



Procurement Contract Risk Management

An extensive and revealing study of procurement contract management practices, risks and controls.



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EXECUTIVE SUMMARY

Introduction

In partnership with APICS, Protiviti Inc. recently published two major surveys and whitepapers. One addressed the topic “understanding supply risk areas, solutions and plans”* while the other was titled “managing the risks of outsourcing”**. The findings from these papers, extensive additional research on related topics, and our risk consulting experience at our clients prompted us to carry out this focused and extensive study of procurement contracting and related contracts management practices and risks.

These are very big dollars and these are very big risks! The survey evidenced that about three-fifths of organizations spend from 30 percent to as much as 80 percent of their revenues on goods and services from third parties. Astonishingly, almost 20 percent of respondents spend more than 60 percent of annual revenues on third party goods and services. This further reinforced data from other surveys that suggested that very many organizations spend 50 percent or more of earned revenues with suppliers.

It would be reasonable to expect that board members, senior executives, and other business leaders and stakeholders demand that strategies, policies, processes, organizational skills, management and control mechanisms, and tools governing and supporting the management of contractual arrangements for this level of expenditure be effective and efficient. Also, those stakeholders would expect that the array and magnitude of inherent and significant risks, potential exposures and regulatory demands, and opportunities in these arrangements be managed and controlled effectively.

Our research reinforces the immediate need to quickly increase the focus and investment in procurement contracting and contract risk management capabilities at many organizations. These weaknesses were somewhat predictable in the areas of non-inventory/indirect procurement. By “indirect” we mean the purchases of products and services not planned/used directly in product manufacturing and distribution processes. However, there were also a very large number of organizations that reported unacceptable contracting capabilities in the “direct” procurement domain.

The above referenced 2004 survey and paper on “understanding supply chain risk areas, solutions and plans”* showed that 47 percent of respondents identified the organization’s inability to manage and control supplier and contract performance effectively as a major area of concern. Now, as you read through this latest whitepaper you will find that this study bears out and heightens those concerns. These issues are clearly quantified and qualified in the form of the **alarmingly high percentage of contract management capabilities at a maturity level of “less-than-satisfactory.”*****

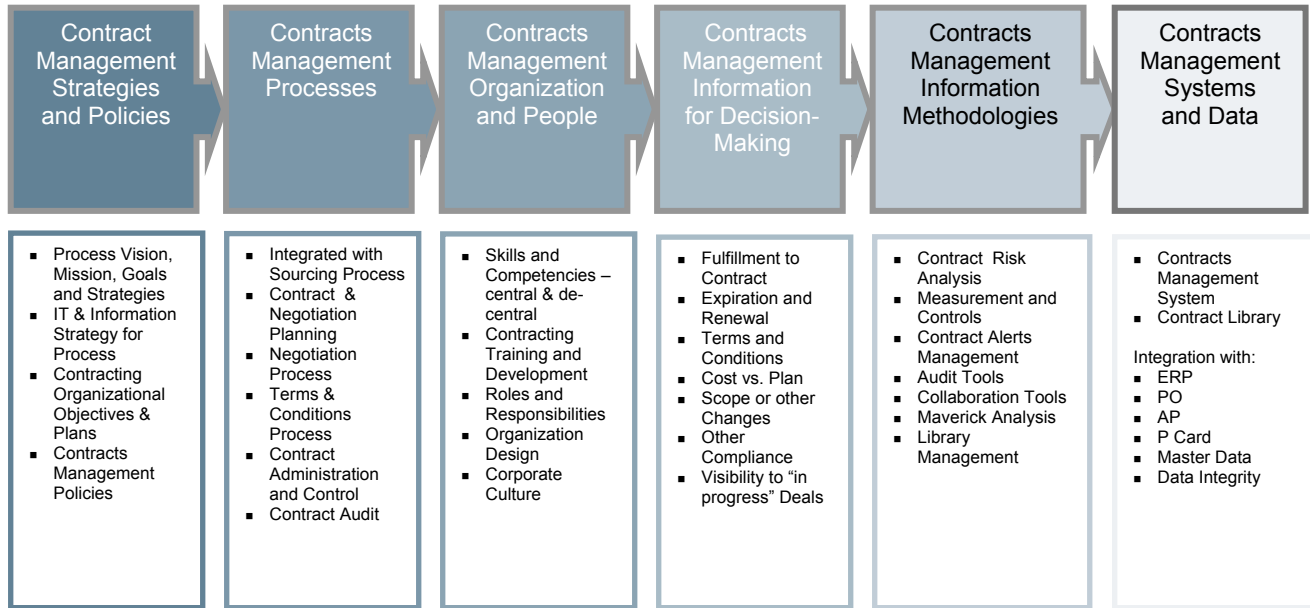
Key:

* Understanding Supply Chain Risk Areas, Solutions and Plans – A Five-Part Series

** Managing the Risks of Outsourcing – Current Practice Effectiveness

*** “Less than satisfactory” is defined as “initial” and/or “repeatable” in Protiviti Inc’s Contracts Management Capability Model – See also pages # 3, 30 and 31.

What are procurement contracts management process capabilities?



Process is at risk if ANY infrastructure component is deficient:



Contracting processes not designed to achieve strategy or comply with policies

Personnel are unable to perform necessary contracting activities & processes effectively

Reports do not provide information for effective management and control of contracts and risks

Contract Analysis methodologies do not adequately produce relevant information

Reliable, Relevant and Timely Business Data is not available for analysis and reporting

Table 1

Keys:

The procurement contracts management process includes all six inter-dependent elements of capability as depicted in Table 1 above (based on the concepts introduced in Carnegie-Mellon's Capability Maturity Model).

The survey was constructed in a way so as to evaluate each capability for two types of procurement - direct and indirect. Tables 2 and 3 provide a summarization of results for each of the two major categories of procurement, direct and indirect, by component of capability.

For the purpose of this report a procurement "contract" is defined as any legally binding procurement arrangement entered into on behalf of the organization. This can range from a very formal and structured contractual agreement document, to a hardcopy or electronic purchase order, to a binding verbal commitment, and so on.

Survey Results Overview

The following results highlight the percentage of respondents indicating procurement contracts management capabilities at a “less than satisfactory” or “ineffective” level for each major procurement category (direct or indirect).

“Less than satisfactory” is defined as either “initial” or “repeatable” in Protiviti Inc’s Contracts Management Process Capability Maturity Model.

Direct Procurement Contracts Management Results

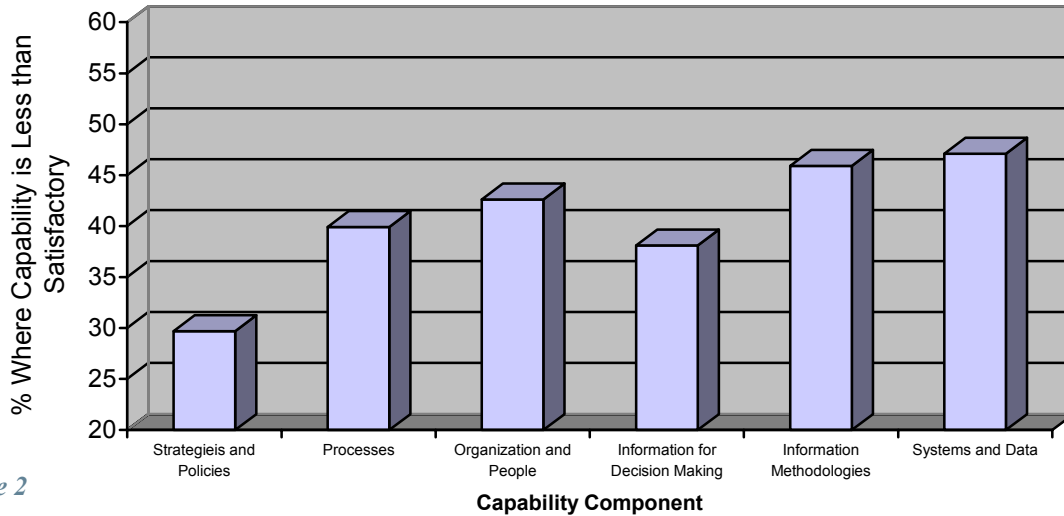


Table 2

Indirect Procurement Contracts Management Results

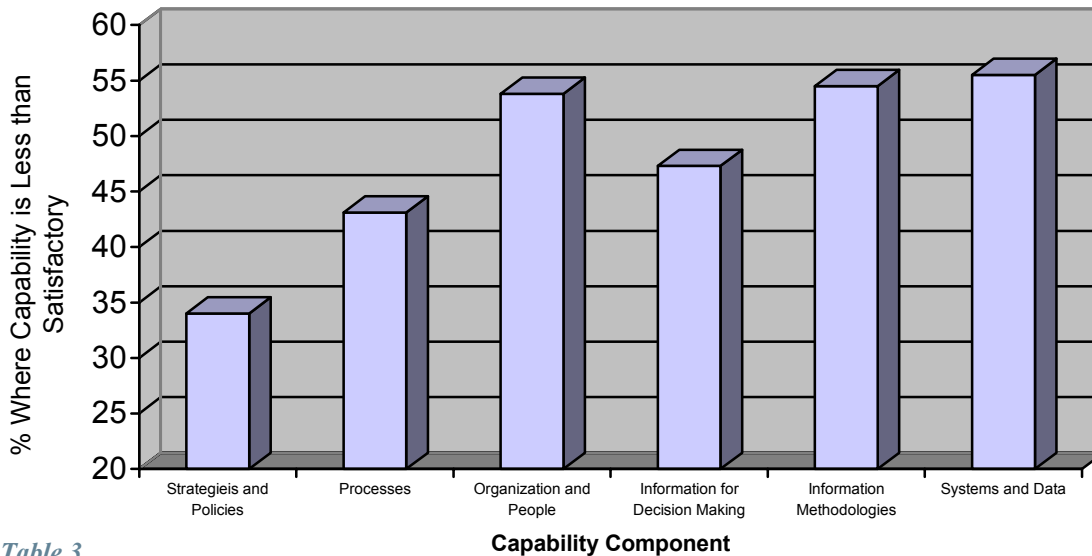


Table 3

Implications and Recommended Actions

The results of this survey highlights a wide range of very significant process and control weaknesses in the procurement contracts management for a large portion of responding companies. Given the level of expenditures involved, the impact on profitability, the potential “financial leakage” at stake, in addition to the host of other significant risks associated with the supply of goods and services (see examples on pages 9 and 10), the potential implications are very serious indeed.

Protiviti Inc. and APICS strongly urge senior management in all industries to act quickly and to consider taking the following steps:

1. Carry out an unbiased and comprehensive assessment of the current procurement contracts management processes and related capabilities (e.g. sourcing process), and then evaluate gaps between the current state and an agreed-upon desired level of capability and performance.
2. Identify immediate short-term actions to address urgent control improvement needs and put the necessary resources behind those short-term actions.
3. Set clear overall strategic and operational objectives and performance expectations for the organization’s procurement contracts management process. Without such a vision and objectives, it is unlikely that the desired level of performance, control and capability will be achieved.
4. Design, develop and implement strategies and detailed, integrated action plans to achieve the desired levels of performance and process maturity, actions that address each and all of the six components of contracts management capability, and cover the immediate, middle and longer term horizons (typically current to three years).
5. Identify the executive management support to make those improvements and include actions in the plan to achieve and maintain that executive-level support for the execution of the short-term as well as mid to longer-term improvement plans.
6. Make appropriate mid to longer-term investments in procurement contracts management process capabilities. These investments should be used to improve strategies, policies, practices, as well as the organizational tools and technological upgrades needed to achieve the targeted level of contracts management process performance and control.

To recap, beyond immediate remedial action, these overall action plans should include steps that address each component of procurement contracts management process capability, consistent with the following:

1. Develop and implement an overall contracts management vision, objectives, strategies and goals. Ensure that these align with enterprise strategies, objectives and expectations.
2. Develop, implement and enforce enterprise-wide contracting policies that reflect overall contracts management process strategy and objectives. Policies should be implemented in a time-phased manner in line with the organization’s ability to absorb and adhere to these directions.
3. Design and implement aligned contracts management practices, work flows and procedures for the process that will enable the achievement of the overall strategic vision and objectives. Standardize procedures.
4. Develop, source and deploy adequate numbers of resources with the appropriate level of skills and competencies, assign well-defined responsibilities and accountabilities, and ensure viable organizational alignment. Typically, these resources should be both central and de-central to effectively manage, execute and control the process and to achieve the strategic objectives.

5. Define information and reporting requirements comprehensively for contracts management. And, provide the support to meet those needs and to ensure that timely, complete and accurate information is consistently used for decision-making and reporting, so as to enable the organization to effectively execute, manage, monitor and control contracting processes and risks.
6. Identify and provide the tools and methodologies for the organization to extract and manipulate data from various systems so as to produce the required and defined measures, analyses, controls and reports to manage, control and monitor contracting expenditures, performance, risk and terms and conditions.
7. Define systems requirements to support the process objectives, and invest diligently in (a) the contracts management system technologies, workflows and necessary interfaces to transaction systems to store and manage contracts and (b) the integrity of procurement data within these systems.
8. Once processes and procedures are standardized, automate key controls, alerts, measures and reporting in support of effective and efficient post-award contracts management and administration.

Survey Process Background

We invited a targeted group of executives, managers and other professionals to respond to a wide range of questions relating to the maturity of the six inter-dependent areas of capability within the procurement contracts management processes at their organizations.

The six areas of procurement contracts management process capability assessed in the survey are:

- Strategic Plans and Policies for the process
- Process Design and Implementation
- Organization and Skills
- Information for Decision-Making and Control
- Methodologies and Tools (for analysis and reporting)
- Systems and Data

Respondents

About 95 percent of the survey recipients responded. A total of 95 responded to the “direct” purchases section only of the survey, while another 142 responded to both the “direct” and “indirect” sections. More than 35 percent of the respondents were from organizations with estimated revenues of over \$500 million annually.

Industry Representation

82 percent of respondents were from the manufacturing, high-tech, consumer products and distribution industries, while the balance was made up of organizations from telecom, media and hospitality, financial services, healthcare, energy and government or not-for-profit sectors.

Role in Organization

10 percent of the respondents fell into the “executive-level” category over 72 percent more were in other “management” levels. About two-thirds of the respondents stated that they had some ownership over procurement-type activities and/or functions.

Therefore, this could be considered to be a form of “self-assessment” by management of the sourcing and procurement communities on their contracting process capabilities, at least for about two thirds of the responding population. The other third represented a wide and diverse array of functions and perspectives.

Organization Model

Over 53 percent described their procurement environments as “centralized or largely centralized”. Just over 16 percent reported a ‘decentralized or largely decentralized’ environment with the remaining 30 percent or so reporting a very “mixed” organizational arrangement.

Survey Results by Capability

The results of the survey can be summarized for each of the six elements/components of contracts management process capability as follows (see also appendices A and B on pages 30 and 31):

1. Maturity of the Contracts Management Process “Strategy and Policy”:

Reported as less than satisfactory* for 30 percent of respondents in direct procurement, and for 34 percent in indirect procurement.

2. Maturity of the Contracts Management “Process/Practices Design and Implementation”:

Reported as less than satisfactory* for 40 percent of the respondents in direct procurement, and for more than 43 percent in indirect procurement.

3. Maturity of Contracts Management “Organization and Skills”:

Reported as less than satisfactory* for close to 43 percent in direct procurement, and for almost 54 percent in indirect procurement.

4. Maturity of Contracts Management “Information for Decision-Making” (performance and compliance reporting, analysis, measurement etc.):

Reported as less than satisfactory* for 38 percent of respondents in direct procurement, and for more than 47 percent in indirect procurement.

5. Maturity of Contracts Management “Methodologies and Tools” (for analyzing/reporting contract-related data)

Reported as less than satisfactory* for 46 percent in direct procurement, and for more than 54 percent in indirect procurement

6. Maturity of Contracts Management IT Systems and Data (Integrity) capabilities:

Reported as less than satisfactory* for 47 percent of direct procurement, and for more than 55 percent in indirect procurement.

Key:

* “Less than satisfactory” refers to the combination of the two lowest levels of process maturity; the “ad-hoc/initial” and “repeatable” levels of maturity. All five levels are defined in detail in Protiviti Inc’s “Procurement Contracts Management Process Capability Maturity Model.”

The “ad-hoc/initial” level is considered to be an out of control and chaotic business environment, whereas “repeatable” level is somewhat or minimally better, but is still rated as below the “acceptable” control effectiveness threshold from an operational risk management perspective (see also Contract Management Risks listing on pages 9 and 10).

In summary, a “less than satisfactory” rating is considered as below acceptable levels of risk control effectiveness in the process. We strongly urge all such organizations to put remediation actions plans in place to improve related risk management capabilities

DETAILED RESULTS AND GUIDANCE

Before reviewing the results in detail let us first revisit and reflect upon some of the many significant, inherent and controllable risks present in procurement arrangements. These risks become more and more apparent and challenging as pressure increases on management in all industries to deal with the need to manage:

- Total costs and profitability
- Complexities of outsourcing and global sourcing deals
- Demands for higher levels of customer service and satisfaction
- Growing regulatory and environmental requirements

Procurement contracts management risks

Procurement contracts management risks include:

- **End-customer satisfaction** risk; the contract is not effectively managed, resulting in poor supplier performance to contract; this affects end-customers and internal users and undermines the company's credibility and predictability.
- **Authority limit** risk; this also includes the common issue of where employees or even contractors act as purchasing agents without the proper authority and/or qualifications, thereby putting the company at risk from bad deals and lower profits. Studies by Protiviti and others show that organizations typically overpay by between 15 percent and 20 percent and more for unauthorized or "maverick" purchases.
- **Regulatory non-compliance** risk; the contract is not well-designed and/or managed and results in fines, reputation damage, lost customers and so on due to supplier-related activities. *See also general and specific industry regulations and guidelines governing and regulating aspects of third party contracts management including the Sarbanes-Oxley Act , FASB, HIPPA, FFIEC, OCC, etc.*
- **Information security, access and privacy** risk; closely linked to regulatory non-compliance risk in many areas (healthcare and financial services, for example), includes unauthorized access to company, supplier, or customer information, and can lead to serious consequences for parties in the agreement.
- **Terms and Conditions** risk; poorly designed and negotiated contracts fail to address key components such as indemnification, product ownership, payment terms, termination, pricing, rights, warranty, obligations, general and specific risk assignment etc., leading to disputes and potentially significant losses or costs.
- **Reputation** risk: bad press and a tarnished corporate image as a direct result of supplier actions or non compliance, or from sourcing and contracting failures such as the absence of contracts with minority, women, or locally-owned suppliers, etc.
- **Environment, health and safety** risk; caused by (a) a lack of clarity in the contract or (b) non compliance; may result in breaches of laws and regulations.
- **Inventory and obsolescence** risk; as a result of or aggravated by poor contract design, the inability to manage the contract, or poor performance versus the contractual intent.
- **Off-balance-sheet inventory liability** risk; in cases where products are outsourced to contract manufacturers and where there may be a level of liability and SOX reporting requirements.

- **Automatic Renewals** risk; unwanted products or services are committed to and purchased automatically due to an absence of effective contracts management and controls.
- **Contractual and Legal (general)** risk; can result in costly legal disputes, the inability to achieve a remedy after supplier failures, or a lack of protection for the company etc.
- **Employee/third party fraud** risk; leads to a loss of cash, poor press or general reputation damage.
- **Outsourcing** risk; the service or product is outsourced, *but the risk cannot be*. Lack of risk management can lead to loss of control over data security, personnel, process performance, outcomes, total cost, delivery performance and so on.
- **Efficiency** risk; the process takes too long, or entails too much bureaucracy, and/or leads people to circumvent the process with serious consequences including legal risks and financial loss.

Capability #1: Strategy and Policy

What is this capability?

A) Contracts Management Process Strategy; this includes a defined set of *process* goals and objectives, a vision and a mission, and related strategies and action plans designed to achieve those objectives for the process. The strategy should span short, mid, and long term horizon.

The strategic plan should include the activities/actions as laid out to design and implement specifically targeted process and risk management capabilities, organizational capabilities, information for decision-making capabilities, information and control-related methodology capabilities (the means to get the information), and supporting IT system strategies and investments, along with associated data integrity standards to meet the strategic objectives for the contracts management process.

B) Contracts Management Process Policies; these are the policies that need to be designed so as to be 1) truly “executable” and 2) to enable and support the implementation of the contracts management process strategic objectives. The policies need to evolve and mature as the process evolves and matures. The key is that these policies are seen as “enablers” for the organization’s procurement contracting process strategic objectives and plans.

Capability #1a. Contracts Management Process: Strategy

By all accounts, it is much more difficult for an organization to reach a high-level of process performance and process capability without a clear vision, objectives, targets and supporting plans and investments to develop and mature that process. That logic applies for any key process. Similarly it is essential that the vision, objectives, and targets for desired process performance be enabled by a comprehensive and integrated set of short, mid and long-range detailed action plans to achieve the desired goals and improvements.

This is especially critical in the case of *strategically relevant processes* such as sourcing and contracting. These processes are rich in both risk *and* opportunity. In our recent survey of “supply chain risk areas, solutions and plans” we found that developing *an overall strategic plan for the process was rated as the “number one” most important risk mitigation solution available to the respondents.*

And yet again, this contracting study evidences that many organizations do not have a satisfactory strategic plan for contracting process capabilities, including as many as 40 percent of this replying for “direct procurement.”

Additionally, our experience in the market evidences that where a strategic plan has been created for the contracts management process, these documents are more often than not one-time, or once-off events. They are generally not comprehensive or long-term, and are often outdated.

In order to develop a strategic plan for the contracting process one must understand the overall objectives and strategies of the organization, as well as examine overall supply chain/procurement objectives and strategies, wherever these exist. Then, with input and buy-in from executives and other key stakeholders, a succinct vision, objectives and a set of matching targets should be created for the contracting process and contract process capabilities. These *must* also reflect the higher-level business objectives and strategies.

Once objectives for the process are defined at a high level, they must be translated into defined characteristics and goals for each of the six elements of contracts management capability, guided by a procurement contract management capability maturity framework. At the same time, it is advisable to assess the “as-is” state for each element of capability. The use of a procurement contract management capability maturity model is highly recommended for defining both the “as-is” state as well as the “to-be” or targeted level of performance and maturity.

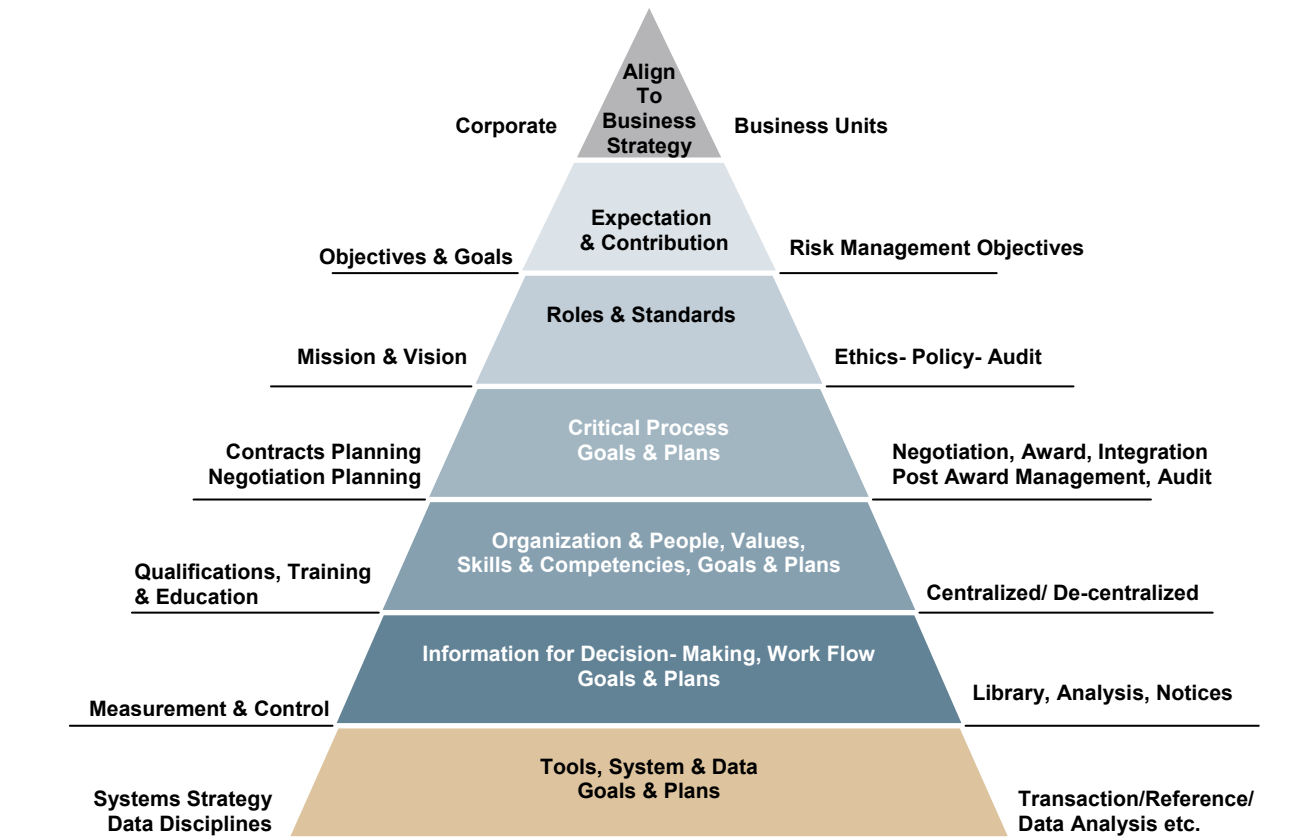


Table 4: The Contracts Management Strategy Pyramid.

Time-phased action plans can then be developed to drive the improvements across each element of procurement contracts management capability, in logical steps and time frames (months and years) from the current to the desired level. Having a vision and objectives, combined with an understanding of the “as-is” and “to-be” for each element of procurement contracts management allows the organization to prioritize the approach to improving and then effectively managing and controlling procurement contracts management processes and risks.

Organizations generally have an understanding of the major risks, opportunities and complexities inherent and common in both current and future contractual arrangements with suppliers of goods and services. The value and importance of developing and maintaining a strategic approach to the design, development and performance of the all elements in such a critical process as contracts management cannot be overstated.

This objectives-driven approach helps cross-functional management to reach a consensus on a set of expectations and goals for the process. It facilitates the implementation of a set of integrated short-, mid- and long-term actions and plans, as well as the prudent and timely investments required to achieve the desired level of performance and return over time.

The use of high-level procurement contracts management capability maturity models allows management to get an excellent overview of the current maturity levels for each of the six capability elements of the process, and to reach an agreement and cross-functional consensus around the desired and expected levels of process maturity and performance.

Once time-phased and resourced strategic action plans are identified to make the transition from “as-is” to the “desired” level, these plans should be presented to and agreed-upon by senior management, thus enabling a consensus-driven and disciplined set of activities and investments to achieve short, mid and longer-term risk and opportunity management goals and plans for the process.

Capability #1b. Contracts Management Process: Policies

Similarly, it is vital that a set of aligned, current and executable policies are documented and implemented by management to help ensure that whatever strategic objectives, targets, plans and expectations in place for the process are supported, and so that overall procurement and contracting risk management and control objectives are achieved.

A primary purpose of contract management policies should be to help reflect and enable management’s overall policies and standards for the business, as well as the strategic intent and objectives of the specific process, in this case the procurement contract management process.

As with all policies, contracts management policies must be current, they must reflect the way things are and can be done today, and mirror the current capabilities of the process and organization. It is unproductive to enforce policies that cannot be followed because some critical elements of process, or skill, or organizational design, or information for decision-making, or information methodologies and tools or systems and data are not in place, or not yet at the desired level of maturity. Policies of that nature are often ignored. Credibility for that policy can be lost (and possibly the credibility of other related policies, both current and future). Policies should be designed and implemented in line with the organization’s capabilities to implement and comply.

Forty-three percent of respondents in direct procurement and almost 51 percent in indirect procurement reported that policy design and implementation were “less than satisfactory.”

There can be several sources for this weakness. Firstly, and in all probability, there is no clear strategic vision and plan for the overall process to help drive and guide the design and implementation of contracting policies or other process capabilities. Secondly, many policies are written once, and never updated – they do not reflect the current practices, capabilities and standards.

Additionally, policies may be written with “a particular vision in mind,” absent any possibility of successful implementation due to the immaturity of the current contracting capabilities. Intent may be good but execution is not possible. Just like with engineering changes and the phase-in and phase-out of products, time-phased design and implementation of key policies is an essential for success. Training and awareness is another key factor in policy implementation. And it is essential that management require compliance with policies. Businesses are loaded with failed policy “guidelines.”

Contracts Management Process Policy should reflect and cover all key aspects of the contracting process, including expectations for the use of standard terms and conditions, contract planning, negotiation planning and negotiation, contract finalization, and post-award contract administration and risk management, measurement, and control. Aligned processes, practices and procedures should be in place to reflect these policies, and to document the process steps and controls.

Contracts Management Strategy and Policy Capability Summary

The contracts management process strategic plan provides the vision, objectives and plans for the process as a whole. It also drives the improvement of all elements of process capability. The plan provides the overall guidance and direction for the design or redesign and implementation of realistic, pervasive and effective contracts management policies with all of the above considerations in mind.

Contracts management policies should represent management’s direction, expectations and intent as to how the organization will develop, manage and control supplier arrangements and the major contract expenditures, risks and regulatory requirements that must be addressed, managed, monitored and controlled throughout the organization.

Other contracts management process capabilities should be clearly aligned with and support the contracting process strategic objectives and contracts management policies.

Capability #2: Processes, Practices and Procedures

What is this capability?

This process capability refers to contracting process steps, practices and work-flows and supporting procedures. These guide and enable the organization to effectively and efficiently achieve the strategic goals for contracting and contracts management in adherence with contracting policies. The process includes such activities as:

- Terms and conditions library management process
- Defining contract needs
- Creating the contracting team (complexity-driven),
- Contract planning and contract selection
- Negotiation planning and contract targeting
- Negotiation and award of contracts
- Contract execution, administration and control (a major and continuous step).

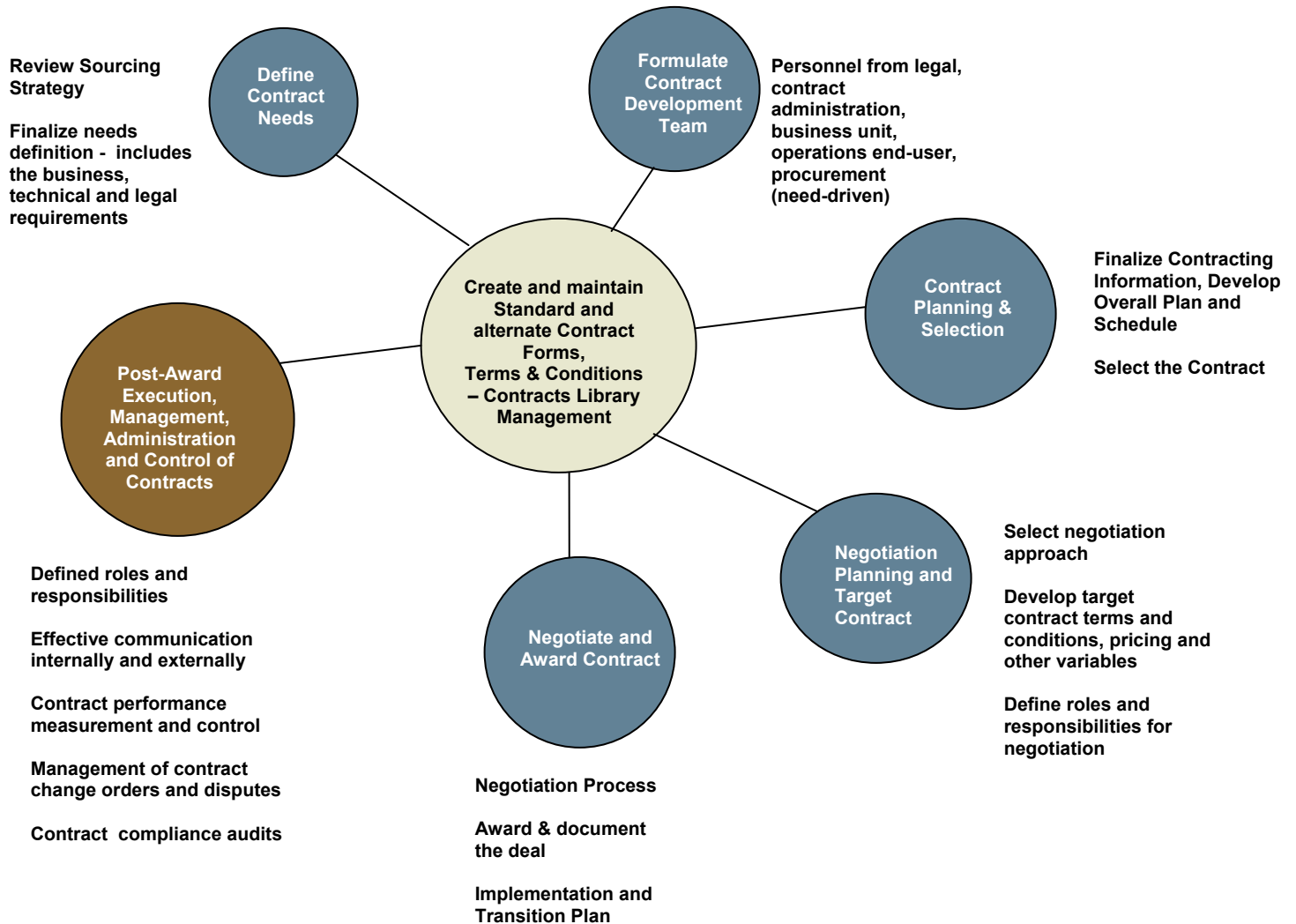


Table 5 - Key Process Risk and Control Areas for Effective Contracts Management

The contracts management survey focused on the following selected steps of process capability maturity (capability #2) for procurement contracts management:

1. Terms and Conditions Management

This proved to be an area of weaknesses for both procurement sectors with more than 32 percent for direct, and more than 37 percent for indirect reporting “less than satisfactory” capability. The design and management of mandatory, optional and alternate terms and conditions clauses and boilerplates for various types of products and services are foundations for contracts risk management. Contracting should NOT entail the reinvention of terms and conditions each and every time a purchase is to occur. Standard, legally-approved terms and conditions provide the organization with significant protection and risk control while greatly speeding up routine contracting activities.

We recognize that certain contractual terms and conditions will need to be negotiated for products and services that are not pure “commodities” by nature. The need for negotiation flexibility and variance from standard will depend on issues such as the nature of the purchase, the sourcing strategy itself and the relative power of the supplier versus the buyer. Certainly it is very unwise to ignore these factors. Even in these instances, standard alternative terms and conditions should be developed to reduce the risks in the process and to speed up negotiations for the good of all parties.

2. Contract Planning and Negotiation Planning:

The survey shows that **almost 40 percent of respondents for direct purchasing and more than 43 percent for indirect purchasing** described their overall contracts management process design as “less than satisfactory.” Within these overall ratings further analysis evidenced that the planning aspects, contract planning and negotiation planning, both better practices, were “less than satisfactory” for **almost 45 percent and almost 54 percent of direct and indirect procurement, respectively.**

Once product or services requirements, scope, quality, quantity and so forth have been finalized, the contract planning sub-process and discipline will help cause the organization to put an overall plan and project schedule in place for the rest of the contracting process, right through to post-award management and administration. Tasks included in the plan are:

- Any finalization of contract requirements and scope
- Contract negotiation planning
- Contract negotiation and collaboration
- Contract award
- Post-award communication with any other competing suppliers
- Finalization of the post-award contract management and administration plan

These steps should be augmented by a post mortem to help ensure that all key aspects have been covered and that the company’s objectives and contracts management and control requirements have been met.

The contract plan and schedule should then be communicated to all key parties. The team should select the most appropriate contract boilerplate to work from based on the clearly defined product/service requirements. This boilerplate should reflect the defined sourcing strategy for the product/service. The sourcing strategy is typically based on business requirements, a market analysis, the procurement risk and impact analysis, and the desired business relationship with the supplier(s) that makes most sense for the organization.

After the initial contract planning step has been carried out negotiation planning normally occurs. At this point the roles and responsibilities of the negotiation team are clearly agreed, including that of lead negotiator and of all others who will be involved. When developing a negotiation plan the organization should be expected to clearly define contractual objectives such as:

- Price and cost scenarios (for internal use)
- Requirements and scope (conveyed to the supplier)
- The terms and conditions that will govern performance (internal and supplier)
- The desired level of confidence in the supplier's ability to deliver (internal)
- Any key exceptions by the supplier when they responded to the RFI/RFP/RFQ
- Contract performance and management expectations of the supplier and vice versa (internal and supplier)

A negotiation plan should leverage all key analyses that occurred during the development of a sourcing strategy for the particular product or service in question. This would normally include:

- The market analysis and the risk and impact analysis
- The documented sourcing strategy that resulted from the market and risk and impact analyses.
- A record of the RFI/RFP/RFQ process (where appropriate)
- Analysis of proposals or bids received and supplier selection rationale
- Detailed analysis of the requirements, scope, price, schedule, quality, etc.

The team should review each element of the negotiation, understand “give and take” scenarios, roles and responsibilities, negotiation tactics, and so on. Negotiation planning, like contract planning, is an excellent practice and discipline and helps position the organization to clearly define objectives, and to then achieve those objectives.

The fact that 45 percent of direct and 54 percent of indirect respondents described their planning activities as “less than satisfactory” for contracting should be a cause for alarm.

3. Post-Award Management and Control of Contracts

From our viewpoint among the *most concerning of all findings* was the level of immaturity in the entire area of post-award contracts management, control and administration, arguably the highest risk area within contracting for most organizations. These post-award contract management activities are intended to help the organization to ensure and to control performance, scope, quality, costs, service, terms and conditions compliance, and compliance with a range of other key aspects of agreements, including those relating to regulatory and environmental concerns.

The survey results tell us that **almost 47 percent of direct procurement respondents and an amazing 58 percent of those in indirect procurement** identified this whole area as “less than satisfactory.” Indeed, the **lowest of all possible levels of maturity (ad-hoc) was recorded for more than 23 percent in direct and almost 31 percent in indirect** purchasing. This is a major area of risk and opportunity for organizations. Senior executive teams and boards of directors should be highly concerned.

Contract management structures and responsibilities must be in place to effectively measure, monitor, manage and control the supplier/contract performance, as well as the supplier relationship throughout the life of the contract. Contract administration and control includes actions, either by the purchaser or supplier (the parties to the contract), from the time the contract is awarded until such time as the deal is formally closed. This can entail a wide variety of people, functions and activities in many agreements.

Post-award contracts management and control involve ensuring that the intent, requirements, terms and conditions of the contract are all met, continuously. No matter how effective the planning and negotiation, if post-award activities, roles, expectations, measures, reporting and controls are not clearly defined and managed, the negative outcomes can range from quite significant to extremely serious. (The post-award aspect of the process also usually includes important follow-up activities, day-to-day expediting and various levels of supplier management functions).

Additional process problems were highlighted in the data. The procedures to continuously evaluate and assess current, open contracts were **“less than satisfactory” for more than 54 percent and more than 65 percent of direct and indirect procurement respondents, respectively.**

This is further aggravated by a lack of effective post-award contract auditing for higher-risk contracts. **Auditing procedures were below-par for more than 43 percent in the direct procurement area and for more than 56 percent in indirect procurement.** These factors have the potential to create severe problems at a very high number of these organizations.

4. Contract Process Efficiency

The survey showed that there was the perception by users and stakeholders that the contracts management process is often cumbersome and very inefficient. **Thirty-seven percent of respondents involved in direct procurement and 50 percent of stakeholders involved in indirect purchasing** view the contracts management process as being below acceptable levels of efficiency.

Inefficient or cumbersome processes and procedures typically lead to circumvention of the formal process. This more often than not encourages “maverick” purchasing, where people make deals without the protection of formal contracting policies and procedures, leading in turn to higher risk in all of these deals and significant “financial leakage.”

Contracts Management Process Capability Summary

The picture that has emerged for contracts management process effectiveness, control and efficiency is not good, particularly as it applies to indirect procurement activities. However, very significant weaknesses also emerged in the area of direct procurement. These risks and weaknesses ranged from a lack of terms and conditions management and control, to process inefficiency, to an absence of contracting and negotiation planning, and lack of critical post-award contract management and control procedures.

Where fundamental contracting processes, practices and procedures (capability #2) are not in place or ingrained at all levels and in all functions, it is very difficult for any organization to achieve important strategic objectives for contracts management and control, or to expect adherence to well-intended policies for contracting and post-award contracts and supplier management.

Formal procedures should be documented to reflect contracts management policies, process design and workflows. This is a very important discipline, but the current study and previous studies reveal ongoing and serious inadequacies in procedure-writing and procedure maintenance for procurement contracting. Risk abounds as a result. Non compliance with policy is also likely to be more widespread in these organizations, and at the very least, substantial money is being lost.

As previously outlined, there are six areas of inter-related capability in the contracts management process. No one capability stands alone. Weaknesses are other areas of contracts management capability identified in this report also have a direct or indirect negative effect on “process” performance.

These weaknesses are discussed from the results of the survey in the other capabilities (capability #1 strategy and policy, capability #3 organization and skills, capability #4 information for decision-making and control, capability #5 methodologies and tools for producing and analyzing this information, and in capability #6, the contracts system and data underpinning the methodology and processes). Cross-capability improvements ultimately define the success and maturity of the process.

Capability #3: Organization and People

What is this capability?

This process capability refers to all organizational and people aspects that apply to the procurement contracts management process. The maturity level of organizational and people capability will have a significant influence on the successful execution of contracts management process objectives, strategies and policies. The successful execution of a well-designed contracts management process and procedures depends heavily upon the strength, qualifications and skills, and commitment of the organization. Contracts management organization and people capability elements include:

- Contracts Management Organizational Structure; centralized, decentralized, mixed model
- Contracts Management Process Roles and Responsibilities; centralized, decentralized, mixed model
- Contracts Management Skills, Qualifications and Competencies
- Contracts Management Training and Education
- Corporate Culture; as it applies to contracts management process strategies, policies, disciplines and controls.

The contracts management survey focused on the following steps of contracting “organization and people” capability maturity.

1. Skills and qualifications for contracting and contracts management.

A variety of skills, competencies and qualifications are required for all those involved in the various stages of the contracts management process, and through the lifecycle of a contractual arrangement. These skills and qualifications range from project planning and project management, to negotiation planning, to contract negotiation, and to contract management and controls skills and competencies.

Whereas roles and responsibilities in the contracting process must be clearly defined, it is also important that *skills and competencies be matched to meet those roles, responsibilities and expectations.*

For post-award contract management, administration and control, the skills and qualifications can be very different from those required in the strategic sourcing, planning, selection and negotiation phases. Post-award management and control skills may also vary from one type of contract to another or from one type of product or service to another.

These competencies include the ability to review and approve receipt of materials, review and approve work or milestone completions, deal with change orders, analyze performance, measure and report performance, manage performance issues, audit for compliance, escalate problems for resolution and so on.

We asked if appropriate skills and qualifications are defined and required for personnel throughout the contracting process, including for personnel holding these responsibilities within as well as outside of the procurement function.

The survey results showed that skills and qualifications were “less than satisfactory” **one-third of the time in the area of direct procurements, another revealing statistic. On the indirect procurement side the number expressing dissatisfaction rose to almost 47 percent.**

This says that in almost half of the cases the personnel asked to play key roles in the procurement contracts management process have “less than satisfactory” skills and qualifications to plan, negotiate and/or manage and control contracts for “indirect” goods and services.

2. Training and education for procurement contracts management.

Training and education are important enablers when attempting to bridge these skill, competency and qualification gaps. We asked the survey respondents to evaluate the quality, availability, and implementation of training and education programs for all those personnel involved in key contract planning, development, negotiation and contracts management activities. The answers were not encouraging.

For direct procurement contracting, more than 62 percent of the respondents said that training and education were “less than satisfactory.” That figure rose to an unnerving 70 percent for those involved in the contracting and contracts management of indirect goods and services.

So, not only are there significant gaps in skills and competencies to plan, negotiate and manage procurement contracts, but there is a serious lack of investment in training and education to improve the capabilities of the people to do this work effectively and efficiently.

All roles should also be clearly defined for contracts management. Contract planning and negotiation roles, responsibilities and related skills, qualifications, and experiences should be clearly documented. Personnel who play those roles should always have qualifications and skills to carry out the task and be provided with development and training opportunities wherever there is a gap (see sample skills and qualifications matrix – table 5).

These expectations should apply whether it is for direct or indirect purchases, and whether the position resides in an official “procurement” function or in an end-user or “decentralized” function.

Position Title: Snr. Services Contracts Specialist	Developmental Tools
Qualifications (goal): ✓ 4-year degree – specialty area ✓ XXX Certification ✓ Negotiation Classes 1-3 ✓ Legal Aspects #1-5	Development path: ✓ Local colleges- business studies (nights/weekends) ✓ XXX institute various programs ✓ XXX institute modules 1-5
Skills: ✓ Excellent oral and written communication skills ✓ Influencing Level 3	✓ YYY Institute advanced class- presentation skills ✓ In-House Class 314
Experience: ✓ Minimum 5 years in procurement & contracting ✓ ✓	✓ Management openings in complementary disciplines (cross-training) ✓

Table 6 – Sample Skills and Qualifications Matrix

Similarly post-award contract roles, responsibilities, skills and qualifications need to be effectively defined and assigned. The complexity and nature of the contract and product or service being acquired will often

drive very specific requirements. Therefore, post-award contract management, administration and control roles should be clearly defined and carefully resourced for significant arrangements. There is evidence of increased risk in indirect procurements of various services, projects, outsourced providers and the like.

The post-award contracts management, administration and control process may have a complex set of roles and relationships requiring differing sets of responsibilities, skills and qualifications to manage relationships, risk and performance. What follows is a sample list of post-award contract management and control roles for a project or service contract, in a mixed centralized/decentralized procurement model:

- Contract administrator: Responsible for the day-to-day management of the contract (may or may not be a “procurement” function individual).
- Quality administrator: Required to verify quality and completion of services, etc., as needed.
- Procurement professional: generally manages the overall supplier relationship and deals with disputes, changes, etc. There may be multiple contracts with the same supplier.
- End users: Internal customers may be involved in approval of receipt of product, services, etc.
- Lawyer: Responsible for dealing with legal matters, as they arise.
- Financial analyst: Provides support as needed.
- Supplier:: Selects and communicates all key names, roles, and responsibilities for day-to-day, overall contract and executive-level relationships (as appropriate to the contract/relationship).
- Subcontractors: The contract is with the supplier and should have specific clauses governing the use of subcontractors. Remember, the buyer’s contract and relationship is with the supplier.
- Buyer’s executive: In the case of significant deals and “alliances” this can be a formal executive position dealing with strategic issues.
- Accounts Payable: Responsible for controls over supplier payments.
- Others: As defined on a contract by contract basis.

3. Organizational Culture for contracts management discipline.

Organizational culture is important if procurement agreements are to be effectively planned, negotiated, managed and controlled across all third-party expenditures. As with most corporate culture issues, the maturity of this capability is heavily influenced by the “tone at the top.”

With a growing focus on corporate governance and control, continued economic pressure, as well as factors such as ongoing dependency on the outsourcing of services and goods, including global sourcing, it can be expected that top-down directives will become more common in an effort to both promote and ensure that contracts management disciplines and controls are effective and pervasive.

However, this survey showed that as many as **43 percent of respondents reported “less than satisfactory” corporate cultural support for disciplined contracts management in - the area of direct procurement.** Again, this is a fairly surprising result for what is considered a more disciplined sector of procurement (inventory purchasing etc.).

The findings were less of a surprise on the **indirect procurement side: 58 percent reported that a less than satisfactory corporate culture and disciplines existed for management and compliance of indirect procurement contracting.**

4. Influence of the procurement function on sourcing and contracting decisions.

This area of the survey was designed to help analyze sourcing and contracting into further subsets in order to understand where procurement professionals have more or less influence on the processes for analysis, selection, negotiation and control of suppliers and contracts. The overall assumption is that the contracting process is more likely to be disciplined and controlled where procurement professionals bring their processes, qualifications, skills and influence to bear.

As with any profession, it seemed reasonable to expect that a more professional job will be done and more appropriate control will exist where the process is managed and influenced by professionals with the appropriate level of skills, expertise and qualifications. It is also recognized that the importance of end-user/internal customer satisfaction and service and the involvement and direction from end-users must never be understated.

This section of the survey was broken into four areas and the following represents grading of “**less than satisfactory**” as it applied to “influence of procurement professionals” by expenditure category:

High Cost/Risk Inventory or Materials Procurement; **12 percent**

High Cost/Risk Services Procurement: **29 percent**

Capital Equipment Procurement: **35 percent**

Low Cost/Risk Goods and Services Procurement: **32 percent**

On face value, at least, results are less concerning than those relating to many other aspects of contracts management capabilities. It seems that most of the time organizations are successful ensuring that the right people are influencing the most important contracting decisions. For high cost/risk inventory and materials purchasing the right people are involved 88 percent of the time. For all other categories the involvement ranges from 65 percent of the time to 71 percent.

On the face of it at least, these results seem to be somewhat at odds with other results of the survey. With such a relatively high degree of influence by the procurement professionals on the key categories, one might have expected somewhat better results in the previously discussed process and organizational areas. Read on for more insight.

Contracts Management Organization and Skills Capability Summary

The above data quantifying the significant influence of procurement professionals on contracting decisions is heartening – at least on the face of it. Be warned however, that one bad deal can get an organization into big trouble. Add to that the distressing level of dissatisfaction with the skills, qualifications as well as training and development of procuring personnel, central and/or de-central.

The right people (by role and title) may be involved in the process. But if those personnel have inappropriate levels of training, skill or expertise, the organization will most likely suffer from ineffective management of procurement contract risks and opportunities.

Additionally, if appropriate process and control capabilities are not in place, the level of risk and lost opportunity rises further for many procurement contractual relationships. The survey showed that about half of all contracts management processes were rated as being “less than satisfactory” (see capability #2).

As you will see, with significant issues relating to “information for decision-making and control” in contracting, and in the systems, data and methodologies to provide this information, the work and effectiveness of those responsible for all aspects of the contracting process is compromised. This will be covered in more depth in the review of the next three areas of contracts management process capability.

Capability #4: Contracts Management Process: Information for Decision-Making

What is this capability?

This process capability refers to all information required and available to manage, control and measure performance and to make informed and wise decisions in the procurement contracts management process. **Organizations rely on the availability of timely, relevant and complete information in order to effectively and efficiently manage, execute and control the procurement contracting process.**

Contracts management “information for decision-making” includes but is not limited to the following components:

- Performance reporting and measures
- Contract compliance
- Regulatory compliance
- Risk profiles
- Financial and other profile information for suppliers
- Pricing
- Expenditures
- Schedules of payment
- Scopes
- Deliverables
- Approvals
- Dates
- Milestone tracking
- Due-date notices
- Process measures and cycle time
- Renewal and expiration
- Threshold notices
- Other notices (proactive, reactive)
- Work-in-progress contracts
- Terms and conditions
- Amendments
- Contract contacts and roles and responsibilities
- And so on.

Contracts management information is among the key inputs to strategic sourcing, outsourcing, commodity management and supplier selection and supplier management processes. The information made available from the contracting process also supports purchasing execution, including invoice payment and reconciliation.

Overall, this proved to be another area of concern and weakness for many organizations. As indicated in the “results summary” of this report, **more than 38 percent and 47 percent of respondents identified this as a “less than satisfactory” capability for direct and indirect procurement**, respectively. The following are some of the specific questions-areas relating to this topic that help to identify key concerns.

1. Is key information readily available to track compliance with contract pricing, supply or service performance, regulatory requirements and other terms and conditions?

Consider the importance of this capability. This is a primary preventative and detective control mechanism for contracts management. It is a means by which management ensures that the product and service supply expectations of the organization are met in compliance with the standards, pricing, terms and conditions agreed upon. It is an essential set of procedures and reports to help management mitigate procurement and contractual risks.

And yet **almost 41 percent of respondents in direct procurement and nearly 56 percent in indirect procurement** reported this as an area of unacceptable capability. This is a serious lack of primary control mechanisms on a process that is full of both risk and opportunity and representing expenditures of anywhere from 30 to 80 percent of an organization’s revenue.

2. Is key information readily available to monitor, evaluate, and manage overall contract and supplier performance over the life of the contract?

This question is similar to question 1, but even more specific. It is focused on the ability to manage the contract performance over the complete life cycle of the deal, from the initiation of the original contract plan through the end of life of the contract. More than 37 percent of respondents in direct procurement and close to 50 percent in indirect procurement rated this as “less than satisfactory.” An organization will have severe difficulty trying to effectively manage and control contract performance without adequate information over the life-cycle of the deal.

3. Is information readily available to manage key milestones and contract expiration dates?

Tracking key milestones in a project or in a contract for product, as well as related deliverables and performance is a key control for many contractual arrangements. Likewise, it is very important to be able to foresee and manage other key dates such as “expirations” so that the contractual arrangement can be revisited, closed or updated. In the survey **36 percent and 48 percent respectively rated this basic capability as “less than satisfactory” for direct and indirect procurement**, exposing another significant contract management and control weakness.

4. Is information readily available to enable ongoing and formal risk assessment of the contract population?

From the contract risk examples listed at the beginning of the detailed section of this report, it is apparent that there is a formidable universe of risks surrounding the procurement of products and services. This question addresses management’s ability to consistently and continuously monitor and reevaluate risk profiles and contract risks across their population of agreements with suppliers. Without such risk assessment capability the organization may be “running blind” as to the evolving nature and significance of contractual risks and associated risk management controls.

Additionally, supplier profiles often change with economic circumstances or with mergers and acquisitions. The survey results show that **more than 44 percent of reporting organizations listed this as a “less than satisfactory” area of capability for direct procurement contracting. This was also the case for more than 58 percent of respondents in the area of indirect procurement contracts.**

5. Is information readily available to enable effective and efficient contract planning and collaboration across various parties/stakeholders?

Given the continued growth in outsourcing and in the number and complexity of contracts, it is important for organizations to be able to communicate and collaborate efficiently and effectively internally and externally when planning and executing contractual arrangements. This is a matter of necessity for many organizations as the factors of time, information-sharing, accuracy of information, inventory liability and version control come into play.

More than 43 percent of respondents reported that this information was “less than satisfactory” for direct procurement, with that number increasing to 50 percent for indirect procurement contracts. Leading companies need to leverage technology, tools and methodology to ensure that this internal and external collaboration and information-sharing is occurring consistently and that risks and opportunities are managed accordingly.

Contracts Management Information for Decision-Making Capability Summary

On the whole, the findings paint a grim picture for many organizations, and they further bear out results from a number of other recent studies by Protiviti and others. Without complete, timely, accurate and relevant information for decision-making, as well as measurement, monitoring and control, even the most skilled, dedicated and professional people will experience great difficulty managing risks and opportunities in the process, even where there is excellent process design. The supporting systems and data, as well as the tools and methodologies to transform the data into information, are often at the root of these information weaknesses (see the next two capability areas, #5 and #6).

Capability #5: Information Methodologies/Tools

What is this capability?

Very closely related to capability #4, this process capability refers to the tools, methodologies, and procedures used for organizing, analyzing and transforming data so that it becomes useful for decision-making, measuring, monitoring and control. That is the means to translate the data stored in the contracts management, procurement transaction and/or other systems into information for decision-making and control.

This capability is another critical enabler for procurement. Absent effective methodologies, tools and procedures for organizing, analyzing, and transforming contract, risk, performance, supplier and other related data into useful information for decision-making, the organization is most unlikely to effectively or efficiently manage and control contracts.

And, this proved to be another area of significant weakness, undermining both the quality and maturity of the contracts management process for a great number of organizations. Let's examine the results from the survey, question by question:

1. Does ongoing and formal risk assessment of the contract population occur?

This question deals with the availability and effectiveness of methods and tools to analyze and report on contract risks and risk profiles. **Almost 48 percent of respondents reported a “less than satisfactory” condition for direct procurement and the number jumped to almost 58 percent for indirect procurement contracting.** What this says is that 48 to 58 percent of organizations do not have a reasonably effective way to continuously monitor and update risks across their contracts.

2. Do risk assessments lead to regular compliance auditing of contract risks?

Linked very much to the previous question, this question relates to the outcome of formal risk profiling and assessments, and whether these lead to reviews and compliance auditing of contract risks. Not surprisingly, given the high level of respondent dissatisfaction with the previous topic, **almost 53 percent in direct procurement and as much as 61 percent in indirect procurement were “less than satisfied.”**

The implication is that a) contract risks are not being assessed and re-profiled on an ongoing and routine basis, and b) there is an absence of effective and targeted auditing to validate that risk management and compliance controls are adequate, in many cases.

3. Is there effective monitoring of day-to-day contract performance and compliance?

This question relates to the methodology and tools required to deal with routine contract performance and compliance monitoring. This essential yet basic capability again proved to be “out of reach” for a startling number of organizations in both the direct as well as indirect procurement areas. **More than 46 percent in direct procurement respondents and an overwhelming 65 percent in indirect procurement said that they did not have the methodology and tools to effectively monitor contract performance and compliance, rating them “less than satisfactory.”**

4. Does root cause analysis, corrective action planning and monitoring of results and actions occur as a result of audits of contract risks and controls?

This question addresses the organization's ability and methods for addressing audit results, for identifying the root cause of issues identified, for developing effective action plans and for monitoring and controlling the implementation of those plans. The internal audit function may or may not be responsible for providing this methodology for organizations.

Following the trend reflected in the responses to other questions in the “information methodology and tools” capability area of contracts management, **50 percent of respondents in the procurement of direct purchases and as many as more than 64 percent for indirect procurement** reported that these capabilities were “less than satisfactory” or below the minimum level of acceptable control.

5. Is contract life-cycle information generated and produced for contract administrators and managers?

This information would include various alerts, warnings, action messages, recommendations and other information for those personnel responsible for controlling and managing various elements of contracts with varying degrees of significance and complexity. This capability should be in place to help prevent problems and/or respond to issues such as renewal requirements, contract expiration, contract milestones, etc. **Almost 61 percent of respondents in direct procurement and a whopping 77 percent in indirect procurement** reported having a “less than satisfactory” capability for this fairly basic functionality.

6. Are all contracts made visible to stakeholders: in-process, open, closed, pending and so forth status?

This functionality is intended to bring more transparency to those who need to know the status of a contract. This helps to reduce confusion, avoid duplication of effort, identify in-progress contractual discussions, etc. **More than 50 percent of direct procurement respondents and more than 65 percent responding for indirect procurement** indicated that these capabilities were “less than satisfactory” in their organizations, meaning in effect that the tools and methodologies to provide such visibility or transparency did not exist or was unreliable.

Contracts Management Information Methodology/Tools Capability Summary

The results of the survey for capability #5 provide strong evidence that many organizations are putting themselves at risk by under-investing. These tools and methodologies are essential to provide the information needed for effective management, decision-making, and control of contracts, contract performance, risk profiling, risk and compliance management.

And, as will become further evident in the next section, there are similar and sometimes even worse results emerging from respondents in the sixth and final area of contracts management capability – systems and data. As discussed early in this document, the inter dependency among the six elements of capability in any key process means that weaknesses in one capability invariably undermines others. Where there is strength and maturity in any single capability, that capability will in itself be undermined over time by immaturity and weakness in other portions of the infrastructure for that process.

Capability #6: Systems and Data

What is this capability?

This capability pertains to the source of contracts management information for decision –making and control – the transaction and reference systems and the data contained therein. The systems involved include contracts management systems as well as related procurement execution transaction systems. For the more sophisticated it also included other sourcing and supplier management-related systems. Contracts management work flows, purchasing transaction records, supplier and item master files, terms and conditions libraries and contract libraries (key reference sources) are among the critical systems and sources.

The data portion of the capability refers to the contents of these master files, transaction, and reference files. And importantly, it also refers to the integrity, quality, completeness and up-to-date status of this transactional and reference data. The advent of excellent technological solutions and the effect on the purchasing transaction, master file, work flow, library, sourcing, as well as other reference and control-type, is a significant boost and enabler for contracts management.

However, there are still many legacy systems in place and far too few investments in valuable technologies to support the organization. Additionally, attention to the integrity of core data remains a problem for many professionals involved in spend analysis, sourcing, contracts management, supplier and commodity management and overall purchasing execution, risk management and control.

The following questions and survey results provide very helpful insight into the maturity of the systems and data capability for the contracts management process.

1. Is the contracts management process supported by a contracting system wherein the work flow steps effectively mirror the contracting process?

In our survey **more than 51 percent of those surveyed in direct procurement and as many as 66 percent in indirect procurement** reported that they had systems that were at or below the “less than satisfactory” level. The implication of this is that more than half of the organizations had no system or a very rudimentary contracts management system implemented to support their processes and people.

And this for a process that is intended to help control expenditures ranging typically from 20 percent of an organization’s revenues to as much as 80 percent and more!

An effective and efficient contracts management system will have attributes such as those highlighted in this survey question. Work flows should be based on best contracting practices, with those step-by-step planning, reference, approval and post-award management activities driven by the online system.

Other recent surveys carried out by benchmarking firms and contracts system software suppliers exhibited similar weaknesses across all industries.

2. Does the contracts management system include a contracts library of actual contracts, as well as various standard contract boilerplates of terms and conditions?

On average **more than 50 percent of the firms responding indicated that this was another area of major weakness, with 47 percent in direct procurement and 53 percent in indirect procurement** indicating the “less than satisfactory” (below tolerance) assessment.

Again, we would suggest that the underlying reality is that these organizations have zero or minimal contract management system capability, which also means an absence of contract library functionality for these respondents.

3. Does the contracts management system contain effective compliance and control mechanisms?

Post-award contract management and administration is a critical function for the management of contract and supplier performance and risk. Organizations need to be able manage and control compliance to contract by suppliers and by internal users. This is essential if management is to ensure that the level of performance and expected value is achieved, and the carefully designed and assigned risk management components of the agreement are implemented and adhered to.

However, **more than 46 percent of respondents surveyed said that this capability was below the acceptability threshold (less than satisfactory) for direct procurement. The percentage further increased to as much as 59 percent in indirect procurement contracting.** The opportunity for improvement is immense.

4. Are procurement transaction and contract systems connected (interfaced or integrated) to enable analysis, reporting and compliance?

Purchasing and payables transactions reside in ERP, stand-alone purchasing and accounts payables systems, other legacy transaction systems, and so on. Contracts typically reside in some other module or reference system, in some other electronic files (MS Word etc.), in manual filing systems, and so forth.

In order to effectively and efficiently manage contracts most organizations require the capability to cross-reference, interface or integrate these purchase and payment transactions with contract information. Obviously the greater the number of suppliers and contracts, and the greater the complexity of the deals, the more important the technological capability becomes as the organization strives to manage risk.

In this the final question, the results continued to highlight significant risks as well as major opportunities for improvement. Those surveyed indicated that **even the most structured form of purchasing, direct procurement, as many as 53 percent of the organizations had “less than satisfactory” capability in this area. In indirect procurement more than 64 percent** rated this below the acceptable threshold.

It is therefore no surprise that many organizations have severe difficulty in managing contract risks and measuring and controlling contract performance and compliance.

Contracts Management Information Systems/Data Capability Summary

The systems and data portion of the survey unearthed serious shortfalls in terms of the technological capabilities available to many, or even most of the respondents. Systems and data is another foundational capability for those committed to successful contract planning, negotiation, post-award administration, risk management and control. The automation of much of the administration, measurement, alerts management and other controls provides a major opportunity for efficiency as well as risk management and control improvement.

The impact of these shortcomings can be seen throughout the fragmented contracts management processes of many organizations and is reflected in the less than satisfactory outcomes that are achieved by many companies in the area of procurement contracts management. At a time of great technological advances it would appear that a great number of organizations are lagging well behind in terms of leveraging contracts management and procurement transaction technologies to support their business and risk management objectives.

The technology to enable effective and efficient management and control of contracts and procurement expenditures must be planned. It goes back to #1 – developing a strategic vision and objectives for the contracts management process and related capabilities and performance. The systems and data investments must be planned so as to enable the contracting processes and organization, and to provide the information for decision-making and control needed by that organization. Methodologies and tools for transforming data from those systems must be included in the technology vision and solutions being planned.

CLOSING COMMENTS AND RECOMMENDATIONS

We offer the following guidance to all readers of this very significant study of contracts management risks and practices:

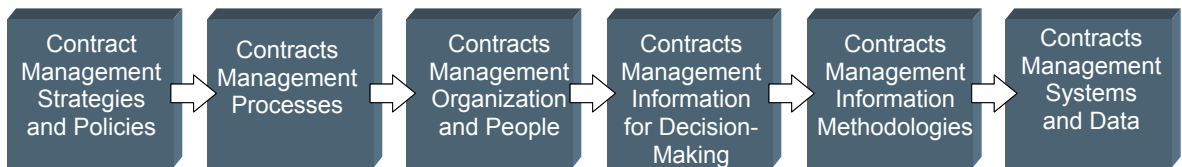
1. Never underestimate the importance of having a clear process vision, and well-designed and defined objectives, strategies, and plans for the process. If you don't know where you are going it is unlikely that you will end up in the most desirable place! Policies should reflect your vision and goals and must be realistic and enforced.
2. We continuously stress the importance of an excellent design and discipline in process. Well-designed processes, practices and procedures create the primary foundation for effectiveness, efficiency in the management of process risk and performance.
3. No matter how well the process is designed, it cannot be effective without the right people and structure. Having the correct organizational skills, competencies, and culture to manage and execute the process is a key to success.
4. It is clear to all that even the best of organizations needs accurate, complete, and timely information to make decisions, to measure and control performance and to effectively and efficiently manage the risks and opportunities, even in well-designed processes. The organization must define their informational needs clearly and completely.
5. In order to provide this critical information the organization needs to invest in the appropriate set of methodologies and tools for data analysis and extraction as well as for reporting and collaboration in order to provide effective information for decision-making, measurement, and control and to do so efficiently.
6. And finally, we recognize how essential it is to leverage technology. And good data is a critical success component in order to provide the source for the analysis, reporting, measurement and management of the process and performance, and the workflows and tools that reflect the process design. This technology must support the overall process strategy and vision for the process, reflect best practices in process work flow, and be planned and implemented thoughtfully along with methodology and tools.

In closing, this major survey of contracts management evidenced serious weakness in all of six elements of process capability. The numbers have revealed across-the-board problems from strategy and policy, through process design and procedures, through skills, organization and culture, thorough information for decision-making and control, to the methods and tools for producing needed information and into the area of supporting systems and data. And, all of this in an activity of such major significance, dripping in risk, opportunity and impact for almost every organization.

We therefore strongly urge all organizations, in all industries, to give this matter some immediate and serious attention and consideration. We suggest that you take time to communicate the insights from this report internally. From there we urge business leaders and board members to adopt the recommended management actions outlined in the executive summary section of this report. We hope that this report provides you with the facts, compelling arguments and a baseline for such action.

APPENDIX A: DIRECT PROCUREMENT OVERALL RESULTS DATA

Procurement Contracts Management Capabilities (Overall Results Data by Component of Contracts Management Capability) “Direct” Procurement Results Summary



Realization of Value Proposition Process Maturity Risk of Failure	Optimized	26.2%	11.9%	9.4%	15%	11.9%	12.2%
	Managed	24%	22.8%	20.9%	23.1%	19.4%	18.4%
	Defined	20.1%	25.5%	27.1%	23.8%	22.8%	22.4%
	Repeatable	17.9%	23.6%	23.1%	23.1%	25.9%	21.2%
	Less Than Satisfactory						
	Initial / Ad hoc	11.8%	16.3%	19.5%	15%	20%	25.9%

Results shown above are aggregations of the combined scores for the groups of questions associated with each of the individual (6) components of contracts management process capability in the study. Results of specific questions are reviewed and discussed throughout this whitepaper.

APPENDIX B: INDIRECT PROCUREMENT OVERALL RESULTS DATA

Procurement Contracts Management Capabilities (Overall Results Data by Component of Contracts Management Capability) “Indirect” Procurement Results Summary

		Contract Management Strategies and Policies	Contracts Management Processes	Contracts Management Organization and People	Contracts Management Information for Decision-Making	Contracts Management Information Methodologies	Contracts Management Systems and Data
<p>Realization of Value Proposition</p> <p>Process Maturity</p> <p>Risk of Failure</p>	Optimized	20.4%	11.8%	9%	11.5%	10%	9.2%
	Managed	23.5%	20%	9.7%	14.5%	11.7%	12.4%
	Defined	22.2%	24.9%	27.6%	26.7%	23.9%	22.9%
	Repeatable	20.4%	25.3%	24.8%	26.7%	27.8%	24.8%
	Initial / Ad hoc	13.6%	18.1%	29%	20.6%	26.7%	30.7%

Less Than Satisfactory

Results shown above are aggregations of the combined scores for the groups of questions associated with each of the individual (6) components of contracts management process capability in the study. Results of specific questions are reviewed and discussed throughout this whitepaper.

ABOUT THE AUTHOR, PROTIVITI INC., AND APICS

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Prior to Protiviti, Mr. O’Keeffe spent over 20 years in executive, management and professional-level positions in industry in various parts of the United States, Ireland and Switzerland. His successful career spans senior-level Supply Chain Management, Procurement and Operations positions in companies in the High-Tech, Telecommunications and Energy industries. He has authored several in-depth though-leadership white papers on supply chain risk management, including several which have been published jointly with APICS.

About Protiviti Inc.

Protiviti is a leading provider of independent internal audit and business and technology risk consulting services. We help clients to identify, assess, prioritize and manage operational and technology-related risks encountered within their industries, and assist in the implementation of processes and controls to enable their continued monitoring. We also offer a full spectrum of internal audit services focused on bringing the deep skills and technological expertise to enable business risk management and the continual transformation of internal audit functions.

Protiviti, a wholly owned subsidiary of Robert Half International Inc. (NYSE: RHI), has more than 40 locations in North America, Europe, Asia and Australia.

As with other service lines within Protiviti, the Supply Chain Risk Consulting (SCRC) service line uses a risk-based approach to assessing and redesigning key process capabilities and strategies. SCRC specializes in helping clients to assess, design and implement strategies, processes, controls and related capabilities in such areas as sourcing, supplier and contracts management, sales and operations planning ,process and services outsourcing, demand planning, supply planning and scheduling, procurement and inventory management and control.

About APICS

The Association for Operations Management is the global leader and premier source of the body of knowledge in operations management, including production, inventory, supply chain, materials management, purchasing, and logistics. The association provides comprehensive education and training programs that significantly improve an individual’s understanding of operations management practices, strategies, and concepts.

APICS administers the internationally recognized certification programs, APICS Certified in Production and Inventory Management (CPIM) and APICS Certified in Integrated Resource Management (CIRM). Through participation in these and other APICS educational programs, operations professionals gain new skills and update their knowledge with hands-on, interactive training through APICS national workshops, online classes, APICS Webinars, and local chapter certification review courses and workshops and through time-tested study materials, including the APICS Dictionary, the global standard for terms and definitions used in the field.

Learn more about the APICS community by visiting www.apics.org or call (800) 444-2742 or (703) 354-8851.