CIO Update

Don’t Give Software Vendors the Upper Hand

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By Jeff Vance

During an acquisition a few years ago, company A reached a deal to acquire company B. However, much of the value of company B was tied to technology services, many of which were outsourced. The principals of the deal, therefore, believed that establishing good terms for the acquisition depended on negotiating a reasonable deal with the outsourced technology service provider.

“The technology outsourcer brought terms to the table that were not just untenable, but also downright rude,” said Matt Podowitz, executive director, of Business Advisory Services at Grant Thornton LLP.

“Unfortunately, the negotiator for my client believed that the only option was to negotiate a deal with the outsourced technology provider,” he added. While the negotiator wasn’t going to accept the terrible terms, he took a defensive position when looking at alternatives.

The situation was eventually resolved. Company A brought its CEO to the table. The CEO had taken the time to prepare alternatives. When the outsourcer restated its ridiculous demands, the CEO laid out an alternative deal with another company that he was ready to accept. In less than a minute, the outsourcer caved and proposed agreeable terms.

The lesson here is that the CEO was not emotionally invested in the negotiation, nor was he blind to alternatives. However, Company A eventually walked away from this deal anyway. This wasn’t immediate—the outsourcer was retained for a few months, until the acquisition was successfully completed—but the outsourcer’s behavior at the negotiating table had so poisoned the deal that company A dumped them at the first opportunity.

The Importance of BATNA

Much of the trouble in the above negotiation could have been avoided if company A had taken the time to develop its BATNA, or Best Alternative to a Negotiated Agreement. BATNA is a Negotiating 101 concept. However, with technology, organizations tend to lose sight of this fundamental principal.

“Never negotiate with just one vendor,” advised Brian Sommer, president of TechVentive. “While this is incredibly obvious, companies routinely make several mistakes on this one point alone.”

For instance, if you don’t control what is communicated and by whom to vendors, they will have an information advantage over you. “Tech sellers continuously poll their prospects. They’ve got several people on the sales team, pre-sales demo people, third parties, and more, coaching them daily as to the status of the negotiations. If the prospect can’t close off this information flow, then there can be no negotiation,” Sommer said.

If the vendor knows they are the “preferred” choice, they know they have a strong hand to play. Worse, if the vendor finds out that they are the “winner” after a list of alternatives has been whittled down to one, the winner will dig in its heels and concede little if anything of value.

“However, smart negotiators know how to use this to their advantage as they can intentionally leak out information that is intended to keep the vendor engaged in negotiations but unsure of their outcome,” Sommer added.
Leaking the threat of a walk-away is a solid negotiating ploy, but only if the threat is real. Not only must you have alternatives in hand, you must also put enough effort into researching alternatives that they are credible.

“Most fail in two areas: identifying their alternatives (or walk-away plans) and valuating their alternatives,” said Michael Rosenthal, CEO of Consensus. For instance, when buying a car, people know where to look for benchmarks and comparisons. Classified ads, Kelley Blue Book, AutoTrader.com, other dealerships, etc. all offer useful information.

With technology, it’s much harder to ferret out information. Often, getting actionable data requires direct contact with another vendor—often to the point of entering into another negotiation. It’s a lot of work but that doesn’t mean you shouldn’t do it.

“The advice we give our clients, and practice ourselves on behalf of clients, is to develop multiple alternatives early on. In this case, explore other vendors, get their pricing, compare apples-to-apples, and determine how much it would cost and the timing involved to develop a similar solution in-house,” Rosenthal added.

With the proper research in hand, you can ask such loaded questions as, “It seems that the market rate for your service is less than what you are asking for. Why should I pay more than that to go with you?” If you don’t get a good answer, you can walk away assured that your alternatives are indeed better.