# Vendor Analysis and Evaluation

**Does your vendor make the grade?**

Working well with your product and service providers is a key component to a successful equity compensation program. Whether you utilize third-party vendors to support recordkeeping systems, outsourcing, brokerage, or other advisory services, you depend on them to supply critical assistance to keep the administration of your stock plans humming, your financial reporting and compliance accurate, and your employee participants happy. When one of these relationships doesn't work as expected, this may present an opportunity to evaluate your current provider's product offerings and performance and determine if a replacement is needed.

**Can you improve your current vendor relationship?**

Before you decide to change vendors, take a look at whether your current relationship can be saved to avoid the cost of a transition and disruption to your infrastructure, administrative team, and plan participants. If you haven't met with your vendor in awhile, this provides an excellent opportunity for your provider to learn how your needs have evolved and for you to understand how the provider's services have changed. This is also a great way to offer feedback to your vendor to help improve their service.

To start this assessment, clearly document your equity program's needs, including environment, participant demographics, system requirements, reporting process, and other aspects that impact or are impacted by the service provider. This process can help to uncover the real reasons you are dissatisfied, information that is vital whether you want to fix the existing relationship or opt for a fullscale vendor evaluation and potential transition to a new provider. Once that review is completed, contact your provider to gain an understanding of their current services, products, and future roadmap. Identify the areas where the vendor's current and anticipated capabilities don't align with your needs and take a look at comparable providers to determine if these gaps are normal and reasonable. If they are, work with your vendor to see how they can address your concerns.

Be open and honest with your current provider. Give them a fair chance to understand your needs and adapt their performance to meet your expectations. While it does require some investment to conduct this preliminary analysis, it could save significant time and money down the road. The outcome of the analysis will help you understand the offerings of the industry as they relate to your specific needs, and determine whether to continue investing in the existing relationship with your current vendor or move on to a new provider.

**What should you know before initiating a search for a new vendor?**

If you find your concerns cannot be remedied satisfactorily with your current provider, a vendor transition may be the best solution. There are many reasons why companies choose to change vendors. A transition enables the company to realign vendor capabilities with their equity program needs, which may have changed since implementing their current provider. Since the equity compensation industry is constantly evolving, new developments, systems, and services may now be available in the marketplace for your company to leverage. The process of selecting and switching vendors allows the company to identify critical gaps in current service and find better solutions to support those needs. Furthermore, the company's circumstances may have changed significantly enough to warrant pricing reductions. As long as clients are able to switch providers, the market will continue to self-regulate and improve itself.

However, there are always risks to changing providers. The temptation to switch is often provoked by the "grass is greener" mentality: how do you really know if a new vendor is better or if you are simply exchanging one set of problems for another? The time, cost, and effort required to change vendors can be extensive, so a hasty decision can become a very costly mistake. Since vendors usually use different systems to manage recordkeeping, there may be fundamental differences in how two platforms handle certain types of data, such as vesting or expense recognition; consequently there may be significant historical reconciliation issues (which in some cases may even require a one-time accounting charge). If the reasons for switching are on the corporate administrative side, employees may be impacted without understanding the motivations behind the transition; they may also have relationships with a current broker and want to keep their assets in the same place, rather than move them to a new provider. Finally, the timing of a transition could be critical if timed with a year-end or fiscal reporting period, employee stock plan purchase, large restricted stock vesting, or other key milestones. Often the time involved to switch providers is underestimated and can exceed original estimates.

**What are the benefits and risks of conducting a vendor evaluation?**

Why is a vendor evaluation a good idea? This process gives you the ability to compare vendors equally using a thorough and systematic methodology, allowing you to analyze different solutions on the same terms. We recommend to many clients that a written Request For Proposal (RFP) be used to carefully document requirements and ask the right questions, reducing the chance of missing vital information in the selection process and to clearly document vendor capabilities. It enables both the vendor and the company to educate each other properly to determine if this is a good relationship fit before a change is made. A vendor evaluation also helps to narrow down the wealth of choices available to you by identifying the differentiators between similar vendors and services to find the best match for your company's requirements. As an added bonus, this process prepares you for a vendor transition, since you can use the time simultaneously to prepare data and understand other requirements in anticipation of conversion.

A vendor evaluation is not without its drawbacks. There is usually a fair amount of time, effort, and monetary investment involved in this process, especially if using a third party to manage it. A vendor evaluation still requires the time of in-house resources to support the project, as a successful outcome relies heavily on the interest level and involvement of the internal team. You may find there are no reasonable alternatives to your current provider, nor is there a solution that meets 100% of your requirements especially if you have unusual plans or plan features; similarly, there may be more than one suitable solution, thus requiring a difficult choice between comparable providers. Important details can still be missed, even in a rigorous evaluation process, since it is impossible to predict everything that may occur. This process also adds significant time to a transition timeline; a full vendor evaluation, contract negotiation, and implementation could result in up to 6-12 months before the switch is effective. Finally, a vendor evaluation does not remove the decision-making responsibility from the company, so you are still accountable for making the best selection out of the information provided.

**How does a vendor evaluation work?**

Regardless of these concerns, a vendor evaluation is a highly-recommended process if the company understands the critical nature of this decision and wants to minimize the chances of an inferior selection. The vendor evaluation process typically involves the following steps:

- Conduct due diligence to collect information regarding your company's equity goals and priorities, environment, equity programs, participant demographics, systems/interfaces, administrative processes, and other vendor requirements
- Generate a list of potential vendors and contact them to obtain interest in participating in the RFP process
- Draft and distribute the written RFP to vendors, allowing sufficient time for them to review and complete the RFP
- Collect the RFP responses from vendors, compile the data, and draft a comparative vendor analysis, including strengths, weaknesses, key differentiators, recommendations and cost analysis
- Conduct meetings/demos with finalist vendors, perform reference checks, and gather additional information as needed.
- Determine the most appropriate vendor for your company's needs

How much will it cost to change vendors?

In estimating typical costs associated with a vendor evaluation and transition, the most significant investment is in resource time to manage and conduct the selection and implementation process. Even if you obtain assistance with some of these tasks using third-party consulting providers or your new vendor, resources within your company still need to be allocated to support these projects. Here are a few considerations:

| Phase/Task | Description | Time/Cost Considerations |
| --- | --- | --- |
| Vendor evaluation | Process to evaluate vendor choices and make a selection | Resources to manage the project, conduct due diligence, coordinate the RFP process, and make a selection |
| Data clean-up and preparation | Vendor pricing typically assumes all pre-implementation data is clean and can be converted to a significantly different format by the client; if not, vendor will increase pricing to manage that work or account for delays in implementation | Resources to audit and clean up data |
| Vendor implementation | Vendor may charge a flat fee for implementation or else build the cost into ongoing administration fees and commissions | Fees depend on the vendor selected; resources to manage the implementation on the client side |
| Process changes | May be required to modify or add processes to support the new vendor, such as data file feeds | Costs depend on the processes to be modified or added; resources to manage the design and implementation of such processes |
| Existing vendor transition | Vendor may charge for transfer of assets or to provide data in a usable format for conversion to a new vendor; may be fees for early termination of the contract | Fees depend on the existing vendor; termination fees may require the client to pay administration costs owed for the remainder of contract or other penalties |

The actual time invested in this process varies significantly depending on the complexities of equity plans, the vendors involved, the extent of equity data to be migrated, and other factors. It is critical to plan carefully to ensure the right resources are assigned to these tasks and adequate time provided to complete the work to ensure a smooth transition.

**How much time should you allow for a vendor evaluation?**

When assessing your vendor, make sure you allow adequate time to conduct this process thoroughly; a hasty decision could end up creating more problems than are solved. If you are planning for a transition, consider when you want the implementation completed and create a timeline backwards from that point. For example, if you want to go live with a new outsourcing vendor by January 1, allow at least 3 months for conversion/implementation, 1 month for contract negotiations, and 2 months for selection, so start the process no later than end of June.

Allow adequate time for the vendor evaluation process itself; based on our experience, SOS recommends 2 weeks for due diligence, 2 weeks to develop the RFP, 3-4 weeks for vendors to respond, 3 weeks to compile responses and create analysis, and 3-4 weeks for additional tasks and decisionmaking. You may be able to accelerate this process to some extent by utilizing third-party consulting providers who conduct vendor evaluations on a regular basis. Availability of internal resources to focus on this process and vendors to respond to the RFP may also impact this timeframe. Furthermore, complicated plans, poor data integrity, lengthy contract negotiations, involvement of an existing outsourcing vendor, and other issues could affect the implementation timeline. These aspects could stretch the timeline another 3-6 months if not anticipated or properly managed.

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