



The Art of Negotiation:
Core and Third-Party Agreements Made Easier

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“In business, you don’t get what you deserve, you get what you negotiate.”

- Chester L. Karrass, author of *The Negotiating Game*

Executive Summary

When a Credit Union engages a vendor in contract negotiations for a new technology platform, the process often becomes muddled, lines are blurred and terms of service become unclear. Expertly executing this process is critical as a wrong decision prompted by certain eager vendors can adversely impact the day-to-day operations of a Credit Union, ultimately diminishing member experience and confidence.

Credit Unions pursuing new technology platforms often approach the negotiating table stripped of the necessary tools to succeed. Without proper due diligence, oversights on behalf of the Credit Union often result in costly after-conversion upgrades and maintenance.

In order to avoid pitfalls, it is prudent to engage an objective third party to oversee this all-important process. An unbiased advocate representing the Credit Union who provides the necessary tools and knowledge to successfully navigate the adoption of a technological operating environment is essential. In the final analysis, the negotiation of an expensive, multi-purposed contract is designed to facilitate the needs of a Credit Union and its members. Therefore, there is but one opportunity to master the art of negotiation.

Industry Overview

In order to stay viable, Credit Unions are required to continually investigate whether they can operate more efficiently, offer competitive products and services and maintain member satisfaction. Therefore, the prime motivation for converting to a new platform is usually the realization of an outdated, under-performing operating environment.

The decision to implement new technology – whether it’s a new core-processing system or ancillary products – is a significant undertaking. The resulting challenge is initiating a costly system revamp which when mismanaged results in both short- and long-term hurdles and hazards.

To further complicate the issue, consolidation within the financial technology industry has resulted in less competition, reduced price advantages, forced conversions from “sunsetted” products, and overburdened conversion teams. Therefore, in today’s market, there is considerable pressure on financial institutions to make the correct technological choice out of the gate as the wrong choice is costly and will sidetrack an organization’s projected growth for countless years.

Our colleagues at the Boston-based Aite Group recently released a study *Trends in Core System Replacement: the Necessary Evil* concluding that during the current three-year period (2006-2008), 1,100 financial institutions are engaged in a replacement mode of their core systems. Aite estimates that during 2006, 92 percent of all U.S. core system replacements

(approximately 325) were completed at Credit Unions and small banks, a trend Aite forecasts continuing for the foreseeable future.

Despite best intentions, many Credit Unions will scramble to keep stride with competition and industry trends by moving forward without having a customized core system replacement plan in place. This is understandable as it is difficult to deal with the daily tribulations of operating a Credit Union without coupling problems associated with deploying a new technology platform.

The reality, however, is that seeking new technology requires meticulous due diligence, an evaluation methodology taking approximately one year. The process officially starts when a Credit Union begins the task of identifying existing operating issues and shortfalls. Next, the search and selection process of a vendor and operating environment commences, a multi-tiered process including discovery process, negotiation, agreement, implementation, and conversion.

Vendor and System Selection Process

Before undertaking the search and selection process, a Credit Union must identify existing issues and concerns. Questions should include:

- How is the Credit Union hindered by existing operating environments?
- What is the organization's overall strategy and what core system variables are required to achieve outline goals?

Once the aforementioned questions are researched, assessed and answered, a search-and-selection strategy is the next step. Initial questions should include:

- What are your vendor expectations?
- Do you want to improve your core system, contact center, ATMs, card portfolio, Internet banking, bill payment, or other processes?

Without a sound starting strategy, some vendors will try to dominate the process by determining rules and setting expectations. As a consequence, Credit Unions are removed from the decision-making process and are too often forced to react rather than initiate. To realize a successful negotiation, a Credit Union must be specific in its goals and stay true to its strategy throughout the varied process.

Therefore, the strength of a negotiation platform is comprised of the elements of an organization's business model. A Credit Union should know the variables and constructs of its business better than a vendor. To this end, it is the Credit Union's responsibility to become an active participant providing the required variables for sound solutions.

Before a successful negotiation can commence, participants must have a clear understanding of the variables comprising their goals – the sticking points. To this end, adherence to these three necessary steps is critical:

1. Listen to your members. One of the decisive advantages Credit Unions have over regional banks is the ability to listen to members and quickly implement suggestions and address concerns. Therefore, incorporate member “wants and needs” into the strategy.

In order to understand the needs of a member base, a Credit Union must have in place a system that tracks members’ activity in relation to products and services. Many members today, for example, demand online and real-time access across all electronic delivery channels. Credit Unions hindered in their efforts to expand these types of services – by systems that do not interface well with ancillary products – must consider rebuilding from the foundation up. While the latter might be expensive, the implied knowledge of knowing specific member needs will provide a firm negotiation stance.

2. Maintain a watchful eye. A thorough selection process goes beyond a simple request for proposal (RFP), sitting down with vendors, and negotiating a contract. In many cases, consultants send out generic RFPs and simply assist in a cursory overview of the operating environment. While unacceptable, this is a common approach. A Credit Union that is aware of perils involving conversion, operations, and after-conversion support will possess a distinct advantage while negotiating.

3. Search for the right system solution. Evaluate the positives and negatives associated with your existing technology. Before entering into a new technology platform, Credit Unions should identify the existence of the following system characteristics: seamlessness, openness, ease of use, stability, flexibility, functionality, price/performance, vendor implementation, and service quality strength.

Three easily avoidable mistakes:

- **Credit Unions do not follow an interview process.** Credit Unions must avoid the natural inclination to follow a demonstration process as this approach only indicates what a vendor’s system does well. It does not indicate how it will impact a Credit Union’s unique situation.
- **Conduct interviews.** A Credit Union should approach vendors as if they are interviewing them for a senior level position. Leave no stone unturned. Questions should center on the vendor’s ability to meet unique operational needs. When executed properly, Credit Unions set the rules and control the selection process allowing a holistic view of the vendor product offerings to emerge.
- **Credit Unions are often too trustworthy.** A vendor’s history might offer some insight into a product; however, it does not assure that a system will work well with respective platforms. Every Credit Union is unique and one size does not fit all when it comes to technology.

Without due diligence, the search-and-selection process will be flawed leading to costly issues after conversion. When executed properly, the process will underscore specific and measurable reasons as to your needs and the offer presented by the vendor.

Therefore, the vendor is forced to commit, in writing, to be an honorable, long-term partner with shared goals of collective success.

Interviews Instead of Demonstrations

Whether it is a core or third party, the selection process is a comprehensive process where Credit Unions are encouraged to proactively conduct interactive meetings with vendors. It is the role of a third party consultant to synchronize participating parties, a process that allows a Credit Union to discover a system that will meet all its requirements.

The latter is achieved by abandoning the demo process and opting for exhaustive, exploratory interviews. More often than not, this results in the selection of a progressive vendor team that will be in place from inception to conversion.

The goal of the interview process is to understand the vendors and their product interface and user-ability. Depending on the services used, or outsourced, and the level of in-house proficiency, financial institutions often hire or confer with qualified independent consultants to ensure proper oversight and execution.

During the screening process, Credit Unions should:

- Make requests for information (RFI) for potential vendors as part of a pre-selection process. RFIs determine the financial technology suppliers required for the interview phase.
- Understand the vendor's major supporting agents (i.e., subcontractors, support vendors, and other parties).
- Analyze the vendors' most recent audited financial statements and annual reports as well as other indicators (i.e., publicly traded bond ratings). This process alerts Credit Unions to mergers or takeovers that often lead to a second, costly future conversion.
- Invite vendors to engage in an interview process. This eliminates the "dog, pony and demo" show providing for an interactive, progressive discussion on specific services.

With these critical steps taken, two or three finalists will emerge. After pre-selecting a finalist and a runner-up, the entire process should repeat including a second-round testing respective products, services and support. At this stage, a Credit Union should identify pricing points from three regional competitors.

Selection check list:

- Ask the remaining vendors to set up a laboratory system onsite to evaluate – operations, front office, back-office, lending, delivery channels, etc.
- Use the hands-on interview and laboratory sessions to ask the vendor hard-hitting questions that impact day-to-day operations.
- Assess the vendor personnel assigned to support the institution – especially during conversion and post-conversion.

If Credit Unions enter into an agreement on blind faith with a vendor, they are doomed to fail. Therefore, evaluate the service provider's experience and ability to provide the necessary services and supporting technology for both current and anticipated needs.

From Contract to Conversion

Once a system is selected, take the necessary time to methodically prepare for the negotiation process. Like the proverbial turtle, pace indeed wins the race. This approach will not be easy as sales people are encouraged to expedite the process. To this end, some vendors try to coerce a Credit Union into making a quick decision by placing a deadline on time sensitive prices. The familiar pitch: “If you sign by a specific date, you will receive huge savings.” Therefore, it is critical that the Credit Union sets the timeframe for the negotiation.

Employing a balanced understanding of project management, contract negotiation, and systems integration will present a level playing field, or better yet, provide the Credit Union with the upper hand.

While some vendors are often quick to close a deal, Credit Unions, too, are faced with time constraints. Therefore, Credit Unions will negotiate what they believe are good terms only to overlook key elements such as vendors who can not commit necessary resources for a seamless and painless conversion, which is common as some vendors use the least amount of company resources whenever possible.

Slowing down the process provides a Credit Union valuable time to effectively assess the system they are about to purchase. Critical support components are often overlooked during the negotiation process. To this end, Credit Unions are encouraged to build conversion assistance into the deal.

Negotiating Tips:

- Identify your leverage early on.
- Who has the most to lose from the deal?
- Determine a timeframe.
- Set limitations and stick to them.
- Avoid committing to positions that restrict further movement in the negotiation.
- Walk away from a deal that is not good for you.
- Regardless of approach, maintain emotional distance.
- Despite discouraging feelings, remain patient and collected.
- Listening is as important as arguing.
- Construct concise and specific questions.
- Never interrupt when someone is responding to your question - they may provide valuable information.

Once an operating environment is selected, perhaps the most critical phase begins: introducing respective legal teams.

Despite an attorney’s merits, he or she is not normally versed in core conversions and, thus, cannot appreciate the tactical terms and conditions comprising a sound agreement.

Attorneys, however, are excellent at determining the legal elements of an agreement and should work in concert with the Credit Union and its consultant.

Without knowledge of technology, methodology, and best practices, unwilling and costly mistakes will be made with repercussions rippling far past the negotiation table. Therefore, experienced consultants provide a distinct advantage in the negotiating process.

Each ripple has a dollar value that increases with distance. Therefore, agreements between the Credit Union and vendor should contain specific time requirements as well as key issues identified during the interview and negotiation phases.

Credit Unions should require performance standards indicators defining minimum service level requirements and cures for performance failures in the contract. The contract should allow for modifications in the Credit Unions operation system; otherwise, it is a subscription and not an agreement.

A properly constructed contract will state in transparent language the rights and responsibilities of parties including:

- Timelines and implementation activities and responsibilities – consider existing systems or interconnected systems that may need development.
- Services performed by the technology provider – these include items such as software support and maintenance and training.
- Obligations of the financial institution – the contracting parties' rights in modifying existing services performed under the contract.
- Cost Accountability – the cost associated with obtaining and maintaining of hardware and software needs. The agreement should list any conditions under which the cost structure changes, including limits on any cost increases.
- Ancillary issues – are there guidelines for adding new or different services and for contract re-negotiation?

The contract must also clearly state:

- Fees and costs for all services, including any development, conversion, and recurring services.
- Charges based upon volume of activity and for special requests.

A typical contract includes obscure legalese which holds some vendors less accountable. In other cases, some vendors will sell a substantial block of consulting hours but a weak service level agreement. Thus, it is money wasted if the Credit Union uses those service hours to fix problems. During negotiating, a Credit Union must have foresight and consider variables that may arise after conversion.

Aside from securing favorable pricing, Credit Unions must negotiate vendor performance standards, a critical component to any agreement. Often this is done in the form of a codicil to the contract.

A critical provision is the provision limiting liability. Some vendors commonly seek to limit their liability for the products and services they offer. Frequently, a vendor disclaims special, indirect, incidental, or consequential damages.

In certain cases, some vendors will negotiate aggressive contracts designed to limit direct or realized damages. If vendors will not be held accountable for direct or realized damages, a Credit Union should walk away from the negotiation process.

The contract review process should be exhaustive. Avoid contracts where:

- The vendor can change terms unilaterally
- The vendor can change fees without consent
- The vendor can disclaim liability
- The vendor has not shared third party documents

When a conversion team led by an unbiased consultant is in place, outlined issues and concerns are avoided making the selection process launch seamlessly. This approach mitigates surprises and saves your organization money. When a Credit Union identifies weaknesses during the sales cycle instead of the conversion cycle, it will save members, management, and staff from operational turmoil.

It is a consultant's responsibility to ensure that specific legal language underscoring the contracts terms and conditions is delivered. Negotiation is not a subscription process; it is an agreement reaching process.

Conclusion

The financial technology market is dynamic and subject to shifting regulations. Transactions in such environments can be both complex and time consuming. Therefore, it is beneficial that a Credit Union's negotiating team understands the financial-services industry and how related technologies develop.

When moving through the selection process for a major project, the ultimate objective is to negotiate the best deal. This requires a Credit Union to remain focused on its strategic goals, which, in turn, maintains a competitive edge. When a Credit Union is searching for the right technology partner, it should render the process predictable. A fair agreement in line with an outlined strategy will preserve expectations.

While there are a number of essential variables to consider, managing the negotiating process properly ultimately saves time and money. The realized savings will eventually benefit members by enhancing the Credit Union's value and quality of service.

In the final analysis, negotiation is indeed an art form; a process rewarding the party dedicated to researching and investigating sound solutions. And whereas art appreciation is subjective, the result of a negotiation is binary: you either win or you lose.

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