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Telecom Negotiations Require Steady Nerves and a Willingness to Change

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Introduction

Telecom costs are typically 1 percent to 2 percent of a company's sales – that represents real money for a multi-billion dollar global corporation. As such, effective negotiations and management of telecom contracts can have a measurable impact on a business' financial performance.

A successful negotiation strategy is built on knowledge of mature and emerging technologies and market-based price and service standards, as well as effective use of contract terms and conditions to define goals and manage vendor performance. Another essential component of negotiation is defining thresholds and decision points for switching service providers – this, in turn, requires understanding the implications and potential risks of changing providers.

This Compass article defines the challenges and goals of telecom negotiations, outlines the prerequisites for an effective negotiation strategy, and examines considerations involved in renegotiating an agreement with an incumbent service provider. The author also describes the process of selecting a new service delivery team, and offers insights into how to develop, solicit, and review proposals, select winners, and implement a transition.

Don't Let this Happen to You

Too often, telecom customers make the mistake of allowing published contracts to be used as the basis of negotiations. Published rates are, for several reasons, exceedingly misleading. First, they don't include the credits, bonuses, and forbearance that typically characterize any large telecom agreement. For example, a major global carrier that executes a new contract with a Fortune 1000 firm generally issues a wide range of special considerations, such as a significant sign-up bonus, free installations, "achievement" bonuses, and/or months of free services.

Moreover, a telecom contract typically includes prices for services that you (the customer) don't use. Since you have no incentive to negotiate prices for unused services, vendors rarely discount them. Then, in the future, vendors reference these prices as representative of the market, when that's really not the case.

Keys to Success

An effective telecom services agreement is based on knowledge of real market rates, and on the actual net fees paid by real customers for existing services. (See "Baselining" below.)

Another imperative: a contractual provision for annual benchmarks to allow for adjustments to new market conditions, technologies, and changing business requirements. Flexibility can also be enhanced through a low minimum annual commitment, which should be less than 66 percent of expected annual spend. In this context, size matters. A $20 billion revenue company will have more negotiating clout than a $2 billion company, and more leverage to demand a low commitment. One way to gain this leverage is through a "preferred vendor" clause, whereby you agree that any new service requirements will be initially offered to the incumbent vendor. If the incumbent cannot meet your requirements, or if they are deemed non-competitive, you have the option to seek other providers.

Another priority: quality of service, which requires negotiating specific service level agreements with meaningful incentives and penalties. Telecom agreements are typically structured so that, in the event of a service outage, the vendor provides "credits" for loss of service, rather than a monetary payment. If the penalty isn't sufficiently painful, the vendor may prefer to dole out credits rather than to fix an underlying problem.

An effective contract escalates penalties after each outage. For example, under an escalated, "non-linear" approach, you receive, say, a week's free service after the first outage in a given month. If another outage occurs during the same month, you get a month's service. In the event of a third outage, the vendor agrees to six months' free service. Under this scenario, the telecom vendor has a clear incentive to investigate and address the cause of the initial outage, in order to prevent future problems.

Risk is a final prerequisite to an effective telecom services agreement. Specifically, to obtain favorable rates and concessions, you must be willing to change service providers, and you must be prepared to demonstrate that willingness.

If you have a clear understanding of the risks and benefits of various options, you are in a position to make informed decisions as to whether to stay the course with the incumbent, or sign on with an alternative supplier.

Plan A: Renegotiate

Changing requirements and evolving technologies demand that telecom contracts be evaluated and renegotiated on a regular basis to respond to new realities. Given the dynamic nature of the market, the first step is to get your bearings. As such, the foundation of any successful contract renegotiation is a baseline analysis that compares your existing services against other organizations, in the context of market standards and actual market rates.

The baseline, or benchmark, quantifies and provides details on your actual telecom services spend. The fact is, chances are that you don't know what you have, what you're using, or what you're paying for. Multiple contracts cover the same services, and charge several different rates for the same service. Baselining addresses this confusion through a detailed inventory of existing services, technologies, and rates. Comparing specific inventory items against specific invoices and contracts is the only way to establish actual effective rates and to define usage forecasts in terms of volumes and technologies.

Once you've completed the baseline analysis, you can use the findings to drive negotiations with your incumbent vendors, along with plans for new technology, business growth, and expectations for future rates and terms. At this stage, vendors typically agree to resolve inventory and billing issues – such as multiple billings – with promises of a "fresh start," in exchange for your agreeing to sign a new long-term agreement. Don't do it, *unless* the new agreement includes specific provisions for annual renegotiations based on market reviews, and not on published contracts. Prices should never be based upon discounts from rate cards, which may be changed at any time according to the vendor's whim.

The outcome of this initial discussion depends on the quality and resourcefulness of the vendor account team. In perhaps one time out of five, the account team will respond adequately to your requests and put forth an acceptable proposal.

The rest of the time (80 percent or so), you'll have to escalate the renegotiation within the vendor organization. Provide written documentation of contract requirements in terms of rates, quality of service, and benchmarking provisions. These terms are sent up the chain of command in the vendor organization for a response. Vendor management must increase the account team's financial latitude to grant special terms and prices. After a period of about four to six weeks, the vendor will respond to your terms.

About half the time, the escalation will elicit a positive response.

Plan B: Seek Alternatives

If the renegotiation process fails to deliver to your requirements, you must be prepared to pull the trigger, seek alternatives, and implement a seamless transition to a new team of service providers.

Write the RFP

The process of finding a new service provider begins with the development of an RFP document.* To craft an effective RFP, you must clearly and specifically understand and articulate your business' requirements. Here, the baselining process described earlier is essential, as it provides a stake in the ground to define targets and expectations.

One priority of the RFP is to state goals and expectations for flexibility and quality. Another key is to define the measurement methodology to be used to track performance and adherence over time. The RFP should include specific terms. For pricing, the vendor should commit to coming within 15 percent of the current market, and prices must be explicit and not tied to uncontrolled price lists or confidential contracts. Given the volatile nature of the telecom market, the RFP should also contain a provision for annual benchmarks against market rates. Finally, to ensure quality of service, the terms must include non-linear credits for service outages.

Review Process

Convene a vendors' conference to address questions and concerns – this is necessary to ensure quality responses and bids. Make it clear that you will only consider RFP responses that comply to your format. Also, consider only responses from vendors that participate in the conference – this eliminates boilerplate proposals that don't address your specific requirements. Additional questions from any vendor must be submitted in writing, with questions and answers distributed to all bidders.

Select a short list of two to three finalists from among the pool of RFP respondents. If the RFP is written with specific questions that require specific answers, the review and paring process can be a straightforward, quantitative comparison of the respondents' respective capabilities. Even so, it presents a significant challenge, since few customer organizations can, on their own, properly assess the credibility of the bidders' responses, particularly if new services are being solicited.

Objective, well-informed, third-party analysts specializing in telecom and network issues can play a valuable advisory role in response assessment.

Negotiation

Negotiations should be conducted with the two best respondents that emerge from the finalist selection process. In certain international networks, it may be appropriate to utilize more than one vendor. Some specific issues and guidelines to consider include:

- Reject the notion that pricing is volumetric (e.g., committing to higher volumes equals a price break)
- Do not allow "best and final" offers
- SLA credits must be nonlinear
- Negotiate charges related to implementation, conversion, and installation
- Don't pay for systems before they are up and running
- Allow escape for beneficial change of ownership of vendor or fall from first tier
- Allow escape to best contract in case of divestment/acquisition of a business unit

Here again, the role of a third-party advisor is essential, particularly since clients rarely understand the vendors' negotiating "hard" and "soft" spots – in other words, where the vendor will stand firm, and where concessions can be gained.

**In many cases, incumbent service providers are included in the RFP process. In this instance, we're assuming that the existing relationship is broken and that the client organization is making a clean break.*

Award and Conversion

The contract award is a serious issue. Allowing the winning bidder to publicize the win may increase your leverage during the implementation period.

If a new network is planned, the detailed implementation and fallback plans within the previously negotiated contract will now be implemented. The vendor's ability to execute this conversion transparently from an end-user point of view will set the tone for the life of the contract. Some things will not proceed exactly as planned, and both parties must carefully work around and, if necessary, re-negotiate any issues. However, problems that negatively impact end users must be rapidly and decisively addressed. During this period, never hesitate to escalate and re-escalate within the vendor organization to as high a level as needed to protect users from impaired services. In addition, billing should not be accepted for any service not operating to plan.

Conclusion

Renegotiation of a telecom contract is similar to any other legal negotiation, and just as serious. The optimal outcome keeps both parties out of court (in this, case out of the RFP business). However, should an incumbent vendor be intransigent and unwilling to meet current market rates and terms, you have a fiduciary responsibility to address the vendor community via an RFP. During this very highly leveraged process, you should use all tools at your disposal to ensure an optimal outcome.

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