



Client Memo  
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## **Kick Off the New Year with a Thorough Review of Contractual Obligations and Commitments**

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Most outsourcing contracts contain provisions that are to be completed post contract execution, require periodic updates, or simply vary over time. As we kick off 2010, the time is right to take a close look at these “active” obligations, identify any elements that require service provider action, and develop a plan and timetable to ensure that your relationships are ready to succeed in 2010.

In the table below, we have identified some typical contract elements that may benefit from an early 2010 review. While there is nothing particularly unique about the beginning of the year as it relates to most contracts, we find that there is no time like the present to revisit and tie up those terms that may have been left untouched. Several of these elements are purely administrative, with little impact on performance or cost, while others may have a significant impact on these areas. However, each is important to address as fulfilling these obligations is fundamental to realizing the full value of the deal as it was envisioned when the initial outsourcing decision was made. Staying current with these elements enables buyers to: (1) ensure that metrics, measurements, and reports provide meaningful insight into the operations and results; (2) obtain a thorough understanding of their outsourced operations and how the service provider interacts with the retained organization; and (3) ensure the services delivered match the services under contract and for which the company is paying. Furthermore, this effort can make a healthy deal more effective, provide a platform for productive service provider interactions for deals that are not yet achieving their expected benefits, and minimize transition risk for buyers that are contemplating transitioning services away from their current service provider(s).

We recommend that buyers of outsourced services kick off the New Year by reviewing their contracts to identify specific terms that require periodic revision or contracted deliverables from the service provider, and set a plan to revisit these items as soon as possible.

**Typical “Active” Contract Areas**

Area	Explanation
<b>Resource Commitments</b>	<p>Many contracts specify the number of service provider resources that will be providing services in each year of the contract and in many cases this is linked to productivity commitments (see below) or volume commitments. Buyers should ensure that the number of resources providing services and other volumetric attributes of services being delivered are correct for the current year.</p>
<b>Productivity Commitments</b>	<p>Many contracts specify a minimum level of service provider productivity in each year of the contract. In many cases, this is linked to the number of resources to be paid for by the buyer (see above) or volume commitments. For example, a contract may specify an increasing number of transactions processed per resource in each year of the contract, or it may specify a maximum number of resources that can be charged to the buyer based on a projected volume of transactions. Buyers should ensure that the productivity commitments are being realized through lower costs or an increased number of transactions with no additional charges.</p>
<b>Pricing and Fees</b>	<p>Pricing and fee structures are affected by factors such as the volume of services being consumed, number of resources being provided, annual adjustment provisions, etc. Buyers should review recent invoices (best practices typically include thorough invoice audits at least once per quarter) to determine whether both the cost per unit and units being invoiced are accurate. Additionally, many contracts link price to escalators (e.g., COLA, currency) that may result in pricing changes throughout the term. Buyers should be aware of the contracted pricing algorithms and indices so they can anticipate, model, and verify that pricing is reflected accurately in the invoices.</p>

<b>Pass-Through Expenses</b>	Pass-through expenses are typically charged as incurred, but are often subject to limitations and restrictions (e.g., compliance with policies, advance approval). These charges can add up to a significant percentage of overall fees. Buyers should review such expenses to determine approaches to minimize, if not eliminate, such charges.
<b>Continuous Improvement Plans</b>	In addition to committed productivity levels or resource reductions, service providers are often required to document proposals for increased efficiency and / or effectiveness. This idea is an important component of overall business optimization and can provide buyers with valuable insight into additional opportunities or non-value added activities that should be eliminated. Buyers whose contracts include these provisions should ensure they have received and reviewed any proposals.
<b>Benchmarking</b>	Benchmarking can be challenging to implement and is a potentially costly activity, but if included in your contract, it can provide for meaningful productivity and cost improvements. Contracts with limited productivity improvement commitments may benefit most from utilizing this clause. Buyers that feel their services are “out of market” should examine their contracts to determine if this type of clause is present, and consider initiating such a benchmarking assessment. A surprising number of buyers go through the arduous process of negotiating such clauses, yet fail to exercise them (or even suggest exercising them) as permitted in the contract.
<b>SLAs and Reporting</b>	Services tend to evolve over time and retained and outsourced organizations must adjust accordingly to determine how to best work together. Similarly, SLAs and reporting requirements should be reevaluated periodically. If contracts do not expressly provide for SLA modifications and improvements over time, if a buyer feels that the current SLAs do not provide the proper incentive for service provider performance, or worse, is not certain the SLAs accurately measure the services being delivered, it is likely time to revisit this area and make the necessary adjustments. Additionally, a buyer may want to exercise

	<p>audit provisions to ensure the service provider is measuring the agreed upon SLAs and metrics correctly and verify that any due performance credits have been provided.</p>
<p><b>Processes and Procedures Documentation</b></p>	<p>Service providers are typically required to maintain up-to-date documentation for all processes and procedures. This is valuable for training new resources, providing specifications for technology requirements, ensuring standardization of common processes, and preparing for transition to another service provider or to internally provided services. Current documentation can also enable buyers to significantly reduce transition timing and risk if / when services are delivered by multiple service providers or locations. Buyers should verify that documentation has been updated according to the contracted frequency and that they have access to the latest versions of this documentation.</p>
<p><b>Audits</b></p>	<p>Periodic audits (e.g., SAS 70 Type II), whether compliance or operations related, may be required by company policy, regulatory entities, standards bodies, or may simply be desirable to validate the efficacy of the services being delivered. Buyers should determine when audits are contractually allowed or due and plan accordingly, especially in the case of mandatory audits.</p>
<p><b>Technology Configuration</b></p>	<p>The technical specifications for applications and hardware utilized by a service provider to administer the service being provided (for example, the service provider may be providing a help desk trouble ticket management application) are typically established at the time a contract is executed. In many cases, these specifications may change over time and may impact provider performance. Some contracts may contain technology refresh provisions that are in place to ensure continued optimal performance. Buyers should understand their contracts and ensure that outsourced resources are operating with the proper hardware and software required to efficiently provide the services.</p>
<p><b>Resource Certification(s)</b></p>	<p>Certifications are often required to ensure outsourced resources are aware of contractual obligations (e.g.,</p>

	<p>confidentiality) or may be required due to the nature of a buyer’s industry (e.g., security clearances for Aerospace and Defense, compliance training for healthcare providers). Buyers should verify the necessary certifications are in place to ensure service provider resources meet all minimum qualifications.</p>
<b>Document and Data Storage / Retention</b>	<p>Most contracts include provisions for document and data storage / retention, established based on company policy or legal obligations. Over time, these requirements and the manner in which they are best provided may change. Buyers should be certain that the current practices meet all necessary requirements.</p>
<b>Business Continuity / Disaster Recovery Plan and Procedures</b>	<p>Business continuity and disaster recovery plan obligations often contain requirements for testing and updating. These provisions are in place to minimize operational interruptions due to unforeseen events. As services evolve, these plans may quickly become outdated and, if left untested, may prove to be inadequate when the need arises. Buyers should be certain that these plans are current and tested.</p>
<b>User Access</b>	<p>High attrition rates can be common in certain areas of outsourcing (particularly when services are provided from offshore locations) and, as such, a robust user access management process is necessary to ensure: (1) only authorized users have access to buyer systems; and / or (2) license and support costs are optimized to the number of active users. Buyers should ensure that user access is current and internal processes to manage proper access are effective.</p>
<b>Key Personnel</b>	<p>Key Personnel and personnel restrictions are often specified in contracts and may link to specific buyer and service provider obligations (e.g., certain service provider resources and/or certain positions may not be swapped out for a minimum time period, buyer right to remove resources, preclusion of service provider resources to serve buyer’s competitors). Buyers should ensure the list of Key Personnel is closely monitored, remains current and is appropriately enforced.</p>

<p><b>Competitors</b></p>	<p>Similar to Key Personnel, buyer and service provider competitors may be specified in contracts for many reasons. Buyers should ensure that this list is current to limit the risk of a competitor benefiting from a buyer’s strategic decisions and best practices, especially if a service provider is also serving a buyer’s competitors.</p>
<p><b>Governance Cadence</b></p>	<p>Governance meetings (at both executive and operational levels) are typically envisioned to take place on a periodic basis throughout the year (e.g., quarterly), with certain governance levels chartered to address certain business and technical issues. Buyers should evaluate that the historical cadence is optimal and schedule these meetings in advance to maximize the likelihood that necessary participants are available to actively participate in such meetings. Additionally, buyers should consider the agenda and invitees of governance meetings to ensure they are sufficient to address the strategic and tactical needs of the relationship.</p>
<p><b>Anticipated Business Changes</b></p>	<p>It may benefit a buyer to consider anticipated material business changes that are likely to occur throughout the next year (e.g., acquisition, divestiture). Such major changes often affect an outsourcing relationship, as transaction volumes, required resources, and services are likely to change. Buyers should begin to develop a strategy to inform and engage service providers so they are prepared to provide modified services when appropriate.</p>