicable for a given vendor, geography, product, contract type, scenario or regulatory requirement also simplifies the authoring step.

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Negotiations are often iterative, but with electronic documents, and supporting robust document management functionality, the changes can be tracked and documented. As common as writing and word processing applications are, it's surprising that the Best-in-Class are more than three times as likely to have "negotiation" capabilities in place, compared to only 18% of All Others.

Approval workflow tools have become more commonplace with contract management applications, and are now almost a requirement. The approval routing and rules greatly improve the efficiency in the contract process.

Electronic signatures have rapidly become more widely accepted, and are one of the last pieces of the puzzle in eliminating the time wasted hunting down and securing wet signatures. Our recent report, [Using Electronic Signature for Best-in-Class Contract Performance, May 2015](#), highlights these benefits. Electronic signatures have become widely accepted in most countries as a legal signature, so many of the misconceptions about passing the legal "sniff test" have been laid to rest.

A searchable repository is the glue that provides the visibility and data mining of the contracts. This in turn enables an organization to gain the needed insights and visibility into their contracts across all their locations to determine compliance, increase savings and optimize their contract management performance.

Along with the data comes the improved visibility from reporting on status, expirations and performance against contract.

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Where to Begin

As the research indicates, there is tremendous value in adopting a robust contract management solution. However, most companies are not starting with a clean sheet of paper and have existing solutions or methods to deal with. In other words, most companies are not in a position to “rip and replace” but want to improve their situation, and for this discussion we will assume that is the case.

There are many ways to approach the problem that may vary from adding a standalone point solution to looking at a solution provider from a long-term perspective. For that reason, consideration should be given to providers that have a platform approach to the contract management solution space, which enables organizations to “start small and scale the solution over time.” However, this is a decision that each organization must decide for itself.

Summary and Key Takeaways

Contract management is a critical function of all organizations, but as the research indicates, not all organizations are performing at the same level. Those that are effectively managing this process are exemplified by the Best-in-Class, where their performance has improved results across the entire contract management process. The following recommendations are intended as a guide to achieving Best-in-Class performance in contract management:

- ➔ Adopt the appropriate technology to create an electronic contract management solution
- ➔ Automate the source capture of information from the request level

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- Automate the creation and authoring of the contract in an electronic format. Begin now and stop the perpetuation of paper contracts
- Negotiate and track all changes in some form of word processing document and a robust change control tool to mitigate risk
- Use electronic workflow to manage the approval cycle
- Where needed, use an electronic signature solution to secure signatures both internally and externally
- Develop/Create a central contract repository for all contracts and supporting content/documents
- Convert active contracts once the process is in place for electronic contract creation and management
- Leverage the searchable repository to identify exceptions and facilitate reporting for managing deadlines, expirations, risk mitigation, compliance, performance, and out-of-tolerance conditions
- Adopt the technology for analytics to leverage the data provided from the searchable repository for vendors and products

Start now and move your organization toward Best-in-Class performance in contract management.

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For more information on this or other research topics, please visit www.aberdeen.com.

Related Research

[Using Electronic Signature for Best-in-Class Contract Performance](#); June 2015

[Best-in-Class Strategic Sourcing: Profile and Approach](#); March 2015

[The Best-In-Class Lead the Way on eSourcing](#); June 2015

[Best-In-Class Strategic Sourcing: Value of Internal Collaboration](#); March 2015

Author: Bryan Ball, Vice President and Group Director, Supply Chain and Global Supply Management Practices (Bryan.Ball@aberdeen.com)

About Aberdeen Group

Since 1988, Aberdeen Group has published research that helps businesses worldwide improve their performance. Our analysts derive fact-based, vendor-agnostic insights from a proprietary analytical framework, which identifies Best-in-Class organizations from primary research conducted with industry practitioners. The resulting research content is used by hundreds of thousands of business professionals to drive smarter decision-making and improve business strategy. Aberdeen Group is headquartered in Boston, MA.

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