

**Contracting for Services:
A Review of the Contracting Process**

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Abstract. Contracting for services differs from the typical purchasing contract for materials and has a different set of challenges. We will review the basics of contracting for services, including what you need to receive from your end users and suppliers prior to formalizing a contract. Some of the important elements include the detailed *scope of work* (SOW), the contract terms and conditions, and the process for finding a supplier. The development of a clear, concise and effective scope of work is essential to ensure that the supplier understands the requirements of the service request. This understanding will lead to superior supplier performance and overall success.

Basic Concepts:

- Understanding the basic components necessary for services contracts
- Knowing the right questions to ask your internal end users as well as your suppliers
- Reviewing the need for a scope of work
- The components of a scope of work
- The items that should and should not be included in a scope of work
- How the items included in the scope of work can enhance or diminish supplier performance

The focus on procuring services for organizations has continually increased in importance. In the past, many industries did not consider services to be strategic commodities; as a result, the involvement of supply management in the services contracting process was often overlooked. But, as organizations looked for ways to reduce their expenses, they discovered the potential for ample savings in their services spend through supply management's involvement.

Some of the techniques for sourcing services mirror the requirements for sourcing goods and materials. However, unlike goods, many services can be extremely specialized or unique, and locating suppliers can be challenging. Because the evaluation process for service suppliers is much more subjective, a very clear and precise SOW is crucial. Without a detailed SOW, suppliers will find it difficult to 1) understand service-level expectations; 2) submit an accurate bid; and 3) perform the actual work. Any leeway for interpretation increases the potential for misunderstanding and dissatisfaction among all parties. A detailed SOW is probably the most important element of a successful services contract. Development of an ideal SOW requires end user involvement; the collaboration must draw upon expertise from the end user and, sometimes, from potential suppliers. While it is not ideal to allow a supplier to develop your

SOW, supplier input can provide a good “sanity check” to the final product; it may reveal costly, unnecessarily tasking requirements or even critical omissions.

Once a detailed SOW has been finalized, the sourcing process can begin. A structured sourcing process will bring the greatest value to the services contracting effort; it will marry the technical knowledge brought to the table by the internal customer group to the purchasing knowledge possessed by supply management. While not every company’s process is identical, a structured sourcing process will evoke a level of formality and credibility often missing from services purchasing in the past.

To determine whether supply management should be involved in a sourcing project first requires identification of the overall spend and the availability of qualified suppliers. In some instances, a true determination of actual services spend can only be determined through use of a spend diagnostic tool. When the spend is relatively low and the number of suppliers is limited, supply management often adds little value to the process; in these circumstances, a self-service tool should be provided for the end user. Even when the spend is larger but the number of suppliers is limited, bidding is often not effective. Negotiating with one or two suppliers can be a more effective means for procuring the services at a fair price. However, when the number of suppliers is fairly substantial and competition among the suppliers exists, supply management can use the sourcing process most effectively.

During this sourcing process, experience proves that utilization of a *request for proposal* (RFP) is usually very effective. Many organizations have found that reverse auctions can also be effective for the sourcing of services; however, for reverse auctions to be effective, it is important to pre-qualify the invited suppliers. This qualification may be done in a *request for information* (RFI) format where suppliers must respond to prerequisite questions. Conducting individual interviews with potential suppliers may also be necessary prior to the reverse auction. Again, to be effective, this process requires a very detailed SOW that clearly defines quality and performance expectations. Finally, it is imperative that your suppliers have the technological skills required to participate in a reverse auction; the supplier bases for some non-technical services (lawn care, etc.) frequently lack the necessary skills to effectively participate in a reverse auction.

Components of the SOW

Because of the criticality of the SOW in the sourcing process, there are several components that should be included in the SOW. While every good and service is different, there may be some variance in the components included. However, the basic components are often constant.

Details of the good/service to be provided may include:

- Product/material specification (grade, type, size, etc.)
- Performance detail
- Deliverables
- Timeline/timeframe
- Acceptance criteria
- Roles and responsibilities
- Pricing criteria (fixed, time and material, per unit rate, rate schedule) actual pricing detail will be documented in the contract

Who should author the SOW?

Development of an ideal SOW requires end user involvement. The collaboration must draw upon expertise from the end user and, sometimes, from potential suppliers. Ideally, the internal customer group (subject matter expert) will author the SOW. Sometimes they need a little help to get started. Providing a good sample SOW will expedite the process. Occasionally, the supplier may provide a basic SOW that can be used as a starting point. While it is not ideal to allow a supplier to develop your SOW, supplier input can provide a good “sanity check” to the final product; it may reveal costly, unnecessary tasking requirements or even critical omissions. After the SOW is written have one or two of your better suppliers review the SOW and provide feedback for your consideration.

When writing the SOW, there are a few things that should be considered to make the SOW clear and understandable. Avoid undefined capitalized terms, avoid commonly used company acronyms or slang, avoid industry jargon. If you can't avoid using any of the above, ensure that you provide a definition of the term in the SOW.

What not to include in the SOW.

Many individuals, particularly suppliers, attempt to put items and sections into the SOW that do not belong in the SOW. Do not include contract terms and conditions in the SOW. Keep these in the contract. Do not give away rights in the SOW that you worked hard to obtain in the contract. Avoid changing legal terms in the SOW to ensure consistency with the contract. Only include items in the SOW that describe the work to be performed or the good that is being purchased.

Once a detailed SOW has been finalized, the sourcing process can begin. A structured sourcing process will bring the greatest value to the contracting effort; it will marry the technical knowledge brought to the table by the internal customer group to the purchasing knowledge possessed by supply management. While not every company's process is identical, a structured sourcing process will evoke a level of formality and credibility often missing from goods and services purchasing in the past.

One of the most time-consuming aspects of services sourcing can be the negotiation of agreement terms and conditions. Most companies have boilerplate T&Cs on the back of the purchase order that are sufficient for purchasing goods and materials. However, these same terms do not generally provide adequate protection when contracting for services. It is important to develop T&Cs that are fair and equitable to both your firm and the supplier; included should be indemnification protection for both parties, liability protection and defined levels of insurance protection. Note: Most supplier-issued contracts are designed to primarily protect the supplier; these boilerplates often limit liability and indemnification to very small amounts, if any. As a rule, it is best to never sign the supplier's proposal or agreement. Instead, provide your firm's terms and conditions upfront as a part of the initial sourcing process; in turn, this will save considerable time and effort during back-end negotiations of the final agreement.

Summary:

There are considerable benefits to be realized with supply management's involvement in the contracting for services. The savings opportunities are greater than ever before. To potential

suppliers, a company's decision to utilize supply management in the sourcing of services will command attention because it validates the company's commitment to professional procurement practices. A structured sourcing process and detailed SOW is a win-win combination that will enhance supplier performance and internal customer satisfaction, thus bringing greater savings and reduced expenses to a company's bottom line.

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