IT Sourcing Renewals:
Alternatives and Opportunities

INSIGHTS by LEXTA // Christoph Lüder

With the end of your services contract in sight - what are your alternatives and opportunities?

Expiring contracts offer both new opportunities and the chance to renegotiate with the existing service provider at a significantly lower cost than the traditional RfP process that you probably used on the first generation outsource. While best practice will suggest that you need a competitive landscape, renegotiating with your incumbent provider on a sole source basis **IS** a viable alternative to the resource-intensive, completely new tendering process.

In principle, there are three options for action. The result of all three variants should always be a modern, future-oriented contract and prices in line with the market.

It is not uncommon for the players involved to be caught by surprise by the impending end of an ongoing outsourcing contract. Too often buyers leave it too late in the contract before considering their options. It feels like you've been with the current service provider "forever", the exact contract details have long been forgotten, disappeared in the drawer and, in the worst case, there is no automatic reminder to the sourcing and governance specialists in good time.

In some cases, it will be the service provider who will remind you that the contractual basis will soon be coming to an end. If they mention in the same breath that it would be absolutely no problem to extend the contract period on the basis of the current conditions, then at least the purchasing department should pay attention. In some, but not all, cases such offers suggest that the terms may favor the provider. **IF** this is the case, a good buyer would certainly be able to negotiate better terms for the company.

The following is a look at possible options for action, how things can proceed without dealing too disruptively with the services concerned. Aristotle has a beacon from the lighthouse ready for the people involved: "We cannot change the wind, but we can set the sails differently."

Option 1: Contract extension with the existing service provider

Often there is an option to extend on the same terms in the contracts. These options can be for one or more years depending upon what was agreed at the time of negotiating the original terms.

If the service provision is generally right; a relationship built on trust determines the daily dealings; there are no fundamental change requests and internal guidelines support a contract extension, then this option is the one that provides the path of least resistance and least work. Depending on the design of the contract, this option can be used unilaterally, i.e. only by the customer, or the consent of both contractual partners is required.

What is important here is that certain deadlines usually must be observed - which in turn speaks in favor of a well-maintained deadline calendar in contract management. If the deadline has passed, the customer is dependent on the goodwill of the provider, which should be present in the scenario described above. This option is also useful to gain time, possibly because there are no resources available to go to market with a full request for quotation. The extension “buys” a further twelve to twenty four months for the client to consider and implement its long term plans.

However, a contract extension always has another side of the coin which potentially disadvantages the client. In most cases, the prices originally agreed a few years ago were at a different, significantly higher level than at the time the contract can be extended. It is therefore essential to check whether a price adjustment can be made, for example by performing a contract benchmark. A corresponding benchmark clause in the contract can ensure significant price changes here.

Even without the opportunity to run a full formal contract benchmark, where there is doubt, the prices can still be reviewed and validated via a short market price assessment. This can be conducted by a benchmark company or a sourcing consultancy which also has a benchmark database to establish any potential price adjustment.

Option 2: Renegotiate and restructure with the existing service provider

If there is a need to modernize or change the contract or the service content, but the relationship with the existing service provider is positive, there is an opportunity to restructure and renew without the need for competition. Here the basic intention is to enter a further contract period under refreshed, restructured arrangements via a process which is carried out exclusively with the existing service provider. Here, too, the general satisfaction with the services provided and performance levels should be in the foreground of the considerations if this process is to be adopted.

In the case of long-term contracts, the ravages of time can gnaw away at both the contractual framework and the service levels. Additionally, the time impact could be compounded by the current general geo-political situation from Brexit and the COVID-19 pandemic. These factors alone could mean that the content of the contract will need to be adjusted. In the run-up to the negotiations however, the objectives should be clearly formulated - from the maximum requirement to the minimum acceptable improvement. In addition to the goals, the negotiation strategy should also be coordinated in advance so that all protagonists are on the same page and speak with the same language. Furthermore, as part of a renegotiation with changed service content, the prices - unlike in the case of an extension on the same terms - can be recalculated and negotiated directly.

If there is little or no know-how in the company regarding the current standards of contracts, service definitions and performance levels, as well as the prices currently paid on the market for these services, it is advisable to consult specialists such as law firms specializing in IT law as well as IT sourcing and benchmark specialists. By leveraging these specialists the client can not only ensure it is taking advantage of the latest market trends and best practices but it can also be a key factor in overcoming the loss of leverage due to the sole source nature of the discussions.

It is important to understand that not all wishes can be fully enforced. There will also be demands on the part of the service providers to modernize the contracts and every service provider is keen to be able to offer their own standard without any restrictions. For this reason, reference is made again to the list of minimum and maximum requirements described above.

Option 3: Request for Proposal (RfP) - competitive tender

The third option is the most time and resource intensive and, as a result, the most expensive of all.

There can be many reasons for carrying out a RfP at the end of term, be it a broken relationship with the existing service provider, prices that are too high, new services that are not offered by the existing service provider, etc. Also, the internal governance requirements may dictate that at certain thresholds, the services and prices must be validated directly on the market through seeking alternative solutions and offers via a competitive process.

Setting aside any of the aforementioned reasons, a RfP always gives the opportunity to bring the service provision to a different level in a disruptive manner, for example from a move away from hosting in a traditional data center to providing the service from the cloud.

As already mentioned, consideration must be given to the fact that a lot of energy and resources must be invested in the careful preparation of the RfP documents. The evaluation and comparison of the offers that will need to be conducted due to a RfP do not just fall from the sky but must be handled in addition to day-to-day business. It is not easy for many companies to provide these resources. But without their own commitment, a RfP project is doomed to failure from the start.

Not to be forgotten here is the service provider situation. Here, too, resources for complex and high-quality tenders are scarce and preparation of these offers cost a significant amount of money. Therefore, more and more providers are starting to qualify these hard. They will analyze and evaluate the chances of success of an offer very intensively with one parameter here very likely the potential customer's "tendency to change". In extreme cases, it can happen that no other service provider besides the existing provider makes an offer at all.

As in the two other options before, know-how can of course be purchased by using a professional IT sourcing consultant, thus minimizing internal effort. An additional factor here is that investment in the use of external expertise by the client may encourage more service providers to enter the process. Typically, the presence of advisors is a factor in their qualification as the investment being made by the client shows intent and will help the providers believe it is a fair process with a real chance of change.

Ultimately however, it is the contracting company that consumes the purchased services, not the sourcing consultant. Therefore, the RfP documents must fit the company and the company will still need to invest in its own resources to ensure this. The standard never really fits no matter how good a start place it is. Of course, another advantage here must not be concealed - sourcing consultants know the market and can thus contribute to the success of the RfP project in a targeted manner. This also includes increasing the "motivation" of suitable candidates so that they can participate in the tender with an attractive offer.

Even if at the end of a RfP project the existing service provider has again secured the service provision for the coming years; they would have done so having faced the competition and have obviously convinced the client that they are still the best choice for them.

In summary, a modern, future-oriented contract with prices in line with the market can be achieved in different ways. Fatal are situations in which the chosen path fails - be it that the quality of the tender is poor or the sourcing process was badly implemented. Whatever process is chosen however, time pressure must be canceled and taken out of the equation.

In many cases, especially in times such as these where external factors like COVID-19 are having a huge impact on cost, there is a tendency to choose the most resource-efficient way possible, if the requirements and the environment permit.

Whatever your chosen path, it can and should be successful if you have invested in the right process and support to deliver on **YOUR** objectives. What may have worked for one of your competitors may not work for you. So it is imperative that you design a strategy, invest in, and follow a process that will deliver on your requirements. Do it right and success will follow.

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LEXTA
is a consultancy company with focus on strategic IT management and offices in Germany, the UK, Austria and Switzerland. Founded in 2003 as an IT benchmarking specialist, LEXTA's competencies since then have broadened and include sourcing advisory, cost optimisation and a range of other areas to support its clients managing their IT agile and efficiently.