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Contract Management Leads to Rediscovering Lost Revenue, Balancing Scorecards, Catching the Long Tail and M&A Due Diligence

Like the chill of winter, reports of economic recession fill the air in 2008. In winter, keeping the house warm, shoveling snow and ice off the walk, fighting off colds, and watching for closings are the things that occupy people's minds. Similarly, in business, companies tend to focus more on managing personnel and operations. Human resource policies, financial statements and tax filings, insurance coverage, and capital financing, activities that cost money but don't exactly make money.

Few businesses with less than 200 employees have a contract manager or hire an independent consultant to manage their contracts, either for their sales or for their partners and suppliers.

If a contract has been signed, why spend any more money on it.

But unlike accountants and lawyers and hiring firms, contract managers can make the company money, and not just in a round about way. Here's how.

EXPIRED END DATES. About one quarter of the contracts used in business are either so called "evergreen" contracts that have no end date, or contracts with end dates that have expired but no

one knows it. Knowing expiration status gives all parties bargaining power to renegotiate or walk away. Hiring and salary levels, switching service suppliers and reducing operating costs, drafting project plans and estimating costs, retaining customers and managing accounts, and projecting sales figures are all dependent on knowing the true length of contracts and how to perpetuate them.

SCOPE CREEP. Most professional services contracts have a funny way of changing over time. Responsibilities shrink, and customers get charged for work they are already paying

for, or the work expands in response to customer demands without charging for it. This phenomenon, called scope creep, is the rule, not the exception. Hundreds of millions if not billions of dollars are lost annually in American business due to scope creep.

UNENFORCED PROVISIONS. The people who perform consulting services or maintain equipment and software in business are not lawyers. They never see copies of the contracts covering what they do, and wouldn't know how to read them in any case.

So how do business people know if they are following all of the provisions? Without contract management they don't. Warranties and service levels are loosely followed or ignored, robbing customers of value. Customers replicate a supplier's processes and systems and bring the work in house, or hire away the supplier's personnel, though the contract prohibits it. Requisite security and confidentiality measures aren't implemented, ending in data breaches and lost trade secrets.

CHANGED CIRCUMSTANCES. Companies negotiate and sign contracts based on current business conditions and economic forecasts. When business doesn't go as planned, companies may find themselves needing to delay payments or break agreements, without filing for bankruptcy.

There are good faith and bad faith ways to break contracts. By strictly interpreting contract terms in anticipation of a break, companies can build a case for material breach. Sometimes contracts contain assumptions that act as "conditions precedent" and offer a way out. For design and build projects, hardware supply agreements, or any other agreement that contains specifications, knowing the contract also enables companies to institute change orders on the fly, realigning the agreement with business conditions.

ACCOUNT MANAGEMENT. From the Balanced Scorecard to Freakonomics, achieving customer satisfaction through setting expectations is a well known business principle. Contracts are the best means of setting customer expectations. Exceeding customer expectations can be as simple as saying "Although the contract only

requires the company to do 'x' and 'y,' we will go the extra mile for you, the customer, and do 'z' as well," leading to higher satisfaction and more business.

LONG TAIL. Standardizing key contract terms across all customers and across all suppliers reduces transactional expenses and allows companies to get into selling a greater variety of products and services, catching Chris Anderson's "long tail" of profiting from lower demand, more specialized products and services.

AUDITING AND DUE DILIGENCE. Getting funding requires due diligence. Getting acquired requires due diligence. Publicly traded companies must undergo annual Sarbanes Oxley auditing which can have a major impact on stock price. By definition, auditing and due diligence require third party legal and accounting services which are grossly expensive. Compliance with Sarbanes-Oxley Sec. 404 by small companies costs 10% of gross revenue, according to the Small Business and Entrepreneurship Council.

One of the few self helps companies can undertake to reduce auditing and due diligence costs, and drive bigger rounds of funding, credible purchase prices and higher stock prices, is to maintain organized contract files and to implement strong processes for payment, assignment and dispute resolution.

GUEST COLUMN



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