

US Companies Can Reap the Benefits of Unit Rate Pricing and Business Service Catalogs

Services, collectively speaking, represents one of the largest and most undermanaged non-payroll spend categories (ranging from plant/equipment maintenance services, large turnaround and capital intensive projects to IT operations outsourcing, with a large number of categories in between depending on the organization). In the aggregate, organizations in the US spend over \$1T per year, but procurement groups are generally not equipped (with adequate resources, expertise, approaches and technologies) to fully manage non-contingent workforce services spend categories. So, it is necessary to choose one's battles.

Gaining visibility into services spend is a fundamental step. But even organizations that have made progress in gaining visibility into swathes of services spend are faced with the question of how to optimize business spend and outcomes and de-risk engagements/transactions with suppliers. One sub-question is: Where to focus to get the most bang for the buck? Other sub-questions include: What approach to take? What technology tools and what expertise are needed?

One fresh approach is the use of unit-rate (versus time and materials) service contracts in conjunction with service catalog technologies.

Time & Materials

vs.

Unit Rates



Time & Material Contracts are set up to **allocate billing to contractors based on the time & materials** incurred over the course of a project. Time & Material contracts, used for many different kinds of services today, **often require the use of quotations and surveying before the work can be performed.**



Unit Rate Contracts utilize pre-negotiated costs per a unit, such as hour, gallon, each, etc., to bill for work performed. Unit rate contracts **rely on the quantity of the unit rate** to be entered for billing and often **does not require the quotation and surveying components of a project to take place for the work to be performed.**

Systems that manage unit rate service contracts can:

- Stabilize and enable control over the costs of the services themselves
- Increase the efficiency and speed of the purchasing process
- Improve internal customer satisfaction and productivity

The effectiveness and ROI of this approach has been demonstrated in the IT setting where it is now a best practice globally. In Europe, many organizations have extended this approach beyond IT services to other business services, with considerable success in reducing the cost and time associated with buying services. US companies should consider following suit.

Benefits of the Approach

There are 3 main types of benefits: Spend Visibility/Management, Purchasing Process Efficiency and Internal Customer Satisfaction/Productivity.

Spend Visibility/Management

- The process of standardizing services, locking in unit pricing with vendors and using a catalog system ensures negotiated prices and cost control for fixed deliverables and discourages misunderstandings of scope.
- Rich data catalog system enables visibility into a range of factors underlying spend (including detailed usage, service quality, etc.) as well as tracking of trends (e.g., volume, cost per activity, etc.).
- A catalog system also allows for benchmarking of cost, time and frequency for recurring services (e.g. maintenance tasks), intelligence that might trigger vendor re-negotiations, etc..
- The transparency and triggering features of a catalog system also support contract compliance and governance and drive process automation.

“ Services procurement has been traditionally ignored from a process optimization and a technology standpoint. But companies have a great opportunity to realize double digit savings through better control and spend transparency with unit rate contracts. ”

*Ralf Dillmann, Global Leader
Sourcing & Procurement,
BearingPoint*

Purchasing Process Efficiency

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T&M Contract



Unit Rate Contract



- Elimination of process steps not only drives out costs and reduces time in the purchase to pay process, it also shortens time-to-value.
- Many suppliers in the US are already using a Unit Rate setup internally and changing their catalogs to reflect the common client setup of time and materials. Switching to a Unit Rate setup can save the supplier time and effort in this regard.

Internal Customer Satisfaction/Productivity

- Greater clarity, reduced administrative hassle and overhead, less project oversight, more reliable outcomes and faster time-to-value lead to higher internal customer satisfaction.
- All these benefits also translate into potentially higher internal customer productivity, fewer missteps and remediations and more agility.

The Right Technology

Designing and establishing effective unit rate service processes is fundamental to the successful launch of this buying model. But executing it absolutely requires fit-for-purpose technology to support standard purchase-to-pay processes and workflows, purchasing policies/rules, rate-based service catalogs and demand, category, supplier performance and spend analysis.

There are various avenues to suitable technologies, including:

- **Purpose-built solutions**

One example of such a solution, AES-32 offered by NDH, specifically addresses external services in the industrial sector (pipeline construction, electrical engineering, process control technology, construction, etc.) based on standard service and standard material unit-rate catalogs. AES-32 integrates with customer and supplier ERPs. NHD has around 5,000 installations globally and supports many major brands.

- **Generic e-procurement solutions**

The majority of e-procurement solutions enable service items in their e-catalog capabilities. The extent to which unit-rate pricing is or can be supported may depend on the solution. In some cases, unit rate contracts/pricing approaches may simply not have been widely implemented (e.g., in North America vs. Europe). In any case, catalog options in e-procurement solutions may provide a basis for implementing a unit-rate contracting and catalog approach.

- **Standalone e-catalogs solutions**

The same qualifications applying to generic e-procurements apply here.

Regardless of the path that makes sense for a given organization, the right technology is essential to executing a unit-rate contracting and catalog approach to services.

“ The operational efficiency achieved with unit rate catalog technology can surpass the savings typical of indirect source-to-pay technology applied to indirect materials spend. ”

*Dietrich Pankratz, US Operations
Consulting Leader, BearingPoint
USA*

What Does It Take?

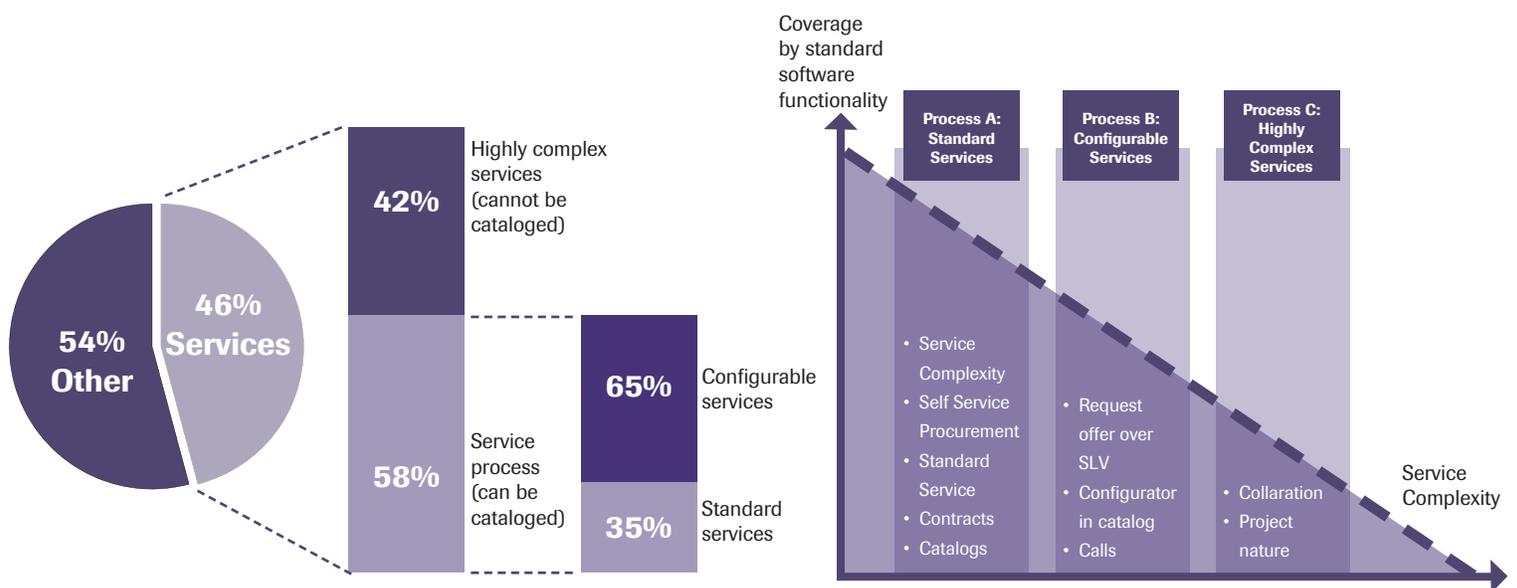
For most US-based companies, unit rate pricing and self-service catalog purchasing of standardized, externally-provided business services means entering new territory. This has many implications for how procurement organizations will approach it and what will be required.

While there will be challenges (e.g., changing internal mindsets and behaviors, etc.), the timing may be good. Examples of how unit rate pricing and service catalogs are being used successfully can be found within IT organizations and a small number of petrochem companies on the US Gulfcoast, and cases of the practice and effectiveness of the approach can also be found among European companies. Furthermore, the Enterprise Services Management (ESM) model applied to non-IT business services may help to support a shift in how internally-provided services are managed and consumed (and thus a way of looking at externally-provided services that can be standardized).

Here are several steps for proceeding in the direction of unit rate pricing and self-service catalog purchasing of standardized, externally-provided business services:

- **Spend analysis and internal customer outreach** to identify higher volume, repeat services that will lend themselves to standardization. The main criteria is being able to delimit services into units which can be uniformly priced, ordered and delivered.

Project Example:



- **Business case demonstrating program savings** to gain the buy-in of senior executives and other managers in the organization. The more case-based and concrete, the better, identifying successful cases, with cost/benefit analysis, if possible.
- **Communication to win over service suppliers** with the prospects for spend consolidation, lower overheads and accelerated cash flows.
- **Selection and implementation of a catalog system** that can be used for purchasing of unit-priced services. There may be few 3rd party purpose-built catalog solutions for standardized services, but potential solutions may be found in some e-procurement and EMS solutions with catalogs designed to support both goods and services.
- **Design of a practical methodology for how unit costs formulas get derived** in economic terms (cost-based, market-based, etc.) and in terms of appropriate units that will be adequate across case variations, volume levels, locations, etc.
- **Establishment of necessary/appropriate legal instruments** that can support unit rate pricing models for standardized services purchasing that is mostly unsupervised on a transaction basis. Supplier contracts will need to be restructured/extended, or even replaced.
- **Plan for catalog implementation and purchasing process** for initial service categories that includes beta or pilot phase to organization go-live and for expansion of categories in the future.
- **Configuration of an effective team to execute all of the above** is mentioned last, but should be one of the first things considered. Because this is new territory for most organizations, the team must contain members that have experience with developing/standing-up these sorts of programs.

It should be noted that assistance with all or part of such an initiative is available from some consulting firms. BearingPoint, in particular, has developed deep experience assisting global companies with such initiatives.

Conclusion

Businesses increasingly initiate and complete tasks and projects within shorter timeframes. Inefficient processes translate into overhead costs and are wasted when they actually can be avoided. Digitally-enabled processes for purchasing services are often incomplete or lacking, and increased visibility on and control over services spend is aspired to, but often seems too overwhelming.

Tackling higher volume, repeat services that lend themselves to standardization by using unit-rate contracts and e-catalogs could be a way to cut the problem down to size, contain spend and supplier costs, increase efficiency and speed in the purchasing process and improve internal customer satisfaction. It is working for many large organizations across the globe, so it is certainly worth looking into.