

# Transforming Vendor Performance through Innovative Contract Management

Andrew Bartolini  
Founder & Chief Research Officer  
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### Sponsor Contact:

Devinder Jeet Singh (DJ)

VP – Marketing, SirionLabs

[Devinderjeet.singh@SirionLabs.com](mailto:Devinderjeet.singh@SirionLabs.com)



## Executive Summary

Ardent Partners research has shown that procurement departments can save between 12% and 18% when they avoid maverick spending. But, managing contracts is about much more than compliance. Contracts are the glue that binds buyers and suppliers, ensuring that buyers maximize the value negotiated during the sourcing process and that suppliers deliver what they promised to provide. In 2020, new and innovative contract management strategies and technologies are changing the way procurement and contract teams can communicate, track, and collaborate with their vendors and directly transform vendor performance. This report looks at how procurement organizations can utilize innovative contract management strategies and solutions to improve internal operations, transform vendor performance, and impact the bottom line.

# Major Trends Impacting Procurement This Decade

It is fair to say that 2020 is unlike any year in recent memory. In an instant, Chief Procurement Officers (“CPOs”) and procurement leaders around the world had to face an entirely new set of challenges, accelerated by a global pandemic that has disrupted an interconnected business world and its supply chain. Now, CPOs have been called to the front lines to defend their businesses, lead their teams, and ensure business continuity. With pervasive uncertainty and tough times ahead in the second half of 2020 and, most likely, 2021, it is worth noting that many of an enterprise’s best opportunities (and most critical priorities) will play to the strengths and expertise of its procurement department, and that contract management has never been more important to these groups.

Before the coronavirus impacted procurement teams around the world, the CPO’s top three pressures this year were the need to (1) drive a digital transformation, (2) improve processes, and (3) increase agility. In the immediate aftermath of the global pandemic, business needs and the CPO’s focus quickly shifted to (1) prioritizing cash management, (2) increasing savings, and

(3) improving supply chain visibility (see *Figure 1 below*). In times of great stress and uncertainty, businesses revert to their more basic selves. This means that right now, “cash is king,” savings has become much more important and sourcing leaders will be reevaluating their suppliers and soon bringing many more RFPs to market.

While the longer-term impact of the pandemic remains unclear, several major procurement trends will continue to shape the industry throughout this new decade. In each of these areas, innovative contract management can play a major role.

## Trend #1 – Speed and Agility

Business continues to change at an accelerating speed, as enterprises and their suppliers are forced to adjust to new, disruptive technologies, intensified competition, and a marketplace that continually resets its expectations. As a result, business requirements have become more diverse and dynamic, lead times are shrinking and getting shorter, and the definitions of performance and success have become moving targets. Mobile devices, cloud technology, and business networks have radically altered how (and frequently, where and when) business professionals communicate, collaborate, and engage with their colleagues, customers, partners, and suppliers and, by doing

Figure 1: Top CPO Pressures Before and After COVID-19



so, have contributed to a paradigm shift in business, where speed, innovation, and agility have become the lynchpins for success.

In the 2020s, the winners in procurement will be the agile organizations that can leverage their strategic prowess and fluid resources to anticipate and support dynamic business requirements amidst more rapidly changing industries, supply markets, and customer behaviors. Agility is the characteristic that will help procurement departments advance and thrive in this new age where innovation continues to expand beyond mere products and services to core business processes and entire business models.

### **Trend #2 – Supplier Innovation**

One outgrowth of the speed and agility trend is that the level of competition and innovation that exists in today's market mandates that enterprises leverage their supplier relationships to maximum effect. This means that the decisions, operations, and performance of an enterprise's suppliers can have a direct and immediate impact on its own results. This trend places procurement squarely in the crucible of business operations, relationships, and results.

Since no enterprise has cornered the market on innovation, businesses can no longer rely solely on their own devices (literally and figuratively) to thrive and survive. Change is happening too fast and approaching from far too many angles for a standalone entity to make it. Leading organizations know that in order to maintain market share and market relevance, they must find strong business and trading partners with shared or aligned interests and develop a coalition of willing forces who can leverage their collective strengths for mutual benefit.

### **Trend #3 – Big Data**

Due to the rise of business process automation tools, cloud-based applications, mobile solutions, and connected devices permeating the modern business environment, more data is being created each year than ever before. The result is a world that has become increasingly data-driven, and businesses around the globe have an extraordinary opportunity to capitalize on it.

In 2020, businesses are now fully engulfed by technology and the data it both creates and captures. The same holds true for procurement departments across the globe. Procurement's "Big Data" has the potential to become the next major force and catalyst for the profession. In fact, over the next few years, Ardent Partners predicts that a new type of intelligence will emerge from this data that enables CPOs to view their operations differently and by doing so, will force these same CPOs to develop new strategies and approaches.

### **Trend #4 – Everything-as-a-Service**

Traditional services spend, including categories like consulting, legal, and maintenance, can comprise up to 40% of total enterprise spend. With the rise of on-demand and subscription-based offerings that are replacing the traditional purchase of many goods, this number is growing. While most commonly seen with software, where subscriptions have replaced the license model, many other categories have experienced this shift. For example, many equipment makers used to sell "products," but now many provide the same product utility via a subscription or pay-per-use model and different contractual and payment terms.

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## The “Traditional” Impact of Contract Solutions

The Source-to-Pay process can be divided into two sub-process areas, what happens before and after a supplier contract is executed. Procurement departments can use contract management solutions to provide significant value in each area.

### Efficiency & Effectiveness

In 2020, the inefficiencies, opportunity costs, and risks associated with manually generating, editing, mailing, signing, storing, and reviewing paper contracts across the globe to codify business relationships have become too great. Resource-strapped CPOs and other supply management leaders remain pressed to drive greater value, faster and more effectively, through the contracting and procurement processes – pressured to constantly do better with less. The ability to standardize and scale contracting processes has a direct impact on team efficiency, operating budgets, and the ability to manage a more streamlined process.

Ardent Partners’ research shows that after the deployment of a contract management solution, procurement and/or contract teams collapse the average contract execution cycle time by roughly one-third (34%). This means that fewer resources can carry a greater workload. These contract solutions also pay an efficiency dividend to suppliers adding a nice win-win element to the sometimes adversarial negotiation process.

Modern, automated contract management tools can save enterprises time, effort, and money during the supplier negotiation all while helping teams avoid costly mistakes. Procurement teams looking for cost effective ways to increase efficiencies, performance, and value, have used automated contract management solutions to deliver results. Smarter, more effective contract management includes smart template and clause selection and usage that can be AI-driven to guide system users down a prescribed contract development and authoring process.



34%

faster contract  
execution  
cycle times

## Plugging Savings Leakage

Savings leakage is defined as the gap between identified (or negotiated) savings and realized (or implemented) savings due to poor contract management, flawed supplier on-boarding, and other sourcing weaknesses. While **the average company loses 21% of its cost savings via leakage every year**, closing the process gap by connecting sourcing and contracts can reduce that number by almost half. Thus, many executives value contract management for its ability to link the source-to-settle process, guard against savings leakage, and realize the savings that procurement identified and negotiated at the time of contract award.

One major challenge for a generation of procurement executives was the establishment of a clear and unambiguous definition of savings. This was caused, in part, by many CPOs who wanted to highlight and report on the savings that were identified/negotiated at the time of contract award and then move onto the next savings opportunity. But, the reality then, as it is today, is that simply identifying the highest value supplier and high-level pricing is one step in a much longer process that has to be managed if savings are to be maximized. What is most important is the savings that are actually realized by the enterprise.

In 2020, savings leakage tends to range between 14% and 26% on the typical sourcing contract. The main reasons behind this leakage are usually poor visibility and communication which create (1) an inability to capture what was negotiated during the sourcing process, (2) challenges during the implementation process in gaining stakeholder awareness, and (3) P2P process and data gaps between contracts, orders, invoices, and payments. In each case, automated contract management solutions can enable greater visibility into the usage of contracts while also enabling better accuracy across the full P2P process.

## Mitigating Risk

At the outset of 2020, Ardent Partners determined that supply risk was at a 20-year high based upon a number of economic and geo-political factors. Despite this, only 34% of all procurement teams are operating today with a supply risk management program (see *Figure 2 below*). This means that for a majority of procurement teams, their contracts program, by default, is the best mechanism to manage and mitigate supply risk.

Figure 2: Supply Risk Management in 2020



With so many forms of risk residing within global supply chains, and that risk extending well beyond first-tier suppliers to other third-parties, gaining visibility into the different supplier tiers to better understand risk has become paramount. Supply risks cannot be managed, mitigated, or avoided if they continue to grow in the dark. They must be illuminated before they can be treated. Fortunately for CPOs and procurement teams, the use of an advanced, user-friendly, contract management solution can help them gain visibility into (and ultimately control over) supply, supplier, and other third-party risks, while also tracking and maintaining internal and external compliance.

Many contract management solutions provide users with customizable, interactive, and user-friendly dashboards and alerting/reporting features that flag sudden global events that could put their operations at risk, like conflicts, labor strikes, or weather-related events. They can also alert users to upcoming expiration or renewal dates and provide them with sufficient notice to take the appropriate action, thereby avoiding the risk of auto-renewing a non-competitive contract.

It should be noted that contract management solutions can also provide visibility into the buying organization's full obligations to the supplier, which can support cash management strategies and limit the exposure of the enterprise to a variety of avoidable risks.

## Contract Compliance

Chief Procurement Officers and enterprise procurement teams have been responsible for achieving and maintaining compliance to supplier contracts and corporate policies for many years. This has not changed and will not change; particularly as greater internal compliance correlates with superior financial and operational performance and reduced risk. If anything, the CPO's responsibility to drive compliance and

reduce risk, in many forms, will continue to increase. This is highly-warranted as overall industry average compliance levels remain low. While not surprising, these rates should, however, be a cause for concern with only 61.4% of all spend and only 69.2% of all transactions compliant with contracts (see Figure 3 below).

Figure 3: Compliance Rates in 2020

Metric	Average
Spend that is contract compliant	61.4%
Transactions that are contract compliant	69.2%

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Additionally, Ardent's research on contract compliance has shown that every non-compliant dollar of spend (also known as maverick spend) costs the enterprise an extra 12% to 18%. A big part of this extra cost is simply paying a higher price than what has already been contracted, but there is also the loss of efficiencies in the order and invoice processes, particularly if a new supplier must be enabled. Low compliance is also costly because procurement loses visibility into the spend details, and therefore, loses an ability to influence it. Failing to comply with internal policies, and in some cases, governmental regulations, frequently creates additional liabilities.

It becomes clear that the hard cost of non-compliance adds up fast when looking at Best-in-Class procurement departments with contract management solutions in place. These groups utilize contract management solutions at a significantly higher degree and report compliance rates that are, on average, 35% higher than their peers.



## The “Innovative” Impact of Contract Solutions

Over the last few years, the contract management (or contract lifecycle management) solution space has seen some exciting new innovations, after lagging behind other areas in the supply management space for some time. These new entrants are driving a renewed focus on contract management solutions. This section focuses on three main areas of innovative solution impact.

### **Automated Contract Compliance**

Over the past decade, the general level of competition has expanded dramatically and suppliers now compete for business across a much wider range of areas than simply price. Pricing, in general, has become more complex, but service levels, revenue models, and contract financing structures have too. The result is much greater complexity in supplier contracts.

There is no doubt that digitizing a business' procurement contracts and gaining a broad view into them and all associated obligations can drive value by enabling greater contract compliance and plugging savings leakage. While digitized 'header-level' information aggregated in a single location

is helpful, the line-item price audits and other compliance efforts that drive great value have traditionally been a largely-manual effort.

However, this is changing with new solutions that can streamline and automate compliance in an advanced and powerful way. These solutions draw out more than basic header-level data and the operational and process info that tracks how contracts are managed. They can capture specific contract obligations, complex pricing schedules, payment terms, associated service-level agreements (“SLAs”) and other guarantees. After extracting data from existing electronic files (like PDFs and Word docs) and images (like JPGs and PNGs), the systems can automatically match or compare them to actual transactions and results.

These capabilities place innovative contract management systems at the intersection of big data management and analytics. These new systems have the ability to take large amounts of unstructured contract data (i.e., obligations, performance SLAs, pricing) and extract and parse it so that it becomes usable intelligence that can support better supplier management, governance, and invoicing. By capturing and centralizing key contract details and organizing them in a way to automate contract and compliance management,

the system helps procurement and other stakeholders track and manage key supplier obligations and their performance while ensuring that supplier invoicing matches what was contracted.

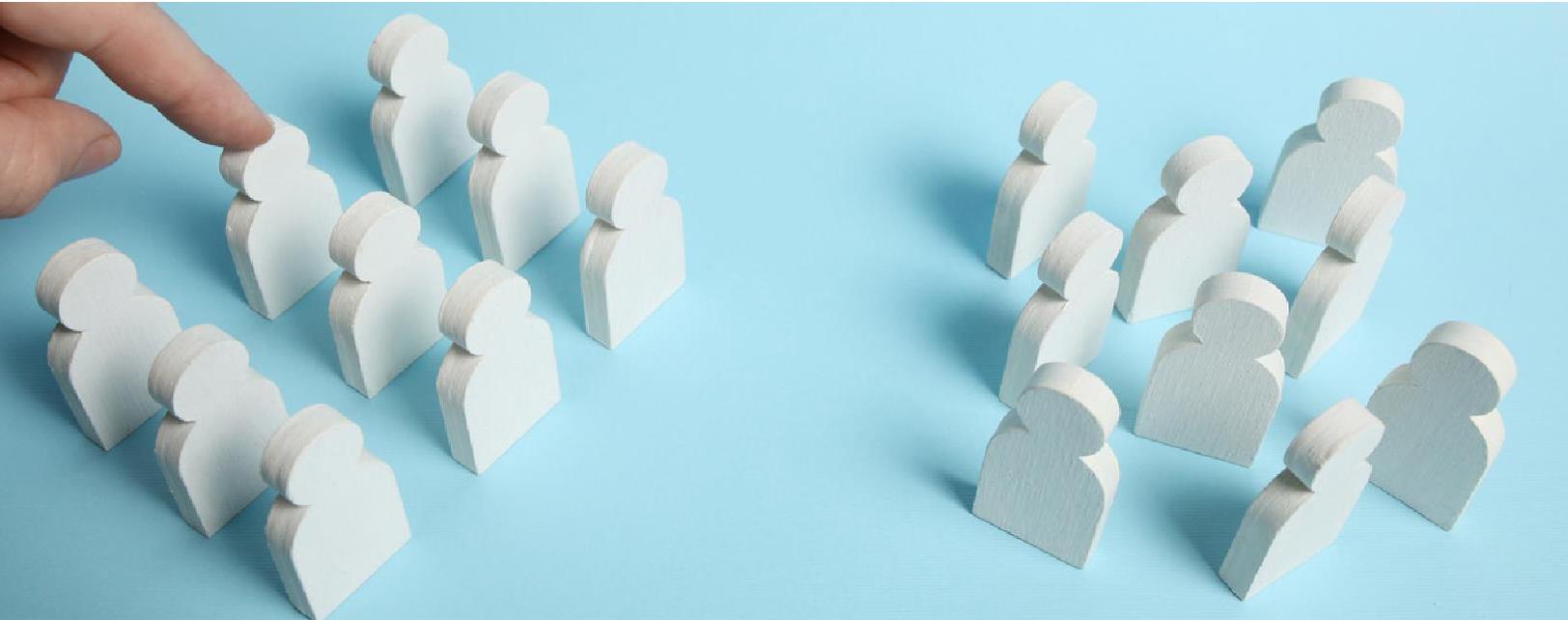
With invoice processing, some modern contract management solutions are able to match orders and use contractual pricing structures to automatically calculate expected invoice values (or pro-forma invoices) before they are received to better manage price compliance. This enables the system to flag mistakes, exceptions, and variances in the invoice matching process and calculate what the value of a supplier invoice should be while also providing a platform for suppliers and AP (or the buying organization) to collaborate and resolve any potential discrepancies or disputes if the actual invoice does not match calculated value.

### **Enhanced Services Management**

There are many implications in moving to an “everything-as-a-service” economy. Chief among them is that a services contract generally requires more effort and focus to manage properly than other contracts. Traditional services contracts tend to be managed more closely by the business stakeholders, but this also happens with on-demand/subscription-based contracts, where the cost is based on usage and/or time and the users are needed to track not only usage but also quality and the other service levels and features that are embedded in the subscription or per-usage cost.

With an ability to extract and present service-level terms to the users, procurement can regain a voice in the overall supplier management discussion and leverage best practices in new RFPs. This is valuable and important because it enables procurement to help the business make smarter decisions when it comes to evaluating subscription renewals or changes and avoid costly and inopportune auto-renewals.

“To drive automated compliance, modern contract management solutions are able to match orders and use contractual pricing structures to automatically calculate expected invoice values before they are received.”



## Transforming Vendor Performance

Supplier relationship and supplier performance management have been areas traditionally reserved for the most mature of procurement organizations as most groups struggle to manage their suppliers at the contract level. That has started to change over the last few years with newer, more advanced contract management solutions enabling more procurement teams to launch programs and advance in this area. Today, traditional supplier performance management utilizes stakeholder surveys and scorecards. The reality is that while these tools can give procurement a general sense of how the stakeholders feel about a supplier's performance, they often fail to capture a more quantified assessment of how a supplier performs against its actual contractual obligations.

Since most business stakeholders never perform detailed reviews of a supplier contract, their supplier evaluations can lack the context needed

to fully-assess supplier performance. This means that there can be a wide variance between stakeholder expectations and how a supplier should be performing. For example, as supplier negotiations and their resulting contracts become more complex, the categories and support that suppliers deliver can shift over time outside the view (and understanding) of business users. By capturing contractual terms, including pricing and targeted service levels, and then tracking actual supplier performance, these newer contract systems empower procurement and the business users with richer context to evaluate supplier performance and to communicate issues and successes back to suppliers with greater accuracy and in a more-timely way. By improving the vendor performance feedback loop, procurement can collaborate with suppliers in formal and ad hoc reviews so that poor performance can be addressed before the issue become chronic and good performance can be more clearly identified, rewarded, and repeated.

**SUMMARY:** Contracts are the glue that binds transactions between businesses and their suppliers, helping to ensure that the negotiated terms and obligations (or value) between the parties is delivered. The visibility and control that contract management solutions provide can help procurement deliver greater savings, higher compliance, and a platform to better manage supplier risk. And, new and innovative contract management solutions are emerging to empower procurement departments to transform vendor performance by combining smart technologies like AI and comprehensive big data management capabilities with advanced analytics to provide more robust and automated tools to evaluate, and ultimately, improve supplier results.



## About the Author:

ANDREW BARTOLINI, FOUNDER & CHIEF RESEARCH OFFICER, ARDENT PARTNERS

With 21 years in the industry and 11 years leading the charge at Ardent Partners, Andrew Bartolini is a globally-recognized expert in sourcing, procurement, supply management, and accounts payable. As the Chief Research Officer at Ardent Partners, Andrew oversees all research and client programs including the annual State of the Market and Metrics that Matter eBook Series', Technology Advisor Reports, Ardent's monthly webinar series, as well as its in-person and virtual CPO Rising Summits. Andrew is also the publisher of CPO Rising, the news and research site for Chief Procurement Officers and other procurement leaders ([www.cporising.com](http://www.cporising.com)).

Advisor to corporate executives and leading solution providers alike, Andrew is a sought-after presenter, having lectured and presented more than 420 times in nine different countries. Over the past decade, Andrew has benchmarked thousands of enterprises across all facets of their sourcing, procurement, supply management, and accounts payable operations and his research is currently part of the Supply Chain/Management curriculum at several US universities. He actively covers the technology marketplace as well as trends in sourcing, procurement, supply management, and accounts

payable and has been published or quoted in leading business publications including The Wall Street Journal, Business Week, Investor's Business Daily, Forbes, and Fortune, as well as the major trade publications focused on accounts payable and supply management.

Prior to becoming an industry analyst, Andrew developed, packaged, deployed, and used supply management solutions on behalf of enterprises in the Global 2000 while working for several prominent spend management solution providers. Additionally, his experience in strategic sourcing (where he managed sourcing projects totaling more than \$500 million in aggregate client spend), business process transformation, and software implementation provides a "real-world" context for his research and writing.)

Andrew's post-MBA work started in management consulting and investment banking where he structured, managed, and advised on large capital market transactions. Andrew began his professional career running a homeless family shelter in Los Angeles. He welcomes your comments at [abartolini@ardentpartners.com](mailto:abartolini@ardentpartners.com) or 617.752.1620.

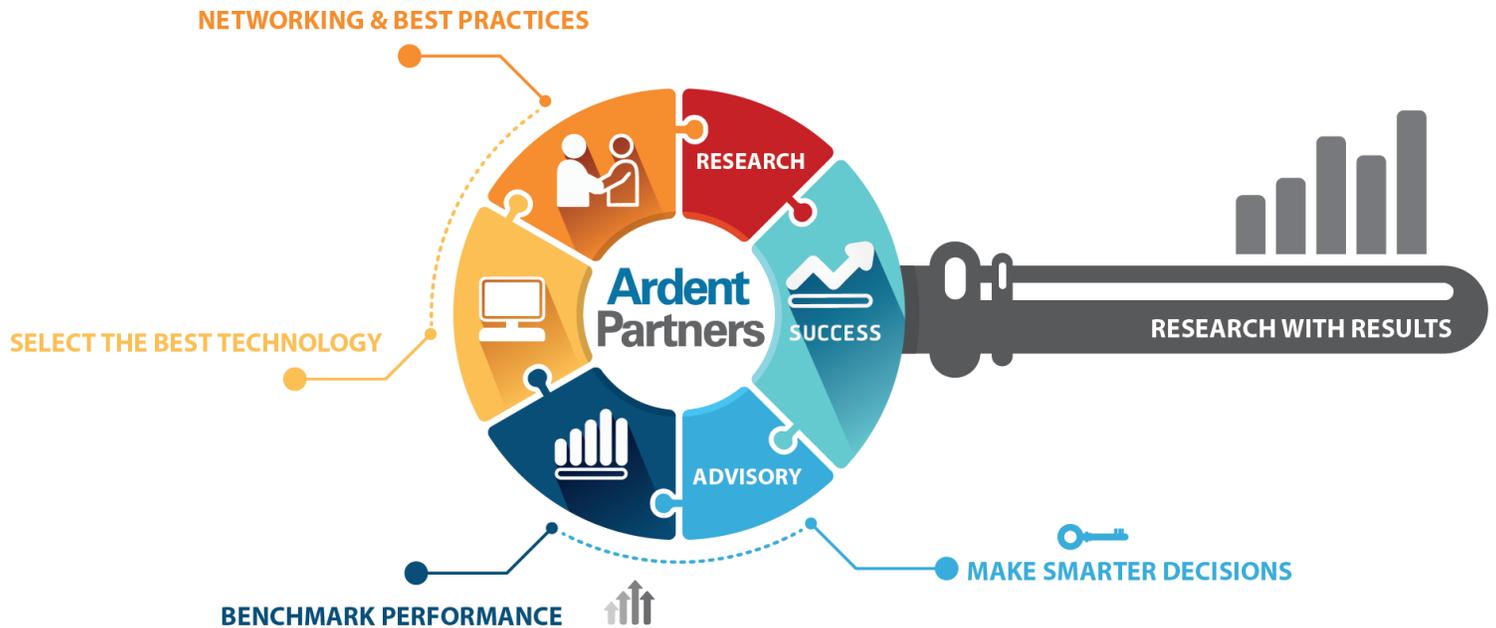
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