



Gladwyne Software Surety Presents:

Best Practices in IT Contracts

A n E x e c u t i v e S e m i n a r S e r i e s





Agenda

8:30 AM

Introduction

Michael McFadden, SVP, Marsh, Inc.

8:45 AM

Using the Contract to Transfer IT Risk

Chris Panaro, Managing Director, Gladwyne Software Surety

9:15 AM

Legal Considerations & Implications

Dean Schwartz, Chair of Technology Practice, Stradley Ronon

9:30 AM

Q&A Session with Panel

10:00 AM

Summary

Michael McFadden, SVP, Marsh, Inc.

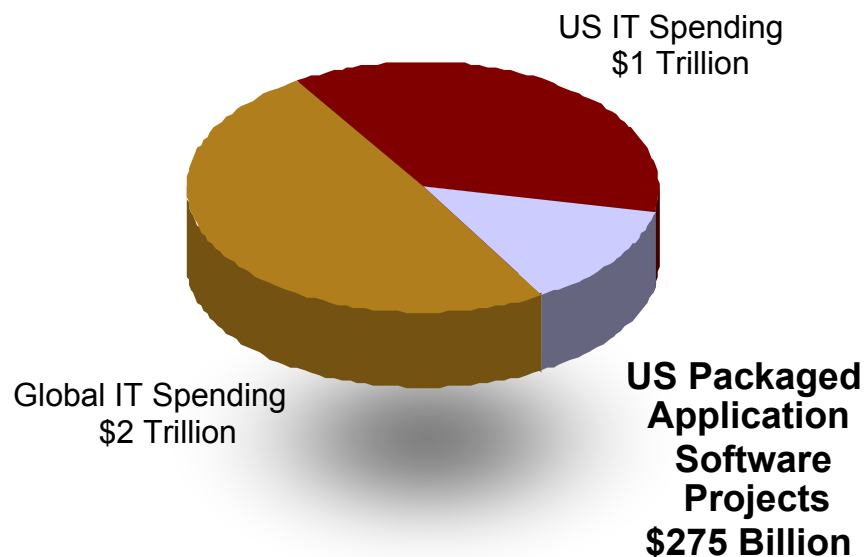


Panel Introduction

- **Mike McFadden**
SVP
Marsh, Inc.
- **Chris Panaro**
Managing Director, IT Contracts
Gladwyne Software Surety
- **Dean Schwartz**
Chair of Technology Practice
Stradley Ronon
- **Dan Brennan**
President & COO
Gladwyne Software Surety



\$1 Trillion Spending on IT in US - 2002



- **US corporate spending on packaged application projects will exceed \$275 billion in 2001**
- **Growing at over 20% annually**
- **Segment maintains a high risk profile with buyers**



Most IT Projects Fail

28% Successful

- On time; on-budget; functionality as originally specified

49% Challenged

- Project completed, but over-budget, over-time, and less functionality than planned

23% Failed

- Cancelled before completion



SOURCE: The Standish Group, 2001



The wired economy has increased the corporate perils of failed IT projects

Hershey Foods	<ul style="list-style-type: none"> • \$150 million in lost sales for the quarter • 16% drop in 3Q earnings per share
Nike	<ul style="list-style-type: none"> • Shipping cost from \$.75 to \$8 • 34% drop in earnings per share
Snap-On	<ul style="list-style-type: none"> • \$50 million in lost sales • 40% increase in operating costs
Tri Valley Growers	<ul style="list-style-type: none"> • Company Bankruptcy • \$20 million in damages
FoxMeyer	<ul style="list-style-type: none"> • Company bankruptcy • \$1 billion in damages
W.W Grainger	<ul style="list-style-type: none"> • \$19 million in lost sales over two quarters • \$22 million decrease in annual profits

SOURCE: Top 10 IT Failures: Damages and Losses, Computerworld



Many companies have taken steps to mitigate IT risk



Airgas



ACCU WEATHER

QVC

SWEDISH MATCH



citi

THE IMMUNE RESPONSE CORPORATION



severan





Summary

- IT risk not adequately addressed
- Enterprise risk management has not kept up
- Buyers generally address risk several ways:
 - Contract
 - Self-insure / contingency budgeting (average 50% added)
- Today's focus is on addressing risk by controlling the contract between the buyer and their vendors



Using the Contract to Transfer IT Risk

Chris Panaro

Managing Director, IT Contracts

Gladwyne Software Surety



Contents

- Overview of Project Life-Cycle
- Inventory Key Contracts
- General Approach
- Specific Approach
- Real World Examples
- Key Contractual Duties



Typical IT Project Life-Cycle



Requirements
Business Case

SW Selection
& License

Integrator RFP
& Selection

SI Contract

SOW 1

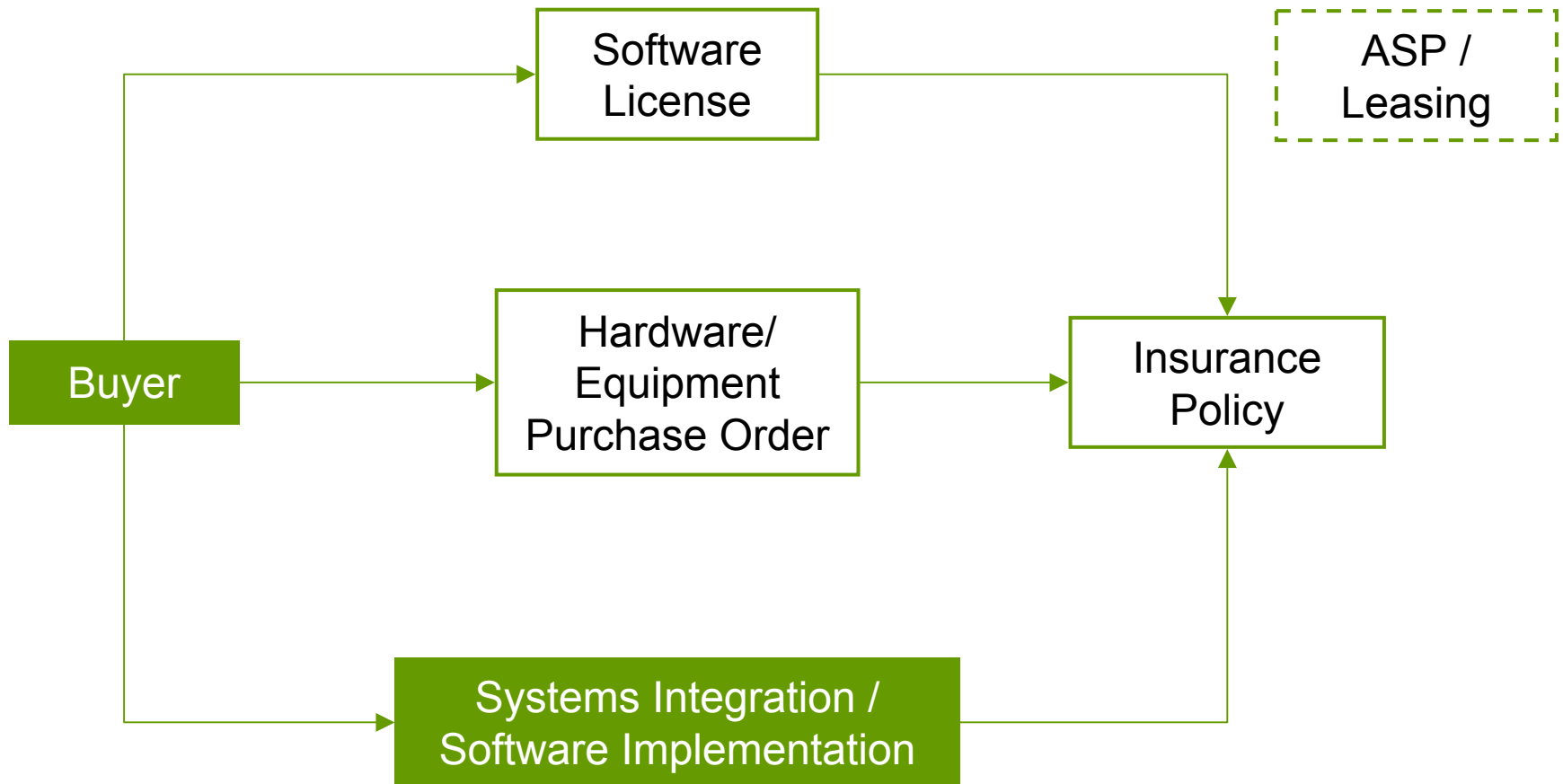
SOW 2

Blueprint

Live
System



Typical Contracts Involved





General Contracting Approach

- Don't disconnect contract from sales and proposal promises / documentation
- Consider the contract the most critical component in Project Management
 - Clarity of duties, time schedules, deliverables, reporting, methods for scope change, acceptance criteria
- Consider and accommodate turnover in staff
 - Write in plain English / consistent terminology (Phase x)
- **Put the buyer in control of the contract document and negotiation process**
 - **Incorporate contract template into RFP / process**

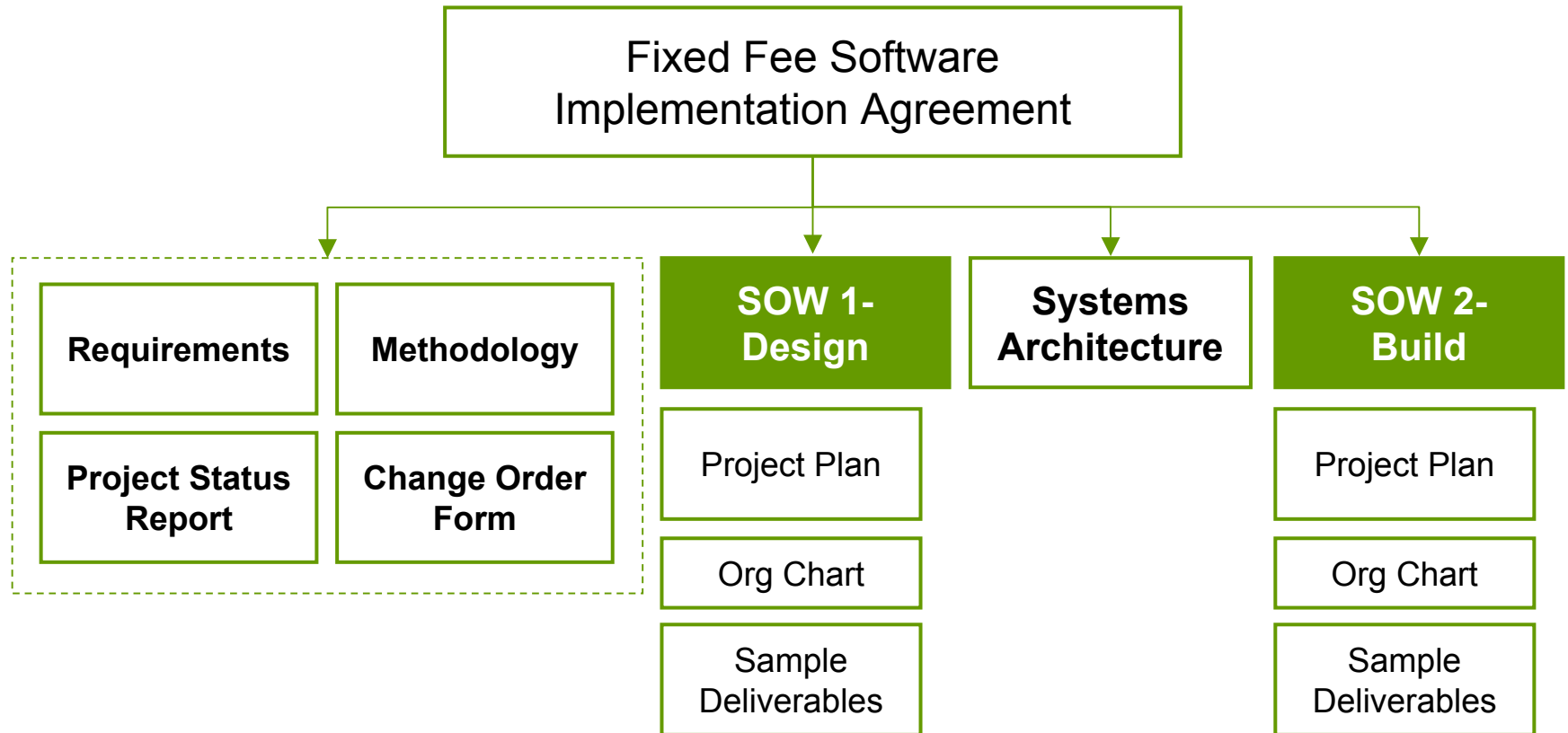


Typical vs. Best Practice

	Typical	Best Practice
Controller of Contract Process / Forms	SI	Buyer
SI Accountability	No	Yes
Contract Used to Guide Project Management	No	Yes
Fee Formula	Time and Materials	Fixed Fee
Payment trigger	Monthly invoice	On acceptance of deliverables (earned value)
Withholding of fees	None	20% until completion
Writing style	Complex jargon	Plain English
Binding impact of sales and proposal process	None	Binding (as attachments to contract)



IT Contract Structure





Statements of Work (SOW)

- Roles and Responsibilities (Client and Contractor)

Role	Individual	Responsibilities	Time Requirement
Contractor -Business Team Lead	Karl Johnson	<ul style="list-style-type: none"> • Work with the Client's resources to develop work-flow diagrams mapped to SAP R/3 functionality to prioritize such functionality for implementation in Phase 2 from data, workflow and screen perspectives. 	<ul style="list-style-type: none"> • All of Phase One • 100%



SOW - Scope of Services

- **Typical**

- “Consultant will assist customer in implementing the standard functionality of the Oracle application, subject to the following assumptions, for which Customer shall pay Consultant an hourly rate of \$275 for time spent by each resource assigned by Consultant, plus materials, taxes and expenses.”

- **Best Practice**

Services to be Performed by Contractor	Deliverable	Due Date	Acceptance Criteria	Att.	Sign-off	Payment upon Acceptance	Holdback (20%) until Project Completion
<ul style="list-style-type: none"> • Contractor shall develop a Change Management Plan to guide the Project team in managing and effectuating the Project Charter 	Change Management Plan	3/2/01	Plan shall conform to the format of the attached sample and provide the level of detail necessary to effectively communicate plans for training, communications, and overall cultural acceptance of the Project.	B-1	J. Jones, VP of HR	\$50,000	\$10,000



Fees / Payments

- Fixed Fee
 - Validate against prior experience with comparable projects
- Payment tied to achievement of milestones / deliverables
- Withholding (20%) until project completion
- Reduction for failure to deliver interim deliverables on time (x% per week)
 - Make up/recover if go-live date is on time
- Expense reimbursement capped between 12 – 15% of total project cost



Key SI Duties

- **Methodology**
 - Require SI to follow a standardized, licensor approved implementation methodology (attached to contract as Exhibit)
 - Requires minimal interruption if a replacement is required to take over the project (blueprint for contractor to follow)
- **Project Status Report**
 - Affirmative duty to submit specific report format
 - To a specific person / committee
 - At a specific time interval (once each week)
- **Scope Change Management**
 - Duty to use specific form (attached to contract)
 - Identify person with authority to approve
 - Impact of change to be captured in form



Client Duties

- Clarity is crucial to avoid unsubstantiated blame being placed on client for project delay or failure
- Avoid use of “assumptions”
 - Convert to a duty of one party
- Understand consequences of client failure to perform
 - Entry of change order adjusting SI due dates and payment structure
- Typical Client Duties:
 - People / Resources / Sponsorship / Decision making
 - Facilities / War Room / Equipment / SW
 - Data / access to systems / completion of technical tasks



Take Aways

- Put the buyer in control of the contract document and negotiation process
 - Incorporate the Buyer's contract template into RFP process
- Consider the contract the most critical component in Project Management
 - Clarity of duties, time schedules, deliverables, reporting, methods for scope change, acceptance criteria
- Payment tied to acceptance of milestones / deliverable
- Holdback / withholding (20%) until project completion



Legal Considerations & Implications

Dean Schwartz
Chair of Technology Practice
Stradley Ronon



Contents

- Warranties
- Intellectual Property
- Dispute Resolution



Warranty

- 3 Tiered approach
 - Services
 - Staff
 - Deliverables



Services Warranty

- Services
 - Performed in a Professional Manner
 - Will Result in a System Operating within User's Environment per the SOWs / requirements



Staff Warranty

- Sufficient staffing to timely perform the services
 - i.e., number of bodies
- Each staff person will have skill, aptitude and experience to perform the services



Deliverable Warranty

- Each deliverable will comply with specifications as to:
 - Form
 - Content
 - Performance
 - Functionality



Warranty Period

How Long?

Acceptance	30 Days	60-90 Days	120 Days
Starts Here	Old Standard	New Standard	Try for



Why is my system not working?

**Software
Licensor**

**Systems
Integrator**

FINGER POINTING

Licensor
Responsible for
Software

Vs.

SI Responsible
for Integration &
Implementation



Answer

- Clear written commitment on part of software Licensor and SI to identify the reason for the malfunction
- Put this in both contracts
 - Software license & SI agreement



Intellectual Property

- IP Warranty
 - No infringement
 - No time limit



Intellectual Property in Systems Integration

Who owns What?

SI Tools

Vs.

**Deliverables
“Work for Hire”**



Intellectual Property in Systems Integration

Who owns What?

Tools	SI	Methods, concepts, ways of doing the integration
	SI	IP existing before the contract and skill / expertise learned on user's job
Work for Hire	Buyer	Code / written material prepared by SI for user



Mechanism(s) for Dispute Resolution

- Desirability of an alternative to litigation
- Options
 - Negotiation
 - Mediation
 - Arbitration (various forms)
 - Combinations of the above
 - Partnering (AAA Model)



Mechanism(s) for Dispute Resolution

- Advantages
 - Control of the parties over the process
 - Speed of the movement
 - Privacy
 - Availability of win/win outcomes
 - Cost efficiency

It is always much easier to take advantage of these options when they are built into the Agreement



Questions & Answers

A Panel Discussion



Panel Contact Information

- **Mike McFadden**
SVP
Marsh, Inc.
 - (215) 246-1085
 - Michael.mcfadden@marsh.com
 - Marsh.com
- **Chris Panaro**
Managing Director
Gladwyne Software Surety
 - (610) 491-8181
 - cpanaro@itsurety.com
 - ITsurety.com
- **Dean Schwartz**
Chair of Technology Practice
Stradley Ronon
 - (215) 564-8001
 - dschwartz@stradley.com
 - Stradley.com
- **Dan Brennan**
President & COO
Gladwyne Software Surety
 - (610) 491-8181
 - dbrennan@itsurety.com
 - ITsurety.com