

Scio's Contract Analytics

Market overview

As businesses have grown more complex, developing increasing numbers of complex commitments and obligations to customers, partners, and suppliers, the use of contracts has grown substantially

Around 80% of business to business transactions are governed by contractual agreements, and nearly half of every dollar that a company earns is spent on goods and services provided by external suppliers. The ratio is growing, as companies across all sectors are moving to drive out cost and concentrate on core competence by increasing their use of outsourcing, licensing, and various innovative forms of alliance.

Recent studies point at ineffective Contract Management (CM) as a major source of excess cost and lost revenues:

- In the US, \$153 billion are lost every year in missed saving opportunity in supplier contracts alone - 2 to 4 percent of contract value. *[Aberdeen]*
- Companies could realize savings that equate to 2% of total annual costs by eliminating inaccuracies and non-compliance through contract automation. *[PWC]*
- Enterprises could experience a potential reduction of 40 basis points in hard and soft costs by using contract management software. *[Goldman Sachs]*

Contract related costs make up a significant part of total costs :

- By year-end 2008, in 80 percent of enterprises, the cost of contract management will have doubled from the 2002 costs of 2 percent to 4 percent of SGA. *[Gartner]*
- A typical Fortune 1000 organization spends as much as 100 basis points of their revenue to manage buy-side contracts and 25 basis points of their revenue to manage sell-side contracts. *[Goldman Sachs]*

Yet, CM is still one of the least automated areas. A recent survey conducted by IACCM (International Association of Contract and Commercial Managers) shows that:

- 51% of the responders reported no automated contract management process.
- 38% of the responders reported a partial system, of which many reported this as an internal tracking mechanism, often built on a database such as Access, and only 16% of those had any links to other systems (ERP, CRM, SRM, Financial).

This is hardly surprising, as CM is a very challenging area - the typical Fortune 1000 company now maintains 20,000 to 40,000 active contracts (up 20% in the last 5 years), each with a series of interdependent terms, pricing variables, payment terms, and service level requirements. *[Institute for Supply Management]*

Recent CM automation implementations show tremendous savings and rapid ROI. A recent AMR research shows that well designed implementation delivered 150%-200% ROI in the first year.

The market has begun to realize the potential. A recent Aberdeen comprehensive survey of 106 companies from all sectors shows that more than 80% of the Supply-chain executives view the effective management of supplier contracts as “very important” or “critical” to their companies’ overall success. Another recent survey of 100+ companies, published in the Journal of Contract Management, shows that the area of Contract Management was keeping contract management professionals awake at night in 75% of the companies surveyed. Tighter regulations, like the 2002 Sarbanes-Oxley act have also contributed to the recent focus on CM.

And indeed, the CM market is poised for rapid growth:

- Gartner: Enterprises will be spending more than \$20 billion a year on software and services for contract life cycle management by the end of 2007.
- Goldman Sachs: The market for contract management software will hit \$3.1 billion US by 2005 as organizations begin to understand the potential and ROI of such solutions.

Currently available tools provide repositories, support access to contract documents, ensure clauses are present, and alerts can be set for events in the document, but the tools *provide poor, or no support for what the contract document means.*

Current vendors depend on a massive transformation of contracts into *templates* - rigid structure with predefined data fields that can be associated with simple rules and conditions. Missing the forest for the trees, this representation doesn’t capture the essential meaning of a contract and the relationships between its terms, conditions and figures, nor can it practically facilitate inter-contract dependencies.

Loading of legacy contracts

According to PWC, loading a single contract into a CM system by a trained worker could take 2-3 hours. This means that loading 100 contracts could take up to 2 months, and 1000 contracts over a year. Loading 5,000 contracts, a conservative number, could cost \$400K - \$900K (using employees) to \$1.25 - \$3.75 million (using consultants). These costs are not included in the implementation and integration costs. Considering the average 20,000 to 40,000 contracts active in a Global2000 company, loading contracts into CM systems could be quite expensive and demanding, way beyond implementation costs.

As similar case exists in the Real Estate market, where large amount of Lease Contracts exists and have to be managed and reviewed.

Current CM vendors offer some assisting tools, or contract digitizing services, however, the process still requires a laborious, painstaking effort of breaking up the contracts into separated pieces and plugging them into templates

Real Time Intelligent Compliance Tracking and Monitoring

Current CM tools offer compliance mechanisms that can prevent off-contract purchases by providing access to the relevant contract documents, notifying people about discounts, etc'. However, they miss significant saving potential, not being aware of the meaning in the business context. For example, a procurement officer interested in buying 500 Ducts can get them from supplier X, but, having a sophisticated CM system he should be informed that if he can wait a week, he can get it from Supplier Y for 20% less, or that if he thinks he will also need Takeoffs and Grills (typically used together with Ducts for AC systems), he can get it all together and save 15% due to purchase volume and cheaper delivery.

Real time compliance management is critical, because in many cases, revenues lost because of bad decisions cannot be recovered, and even if they can, it involves a tedious process and additional costs.

Studies suggest that using sophisticated CM tools can results in 50% improvement in compliance, even without optimization. Intelligent procurement optimization could conservatively add 20% in cost savings.

Enter Scio Systems

Scio extracts the complete logic of the contracts and incorporates it into its Analytical Engine. The system captures the full meaning of contracts in a fully automated process, directly from the contract document. Scio combines its capabilities for free text understanding, data mining, and constrain and probabilistic reasoning to provide a powerful and superior CM tool.

Main advantages of Scio systems are:

- **Automatic loading of contracts**
- **Real time Intelligent Compliance Tracking and Monitoring**
- **Monitor and analyze risk transfer between contracts**
- **Identify risks from contracts**
- **Simulation engine**
- **Dynamic analysis of contracts, policies and regulations**