

February 2003

## Contracting Options

Many Clients are not familiar with the various contract types available from contract management firms for their service departments. Without changing contractors there are many options available that may better meet your objectives. Even if your contract is years from expiration, you should not hesitate to have your contractor modify a service agreement to better meet your needs.

In addition to capturing all legal aspects of the agreement the contract must deal with two key areas: **operational responsibilities** and **financial obligations**. The Client can and should make the operational responsibility decisions for their institution. After these are made, the financial obligations can be negotiated with the contractor.

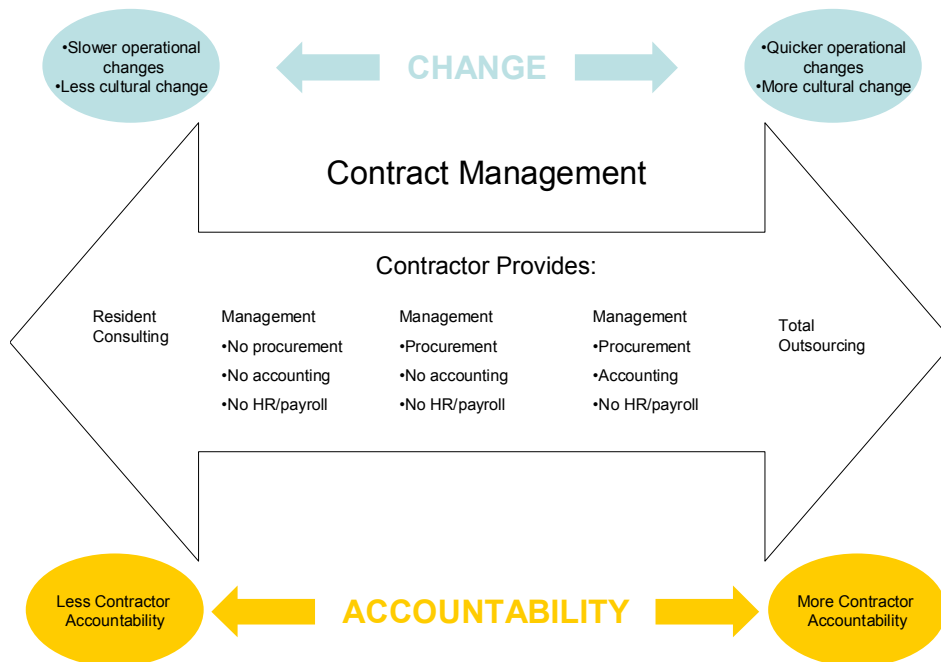
**Operational responsibilities** – Identifies the functions that each party is responsible for providing. Examples: Who will pay the hourly staff? Who will be responsible for procurement? Who will pay for equipment maintenance and replacement? Who will be responsible for the accounting?

**Financial obligations** – Identifies each party’s financial risk for the agreement, no matter which party assumes the operational responsibilities.

It is important to note that these should be treated independently, when determining the best contract to meet your objectives.

## Contracting Spectrum

The chart below identifies the range of contracts available to capture the **operational responsibilities**. Agreements can be designed to fit anywhere on the spectrum, prior to deciding the **financial responsibilities**.



Recent Client  
 Quote:

**“Support Service Group exceeded our expectations in all areas...”**  
 - Vice President of Business Affairs

---

## Negotiating Financial Obligations:

Now that you've determined the operational functions that the contractor will provide, it is time to determine the risks that each party will bear. Every agreement should contain financial and performance guarantees from the contractor. Such guarantees insure that the contractor stays focused on meeting your objectives. The amount of financial risk assumed by the contractor should be balanced with incentives for performance above the expected levels.

### *Creating the balance...*

The amount of risk assumed by the contractor must be balanced with the amount of additional incentive they can earn **and** the operational accountability that they have for achieving the results.

It would be impractical and expensive to expect a contractor to assume total financial risk for a department without any operational accountability. You should not expect a contractor to take risks for areas that they cannot control. For example, if you elect to keep the hourly employees on your payroll, the contractor will have no control over wages and benefits. However, the contractor does have control over the number of labor hours used and incentives/penalties can thus be tied to labor hours vs. labor dollars.

In summary, the base fee structure (either management fee or expected profit level) should reflect reasonable expected performance levels. Additional incentives and penalties should be built into the contract for results (both financial and quality) above and below the expected levels.

---

## Glossary of Terms:

**P&L Contract** Historically, where the Contractor assumes the financial risk for the department. The Client is billed a rate per unit of service (board day, patient day, square foot).

**Management Fee Contract** Historically, this was a cost plus contract with the Client maintaining the financial risk. However, with guaranteed budgets and incentive/penalty arrangements, any level of risk can be shifted to the Contractor.

**Full Service Contract** Another term for total outsourcing, typically used in facilities contracts. Historically the financial risk was with the Contractor, but like all outsourcing agreements, these can also be cost plus.

**Control Budget Contract** Under these agreements, the Client is billed for the total department budget and then credited back for any expenses (such as labor) that the Client provides. These contracts, initially created for healthcare housekeeping, have historically been the most financially lucrative for the Contractor.

---

## Feedback:

A new position paper will come out every month or so.

If you'd prefer to receive future position papers electronically, send me an email. Make sure and let us know what format you prefer. They are available electronically in MS Word (.doc) and Adobe Acrobat (.pdf) formats.

The position papers are also available on our web site [www.supportservicegroup.com](http://www.supportservicegroup.com) for your future reference.

We welcome your comments and suggestions for future position papers. Either drop me an email or give me a call.

If you'd like to explore how Support Service Group, LLC can help you maximize the results from your food service, housekeeping or facilities departments, I'll be happy to meet with you.

**Owen Pruden, President**

[opruden@supportservicegroup.com](mailto:opruden@supportservicegroup.com)

**Web Site:**

[www.supportservicegroup.com](http://www.supportservicegroup.com)

**Support Service Group, LLC**

**828 Pebble Brook Place**

**Noblesville, IN 46060**

**317.345.4421 (Phone)**

**317.896.3273 (Fax)**