Sole Source

Sole Source – an efficient procurement and renegotiation approach resulting in a contract based on virtual competition.

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When it is time to renegotiate an outsourcing contract, a minority of the clients choose to initiate a selection process involving more than one supplier. Hence, the majority of the contracts are renegotiated with the incumbent supplier.

An advantage with renegotiating with an incumbent supplier is to avoid cost, effort and risk when making the transition to a new supplier. Another advantage is to avoid the time it takes and the cost involved with a long selection process. A disadvantage is that there is a risk that you can’t benefit fully from what the market has to offer and that prices and contract terms might be less attractive.

There is often a pressure on the person responsible for the contract, often living with constant expectations on reducing cost and change, to go out in a full-scale competitive selection process. The perception of the existing supplier is often that they have not performed as well as expected and that they have not been as innovative as was hoped for and one might think that it is possible to get a better price elsewhere. There can also be a de facto policy in the organization that important deals are made in full competition, i.e. you have to invite several suppliers in the bidding process. It can be perceived as the only way to get lower prices and to have a supplier that is proactive and really interested in the well-being of the client.

For a client, not really keen on changing the existing supplier and who would rather prefer to continue building this relationship, a sole source process appropriately used can be a very good alternative. However for us as advisors to be able to recommend this approach, a number of criteria need to be met.

But using the methodology we call Sole Source, a renegotiation process with an existing supplier, or a procurement process with one selected supplier, can be managed in a way to create the same bargaining power as a procurement with several suppliers involved.

A sole source process can also be relevant when redefining a current ongoing outsourcing relationship, e.g. related to new prerequisites for the client or the development of new technologies and services. Then, a new contract can be signed for a new period, but based on completely new conditions.

SUPPLIER SELECTION – WHEN IS SOLE SOURCE APPROPRIATE?
There are basically three different ways of designing a supplier selection process in order to end up with an outsourcing contract:

1. Fully competitive
2. Comparative
3. Sole source

FULLY COMPETITIVE
A fully competitive supplier selection process is characterised by several suppliers bidding in an RFP process (Request For Proposal), where extensive documentation with requirements and conditions are sent out to a number of suppliers. Then, quite often a selection of these suppliers end up on a shortlist for further evaluation. Finally one of these suppliers is down-selected for final negotiations.

The model is the most common and a standard procedure for most procurement departments.

COMPARATIVE
The comparative supplier selection process is characterised by a few selected suppliers (often between two and four suppliers) who often together with the client in a workshop format develop client-specific bids. Typically one of these suppliers are down-selected for final negotiations.

SOLE SOURCE
The sole source process is a procurement process characterised by the client only inviting one selected supplier to bid. There is no selection process and it is a streamlined process aiming at reaching a contract including competitive prices and terms.
SOLE SOURCE
A single selected supplier

• No selection process
• For all parties, least amount of cost and time
• Strong relationship with the supplier to be selected is required
• Advisor support to ensure negotiation power and implementation

The sole source approach can be recommended and is mostly applicable when at least a couple of the following criteria are applicable:

✔ Sourcing expertise
   If the client is an experienced buyer or outsourcing services, with a good knowledge about what is offered on the market and the existing suppliers and/or if third party advisors are hired.

✔ Relationship
   If the client has a good existing relationship to the supplier in mind and the supplier on a strategic level is well enough aligned to the business goals of the client.

✔ Few candidates
   If there are few real candidates due to e.g. geographical requirements or the services in scope being so complex or emerging that there are only one or a few candidates to be considered good enough and competitive.

✔ In fact only one supplier
   If the services are continuously changing to a degree where there is in fact only one potential supplier.

✔ One supplier with a big competitive advantage
   If one supplier has such a competitive advantage, technological or operational, of such a value to the client that no other suppliers can be expected to compete.

SAVE TIME AND MONEY
There are several advantages with the sole source process, for the client as well as for the supplier. The procurement process is often more suitable when renegotiating existing agreements, rather than for the first generation of outsourcing (when for the first time outsourcing something that has been done in-house, possibly including staff transfer), since the sole source process is more appropriate for a mature buyer and a good existing relationship between the client and the supplier.

The advantages often mentioned about sole sourcing generally has to do with saving time and money, since it is a very time-efficient process, both when it comes to actual calendar time as well as the number of man-hours needed. To save time and money are normally two important motives for outsourcing and when choosing a sole source approach rather than a fully competitive approach this effect becomes even larger.

When outsourcing something for the first time, the main focus when the contract is to be signed often is on the price. When later renegotiating contract issues like governance and how to co-operate with the supplier often become more in focus. Sometimes the relationship is really working poorly and a supplier with e.g. a higher degree of innovation partnership and well-structured processes are highly requested. But when it doesn’t work properly it is often the result of poor governance from both the client and the supplier. The client could be very keen on finding a new supplier, but is often intimidated by the costs for transition and the amount of work required. For these kind of clients, the sole source process is really worth considering and can save a lot of time, money and effort.

For clients with a good relationship with a motivated supplier it can be a good way to raise issues about price and contract terms as well as to put some pressure on things like improved documentation, innovation, co-operation etc. At the same time you avoid the risk of distrust and uncertainty which an open competitive process can lead to. By bringing these things up on the table so that the supplier can be guaranteed an exclusive negotiation for a new contract, it can rather be viewed upon as an opportunity.

In some areas there is a chance that prices might have changed dramatically over the last few years, which can be an important driver for renegotiating the contract. Then you might want to renegotiate without adventuring a high delivery quality and a good relationship with a high degree of commitment from the supplier. In such a case it could also be an idea to review the price and quality without even involving the supplier, but possibly by involving a third party advisor, in order to get an indication of the current market price of the services in scope.

It is also common to start by outsourcing just a few processes or part of an environment and at a later stage extending the scope, when the trust for the supplier has grown. In such a case a sole source process is typically often chosen.
Through a well managed sole source process a renegotiation with a supplier can be done in a way that for both parties mean a renewal and a revitalisation of the co-operation.

**BENEFITS AND CONCERNS**

As we have described earlier there are some criteria that should be met for the sole source process to be relevant and applicable.

The potentially reduced bargaining power is the most obvious risk with the process. This is mitigated through ensuring a very good market knowledge and/or using a third party advisor who can contribute with that. An advisor who is involved in many purchasing processes within the area in scope and who is updated on suppliers, pricing and conditions on the market, can many times put a large pressure on the supplier, since the (“virtual”) competitors are in fact a number of good deals recently signed in competition on the market. This knowledge and experience can also contribute in another way, through making it easier to balance between price and quality (when it might be possible to get a really low price, but with the consequences of a decrease in quality).

In order to increase the bargaining power the process should make it clear that it is a unique opportunity with an exclusive right for the supplier, although if not reaching the objectives of the process quickly enough, a “plan B” can be evoked where the client turns to the market.

Sometimes the arguments against sole source are that a traditional RFP is necessary since development has led to a completely changed scope. But with the sole source process the supplier can be required to accept terms regarding following best practice and commitments when it comes to CIP (Continuous Improvement Process/Program) as prerequisites for the process. And an agreement should normally be able to manage changes in the delivered services and be more functionally oriented.

When a sole source process is implemented it is most often more than just a renegotiation of an existing contract. It can also consider how the services in scope are to be delivered in the future and on what conditions, which can be completely different from how it has been done in the past. It can lead to a completely new contract and not just changing a few appendicies.

Arguments against sole source concerning the lack of price competition compared to an RFP and concerning the supplier feeling to secure, makes it necessary to ensure that the process is very well managed and well planned.

**COMPARISON BETWEEN SOLE SOURCE AND RFP**

A traditional, “fully competitive” RFP process (Request för Proposal, with many suppliers getting a detailed requirement specification) can often last between 10-15 calender months in time, including the time to define the process and collect data, until a contract is signed. (The transition phase can thereafter vary significantly in time between different projects.)
The time is saved through less time-consuming work with requirement specifications, before the suppliers are involved (requirements that anyhow often don’t match with what the suppliers actually can deliver). The work in the qualification process can also be managed in a more efficient way with a focus on only one supplier instead of many.

Other advantages for the client are:
- Reduced cost for evaluating the market.
- Reduced internal cost for producing purchasing documentation.
- Reduced cost for evaluating bids.
- Reduced cost for reaching a signed contract, if the parties can agree on basic terms before the negotiation and especially if it is a renegotiation process based on an existing contract.

For the supplier, advantages are for example:
- Reduced cost for producing bids.
- Reduced cost for reaching a contract.
- The risk of putting money on something that later proves to be unnecessary is reduced, through the sole source process being an interactive process. A continuous dialogue through the process regarding needs and solutions reduces the risk of doing the wrong things.

However it is always of great importance to identify the risks with a sole source process in order to minimise and mitigate these, through for example:

- Establish and agree on a number of principles for the procurement process, for the contract and for the co-operation to follow.
- Ensure that the option of a competitive selection process has been considered and that the decision to choose the sole source process is well documented and sufficiently communicated.
- Ensure that the bargaining power remains and that the supplier isn’t too comfortable, in order to get the prices and SLAs (service level agreements) that are requested. This also needs to be connected to how the process is communicated internally in order to avoid the “wrong” message eventually reaching the supplier.

The overall sole source process is in many ways similar to the fully competitive selection process, even if many of the activities are managed in different ways, the risks differ and the activities are more flexible and involve people in a better way.

THE IMPLEMENTATION
The project implementation can be described in a generic model based on phases and steps as described below:

The overall process is similar, whether it is a sole source process or a fully competitive selection process. One of the big differences is the time it takes with the work and with managing many suppliers. When there are many suppliers in a more formal process the suppliers normally also put less focus on things like innovation.

One of the biggest differences is that, when renegotiating, the cost and risks involved with the transition to a new supplier, are avoided.
DID WE SUCCEED?
A well managed sole source process is characterised by among other things a time and cost efficient process as well as a cost efficient and sustainable end result. It can be described as:

Sole source has succeeded if...

Service content is according to best market standard.
Solution: The content is based on market best practice from recent deals (e.g. through using a third party advisor).

The SLAs of the supplier are aligned with business needs and according to best market practise.
Solution: Define business requirements on an end-to-end basis, in order to define the relevant SLAs for the supplier. Use market best practice from recent deals.

The price of the supplier is competitive.
Solution: Use a market benchmarking approach, based on recent deals.

The contract is based on best market standard.
Solution: Use a market benchmarking approach, based on recent deals.

The deal is design is based on a competitive situation with sufficient negotiation power.
Solution: Establish a well-proven sole source process with a “plan B” transparent for the supplier. This means that at a certain moment the process can be stopped and a more extensive procurement process is initiated. The supplier which was initially selected will not be invited to participate in a plan B approach.

RECOMMENDATIONS AND CONCLUSIONS
Before choosing the appropriate approach for supplier selection it should be clarified what the drivers for the business are with the outsourcing in scope. What are the business objectives? Are they reduced cost, increased quality or greater flexibility? Through clarifying this it will be easier to evaluate the proposals in a good way and to verify that they really support the defined business objectives.

When preparing for an important procurement, the sourcing strategy should be reviewed. How do the plans match with the existing sourcing strategy and how is it affected? Do we need to change the sourcing strategy?

In a sole source process it is important that the client owns and controls the process, and not the supplier. This can especially be challenging in a close client-supplier relationship. It can be achieved by e.g. identifying a number of principles in order to reduce cost, by ensuring a good knowledge about alternative suppliers and services in order to increase the bargaining power, by clarifying to the supplier that there is a “plan B” that can be evoked with full competition, by ensuring that the overall time plan allows a plan B and even a scenario where the final negotiations break down.

A sole source process well planned and managed can reach the same price levels and contract terms as a fully competitive selection process. The sole source process can also benefit from advantages of being an interactive workshop based process resulting in a well-defined and agreed upon solution, an enhanced co-operation between client and supplier, time and cost savings on the buying side as well as lower risk and reduced sales cost on the selling side.

But sole sourcing should not be compared to sloppy negotiations managed with too little planning. When a sole source is managed correctly it still requires a whole lot of time and commitment.