



THE OPERATIONAL GUIDE

CONTRACT AND COMMERCIAL  
MANAGEMENT

 **IACCM**  
International Association for  
Contract & Commercial Management

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Contract and Commercial Management  
The Operational Guide

*This book is dedicated to the memory  
of Margaret Carey who inspires us all  
by planting small seeds of partnerships  
and friendships worldwide.*

# **CONTRACT AND COMMERCIAL MANAGEMENT**

## THE OPERATIONAL GUIDE



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# Foreword: By the Board Members of IACCM

As executives and senior managers in some of the world's major corporations, each of us has had direct oversight for aspects of contract and commercial management within our business. Individually, we have observed the growing role and complexity associated with contracting and this has been reinforced through our experience as elected members of the IACCM Board of Directors.

It is clear that contract management is an increasingly diverse and important organizational competence and this demands greater consistency and efficiency in its management. It also requires more creativity and the tools and techniques that are necessary to improve the quality of judgment and decision-making. Each of us is aware of the difficult balance between control and compliance on the one hand, and agility and flexibility on the other.

While such tools and techniques are fundamental building blocks, the skills, competence and professionalism of the people who work in and around the contract management space are also key. This book represents an important contribution to that heightened competence, offering as it does the first comprehensive view of contract and commercial operations from a cross-industry, bi-partisan, worldwide perspective. It is an ambitious work that seeks to rise to the challenge of managing business relationships in today's complex global markets and equipping the practitioner with a robust 'body of knowledge' that reflects leading practices.

Dave Barton	Director of Contracts	Agilent Technologies
Adrian Furner	Commercial Director	BAE Systems
Diane Homolak	Global Legal Operations Quality and Strategy Manager	Hewlett-Packard
Monu Iyappa	Executive Vice President Legal	GMR Infrastructure Ltd
M.C. McBain	Vice-President Global Alliances & Contract Development	IBM
Steve Murphy	Vice President, Contracts	Raytheon Integrated Defense Systems
Nancy Nelson	Global Contracts Director	CSC
Gianmaria Riccardi	Director, Commercial Business Management Europe	Cisco Systems
Alan Schenk	VP Common Process, Contracting & Compliance	BP

Craig Silliman	Senior Vice President & General Counsel	Verizon
Margaret Smith	Executive Director Contract Management	Accenture
Peter Woon	VP, Procurement and Supply Chain	Marina Bay Sands Pte Ltd

# Preface

## About this book

All around us is rapid change and growing complexity. The demands on contract negotiation and management have never been greater. There is an urgent need for sustainable practices that support flexibility and dynamic change.

Those who are responsible for contract management must heed the calls for greater collaboration, more innovation, greater readiness to simplify the rules and procedures that will allow management to address turbulent market conditions. At the same time, we must achieve increased rigor, greater compliance and improved controls in our contracts and relationships.

Making sense of these conflicting issues demands a more consistent view of contracts – their purpose, their structure and the terms we use within them. It demands the use of common methods and techniques, common terminology and attitudes to risk and opportunity.

To add to these pressures, we are witnessing a steady increase in the influence of emerging markets and newly powerful economies that cause us to question some of the well-established traditions of contract management and the law. This means we must engage in dialog between different business, legal and social cultures to establish clear and mutually acceptable first principles.

It is in this environment that we offer this Operational Guide, to equip those who must manage the complex contracting requirements demanded by today's global markets.

## About the authors

The International Association for Contract & Commercial Management (IACCM) is a non-profit organization that owes its origins to the growing complexity of world trade and the consequent need for increased and more consistent skills, knowledge and procedures in the field of contract and commercial management.

The Association was founded in 1999 to fill the gap in international understanding and competence in contracting. Its purpose is to explore and disseminate 'best practice' in the formation and management of trading relationships, as well as equipping business managers and negotiators with the knowledge required to navigate within today's environment.

Through ongoing research, IACCM provides many of today's top corporations and government agencies with the knowledge they require to develop the process and skills that ensure the integrity and success of their contracts and commercial practices. IACCM is unique in representing both buyers and sellers, ensuring a consistent body of knowledge and reducing the risk of unsuccessful outcomes through the promotion of mutual understanding and more collaborative working.

This book is an operational guide to those practices and methods. It has been compiled and reviewed by a wide variety of professionals and academics, representing multiple industries, countries and commercial disciplines. The book is therefore a practical resource for anyone involved in contracts, their negotiation or management.

**Tim Cummins,**

CEO, International Association for Contract & Commercial Management

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

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## Team

Ravindra Abhyankar	Purwa
Natarajan Balachandar	TECHNIP INDIA LIMITED
Gerlinde Berger-Walliser	ICN Business School
Guillaume Bernard	Schneider Electric
Alexander Beyer	complon
Chris Caro	IBM
Arthur Cohen	Praxis Consulting, LLC
Jacqui Crawford	BP
Arvind Dang	Central Park Estates Private Limited
Xavier Darmstaedter	DACOTA Consulting
Alvaro de Leon	Transcom
Vivek Durai	tman Law Partners
Eric Esperne	Dell Healthcare & Life Sciences
Jesús Álava Fernández	INITEC TR Group
Jean-Marc Fraisse	NNEPharmaplan
Ernest Gabbard	Allegheny Technologies
Claudia Gerlach	Nokia Siemens Networks
Max Gutbrod	Baker & McKenzie – CIS, Limited
Margo Lynn Hablutzel	CSC
Roselle Harde	Accenture
Robert J Hatfield	Improvement Advisory Services

Phoebe He	Avnet
Jan Heidemann	Consultant
Paul Carter Hemlin	Contract Management Direct
René Franz Henschel	Aarhus University
Christof Höfner	Nokia Siemens Networks
Diane Homolak	Hewlett-Packard Company
Linda Hopkins	Accenture
Doug Hudgeon	Operating Efficiency
Monu Iyappa	GMR Group
Agustín Garzón Jordán	Agilent Technologies
Amit Kapoor	Mahindra Satyam
Tiffany Kemp	Devant Limited
Anton Klauser	Nokia Siemens Networks
Ingo Köhler-Bartels	Dimension Data Germany
Mireille Lafleur	Alstom (China Investment Ltd.)
Tom Larkin	Solathair Management Consulting, LLC
Ashif Mawji	Upside Software Inc.
Tim McCarthy	Rockwell Automation
Peter McNair	SEA Business Management Pty Ltd
Stefan Moecking	Unisys Outsourcing Services GmbH
Daniel Nagel	BRP Renaud & Partner
Jamie Napper	Best Buy Europe / Carphone Warehouse
George Neid	Raytheon Company
Nancy Nelson	CSC
Viv Nissanka	BBC
Jeanette Nyden	J. Nyden & Co
Thomas Oswald	Booz & Company
Makarand Parkhi	Aquatech Systems
Elekanyani Phundulu	Transnet Freight Rail
Carlos Pistone	Alcatel-Lucent
Philippe Poisson	BT Global Services
Ramakrishna Potluri	SAP
Gianmaria Riccardi	Cisco Systems
Ignacio Romera	INNOKEY
David Ross	BT
Greg Russell	Project Advice Services Limited
Ronnie Sefoka	Sasol
Satender Sharma	Petrofac International
Jan Ole Similä	Nord-Trondelag University College
Abhishek Singh	Adhani Institute of Infrastructure Management
Nigel Spink	Thales Rail Signalling Solutions Inc

Kokkula Srinivas	Bharat Biotech International
Mark Swarthout	CSC
Anita Thussu	Infosys Technology
Rajeev Thykatt	Infosys BPO Ltd
Mike Tremblay	HP
Amina Valley	SAIC
Daniel Vohrer	The Linde Group
John Weiss	The Highland Group
Lyndon White	Dial Before You Dispute Pty Ltd
Joginder Yadav	Nokia Siemens Networks
Alexander Yavorchuk	Oracle Inc.
Edwin T Y Yeo	

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## MANAGE PHASE

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## CHAPTER 1

# Introduction: contract management – a global context

The concept of trade is a characteristic unique to the human species. With each advance in human communications, the complexity of trade has increased<sup>1</sup>.

It is this growth in complexity that drove the need for contracts, as a written record to ‘memorialize’ the negotiation that had taken place and which committed the parties to some future exchange of value.

Over time, the knowledge gained from past transactions led to a body of experience which became enshrined in laws or customs, influencing the process by which trading relationships were formed, the parties involved in their formation and the means by which they were recorded.

Today, we are at the beginnings of a new era for communications – a world connected via electronic networks that allow unparalleled speed, enabling relationships to be formed and managed in ways that were never previously envisaged. It is the unknown nature of this networked world that represents a new level of complexity for society as a whole, but especially for the politicians who are charged with its regulation and the business leaders who must navigate through the risks and opportunities that it represents.

A survey by IBM Corporation<sup>2</sup> revealed that 79 percent of Chief Executive Officers (CEOs) see ‘increased global complexity’ as a major challenge over the coming years. Of course, mastering complexity has been a key trait of humanity over the centuries, but at this time it has taken on a new intensity. At its heart, according to these CEOs, is the difficulty created by ‘the growth of interconnections and interdependencies’. What do they mean by this – and how does it relate to the world of contract management?

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1 ‘Before the Dawn’: Nicholas Wade

2 IBM Corporation ‘2010 IBM Global CEO Study’ May 2010

## 1.1 The challenge of choice

Globalization has driven a massive expansion of choice, in particular in the world of trade. Whether as a buyer of goods and services or as a seller, there are few corners of the world where it is no longer possible to find a trading partner. For some, this means new markets; for others, it may mean access to new resources, improved skills, or lower cost supplies. The problems that come with this explosion of choice are many. For example, how do you assess which options are best? How long will that assessment take you? What risks may be associated with your choice – and how do you find out about them? And at the same time as one business is on this journey of discovery, so are its competitors – are they moving faster, or smarter? Will they innovate before me? Do you any longer know who your competitors are – who may emerge from parts of the world where you did not previously play?

Businesses face dramatic and exciting new opportunities, but also very real threats. Many of the CEOs were concerned about issues such as customer loyalty and reputation risk. Why? Because networked technologies mean there are no secrets any more and customers can be accessed by competitors, new and old, at far lower cost. It has become much easier for a customer to undertake regular re-bids using e-procurement technology. It has become inevitable that the media, or bloggers, or disgruntled members of the public will highlight any slip in quality, governance standards or organizational integrity. Misjudgments, mistakes and ethical lapses take only minutes to appear on the worldwide web.

## 1.2 Impacts upon contracting

Many of these issues touch upon the contracting and commercial capabilities and practices of the organization. The CEO survey offered more detailed insight. Executives are hoping for greater creative leadership from within their organizations. They highlighted three particular areas for focus. They want staff who are:

- Better at managing risk
- Better at eliminating rules and bureaucracy
- Better at forming and managing customer relationships

In the opinion of many executives today, those charged with contracting would certainly be found wanting on at least one of these focus areas – and in some cases, all three. The question for many professionals is whether they wish to have change imposed upon them by others, or to be drivers of that change – the ‘creative leaders’ who are being sought by the CEO community.

The contracting process can operate at two very distinct levels. In some organizations, it is seen as the discipline through which corporate or organizational policies and practices

are implemented. Those charged with the role of contract negotiation or management are essentially compliance managers or administrators, either preventing or limiting the scale of deviation from ‘the rules’. Their discretion may be limited or non-existent and they typically rely on others to make operational decisions. They have no meaningful role in the strategy that underlies the standard policies or practices – and feel no sense of responsibility for ensuring that these standards enhance competitiveness or economic performance.

At the other end of the scale, the contracting process is seen as a key instrument for quality control and brand management. It is understood to be not only the instrument through which policy and practice are implemented, but also the closed-loop system through which they are maintained or challenged. Contract and relationship structures, individual terms and conditions and contract governance procedures are constantly under review to ensure they support market advantage and reinforce brand image and reputation.

In either case, operational management of contracts is a critical discipline. This book focuses on the operational aspects, with limited reference to the over-arching strategies and policies that determine the quality of the contracts themselves. These will be addressed in a separate Contracting Strategy volume.

This book is about contracting. But of course there are multiple forms of contract and therefore it is important to define the scope of the types of agreements or relationships that are covered.

First and foremost, the book is about business contracts and it is predominantly about business-to-business relationships. Within this there is some discussion and distinction between public and private sector and passing reference to issues associated with consumer contracting. While the primary focus is on the provision of goods and services (including intangibles such as software), there is also reference to distribution, alliances, teaming arrangements and joint ventures. Finally, it is written with a global perspective, acknowledging the variations created by different cultures and jurisdictions.

### **Philosophy**

It may appear strange to start a book on contracting with a statement of philosophy, but it is important to state that this work has the aim of increasing the probability of successful trading relationships. We present the view that contracting must become a core business competence to assist in understanding, evaluating and overcoming the complexity and challenges of today’s global markets.

This position is reflected in the work of a growing number of academics who show particular interest in the connection between contract management and relationship

management. Specific examples include Nobel prize winner Professor Oliver Williamson, author and educator Kate Vitasek, outsourcing guru Professor Leslie Willcocks and a host of thought-leaders who collectively belong to ‘the school of pro-active law’ (Professors Tom Barton, Kaisa Sorsa, Henrik Lando, Rene Henschel and Gerlinde Berger-Walliser being notable examples).

To achieve that end, it seeks to be inclusive of a wide range of viewpoints and to encourage balancing of interests and needs, in a way that is appropriate to the extent and duration of the contract that is being formed. It encourages openness and honesty, but of course we cannot prevent our readers from using the information in whatever way they deem appropriate. In general, we suggest that adversarial or confrontational relationships do not tend to work; but as with all things, this is not always true. Suppliers in particular may choose to stick with domineering customers and learn how to leverage their relationship. But we see limits in how much such a relationship will achieve.

This philosophy leads us in general to warn against unbalanced or inappropriate allocations of risk. It also encourages the parties to question transactional, as opposed to relational, behaviors, recognizing that all choices carry a cost. A good example of this readiness to question is contained in an article by British economist John Kay, entitled ‘It’s time to rip up your unwritten contracts.’ In it, Kay suggests that the shift from performance based on long-term relationships to performance based on transactional contracts has reduced input prices, but damaged longer-term profitability.

We seek to explain and bring those costs to the surface, in ways that will assist good business judgment and support sustained business success.

### **The role of law**

The role of law is acknowledged as fundamental to contracting practice and process. Any contracts expert must appreciate the impacts of different legal traditions – for example, statute law versus common law. These differences will impact the attitudes of the contracting parties; they will affect the length and content of the contract; they are likely to influence the language and will certainly determine the choice of words.

This book briefly describes different legal systems and how these may impact certain aspects of the contracting process. However, it is not a legal textbook and takes the position that contracts are first and foremost economic, rather than legal, instruments. The earliest contracts were to record business and economic principles; the legal aspects came later and in many cases appear to have overwhelmed or obscured the original purpose, often undermining the economic value or rewards. In attempting to redress this issue, there is no suggestion that the law – and the role of lawyers in contracting – is not important. It is simply to remind readers that the law is just one of many interested parties – or

‘stakeholders’ – in this process and by allowing it (or any other stakeholder) to dominate, we will frequently end up with a poor or failed outcome.

The conflict between rules and good outcomes is perhaps most apparent (or at least most widely reported) in government and public sector contracting. There, rigid application of acquisition procedures can often work against the interests of those they are designed to protect.

### **Understanding the other side**

Human relationships cover a spectrum, from the mere acquaintance to the deeply committed. As they cross this spectrum, the extent and depth of communication, mutuality of interests and cooperation shifts. The importance of considering the needs and interests of the other party grows and indeed becomes a determinant of the relationship’s success and a dependency for its increased depth.

Thus it is with business relationships and that is why this book presents the perspectives of both customers and suppliers. In some areas, their interests converge; in others, they may appear polar opposites. But in every case, the parties form a relationship because each believes it will be better off with it than without it. The contracting process is a voyage of discovery – first in establishing the potential for a match, then in attempting to shape and define it, finally in overseeing its implementation and – perhaps – termination.

It is in fact ironic that many of those who lead today’s contracting process or contract preparation come from professional backgrounds that encourage adversarialism and ‘winning’. Lawyers, procurement specialists and even CEOs tend to be highly competitive individuals and their training promotes a ‘them and us’ attitude, often bereft of trust. Yet today’s business philosophy is more and more about ‘collaboration’ and ‘partnering’ in ways that are entirely alien to many established contracting models and procedures. The old world was about ‘winning the deal’ on terms that were to your innate advantage; the new world is about ‘winning the outcome’ – that is, ensuring that each side is motivated to optimize the final results by a sense of shared benefits.

All good contracts and successful relationships require some level of collaboration and they tend to flourish if there is an appreciation – and respect – for the needs of the other side. Hence this book seeks to offer its readers an appreciation of alternative values and points of view. This does not imply weakness or compromise; such understanding in fact strengthens any deal-maker or negotiator, or anyone preparing a draft contract or managing a trading relationship. Through understanding, we can consider a range of possible ‘value trades’; we can reduce cycle times; we can encourage all stakeholders to develop consensus and to work towards common goals and targets. Ultimately, a failure of understanding leads to weakened communication and heightened probability that the contract will fail.

This is reflected in research such as IACCM's annual 'most frequently negotiated terms' study, which also explores the most common sources of claim and dispute. Unclear requirements, mismatched measurements and selection criteria and inadequate communication and governance standards are the drivers of disagreement and potential failure.

Traditional contracting does not always reflect this view. Indeed, many procurement processes or standard forms of contract appear deliberately adversarial. Large corporations tend to a 'take it or leave it' approach – they see limited need or purpose in efforts to understand the other side. Such an approach is of course legitimate and supports internally driven views of managing risk and efficiency. However, this book may lead many to question the extent to which such an attitude is beneficial and it will provide the counterparty with suggestions on how to deal with 'the non-negotiator'.

Overall, our purpose is to increase the probability that contracts will succeed and will underpin healthy, mutually rewarding relationships. And that is why we consider it essential that the book covers the point of view of both sellers and buyers.

### Who does contracting?

It is inevitable that many readers will want to know what skills are needed or what organizational model will work best to ensure successful contracting. This book does not seek to answer those questions in any depth because the answer is 'It depends'. A companion work on 'Contracting Strategy' will address these topics in depth and offer detailed guidance on how to develop the skills and resources needed to ensure successful contract procedures.

Therefore this book endeavors to focus on the operational aspects of contracting, remaining neutral on who it is that performs the relevant tasks. In truth, the scope of work that is covered will rarely be performed by just one individual, function or department. Contracting is by its nature a diverse activity, drawing on many areas of skill and knowledge.

However, it is inevitable that certain terms are used in the book that may imply certain job roles or organizational alignments, so it is important to briefly describe or define what these terms mean.

**Commercial:** in general, commercial management or the commercial process tends to be broader than the role or activities implied by the term 'contract management'. However, we find that gap is narrowing (see the definition of contract management below). 'Commercial' is often used to describe activities that are non-technical and can therefore embrace areas such as sales, marketing and business operations. Our definition is not so wide and embraces only those areas that are of direct relevance to the structuring, content and performance of the contract. We see the role of a 'commercial manager' or of the 'commercial process' to ensure that all relevant stakeholder views have been incorporated and evaluated, to ensure

that the needs (of the customer) and capabilities (of the supplier) have been aligned. In this sense, we view the contract as a tool to undertake and oversee ‘commercial assurance’ of a deal or relationship and this may be from either a customer or supplier perspective.

**Contract management:** historically this has been viewed as a more administrative – and therefore much narrower and more reactive – activity than commercial management. It has often been a role that safeguards the rules or practices of others, rather than changing or questioning those rules. However, this book challenges that narrow definition and positions contract management as an activity equivalent to commercial management.

**Procurement:** as with other terms in this section, today we face a wide variety of job titles for those in the procurement function and indeed, in many organizations, procurement activities may be conducted by people who are not procurement professionals or within a procurement organization. Unless the context is clearly otherwise, the word must be seen as a broad description of an activity, rather than a formal job role or functional definition.

**Contract or Commercial Manager:** as stated above, we have in general sought to avoid the implication of specific job roles. These terms should be taken as indicating the performance of particular tasks, irrespective of who is actually performing them. We recognize, for instance, that ‘the contract manager’ in many cases might actually be a project manager, or a lawyer, or an engineer or a sales representative – and indeed, during the lifecycle of a specific contract, all of these individuals may be involved in performing contract-related tasks. However, we also recognize that many of our readers will be dedicated contracts or commercial professionals who see these terms as job titles – even though they too will acknowledge that the process we lay out in this book probably goes beyond the average scope of a contract professional’s job. This breadth of content may lead some to question whether the book goes too far in its claims to be about contracting operations. Our perspective here is that if we are to produce successful contracts and trading relationships, we must understand the overall process by which they are produced and take steps, as professionals, to ensure the quality of that process and our eventual work product.

**Contracting process:** as the previous definitions explain, this book seeks to describe a high-performing business process through which successful contracts and trading relationships are formed and managed. To the extent that it is practical, we try to describe differences that will result from the types of contract or relationship that a business wishes to enable. For example, high volume commodities demand a fundamentally different model from complex services or major, long-term projects. However, while the complexity of the task to be performed is dramatically different, the list of tasks remains highly consistent; the big difference is over who performs those tasks, how they are performed, and the time it takes to reach completion. It is these factors, of course, that lead us back to the opening statement about variations in job roles, skills and organization.

## The structure of this book

The aim of this book is to provide an operational guide to contracting that is independent of variations in organization or role. It is structured to reflect a process-based view, broken into the following phases:

**Initiate:** this phase is devoted to ensuring understanding of markets and their interaction with business needs and goals. It explains the importance of aligning these factors with contract structures, terms, policies and practices, to increase the probability of successful trading relationships and the overall efficiency of the contracting process. Without such alignment, contracts rapidly become viewed as an impediment to doing business.

**Bid:** this phase explores the bidding and proposal activities undertaken by each party to determine the extent of the ‘fit’ between needs and capabilities. It examines the financial aspects of the proposed relationship and highlights the legal and regulatory issues surrounding bid and proposal activity.

**Development:** this phase is dedicated to the development of an appropriate form of contract and the considerations and issues that most frequently require attention. It provides a framework that should enable better understanding of the risks associated with the specific relationship that is being evaluated and also provides a base for negotiation planning.

**Negotiation:** this phase provides an in-depth guide to negotiation of a contract. It recognizes that a growing number of negotiations are today ‘virtual’, using technology as an alternative to face-to-face meetings. It also highlights many of the issues and challenges that contract negotiators tend to encounter, both within their own organization and with the behavior or attitudes of the other side.

**Manage:** this phase examines the approaches needed to ensure successful implementation and management of the signed agreement. Many contracts span multiple years and it is frequently the case that they undergo major changes and, potentially, fundamental renegotiations. It is this phase that determines whether or not the results or outcomes envisaged at the time of contract signature are in fact achieved – or perhaps even exceeded.

## Moving forward

This book is based on content that was developed for IACCM on-line training modules. It has been developed in response to the wishes of many contracts practitioners to have a formal operational guide that supports their day-to-day activities, and can also be used by others who have a periodic need for guidance on contract management.

As with most disciplines, contract management is not static. Indeed, today’s global business environment suggests that we face a period of dramatic and rapid change in the way we

create and evaluate terms, conditions and contracts. It is envisaged that ‘best practice’ will demand regular updates. These will be achieved in part through the on-going interactive nature of IACCM on-line training materials, where students form active discussion groups and where message boards offer a forum for new issues and approaches.

Readers are invited to use these forums, accessible at [www.iaccm.com](http://www.iaccm.com), to share their experiences and raise questions that are not adequately answered by this book. The Lead Authors also welcome direct communication and undertake to ensure that all contributions are taken into account for future editions of this work.

