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10 Ways to Negotiate Lower Costs in Outsourcing Contracting

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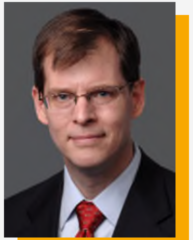
Today’s Speakers



Brad Peterson is a partner in Mayer Brown's Chicago office. He leads Mayer Brown’s global Technology Transactions practice. Also, he co-leads Mayer Brown’s Supply Chain & Distribution practice and its Fintech practice.

Brad’s practice focuses on helping clients reduce cost, improve operations, innovate and increase revenue through services and license agreements with technology providers. His experience includes information technology outsourcing (ITO) and business process outsourcing (BPO); cloud services such as IaaS, PaaS and SaaS; platform and marketplace services; data licensing and data monetization projects; and core systems modernization, ERP and other software licensing, development and integration transactions.

Alan Velasco is counsel in the Palo Alto office of Mayer Brown. He is a member of the Technology & IP Transactions practice and the Corporate & Securities practice. Alan advises clients in all types of complex transactions relating to digital services, outsourcing and information technology, including IT outsourcing, business process outsourcing, implementation of automation solutions and cloud computing transactions.

About Mayer Brown

With extensive reach across four continents, we are the only integrated law firm in the world with approximately 200 lawyers in each of the world's three largest commercial centers, New York, London and Hong Kong.

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About Our Practice

- **More than 50 lawyers** around the world are focused on helping clients **develop and manage relationships with suppliers** of critical services and technology
- Experience in **critical services sourcing deals** with a **total contract value exceeding $250 billion**, including data, digital, outsourcing and software
- We regularly advise clients in **outsourcing**, **cloud** and **digital transformation**, including the use of emerging technologies such as **artificial intelligence**, **robotic process automation**, **platform agreements**, **SaaS**, **big data** and **blockchain**, among others.

MARKET RECOGNITION

- ***Chambers & Partners*** – Top Ranking in Technology and Business Process Outsourcing category for 17 consecutive years. In 2021, Chambers USA ranked Mayer Brown as the role law firm in "band 1" in the Technology category.
- ***The Legal 500*** – Top Ranking in US Outsourcing for as long as it has ranked outsourcing lawyers and previously named us "Team of the Year."
- ***International Association of Outsourcing Professionals*** – Ranked as one of the top law firms on The World's Best Outsourcing Advisors list for The Global Outsourcing 100™ for 10 years. In 2019, Mayer Brown was recognized in the "Top Customer References," "Multiple Appearances" and "10 Year Club."
- ***Law360*** – Named "Technology Practice Group of the Year" in 2016 and "Law Firm of the Year" in 2016 thru 2020.

Basics & Agenda

Basics

- “Outsourcing” – a transaction in which a company turns over responsibility for an ongoing non-core business function to a supplier
- Does not include:
  - Staff augmentation arrangements
  - Professional services arrangements
  - Service contracts for a single project
  - Contracts for commodity services
- Suppliers perform at lower cost using lower cost resources, better practices, and better technology

10 Ways to Negotiate Lower Operational Costs

1. Reduce Supplier Cost
2. Reduce Risk Premiums
3. Allow Supplier to Make Transformative Changes
4. Commit to More Collaboration by the Company with its Suppliers
5. Leverage Competition
6. Partner with Supplier in its Technology Development
7. Pay in Future Years
8. Address Total Cost, Not Just Price
9. Contract for Options, Incentives, and Alignment
10. Build a Strong Contract

Ways to Negotiate Lower Costs

1. Reduce Supplier Costs

Outcome: Reducing a supplier's costs allows the supplier to lower its charges while preserving its profit

Issue: Complying with contract requirements is a cost for supplier but provides value for the company

Examples:

- Agree to utilize Supplier policies (with or without modification)
- Contract for what drives value instead of the current state

2. Reduce Risk Premiums

Suppliers bid based on both known costs and a risk premium for unknown costs.

Outcome: Reducing risk for the supplier will allow the supplier to lower its price

Issue: Having the supplier bear risk motivates the supplier to avoid damage and reduces risk for company

Examples:

- Making the deal itself less risky by better contracting
- Allocating less of the remaining risk to supplier

3. Allow Suppliers to Make Transformative Changes to Outsourced Operations

Outcome: Suppliers reduce cost dramatically by:

- Standardizing and automating manual processes
- Leveraging RPA, AI, SaaS and other third party technologies

Issue: Supplier might reduce supplier costs in ways that impose additional costs on the company

Examples:

- Reducing the company's rights to control supplier's methods
- Securing commitments to deliver value and avoid costly pitfalls

4. Commit to More Collaboration

Typically, outsourcing contracts envision a supplier to take full responsibility for delivering business functions.

Outcome: Suppliers bid lower prices because help from the company reduces suppliers' cost

Issue: Contract drafting must be broad enough to provide a credible benefit to supplier without increasing total cost for the company

Examples:

- Technical support
- Rapid decisions and access to information
- More direct access to company systems

5. Leverage Competition

Outcome: While competitive and sole source negotiations both provide opportunities to create value, competitive processes drive additional value to customers

Issue: Achieving benefits of competitive processes requires sophisticated planning and execution, including by legal teams

Examples:

- Invest in a clear, fair process with the right bidders
- Use to earn what savings are available using technology.

6. Partner with Supplier

Outcome: Suppliers bid lower prices because the company helps them to increase profits from other customers

Issue: Risk to the company's competitive advantage or reputation

Examples:

- License or permit use your data to train supplier's machine learning platforms
- Grant IP licenses or ownership of innovations developed for you for other customers
- License your name in marketing, subject to trademark policies and other restrictions
- Commit to act as a pilot customer for new products
- Commit to act as a reference customer
- Agreeing to publicly grant awards to suppliers who perform well

7. Pay in Future Years

Outcome: Price is reduced in first year

Issue: Supplier incurs the costs of transition and transformation in the first year

Examples:

- Fixed annual pricing based on average cost over the term
- Supplier purchasing assets from the company for credits
- Longer terms and higher termination charges to increase supplier's estimated profit over the life of the deal

8. Address Total Cost, Not Just Price

Outcome: Maximizing cost savings and avoiding costly pitfalls by considering the all-in cost of the outsourced service

Issue: Investment required to estimate and describe costs beyond "headline" contract price

Examples:

- Hidden costs and surprise charges
- Contingent costs of likely events
- Effect on other contracts and relationships

9. Contract for Options, Incentives, and Alignment, in Addition to Commitments

Outcome: Increased resilience

Issue: No company knows enough during the initial contracting phase to obtain commitments for all of needed services in a long-term contract

Examples:

- Options to increase, decrease, change or terminate services
- Incentives to prevent surprise costs from occurring
- Alignment on how the parties will work together

10. Build a strong contact

Outcome: Supplier delivers outsourced services in compliance with the company's expectations for a reasonably firm price

Issue: Deal fatigue and pressure to finish the deal and sort the details later means that there are gaps and ambiguities in the contract

Examples:

- Clear, simple, auditable promises in active voice
- Workable, team-based processes to complete gaps in the contract within fixed periods

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