



# **An Analysis of Contract Management Issues for Small- and Medium-Sized Organizations**

A Whitepaper  
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## INTRODUCTION

In the average company, 80% of the buying and selling that goes on is governed by contracts. Contracts with suppliers. Contracts with customers. Contracts with vendors. Contracts establish the value of each of these business relationships, in black and white, in dollars and cents.<sup>1</sup>

However, in the average company, contract documents are neglected and abused.

It can take weeks and months to negotiate a contract. You draft and redraft the terms, bake in safeguards and set service-level standards. But then the document itself is typically filed away and forgotten. Several departments may have a stake in the deal, but the paper may land in the filing cabinet or hard drive of just one of them. When an administrative assistant leaves, the person who knew which cabinet or hard drive the document was placed in may be gone.<sup>2</sup> Just finding contracts is a challenge at most companies, according to the Aberdeen Group:

*[It is alarming...that many customer and supplier contracts remain locked away in filing cabinets or stored on the hard drives of individual (and often inaccessible) PCs across the enterprise. Certain subsets of contract information - such as pricing, sales, purchase orders (PO), or payment data - are located in various business systems within and outside the enterprise, from internal ERP systems to the accounting systems of various trading partners. The segregation of contract information makes it difficult to drive compliance, maximize contract usage and fulfillment, and conduct thorough analyses of contract performance.]*<sup>3</sup>

It's no wonder the estimates on how much companies waste because of poor contract management are so high - \$153 billion a year, according to the Aberdeen Group.<sup>4</sup>

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An IACCM report cited an example that rings true for many small businesses. A 25-year-old company had long ago lost track of its founding documents and contracts. Knowledge of the contracts was in just one place - the head of one of the executives who had been there at the beginning. "...Discussion revealed that many of [the original contract] obligations were inappropriate and irrelevant to the current status, strategy and composition of the organization. Some had matured or expired years previously, at which point material amounts of deposits and rebates should have been recovered, but were forgotten!"<sup>5</sup>

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## WHERE IS ALL THE MONEY GOING?

Here's how some of the waste comes about:

### When contract processes are manual and uncoordinated across the organization...

- Contract creation, routing, filing and retrieval all take unnecessary administrative time and trouble.
- Contracts can be lost when the person who filed it forgets where he or she put it - or leaves the company.
- Contracts can be damaged or destroyed by fire or flood.
- The contract may be at one of the company's locations when it's needed at another.
- If an issue arises on the weekend, the contract may be inaccessible until the start of the work week.

### When contracts can't be easily retrieved and reviewed...

- Off-contract buying happens. It's usually at a higher price than was negotiated, and it can invalidate lucrative contracts with important suppliers.
- Sales may not know the company has an arrangement with a corporate client and may quote prices that don't match those negotiated - or may miss sales opportunities altogether.
- When there is no previous contract to draw on or refer to, sourcing and sales cycles are longer, because document drafting and approvals take longer. The contract ultimately negotiated may be uncompetitive or even risky because history was lost - well-crafted terms (prices, protective clauses, restrictions and penalties) from previous contracts aren't incorporated.

- If those charged with monitoring a vendor's performance aren't aware of contract stipulations and SLAs, the vendor may fall far short.
- Rebates and discounts may be unclaimed or lost.
- Inadvertent renewals may take place, prolonging a relationship that may not be profitable.
- Inadvertent terminations may take place. The company may incur fees and have to spend significant time to reinstate the agreement.

### Beyond the direct revenue, cost and performance impacts, there are compliance risks. For example...

- Sarbanes-Oxley (SOX) makes executives in public companies attest to the company's adherence to contract terms. They are putting themselves and their companies at risk if they don't have access to the contracts.<sup>6</sup>
- Banks are legally as responsible for their vendors' actions as they are for their own. If management can't access contracts, they can't monitor performance.<sup>7</sup>
- Healthcare companies face HIPAA penalties if their vendors don't live up to contracted information handling guidelines. Again, if contracts aren't accessible, vendors' performance may go unreviewed.<sup>8</sup>



There's an extraordinary downside to poor contract management. There is also an extraordinary upside to good contract management. Aberdeen Group has published the estimates below of cost saving or revenue/performance improvement for companies that reengineered contract management: <sup>9</sup>

IMPROVEMENT AREA	PERFORMANCE IMPACT
Rebate/discount management	Improved 25% to 30%
Sales contract renewal rates	Improved 25%
Revenues	Improved 1 % to 2%
Administrative costs	Reduced 25% to 30%
Evergreen contracts	Auto-renewals essentially eliminated
Contracting cycles	Cut in half
Procedures and terms	Standardized, mitigating risks and enforcing company policies
Documentation and reporting	Time spent reduced from days to minutes
Contract analysis	Finally possible for every contract
Compliance management	Compliance improved 55%



## STEPS TO BETTER CONTRACT MANAGEMENT FOR THE SMALL OR MEDIUM-SIZED BUSINESS

If you're interested in realizing the cost-reducing, revenue-protecting benefits of better contract management, how do you do it? Where do you start?

### Assessing your current situation

The first step is to determine what internal resources are utilized to address the issues. In evaluating your internal resources, you will want to understand what your company's current processes are for storing contracts, obtaining needed information from them and monitoring them. Where are the documents? How many are there? Who are the stakeholders, who has oversight responsibility and how long do personnel spend getting objective data from agreements?

### Estimate the cost

It's important to understand the impact of your company's current contract management processes in dollars and cents. List and estimate the following:

- **revenue leakage from off-contract activity**
- **cost due to inability to take advantage of discounts and rebates that managers overlooked or forgot about**

- **cost of unprofitable vendor relationships that continue because managers can't analyze and assess vendor performance - or because a contract auto-renewed**
- **administrative cost of your current contract processes**
- **costs of storing paper copies of contracts, addenda and renewals**
- **penalties your company paid because of a vendor's failure to meet service level agreements or to comply with the regulatory guidelines your company must meet, e.g., HIPPA.**

### Identify the changes your company needs to make

The review will give you insight into how contracts are being managed now, and the cost estimates will help you understand what changes you need to make. As you define these changes in structure and behavior, you're likely to find that serious change can't happen unless you get support from a system.<sup>10</sup>

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With this whitepaper, we provide some tools that can help you assess your situation.

**Appendix A** is a battery of questions you can use to perform an assessment.

**Appendix B** represents another approach to gathering information, a review. This method can work well in a larger organization where no one person has a general sense of where the contracts are and who's in charge of them. The form in Appendix B is partially filled in with sample data from a fictitious linen service.

As the sample data in the review form suggest, you may turn up interesting, and sometimes alarming, information about how casually contracts are stored, and you'll see very clearly what price your company is paying for poor contract monitoring and management.

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## WHAT CAN A CONTRACT MANAGEMENT SYSTEM DO FOR YOU?

Your analysis and common sense will lead you to many of the features you'll want in a contract management system.

### Centralized database

A centralized database where all contracts reside is almost essential. Most databases within a company are Balkanized affairs, each supporting a single department, set up in Word, Excel, Access or whatever the administrative assistant is most comfortable with. Finance, legal and stakeholders in other departments have no way to access the document - or they have put their copy in their own idiosyncratic databases.

### Useful summaries

Summaries of important terms can help employees and stakeholders at all levels in the company. They get the information they need from contracts without laboring to locate the term in the agreement and decipher its meaning.

### Alerts

Contracts in a drawer or on an assistant's hard drive do not rise up and remind you that a renewal date is approaching, an SLA is being breached, or that you're imperiling your chances to earn a discount or bonus that was hard-won in the negotiations. A good contract management system will have reminders and warnings of key deadlines and danger zones.

### Support for analysis and reports

It is essential that the system be able to link related documents and sort by criteria that are important to your company. Your finance and executive team will be able to use their new visibility into the companies' contracts to do a better job of cost and risk analysis and produce more reliable reports.

### Data quality

Data quality is critical. The centralized database, the contract summaries, the alert system, the analysis and reports - will only be as good as the data that is transferred from the filing cabinet or the hard drive into the contract management system. Look for a vendor that helps you move contract data into the system and, when complete, offers assurances that the information in the system is accurate.

## How Technology Can Facilitate Efficiencies and Improve Profitability

Significantly better contract management is almost always a combination of a) changes to manual internal processes and b) electronic/systems support. The two should work hand-in-hand: the system should help contract managers and administrators do a better job.

This chart relates manual processes you may have identified in your current organization with features that a good contract management system provides.

### FEATURES OF CONTRACT MANAGEMENT SYSTEMS THAT ALLEVIATE RISKS OF MANUAL PROCESSES

	Centralized Database	Useful Summaries	Alerts	Support for Analysis and Reports	Data Quality
<b>Manual Processes:</b>					
Multiform contract storage procedures	X			X	X
Labor involved in contract management, including finding agreements and important objective terms	X	X	X	X	X
Contract monitoring and management at the department level	X	X	X	X	X
Oversight and assessment by finance and senior management	X	X	X	X	X



## OTHER CONSIDERATIONS FOR A CONTRACT MANAGEMENT SYSTEM

Small and medium-sized organizations should consider two other factors as they look at their contract management system options: Should it be web-hosted or installed, and what is the cost?

### Benefits of a hosted solution

For most businesses, a hosted solution makes sense.

- **The system is available to all stakeholders 24/7.**
- **Quicker implementation.**
- **Maintenance is the vendor's job, not your IT department's.**
- **Often less expensive. You usually pay a licensing fee based on the number of users or hours logged on. This is often far less than the purchase price of software and the installation/configuration fees.**
- **More flexibility. With a hosted solution, you don't own it, so you can adjust the service or eliminate it when your renewal date comes up.**
- **Your IT department doesn't get deflected from other projects.**

Security and up-time were concerns with hosted contract management systems in the past. But even large companies and large vendors are moving to the "cloud" as hosting services and Internet service providers become more and more reliable.<sup>11</sup>

### Cost

One of the nice surprises for owners and managers of small- and medium-sized organizations is that they can get full-featured contract management systems at far more reasonable prices than were available just a few years ago.

In 2005, Aberdeen Group reported that the average first-year cost of a contract management system was \$600,000. In subsequent years, the cost would still be two-thirds of that - or \$400,000 - in annual license and maintenance fees.<sup>12</sup>

Today, businesses can find hosted solutions that cost between \$15,000 and \$50,000 a year - and do more than a \$600,000 system would have done four years ago.

You may be thinking, "Sure, the price has come down, but that's still a lot of money for a company like mine. How do I sell this to my CEO?" Here's where your earlier review and ROI estimates come into play. If your estimates of cost reductions and rebate and discount improvements approach those published by the Aberdeen Group<sup>13</sup> you may be able to show that a system would pay for itself in the first year.

The cost-benefit analysis is even more compelling as you account for the internal savings from alleviating the current manual processes with a full-featured contract management system.

**This checklist summarizes the features a small or medium-sized business should look for in a contract management system.**

- ☐ **Centralized contract storage and retrieval system - accessible by all key stakeholders 24/7**
- ☐ **Electronic alerts for renewal dates, penalty triggers, automatic increases, product/service delivery dates, performance review dates**
- ☐ **Ability to track amendments and other changes to a contract and link it to other contracts and documents**
- ☐ **Ability to sort and analyze contracts by a variety of parameters and produce ad hoc reports**
- ☐ **Useful summaries of key contract terms**
- ☐ **Vendor assistance to implement the system, assuring a high level of data quality**
- ☐ **Web-hosted by the vendor**





## MAKING CHANGE HAPPEN

An IACCM presentation from 2007<sup>1</sup> listed the characteristics of a successful contract management system deployment. Their focus was how to introduce new technology to a company, but the approach applies to effective change of almost any kind.

- 1. Powerful and committed sponsor**
- 2. High-quality, focused project management**
- 3. Realistic and achievable goals (quick wins)**
- 4. Market the system well to stakeholders**

Once you've defined the processes and practices you want to change and the technological support you require to support it, you'll need to get top management support. Successful implementations have a champion in the C suite.

They also have a good project plan and a project manager. Migrating contracts from paper files and managers' hard drives to a centralized database can be a big job, as is the process of extracting the key contract dates, penalties, discounts, SLAs and other contract terms that the alert system will point to. If you select a vendor that just provides software, you will have a fairly complicated set-up and implementation process.

Change is never easy, so marketing the program well, stressing the benefits for the people who change their current manual processes, is essential. Focus on realistic goals and visible, quick wins to keep your colleagues focused and on board.

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## THE BENEFITS OF BETTER CONTRACT MANAGEMENT

### Compliance benefits

Better regulatory compliance, penalty avoidance.

### Costs and savings

The discounts and rebates anticipated in your contracts are actually realized, because managers know to ask for them and 'maverick,' off-contract spending is reduced.

Contracts don't automatically renew or cancel without review and/or renegotiation. Lucrative deals stand a better chance of being continued. Sub-optimal deals can be improved or cancelled.

Increased administrative productivity and reduced administrative time spent in contract creation, storage and retrieval.

Reduced storage cost. Contracts can be scanned and maintained electronically in a central repository.

### Consistency and efficiency

Managers and other personnel can draw from previous contracts, accessing language, prices and SLAs. Contracts take less time to draft, negotiate and review.

### Service

Better compliance with service or delivery standards or other contract terms. When the service standards are accessible to managers, they make their vendors live up to them.

### Management visibility

Managers are better able to assess their vendors' performance. Top management and finance get a window into contracts to assess corporate risk and create better forecasts. They are also in a better position to consolidate work with preferred vendors for deeper discounts.



## CONCLUSION

Good contract management has many benefits, from the ability to fully realize contractual discounts and rebates to better regulatory compliance to savings in administrative costs.

And poor contract management has costs. Aberdeen Group has estimated that American businesses waste \$153 billion a year because of poor contract management.<sup>15</sup>

To realize the benefits and avoid the costs of poor contract management, you need to review where your organization is today, what its contract management practices are and what they are costing your company.

Some of the changes you will need to make may involve redefining roles and responsibilities. Processes will have to change related to the storage and monitoring of contracts.

Those procedural and organizational changes are almost impossible to make without technological support in the form of a contract management system. No longer just for large companies, good systems are now available for under \$50,000. So a technology solution is now in scope for **small- and medium-sized organizations**. [N](#)



## FOOTNOTES

- <sup>1</sup> "Enterprise Contract Management: A Practical Guide 5 (2008);' Anuj Satena
- <sup>2</sup> "Contract Management Organizational Assessment Tools 15 (2005);' Greg Garret and Rene Rendon
- <sup>3</sup> "Contract Optimization: A Recession-Proof Strategy for Maximizing Performance and Minimizing Risks," Aberdeen Group, May 2003, page 6
- <sup>4</sup> "Contracts and knowledge management principles; August 2009 IACCM Newsletter, <http://www.iaccm.com/contractingexcellence.php?storyid=939&PHPSID=8d0c0360754caf399dcf71450e8cecc0>
- <sup>5</sup> "The Contract Management Benchmark Report: Optimizing Supplier Relationships; Aberdeen Group, June 2003, page 31
- <sup>6</sup> "Major Themes of the Sarbanes Oxley Act;' Texas Journal of Business Law, 42 TXJBL339, 2008, pages 410-411
- <sup>7</sup> FDIC Guidance for Managing Third Party Risk, FII:44, 2008
- <sup>8</sup> "Sorting Out Privacy Changes," Health Data Management, v. 17, n. 4, 2009, page 24
- <sup>9</sup> "The Contract Management Solutions Selection Report;' Aberdeen Group, June 2005, page 4
- <sup>10</sup> "Do You Know Where Your Contracts Are?" Entrepreneur.com, August 2009
- <sup>11</sup> "Highlights from Spring SNW Cloud Computing Summit," DCIGinc.com, April 16, 2009, <http://www.d ciginc.com/2009/04/highlights-from-the-spring-snw-cloud-com-putin..html>
- <sup>12</sup> "The Contract Management Solution Selection Report," Aberdeen Group, June 2005, page 7
- <sup>13</sup> "The Contract Management Solutions Selection Report," Aberdeen Group, June 2005, page 4
- <sup>14</sup> "Contract Lifecycle Management: State of the Market and Lessons Learned," IACCM, July 2007
- <sup>15</sup> "The Contract Management Benchmark Report: Optimizing Supplier Relationships," Aberdeen Group, June 2003, page 31



## APPENDIX A

### CONTRACT MANAGEMENT: HOW IS YOUR COMPANY DOING?

Here is a set of questions that can guide you as you assess contract management within your company. We have adapted for small and medium-sized organizations a battery of questions posed by Aberdeen Group in its June 2005 whitepaper “The Contract Management Solution Selection Report.”

#### Organization (structure, skills and decision-making alignment in the company)

- Is contract responsibility centralized in any way?
- Is it connected with the head of Finance?
- Are contracts reviewed in a consistent way throughout the company?
- Are controls in place so that contracts that are critical to the operations of the company are monitored?

#### Process (standardization and efficiency)

- Are contracts monitored in a consistent way throughout the company?
- Do you have procedures for contract administration (storage, cataloging, reporting)?
- Do you have a summary of important contract terms?
- Are all contract terms enforced?
- Can legal keep up with your requests to find contracts or obtain information from agreements?

#### Knowledge (management’s visibility into contracts and awareness of compliance issues)

- Can managers quickly and easily access all contracts that meet certain criteria (e.g., for a specific supplier, or that include a specific clause)?

- Can managers compare terms across a range of contracts - pull up, for example, the service level agreement paragraphs from all supplier contracts?
- Can managers generate reports on vendor performance compared to standards within agreements?

#### Technology (what parts of the contracting/contract management process are already automated?)

- What internal processes have been automated?
- Has automation had any impact so far on contract management efficiency or effectiveness?
- What decision support and reporting tools are in the hands of managers who make and/or manage contracts?

#### Performance measurement

- What metrics and procedures does your company use to measure contract compliance and performance?
- Are the metrics/procedures you use consistent throughout the company?
- Are you capturing all rebates and discounts in contracts with your suppliers?
- Are you capturing all revenue in contracts with your customers?
- Does your company invoice promptly, in accordance with contract milestones?

## APPENDIX B

### CONDUCTING A REVIEW TO DETERMINE YOUR COMPANY'S CURRENT CONTRACT PROCESSES

In many small to medium-sized firms, managers, particularly in finance or purchasing, have a general idea of where most of the contracts are and how they're being monitored. But in some companies, no one really has a handle on it. In that case, it may be helpful to conduct a review.

To begin, ask your accounting department to generate a list of suppliers, vendors and customers, ranked by dollars paid (on the vendor side) and revenue received (on the customer side).

Then the job is to ascertain whether your company has a contract with each vendor or customer and gather some basic information about it. It's especially important to note the dollars each contract represents, who the stakeholders are, who manages this contract, where it physically resides and whether there are any issues regarding the contract or the vendor/customer relationship.

This chart format can guide the review process. We have populated this sample chart with some data from a fictitious linen service.

#### Contract Management Review Format (Sample)

PROCUREMENT CONTRACTS					
Supplier	Service/ product	YTD payments	Stakeholders/roles	Contract location(s)	Contract management issues
Harris Insurance	Liability Insurance	\$20,000	Jean Morgan, CEO Marian Fowler, CFO	Original in CEO office files Jean's Assistant's PC Marian Fowler's PC	Missed annual renewal date last year; paid late penalty to reinstate policy.
Ace Lawns	Landscape Maintenance	\$16,500	John Miller, Facilities Manager Marian Fowler, CFO	Facilities files John Miller's PC Marian Fowler's PC	Ace has not been meeting all service dates. Penalties are in the contract, but have not been enforced. Approximately \$2,000 in discounts have been foregone.



SALES CONTRACTS					
Customer	Service/ product	YTD revenue	Stakeholders/roles	Contract location(s)	Contract management issues
The Spot Cafe	Linen Service	\$12,500	Helen Leason, Customer Service Manager  Elsa Paine, Accounting and Finance	Copy in Helen Lea- son's Desk Drawer  Original in Elsa Paine's files	<p><b>Issue 1:</b> Payments from The Spot have been late 6 of the past 9 months. Helen, who is relatively new, was unaware that late-payment penalties were in all our standard contracts, so penalties have been foregone.</p> <p><b>Issue 2:</b> Customers who came on board in the past two years, as The Spot did, have an automatic renewal clause in the contract. Helen was not aware of this, and Elsa Paine did not have a note about this in the spreadsheet she uses to manage all our customer contracts. As a result, The Spot contract recently auto-renewed for 12 months.</p>

### About Ncontracts

Ncontracts® is a leading provider of risk management software and services to financial institutions. While we started with our industry-leading vendor management platform, our portfolio offerings have evolved to feature enterprise risk management, business continuity risk management, findings management, and cybersecurity management. More than 800 financial institutions use Ncontracts to manage risk more efficiently and effectively using our integrated suite of software and services.