

Managing SOW-based Project Services

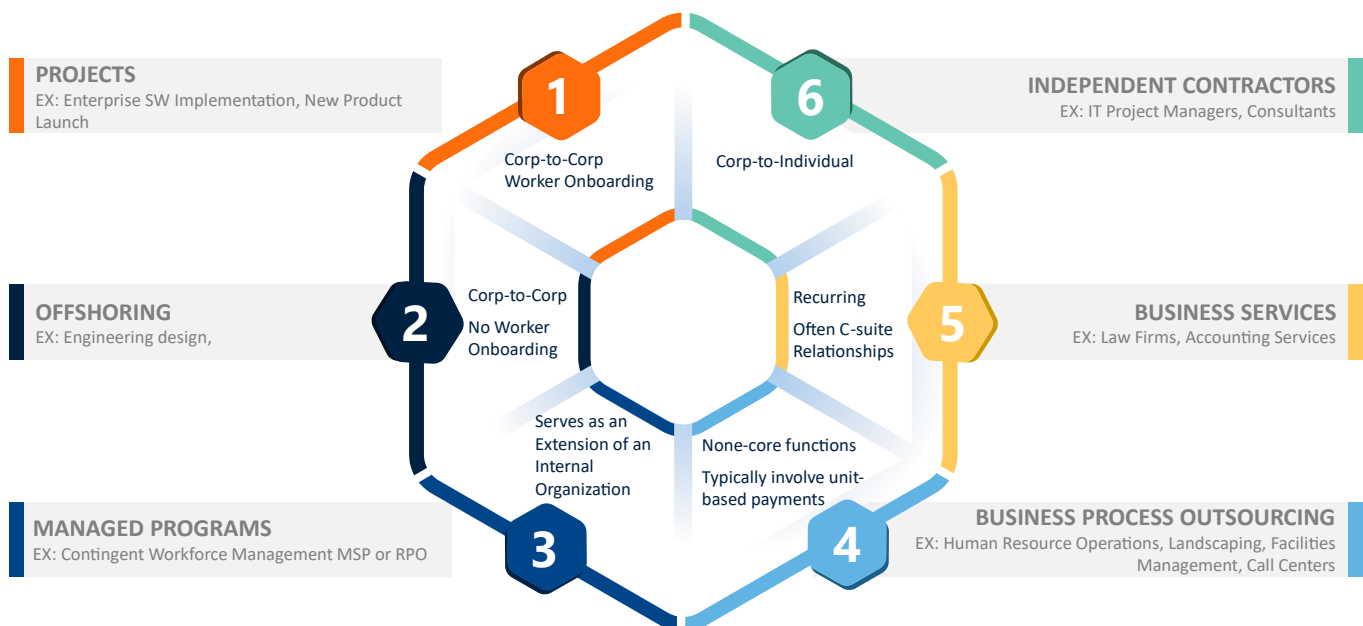


INTRODUCTION

Today's business climate requires agility. For many, that is achieved by supplementing their capabilities and bandwidth using Statement of Work (SOW)-based external services. This is nothing new. Nearly every company engages an external auditor. Many rely on outside legal counsel. And, for decades, virtually every company's functional groups have called on outside assistance at some point. The use of third parties is so pervasive that each year in the U.S. more than \$1.1 trillion is spent on SOW-based external services.

SOW-based services apply to different types of engagements. Most typical are project-based services (e.g., enterprise-wide systems integration or department-specific projects), independent contractors, offshore/nearshoring (e.g., call centers), business services (e.g., financial auditors), managed program (e.g., contingent workforce managed services provider) and Business Process Outsourcing (BPO) (e.g., outsourced payroll services). In this whitepaper we will explore the implications of SOW-based projects.

TYPES OF SOW ENGAGEMENTS



Effective management of SOW-based projects can yield huge savings

When engaging temporary talent, SOW-based project spend in most companies is as much as six times the amount spent on staff augmentation. There is a “value threshold” under which Procurement doesn’t get involved in awarding SOW-based engagements. This is referred to as tail spend. Control of the tail spend is a strategic imperative. It generates significant value and savings.

- Generally, Procurement organizations manage the service providers that represent “big spend” on enterprise-wide, C-suite engagements. The 25+% spent on smaller engagements are engaged on a case-by-case basis by individual departments and is not on Procurement’s radar.

What does this mean? If a company is tracking \$50 million in traditional staff augmentation spend, you may have as much as \$300 million spent on SOW-based projects, of which \$75 million dollars are not controlled through standard procurement processes and company policies!

- Drilling down further, SOW-based project services are relationships between a company and another business entity. In our experience, service providers engaged for as much as a third of the smaller projects are actually populated by individuals or very small teams and are working under agreements better met by agency-supplied contractors at a rate that is 20+% lower than that charged by the SOW services provider.

What does this mean? Using the example above, one-third (\$25 million) of the spend on small projects can be transitioned to staff augmentation agreements with suppliers or the payroll provider at a 20% reduction, a savings of \$5 million.

- When examining the largest service providers, we find that they are not staffing projects with 100% full-time employee (FTE) resources, frequently engaging temporary workers sourced by staffing agencies and providing them at significant mark-ups. Those resources not directly working under a deliverables-based agreement should be replaced by resources sourced by your preferred staffing agencies.

What does this mean? When large professional services firms structure an agreement to include a time-and-materials (T&M) element, the T&M rates charged typically range from \$125 - \$250 per hour. Equivalent rates for agency-supplied contractors would be 45 -50% of the SOW rates.

SOW-BASED PROJECT SERVICES DEFINED

Well-managed SOW-based projects delivered by external resources can serve as an effective lever when responding to market opportunities while controlling costs and increasing efficiency. They enable internal resources to focus on the core business, bring expertise that is only needed for one project, and provide a fresh perspective, suggesting solutions that may be overlooked by internal resources.

So, what exactly is a SOW-based project engagement? In defining SOW, research firm Staffing Industry Analysts (SIA) points out that the term is used to refer to “a document that captures the work products and services, including, but not limited to the work activities and deliverables to be supplied under a contract or as part of a project timeline” and also refers to “a type of worker class that is applied to finite, project-based work activities.” SIA clarifies that “In contrast to a typical temporary or contingent work arrangement which is billed based on time worked, SOW agreements are sometimes billed based on a fixed price deliverable or for hitting specific milestones.”

NEED	WORKER TYPE	SOURCING MODEL	PAYMENT MODEL	CONTRACTING MODEL
Skills-driven Specified duration Unclear deliverables	Agency Contractors	Staff Augmentation	Time-and-Materials	Work Order
	Independent Contractors/ Payrolled Workers	Self-Sourcing; Talent Communities	Time-and-Materials	SOW (ICs) Work Order (Payrolled)
Clear deliverables	Corp-to-Corp Project Services Teams	Service Provider Selection	Fixed Price, Milestone-Based	SOW

Simply put, to deliver a desired project, an organization engages one or more external providers through a formal document that specifies the scope of the work, details, deliverable, costs, and timelines involved. Every SOW-based project has two common elements:

- A description of the outcome to be provided, which might be expressed in milestones.
- A statement of the resources to be provided by the service vendor. This includes people, expertise, tools, technology, and data.

The service provider is paid upon completion of a pre-defined set of deliverables.

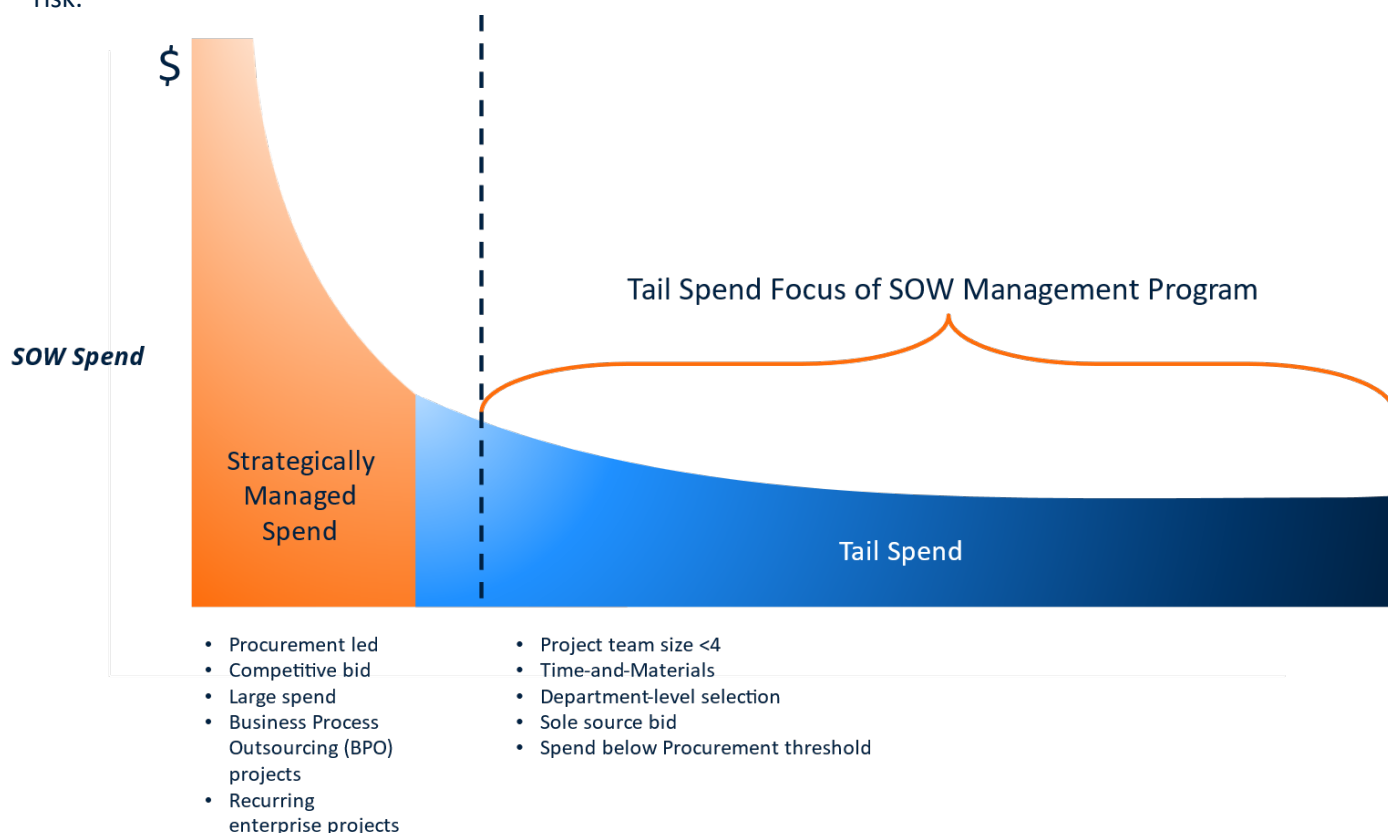
This simple definition masks the tactical business process complexities involved in every SOW-based project. Many projects have numerous interdependent sub-projects that must be coordinated. Multiple project teams may be working on the same project. A single team may be engaged on more than one project within the company, or multiple sub-projects each with its own fee. External team members may share an assignment with full-time employees. The provider's team should undergo a formal onboarding process and track timesheets even when payment is based on milestones rather than hours of effort.

THE TAIL SPEND CHALLENGE

When engaging third parties for very large projects or ongoing assignments, most companies engage their procurement organizations to ensure that the SOW process is well established, and the necessary checks-and-balances are in place to manage budgets and service providers. However, the risk of project failure arises when the spend level of an SOW project isn't high enough to warrant Procurement oversight. Money spent on these smaller projects is referred to as “tail spend”.

While the traditional definition of tail spend is “20% of the total spend with more than 80% of providers accounted for”, a better understanding comes from the attributes: ad hoc, off-contract purchases; low-volume, low-frequency; low-value, non-strategic; use of one-time provider – in short, not on the Procurement or Finance organizations’ radar.

With poor data visibility and persistent reliance on labor-intensive manual processes, organizations have found dealing with a vast number of transactions and a largely anonymous supply base has drained profits and added risk.



PROJECT FAILURES

The combination of project complexity and ineffective project controls has historically resulted in a high failure rate, especially among tail spend projects. Research into project failure rates ranges from a low of 40% to a high of 72%, with failure defined as projects that significantly miss deadlines, budget, or quality goals. This translates into an average of 9.9% of the project budget wasted on rework or activities that do not directly contribute to the project deliverable. Causes frequently cited in After Action Reviews include:

ABSENCE OF STANDARD, CENTRALIZED CONTROLS

Projects are initiated and driven within individual departments and functions. Ad hoc processes are used to implement individual projects. As a result, the organization fails to gain significant synergies across projects related to sourcing, procurement, risk management, contract life-cycle management, ongoing monitoring, and other project-based activities.

SOW AGREEMENT THAT LACKS NEEDED SPECIFICITY

The SOW document is the basis for strong governance and oversight. It enables greater control of risk and opportunities, going beyond a simple specification of work to be completed to define approaches to achieving visibility and performance control over project personnel. Risk areas such as intellectual property protection, deliverables ownership, cybersecurity, financial crime, and more should be addressed within the agreement. In some situations, large projects will be designed as several small projects, each with its own SOW. This enables the project to fall below the threshold requiring Procurement oversight.

INCORRECT ASSIGNMENT CLASSIFICATION

Work classified as a SOW-based project when, in reality, the work requires a single individual or small group of resources that can usually be sourced by a staffing agency at a lower price point.

INCONSISTENT RATES PAID FOR SIMILAR WORK

Without a market-based rate analysis and visibility across all projects, there often is a wide range of rates paid across providers and even to a single provider working on multiple client projects requiring similar skills.

INCOMPLETE RESOURCE ONBOARDING

Project service team members who do not undergo the corporate onboarding process add to risk as these individuals have access to facilities, systems, etc.

POOR TRACKING OF MILESTONES COMPLETION

Lack of visibility into budget versus spend, and a lack of a formalized process for managing vendor performance against budget or timelines leads to payments made although the milestone has not been completed as specified.

APPLYING THE PROGRESSIVE PROGRAM MODEL™ FOR SOW-BASED PROJECT SUCCESS

When launching a new project, there are 10 critical considerations that must be addressed to ensure that the project will be delivered on time, on budget, with the promised deliverables. The project manager will be challenged to simultaneously oversee the project, select and coordinate inside and outside personnel needed to deliver the project, ensure compliance with all Corporate and Procurement policies, track spend against budget, ensure the quality of each deliverable, and provide the needed reporting, analysis and communication to update stakeholders on project progress. This is particularly challenging for tail spend projects that are initiated and driven at the department or business unit level.

ELEMENTS OF A SUCCESSFUL PROJECT



Engaging the services of a Managed Services Provider to address tail spend management challenges is the most effective path forward for organizations for whom internal expertise, investment, or approach to effective tail spend management is unclear. This enables Procurement organizations to continue to provide the focus required for large, enterprise-wide projects while being assured that tail spend projects are equally well managed in alignment with established procurement policies.

nextSource applies a structured approach to SOW-based project management - the Progressive Program Model - to deliver the flexibility needed for each specific project while specifically addressing the tail spend challenges listed above. Acting as your sourcing partner, nextSource can advise on workforce composition, facilitate contracts and Statement of Work, ensure compliance, confirm that each provider delivers against commitments, and provide the business intelligence needed to drive desired results.

Each client's needs differ. nextSource offers an extremely flexible approach that augments your internal capabilities. Acting as an extension of your internal team, we can serve as your advisor, assume responsibility for selected activities, or take full responsibility for managing your tail spend. The choice is yours.

INCORPORATING PROJECT SERVICES INTO YOUR CONTINGENT WORKFORCE MANAGEMENT PROGRAM

When incorporating SOW-based project services into a Contingent Workforce Management program, a comprehensive planning and discovery session should be initiated to evaluate your current state, and then make strategic decisions regarding the scope of management to be provided. Our efforts include:

Segmentation

- By examining current and prior projects, we will categorize spend and/or service provider types in a way that is meaningful to each client, clustering them into manageable sub-categories.
- To enable comparisons across worker types, we will develop a standard services taxonomy.

Tail Spend Analysis

- Projects staffed with teams of three or less people and/or delivered under a time-and-materials pricing agreement will be identified.
- For each of these, nextSource will assess rates charged against market-based rates as well as rates that would have been charged, if applicable, by a staffing supplier.
- Based on this analysis, nextSource will project potential savings at the transaction and spend level.
- Periodic Accounts Payable data reviews will ensure that tail spend is well managed.

Governance

- nextSource will work with our client to determine the threshold of spend to be managed by the client's professional sourcing group with the rest left to nextSource oversight within the MSP program.
- Alternatives to phase in the management of the SOW engagement spend types (i.e., terms of what might be captured first and what to bring in later, if ever) will be considered.
- nextSource will also work with the client to establish policies and procedures for issuing requests for project services, selecting and negotiating with providers, onboarding, engaging, payment authorization and processing, change orders, and offboarding. Well-established project and procurement management disciplines will yield better project outcomes and greater return on investment.
- Some client executives will be directly impacted by the project, particularly those who use Consulting regularly. Through tail spend analysis, we will identify the individuals or departments with the greatest

small project spend. These individuals will be interviewed to better understand and address their needs.

- Using data gathered during the discovery process, nextSource will generate a well-built business case for SOW tail spend inclusion within the MSP program. A formal change management initiative will minimize resistance to change and drive high levels of program adoption.
- Some companies are concerned that the use of an external Managed Services provider will discourage service provider participation. Our comprehensive change management program emphasizes benefits to those providers, including visibility and access to additional opportunities within their client's other departments, "level playing field" opportunities where competition for additional business opportunities is performance-based, and faster payment through automated invoicing and payment with on-demand access to pay status information.

Preferred Provider List

- Each project's success is directly tied to applying the right resources to the project. To eliminate the "pick your own" approach, nextSource will establish and manage a range of pre-qualified service providers with pre-negotiated rates across categories. This eliminates the need to spend extra time contracting or onboarding new providers while empowering the buying organization to tap into a wide service provider network.
- nextSource will establish or enforce standard provider criteria to include verification of experience and expertise in the needed skills category, applicable credentials, agreement to the terms established in a master services agreement, relevant references, and more. This reduces operational and legal risks associated with infrequently used providers.
- We will align existing providers to specific categories as described above, optimizing the use of performing, high-value providers.
- By matching coverage to predictable needs, we will ensure readily available, pre-qualified service providers.
- If desired, we will assist in the creation and execution of a competitive bid (RFx) process to identify preferred suppliers for most common needs.
- The customer satisfaction surveys conducted semi-annually by nextSource will include specific questions that provide feedback on the quality of service delivered by service providers.

Services Procurement Tools and Templates

nextSource will work with the client to generate the tools needed to standardize operational processes. We will create:

- A SOW template containing boilerplate content specifically designed to manage tail spend
- An RFx document for competitively sourcing service providers
- A process for evaluating RFx participants, including selection criteria, selection team identification, roles and responsibilities, and work steps
- Standard Service Provider compliance checklists and performance audit plans
- Market-based rate information

Enabling Technology

nextSource will work with the client's VMS provider to ensure that a SOW module is enabled and configured to support the unique requirements of a SOW-based project.

- The most common challenge faced by organizations while trying to segregate tail spend is "poor data quality" resulting from inconsistent data entry and an absence of data validation. nextSource will work with the client and VMS provider to determine if integration to additional systems is required.

- nextSource will ensure that the VMS SOW module is configured to effectively track spend vs. budget, progress against milestones, onboarding of all workers, tracking time (even though payment is based on milestones rather than time invested), effective invoicing, and more.

SOURCING SERVICE PROVIDERS FOR A SOW-BASED PROJECT

- When budgets are based on estimated hours rather than clear requirements specifying the roles and deliverables of each team member, projects can extend indefinitely. When a new project is initiated, nextSource can conduct a rate evaluation, comparing rates paid under the SOW vs. rates paid if the worker(s) were transitioned to a staffing agency under a staff augmentation agreement.
- As part of the requisition process, nextSource can issue parallel requisitions – one for a SOW-based engagement and another for a staff augmentation engagement – to determine the best option for sourcing the needed resources. This also drives competitive rates.
- nextSource can lead or support the sourcing effort, developing Rfx documents that uncover needed competencies, defining provider selection criteria and scoring mechanisms, executing the Rfx process, and evaluating and shortlisting service providers for each project.
- nextSource can invite multiple qualified providers to bid on a common scope of work. By leveraging competing bids nextSource can negotiate improvements in price and quality.
- nextSource can track bids-contract-actuals to continuously improve category and service provider strategies.

CONTRACTING WITH SERVICE PROVIDERS FOR A SOW-BASED PROJECT

Great talent will not deliver great performance without a common understanding of the assignment. The Statement of Work (SOW) serves as the project's blueprint, communicating the detailed assignment to all project personnel. nextSource can assist by:

- Verifying that a Statement of Work has been established with each project team.
- Reviewing SOWs to ensure that they contain a well-defined scope of work including work location, period of performance, deliverables schedule, budget and payment model, milestone acceptance criteria, and other terms and conditions.
- Establishing service level agreements.
- Verifying that expected commercial terms have been incorporated into contractual agreements.

ADMINISTRATION AND COMPLIANCE OF A SOW-BASED PROJECT

Risk levels can be mitigated by nextSource. For example, nextSource can:

- Conduct a 1099 classification analysis for all one-person service providers, identifying those who would fail to comply with IRS and State standards for qualifying as independent contractors. When that occurs, we will transition the worker to a payrolled W-2 employee of nextSource or to a contract worker employed by a staffing supplier.
- Apply and enforce procurement process and policies and applicable external regulations.
- Ensure that all onboarding requirements have been successfully met, eliminating risks associated with prior criminal activity, drug-related issues, and non-compliance with government regulations and corporate policies.
- Assist the project manager in verifying that payment is only authorized for completed milestones.
- Ensure that system and facilities access has been terminated to all project services personnel at project completion.

Operational enhancements will reduce costs and cycle times and minimize manual effort. This includes:

- Conducting regular project status meetings. Frequency will be determined by the client.
- Ensuring timely and accurate payments if nextSource is holding the contractual agreements with each service provider. Conducting quarterly program compliance and optimization reviews as part of the established MSP Business Reviews.
- Administering the VMS SOW module, including Level 1 usage support.
- Re-engineering inefficient, non-value-added steps. The application of total quality management techniques such as RCA (Root Cause Analysis) will be used to identify and test preventive controls.

Greater insight and control require accurate and timely reporting, predictive analysis to recognize trends, and quantifiable measures of success expressed in Key Performance Indicators (KPIs). nextSource will:

- Work with the client to include in the MSP Service Level Agreement - a set of metrics to measure progress of tail spend management. This will track efficiency and identify areas of improvement.
- Deliver reports and analysis of spend and performance regularly and provide data and trend analyses, including pricing benchmarks.
- Ensure that reports clearly indicate the correlation between work activity, payments made, and available budget.



BENEFITS OF MANAGING PROJECT SERVICES TAIL SPEND

Highly Qualified Service Provider Personnel

- Pre-screened service providers who meet all criteria
- Competition across providers for assignments
- Increased diversity of the service provider base
- Increase in user satisfaction score of up to 20% over a 3 year period
- Improvement in supplier relationship management score

Risk Mitigation

- High Contract standardization and compliance
- IC Classification assurance
- Worker onboarding compliance
- Increase in SOX compliance
- Increase in MWVDBE goals compliance



Cost Savings and Avoidance

- Tail spend savings in excess of 20%
- Extension of procurement controls to 'tail spend' projects
- Identification of work that can be performed by agency contractors at a lower price point
- Market-based rates
- Reduction in transaction costs

Operational Effectiveness

- Standardization of processes across business units
- End-to-end execution support
- Increased compliance with the procure-to-pay process
- Reduction of transactions

Projects can be complex. However, by working together to develop a crystal-clear upfront understanding of project goals, a realistic budget, a detailed project plan, and an efficient process for linking effort and progress to payments and budget, Companies can potentially realize significant savings while achieving project goals within the established timeframe and budget!

GENERATING REAL SAVINGS THROUGH TAIL SPEND MANAGEMENT: A CASE STUDY

THE CHALLENGE:

When market dynamics forced a leading F1000 company to rapidly introduce online, self-service capabilities, it depended on third-party service providers to deliver needed IT, project management, and marketing offerings. These firms were selected and managed by individual department heads. The result: inconsistent contractual terms and rates for similar work. As importantly, the company did not know who was working, how many workers were engaged, where they were working, or what they were doing. nextSource was retained to address their project management tail spend.

The nextSource analysis identified:

- 10 projects for which there was no established Statement of Work specifying activities, deliverables, timeframes, nor financial penalties for non-performance.
- 60 project service teams consisting of one or two people.
- Three major providers that were subcontracting the work under a T&M agreement.

THE SOLUTION:

- Projects were sorted by category and the client's job titles were aligned with standard taxonomies to conduct a comparison of actual to market-based rates. Potential savings, tied to required actions, were presented to the client for consideration. The client elected to have nextSource establish a corrective action plan to focus first on issues 1 & 2 listed above, followed by the third issue in a subsequent phase.
- Working with the client's Procurement group, a customizable template containing standard language for all tail spend SOWs was proposed. Statements of Work were established for the 10 projects, and others were reviewed for alignment with the desired terms. The client determined which SOWs would be modified based on level of project completion and other factors.
- Sourcing and negotiation processes for smaller tail spend projects were established. They were designed to ensure ease of use for the hiring managers.
- A major change management initiative was launched to ensure complete engagement by service providers and client users.
- A 1099 classification analysis was conducted on all personnel within project services teams consisting of three or less members.
- The work to be performed in all projects with time-and-materials-based payment structures was examined. Depending on the nature of the work, either the agreement was rewritten to be fixed-price/milestone-based, or the work was transitioned to a staffing agency at a lower price point.
- A formal onboarding process was established for all external workers, regardless of whether they were directly billable. This included verification of right to work, Visa handling, background checks, drug tests, and more.

THE RESULT:

- In the first six months, the client realized cost savings of \$1 million and estimated cost avoidance of an additional \$800K.