



# IAOP Midwest Chapter Meeting

## Effective and Efficient Outsourcing Contracting

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## Agenda

- Overview: The Contracting and Negotiating Process as a Relationship-Builder
- Top Ten Tips for Negotiations

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# Overview: The Contracting and Negotiating Process as a Relationship-Builder

## Overview: The Contracting and Negotiating Process as a Relationship-Builder

### The Relationship Mindset: Attitude Toward a Possible Relationship

- There is a tendency to think of sourcing as procurement
- It is helpful to think of outsourcing or other long-term sourcing transaction as a relationship akin to a marriage
  - Two parties making a long-term commitment to one another
  - The sourcing agreement as a “pre-nup”
- The sourcing relationship may create an exclusive (*de facto* or *de jure*) monopoly supplier to a certain degree

# Overview: The Contracting and Negotiating Process as a Relationship-Builder

## Courtship: Getting to Know One Another (due diligence)

- From a customer standpoint, the provider selection process should be robust and thorough
  - Assess provider's track record of service and flexibility, ability to achieve objectives, financial viability, reputation, corporate structure (*e.g.*, for parent guarantee), and litigation history
  - Communicate thoroughly throughout the process
    - Include management, operational personnel, subject matter experts
    - Use regular meetings and broad access to keep process on-track
    - Consider internal sensitivities regarding communications

# Overview: The Contracting and Negotiating Process as a Relationship-Builder

## Courtship: Getting to Know One Another (due diligence) (cont.)

- Communicate thoroughly throughout the process (cont.)
  - Interview past/existing/current customers of provider; interview different business constituencies of customer
  - Consider the quality of infrastructure and personnel and long-term health of provider
  - Perform background checks -- security measures, privacy, protection of confidential information, intellectual property, litigation history, media search, etc.
- From a provider standpoint, “know thy customer” is crucial to a successful engagement

## Overview: The Contracting and Negotiating Process as a Relationship-Builder

### The Contract: A Prenuptial Agreement

- View the contract as an opportunity to improve understanding of the other party, the parties' respective interests, and the transaction -- not as a hindrance or box to check
- Approach the contract as the last best chance to establish the relationship on a strong foundation
- Allocate time and resources sufficient to allow a comprehensive process and quality analysis and work product
- Involve counsel at inception
- Consider privilege issues when engaging and communicating with advisors

# Overview: The Contracting and Negotiating Process as a Relationship-Builder

## The Contract: A Prenuptial Agreement

- Identify potential issues in the relationship
  - Issues related to fundamental commercial terms (*e.g.*, scope, price, and performance)
  - Specific risks and concerns of each of the parties (*e.g.*, provider's concerns regarding revenue recognition, protection of IP, limitation of liability, data security)
  - Extrinsic issues (*e.g.*, change in law, geopolitical risk)



# Overview: The Contracting and Negotiating Process as a Relationship-Builder

## The Contract: A Prenuptial Agreement

- Build a foundation of trust and cooperation through the contract negotiation process -- the living together
  - The provider will be taking over a critical function of the customer and potentially changing it in fundamental ways
  - The parties must establish a solid working relationship to address change and other issues in the future
  - One-sided contract with onerous burdens on the provider may be a Pyrrhic victory that creates a “breach-in-waiting” or work-to-rule approach

## Overview: The Contracting and Negotiating Process as a Relationship-Builder

### The Marriage Contract: A Good Relationship Alone Is Necessary but not Sufficient ...

- Note that an effective sourcing agreement must have clear governance and dispute resolution processes and appropriate incentives and disincentives to keep the parties' interests aligned
- Do not underestimate the need for a solid agreement with detailed exhibits and schedules because as time passes, the individuals initially involved may move on
- Ultimately, even the best contract might not save an engagement if the parties are poorly matched or their respective interests are misaligned

## Overview: The Contracting and Negotiating Process as a Relationship-Builder

### The Marriage Contract: A Good Relationship Alone Is Necessary but not Sufficient...

- Contract has many different functions/purposes
  - Memorializes the agreement and the intent of the parties at the time of entering into the agreement
  - May be necessary to satisfy legal requirements (*e.g.*, Statute of Frauds; assignment of IP rights)
  - Serves a prophylactic purpose (but note that in litigation, even if you win, you lose)
  - Allocates risks and responsibilities
  - Provides incentives and disincentives to shape behavior
  - Provides a roadmap for actions when things change or go wrong

# Top Ten Tips for Negotiation

## Top Ten Tips for Negotiations

### Tip #1: Do Not Start Work before all Contract Documents Are Executed

- Beginning to engage a provider for work prior to executing the definitive contract documents can reduce flexibility
  - More difficult to walk away from an engagement if the provider has already started performing the engagement
- If the parties must commence work prior to executing the definitive contract documents:
  - Ensure that the work product has intrinsic value
  - Shape the engagement as a pilot that is not dependent on the ultimate engagement
  - Have alignment mechanism in place (*e.g.*, tie all or some portion of the payment to the provider to completion of the definitive documentation)
- Agree upon how any pre-definitive/interim agreement will be rolled into the definitive agreement and scope of work

## Top Ten Tips for Negotiations

### Tip #2: Recognize That Negotiation Is Not a Zero Sum Game

- Parties should not look at negotiation as a battle to be “won”
  - Final contract documents should be “fair and balanced” to reflect the appropriate risks and incentives for optimal outcomes and performance by both parties
  - “Winner take all” mentality is not conducive to building a strong foundation for an ongoing, long-term relationship
- However, parties need to understand that risk of failure often falls disproportionately on the customer – therefore, agreements must appropriately address balance of risk

## Top Ten Tips for Negotiations

### Tip #3: Do Your Homework

- Understand the contracts to be negotiated and the background materials (*e.g.*, RFP response, customer's business case, etc.)
- Work from a term sheet if appropriate or helpful
- Research the other party's agreements – prior agreements and public domain sources (EDGAR, other regulatory filings, court documents, etc.)
- Prepare issues lists, document summaries, and potential compromise and fallback positions

## Top Ten Tips for Negotiations

### Tip #4: Develop a Good Working Relationship

- Strive for face-to-face meetings for key negotiating sessions
  - Read body language
  - Be sensitive to nuance, particularly when dealing with foreign counterparties
- Use a “partnering” approach - engage in give and take
- Maintain long-term focus
- Avoid extreme positions
  - Do not take false hard line positions
  - Consider loss of credibility when a party ultimately caves on an extreme position or line in the sand



## Top Ten Tips for Negotiations

### Tip #5: Have the Right People in the Room

- Negotiate during scheduled sessions, on home turf if possible
- Make sure each party has its decision-makers available
- Identify members of the deal team on both sides early on
- Even if not leading the negotiations, have business people present even when the lawyers are going through the terms and conditions (there is no such thing as a purely “legal issue”)
- Limit/control operations personnel’s involvement in negotiations
- Leave option open to bring in senior personnel to resolve thorny issues or to reinforce hardline positions

## Top Ten Tips for Negotiations

### Tip #5: Have the Right People in the Room (cont.)

- Lead negotiators likely should not be the individuals who will have direct, day-to-day responsibility with respect to the implementation and operation of the sourcing arrangement
  - Negotiations can become contentious
  - This helps avoid putting operations personnel in position of taking unreasonable positions with people with whom they will have to work
- On the other hand, it can be helpful to have present the representatives from both customer and provider who will have to live with the contract
  - Helps them understand the dynamics of the deal
  - Precludes future disclaimer of responsibility on basis they did not have input into the deal thereby improving accountability

## Top Ten Tips for Negotiations

### Tip #6: Check Your Ego/Emotions at the Door

- Remember, the negotiation is not about you or about whether you “win” or “lose” (see also Tip #2)
- Never lose sight of what is best for your organization as a whole
- Do not take a failure of the parties to agree or the other party’s position on an issue personally
  - Remember that at times, there will simply be disagreement
  - Remember that “no” is not a bad word
- Use posturing sparingly and judiciously
- Consider the degree of openness in communications but do not lie

## Top Ten Tips for Negotiations

### Tip #6: Check Your Ego/Emotions at the Door (cont.)

- Note that each party should air all issues in the negotiations and trust the other party to escalate issues internally as appropriate
  - Going over the head of the other party's negotiating team to bring an issue or concern directly to that other party's senior management poisons the well going forward
  - Trust and transparency are lost, potentially leading to drawn out negotiations and a greater likelihood that the negotiation becomes an emotional issue for some

## Top Ten Tips for Negotiations

### Tip #7: Document Everything You Can; Do Not “Agree to Agree”

- Document entire transaction to the greatest extent possible for execution with the master agreement so as to minimize loss of interrelatedness of terms and to avoid loss of leverage
- Do not assume that schedules and exhibits are business or technical documents that can be detailed at a later date
  - Do not leave schedules and exhibits to the last minute
  - Note that these are where the performance requirements, scope of services, pricing, and many of the most important details are going to be addressed
- Where details must be provided at a later date, include default approach (for when parties are unable to agree) in master agreement

## Top Ten Tips for Negotiations

### Tip #7: Document Everything You Can; Do Not “Agree to Agree” (cont.)

- Get agreement on the principle, then on the language
  - Prepare business people for this approach so they understand why the parties may not trade drafts after each negotiation session
- Agree on the issue and make sure each party understands what has been agreed
  - Do not rely on ambiguity (usually)
  - Clarify where the agreement is unclear (and do not be afraid to restate the conclusion for clarity)

## Top Ten Tips for Negotiations

### Tip #8: Understand the Totality of Issues

- Tendency to want to try to resolve issues as they are identified
  - Customary approach to negotiations is to walk through agreement from beginning to end
  - Some negotiators and many stakeholders are inclined to try to minimize the number of issues or the appearance of there being a lot of issues as the parties proceed through the agreement
- However, issues are often interrelated, or come up in multiple places throughout a document
  - Parties should be careful about agreeing to a change or making a concession in one place where that might be inconsistent with treatment of a similar issue elsewhere
  - More productive to “trade” on issues when they can be grouped and handled on a global basis

## Top Ten Tips for Negotiations

### Tip #9: Shut up

- Remember, silence is golden
  - Listen -- the less said, the better
  - Once your position is stated, stop talking
  - Do not be afraid to let the other party talk itself into making your point
  - Once an issue is closed, stop talking
- Try to understand specifically what is motivating the other party
- Let the other party make the first move/offer
- Do not bid against yourself



## Top Ten Tips for Negotiations

### Tip #10: Know When to Fold ‘Em

- Be willing to walk away from a bad deal (and do not be afraid to communicate that)
- Drive the process with a sense of urgency but be patient
  - Do not let other party “run the clock” against you
  - Note that a stated deadline can operate as a disincentive to completion unless you are willing and able to walk away

Thank You

Questions?

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