

## BSB60915 - ADVANCED DIPLOMA OF MANAGEMENT (HUMAN RESOURCES) Study Support materials for PSPPCM023 - Manage Strategic Contracts



## STUDENT HANDOUT

This unit covers the competencies required to manage contracts for strategic purchases, to effectively minimise risks and achieve value for money to meet an organisation's core objectives. It includes managing the establishment, performance and evaluation of strategic contracts.

In practice, managing strategic contracts may occur in the context of other generalist and specialist work activities, such as maintaining and enhancing confidence in public service or local government, establishing and maintaining strategic networks, managing compliance with legislation in the public service or local government, managing risk, developing a business case, planning for strategic procurement, coordinating strategic procurement and negotiating strategic procurement.

No licensing, legislative, regulatory or certification requirements apply to this unit at the time of endorsement.

## Elements and Performance Criteria

ELEMENT	PERFORMANCE CRITERIA
<b>1. Manage contract establishment</b>	1.1. Requirements of <b>contracts and strategic initiatives</b> are discussed, clarified and agreed by all parties. 1.2. Responsibilities for establishing and carrying out procedures are assigned to achieve contract outcomes. 1.3. Effective communication strategies and processes are established and implemented to assist ongoing communication between internal and external <b>stakeholders</b> and contractors. 1.4. Relationship management is undertaken of all levels of personnel involved in procurement and contract management, within probity boundaries. 1.5. Strategic relationships are established and managed within probity boundaries to improve procurement capability and performance. 1.6. Risk management plans are updated according to organisational policy and procedures.
<b>2. Manage contract performance</b>	2.1. Progress of contracts is <b>monitored</b> against set targets and performance measures to ensure success of procurement activities. 2.2. Should monitoring find that set targets, performance measures and probity requirements are not being met, action is taken to rectify performance in a timely manner. 2.3. Advice and support are provided to solve problems, make improvements and maintain progress. 2.4. Disputes are managed promptly according to contractual conditions to achieve resolution and maintain contract performance and progress. 2.5. Opportunities to continuously improve procurement outcomes are sought and negotiated with contractors. 2.6. Approvals are provided or gained for <b>contract variations</b> that are negotiated and agreed between the parties. 2.7. Opportunities are provided for stakeholders and contractors to have input into and receive feedback on progress during the performance of the contract. 2.8. Internal and external stakeholders are engaged as necessary throughout the life of the contract to maintain progress.
<b>3. Manage contract evaluation</b>	3.1. Evaluation of contract performance is undertaken relative to planned performance measures and in consultation with stakeholders and contractors. 3.2. Where stakeholders and contractors do not agree, dispute resolution is undertaken according to organisational policy and procedures. 3.3. Conclusions are detailed against agreed criteria to provide a complete picture of <b>performance of contractors</b> , organisation's <b>procurement processes</b> and <b>value for money</b> . 3.4. Performance of strategic initiatives is measured relative to planned outcomes in consultation with industry and other stakeholders. 3.5. Lessons learnt from evaluations of contracts and strategic initiatives are documented according to organisational requirements and used to continuously improve future procurement activities. 3.6. Contractors and stakeholders are advised of evaluation outcomes in a timely manner according to organisational guidelines.

## What is a contract?

A *contract* is a *legally binding* or *valid* agreement between two parties. The law will consider a contract to be valid if the agreement contains all of the following elements:

1. offer and acceptance;
2. an intention between the parties to create binding relations;
3. consideration to be paid for the promise made;
4. legal *capacity* of the parties to act;
5. genuine *consent* of the parties; and
6. legality of the agreement.
- 7.

An agreement that lacks one or more of the elements listed above is not a valid contract. Each of these elements is dealt with in more detail below.

Not all *contracts* need to be in writing. Contracts that are required by law to be in writing include contracts to buy and sell land or to buy a motor car and door-to-door sales contracts. However, it is always useful to have the terms agreed between the parties written down and attached to or kept with any other relevant papers; for example, copies of quotations, brochures, pamphlets, etc. that were supplied at the time the contract was entered into. Receipts for money paid should always be kept. If a dispute arises, these documents will assist in resolving differences between the parties.

A written contract can be drawn up by listing all the terms agreed between the parties and getting each of the parties to sign and date the document at the end.



A business contract is a legally binding agreement between two or more parties to do or not to do certain things. *For example, a business contract could be for the sale of goods or supply of services at a certain price.*

There are many different types of contracts including:

- the sale and purchase of a business agreement;
- partnership agreements;
- leases of business premises;
- leases of plant and equipment; and
- employment agreements.

The process for creating a contract generally includes information exchange, discussion, and negotiation and employment agreements.

## **What are the essential elements of a contract?**

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To be legally binding a contract must contain four essential elements. These four elements are:

- offer;
- acceptance;
- intention of legal consequences; and
- consideration.

The four essential elements of a contract can be briefly explained as follows; a contract is formed when one party makes an offer and that offer is accepted by another party for an exchange of some benefit or something of value by the parties (this is the consideration element). The intention of the parties is that they are legally bound by the contract.

## **When can a contract be invalid?**

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Even if the four essential elements are present a contract could in be invalid if:

- It is an illegal contract. Examples of illegal contracts are an agreement to commit a crime and an agreement that breaches legislation, such as unconscionable conduct under the Competition and Consumer Act 2010.
- The person or entity lacks the capacity to enter into the contract. Examples of persons lacking capacity are minors and bankrupts.
- The contract involves misleading or deceptive conduct, mistake, duress, undue influence, unconscionable conduct or other categories that at law can cause the contract to be avoided.

## **Can a contract be verbal or written?**

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Contracts can be verbal or written, provided they contain the four essential elements of a contract. However, a verbal contract is much more difficult to prove. Some types of contract such as those for buying or selling real estate and credit must be in writing.

A written agreement is recommended as it:

- becomes your proof of what was agreed upon;
- prevents ambiguity or misunderstanding;
- prevents either party forgetting or changing the terms later; and
- makes the parties focus on the essential issues and come to a definite agreement.

Unless you're a lawyer nobody expects you to write your own contracts. However, as a business owner you're expected to be able to read a contract and understand what it means.

## **What general matters are covered in a contract?**

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Some of the general matters that a business contract can cover include but are not limited to:

- parties to the contract
- date of the contract
- definitions used in the contract
- description of the goods and services that your business will provide or receive
- payment amount and details of payment dates
- interest on late payments
- delivery dates of goods and performance dates for services
- insurance provisions
- guarantee provisions
- termination dates of the contract
- renewal terms
- damages for breach of contract
- termination conditions
- special conditions.

## Standard contracts and obtaining legal advice

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The Small Business Development Corporation (SBDC) is frequently asked for standard business contracts for a variety of purposes such as buying a business, leasing commercial premises, partnerships or employment contracts.

We do not provide standard contracts or templates, although some 'standard contracts' may be available through industry associations. We recommend contracts are drafted to reflect the unique commercial circumstances of the parties negotiating the agreement. The lawyer drafting the contract will take into account their client's concerns, commercial risks and matters agreed during negotiations.

***Keep in mind that you should always get legal advice before signing a significant contract.***



## Get the right advice

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In business it is particularly important to get the right advice before entering into a business contract, or you could face significant and far-reaching consequences.

Legal advice will ensure your rights are protected and favourable terms are negotiated on your behalf - terms that better suit your business and allow you to trade profitably, which means the likelihood of costly disputes in the future is reduced.

Furthermore, the underlying transaction of a contract can have GST, taxation and stamp duty consequences and this aspect of the contract could also require professional advice.

<http://www.smallbusiness.wa.gov.au/business-contracts/>

## Identify and manage risks

Risks identified previously may be relevant at this stage of the cycle and should be considered along with any risk management plan that has been developed.

Risks to the management of individual contracts can include the following:

Sources of risk	Examples of risks
Contract management capability	<ul style="list-style-type: none"> <li>Failure to have sufficiently skilled and experienced resources to effectively manage the contract(s)</li> <li>Lack of recognition of the importance of contract management</li> <li>Failure to act on contractor underperformance</li> </ul>
Contractor performance	<ul style="list-style-type: none"> <li>Failure to provide contract deliverables on time, to the agreed quality standards</li> <li>Failure to adhere to the agreed budget</li> <li>Failure to comply with all contract provisions, for example, privacy, security, recordkeeping</li> <li>Fraud and/or unethical conduct by the contractor</li> </ul>
Changes in circumstances and/or requirements	<ul style="list-style-type: none"> <li>Contract changes not dealt with as contract variations</li> <li>Contractor not prepared to agree to contract variations to accommodate changes in entity requirements</li> <li>Changes in circumstances not managed in a timely manner</li> </ul>
Stakeholder relationships	<ul style="list-style-type: none"> <li>Stakeholders not consulted and/or kept informed about contract performance</li> <li>Changes in stakeholder expectations not communicated to contract manager</li> <li>Differing and/or conflicting stakeholder expectations</li> </ul>

**Ensuring that any identified risks are dealt with appropriately may require a specific risk mitigation plan to be developed.**

Ensuring that any identified risks are dealt with appropriately may require a specific risk mitigation plan to be developed. Such a plan need not be long and cumbersome; it may consist of a simple checklist or it may be a detailed plan that requires periodic review and updating throughout the life of the contract. Where a contract is to be managed by a team over a longer period of time, a plan may assist with coordination among team members and stakeholders. The issues discussed below should be addressed by any plan or checklist developed to guide the contract management.

In addition, consideration should be given to the need to develop appropriate contingency plans to address unplanned or unexpected events. Such plans may be required where the consequence of contract failure is critical to a range of stakeholders, such as members of the public.

### Contract Management Plan

As discussed in Part 2 of this Guide, irrespective of the size, nature and duration of the contract, a contract management plan is a useful tool to assist in managing and administering the contract, including risks to the success of the contract. Such a plan may be a checklist or a formal plan that addresses in detail the issues discussed in this part of the Guide.

As noted earlier, much of the work required to develop the contract management plan can and should have been done at the time the contract was being developed. Thereafter, the plan should be routinely reviewed and updated.

[http://www.anao.gov.au/html/Files/BPG%20HTML/Developing%20and%20Managing%20Contracts/5\\_2.html](http://www.anao.gov.au/html/Files/BPG%20HTML/Developing%20and%20Managing%20Contracts/5_2.html)

**Contract management** or **contract administration** is the management of contracts made with customers, vendors, partners, or employees. The personnel involved in Contract Administration required to negotiate, support and manage effective contracts are expensive to train and retain. Contract management includes negotiating the terms and conditions in contracts and ensuring compliance with the terms and conditions, as well as documenting and agreeing on any changes or amendments that may arise during its implementation or execution. It can be summarized as the process of systematically and efficiently managing contract creation, execution, and analysis for the purpose of maximizing financial and operational performance and minimizing risk.

Common commercial contracts include employment letters, sales invoices, purchase orders, and utility contracts. Complex contracts are often necessary for construction projects, goods or services that are highly regulated, goods or services with detailed technical specifications, intellectual property (IP) agreements, and international trade.

A study has found that for "42% of enterprises...the top driver for improvements in the management of contracts is the pressure to better assess and mitigate risks" and additionally, "nearly 65% of enterprises report that contract lifecycle management (CLM) has improved exposure to financial and legal risk."

## Areas of Contract Management

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The business-standard contract management model, as employed by many organizations in the United States, typically exercises purview over the following business disciplines:

- Authoring and negotiation
- Baseline management
- Commitment management
- Communication management.
- Contract visibility and awareness
- Document management
- Growth (for Sales-side contracts)

[http://en.wikipedia.org/wiki/Contract\\_management](http://en.wikipedia.org/wiki/Contract_management)



## Managing the Contract Checklist

This checklist could be used by the contract manager or a senior manager with management responsibility for overseeing a contract or contracts to gain assurance that the necessary governance arrangements are in place at the commencement of the contract. The ongoing management section of the checklist could be used periodically, say every three or six months, to check that the necessary actions are being taken to manage the contract.

### Contract commencement

- Does the contract manager have the required level of skills and experience?
- Does the contract manager have a satisfactory level of understanding of the contract and of the relevant subject matter?
- Have risks to the management of the contract been identified and risk treatments identified?
- Is it clear who is responsible for implementing/actioning any necessary risk treatments?
- Has responsibility for all aspects of managing the contract been clearly assigned?



- Do delegations exist for the approval of contracts, contract variations and the approval of expenditure?
- Have all stakeholders been identified and arrangements agreed to obtain feedback/input throughout the life of the contract?
- Have the benefits of flow charting internal processes, e.g. dispute escalation arrangements, been considered?

### Ongoing management

- Are contract payments linked to satisfactory contract performance?
- Are all invoices, and any supporting documents, checked to ensure they are in accordance with contract requirements and are in order to pay?
- Is timely action taken when contract performance is unsatisfactory?
- Are all variations to the contract agreed on value-for-money grounds?
- Are all amendments to the contracts subjected to formal contract variations? Is a record maintained of all contract variations?
- Where the contract does not meet agreed levels of performance, are any actions taken adequately documented? Where it is decided not to take action, is this decision properly approved and documented?
- For longer term contracts, is the contract subject to periodic review?
- Are any disputes addressed in a timely manner and satisfactory efforts made to resolve them?
- Is the contract being actively managed so that there is reasonable assurance that the contract outcomes are being achieved?

### Contract extension/renewal

- Do systems/procedures enable the timely consideration of the need for contracts to be extended or renewed?
- Are all contract extensions justified on value for money grounds?
- Are there arrangements in place designed to ensure that probity issues are identified and addressed during contract extension and re-tender processes?

### Ending the contract

- Has the contractor delivered all the required contract outcomes?
- Has the contractor met all their contractual obligations?
- Has the contractor returned all Commonwealth material, equipment or other resources used or generated during the life of the contract?
- Have all access arrangements been terminated?
- Has an evaluation of the contract been undertaken and, where appropriate, lessons learned been built into future contracting activities?
- Has the contractor's performance been evaluated, properly documented, and feedback provided to the contractor?

[http://www.anao.gov.au/html/Files/BPG%20HTML/Developing%20and%20Managing%20Contracts/managing\\_checklist.html](http://www.anao.gov.au/html/Files/BPG%20HTML/Developing%20and%20Managing%20Contracts/managing_checklist.html)

**Contract life cycle management** “is the process of systematically and efficiently managing contract creation, execution and analysis for maximising operational and financial performance and minimising risk”.

Importance of contract management Organisations in both the public and private sectors are facing increasing pressure to reduce costs and improve financial and operational performance. New regulatory requirements, globalisation, increases in contract volumes and complexity have resulted in an increasing recognition of the importance and benefits of effective contract management.

The growing recognition of the need to automate and improve contractual processes and satisfy increasing compliance and analytical needs has also led to an increase in the adoption of more formal and structured contract management procedures and an increase in the availability of software applications designed to address these needs.

It is worthwhile noting that contract management is successful if:

- the arrangements for service delivery continue to be satisfactory to both parties, and the expected business benefits and value for money are being realised
- the expected business benefits and value for money are being achieved
- the supplier is co-operative and responsive
- the organisation understands its obligations under the contract



- there are no disputes
- there are no surprises
- a professional and objective debate over changes and issues arising can be had
- efficiencies are being realised

**Assembling the project team**

The need to assemble a team to manage a contractual procurement programme will be determined not only by the scale, nature, complexity and significance of the procurement and the necessary skills and experience but also by the extent to which it is considered appropriate, beneficial or a requirement to comply with organisational policy to involve stakeholders in the project.

Factors to be considered when assembling the team are:

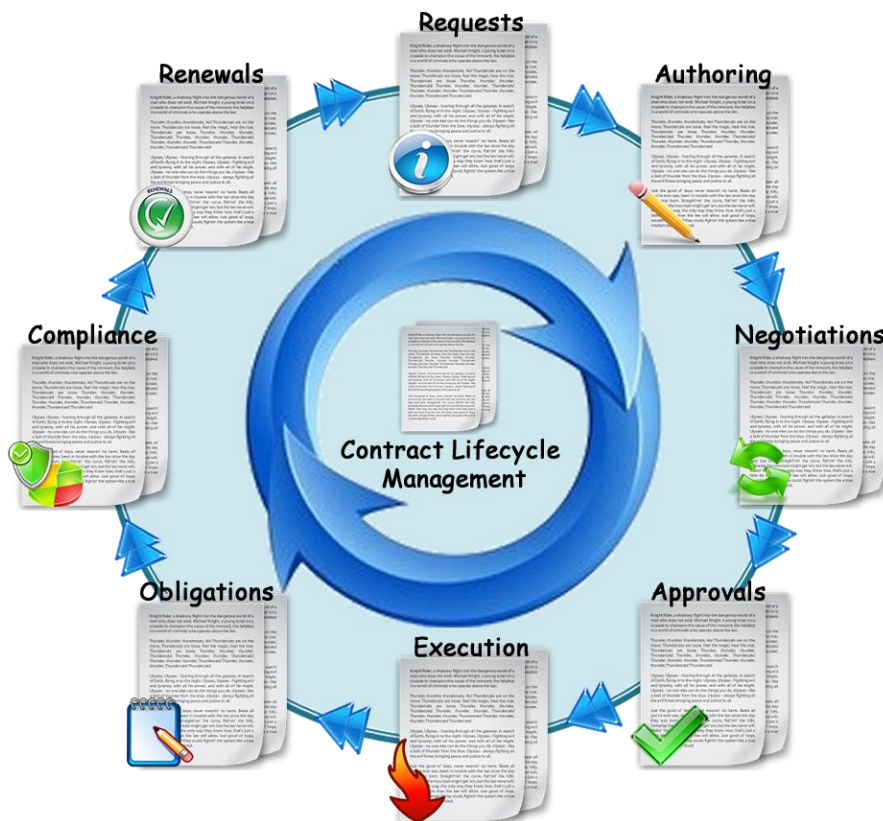
- the nature of the project
- the nature of the work environment and the management style of the team
- communication

In addition to procurement, the project team may be drawn from any and all disciplines within the organisation as appropriate and relevant. The following are examples; design, research and development, production, quality control, logistics, marketing and sales, legal, finance and human resources. The project team may also advantageously include representatives of the end users, whether internal or external, and representatives of disciplines within supplier organisations such as design, production, production planners and logistics.

Clearly, these individuals and groups will not need to meet all the time but, depending on the size and complexity of the project, there may well be a core group that meets regularly and this will be the project team. Others will then be called on as and when required.

In addition to the need to identify the necessary technical skills, knowledge and experience with the appropriate level of authority required of the members of the team, the importance of the ability of team members to work together effectively and the significance of the role of the project leader should be recognised.

[http://www.cips.org/documents/CIPS\\_KI\\_Contract%20Management%20Guidev2.pdf](http://www.cips.org/documents/CIPS_KI_Contract%20Management%20Guidev2.pdf)



**Managing contract variations**

Over the course of the contract, it may be necessary to manage variations to the contract, in terms of price, quantities, timing, delivery, changes in policy, etc. Contract managers should ensure that any such changes are made in accordance with the provisions of the contract.

A contract should not be varied to such an extent that it substantially changes the nature of the goods or services being delivered. A variation is an amendment to a contract that changes the original terms or conditions of the contract. Variations are usually to alter services, personnel or to change pricing. Provisions to allow and regulate contract variations should be a standard feature of all contracts. The ability to vary the contract should be directed or controlled by the acquiring entity and should only occur in defined circumstances. It is accepted practice for the variation mechanism to provide for variations to be agreed between the acquiring entity and the contractor in writing through a formal amendment of the contract. In some circumstances it is possible to inadvertently amend a contract by oral agreement or conduct, even where there is a contract provision expressly requiring a formal process to be followed. It is therefore important that those involved in managing and administering the contract do not agree to informal contract amendments.

Any proposed variations should be assessed to ensure that they do not breach Australian Government legislation or policy. Variations should be undertaken in line with the procedures set out in the contract or specific entity procedures. These procedures may cover explicit authorisation and reporting arrangements for contract variations, particularly for large, complex contracts of long duration.

**Variations should not be used to mask poor performance or serious underlying problems and the effect on original timeframes, deliverables and value for money should be assessed.**

The reasons for the variation should be clearly documented. Variations should not be used to mask poor performance or serious underlying problems and the effect on original timeframes, deliverables and value for money should be assessed. If the effects are significant, senior management and other stakeholders may need to be consulted and/or advised.

Changes to contractual arrangements have the potential to affect the scope and viability of the contract for either or both parties, and making substantive variations to a contract will require some of the actions and issues involved in developing the original contract. They should therefore be planned accordingly. Acquiring entities should be alert to the risk that multiple changes made to a contract over a period of time may shift the overall allocation of contract risk or transfer particular risks to the acquiring entity. It is important to analyse all consequences of a proposed contract amendment and to make sure there are no unintended effects of the change.

Contract managers also need to ensure that the contract variations are not of such a level that they significantly change the contract requirement and/or substantial parts of the original transaction. If this is the case, it may be necessary to undertake another procurement process because the revised arrangements are substantially different to those selected through the original procurement. The determination of when the contract has been so substantially changed so that it becomes a new contract can be a difficult matter of judgement. It is fundamentally a procurement decision that may require specialist advice.

### **Contract variations checklist**

Key issues to consider in managing contract variations include:

- following the procedures required by the contract;
- assessing the reasons for the proposed variation and whether these may indicate an emerging or actual performance problem;
- assessing the impact of the proposed variation on the contract deliverables, particularly whether the variation or the work it represents is actually required and whether it was part of the original contract deliverables;
- determining the effect the proposed amendment will have on the contract price;
- considering the authority for making the variation, and obtaining and documenting the required approvals;
- properly documenting the details of the variation and its impact; and
- meeting any reporting requirements, such as updating the entity's contract register and including details in AusTender, where appropriate.

[http://www.anao.gov.au/html/Files/BPG%20HTML/Developing%20and%20Managing%20Contracts/5\\_10.html](http://www.anao.gov.au/html/Files/BPG%20HTML/Developing%20and%20Managing%20Contracts/5_10.html)

### **Managing disputes**

Disputes should be identified and addressed as soon as possible to ensure effective resolution. You should refer to the contract for the dispute resolution mechanism agreed at the time the contract was entered into.

While a sound understanding by both parties of their contractual responsibilities and professional relationship management should reduce the potential for disagreements and disputes to arise over the life of the contract, these can still occur.

As a general rule, a disagreement becomes a dispute when it is not possible for the parties to resolve it without resort to a formal resolution mechanism. Generally, what a dispute is and when it is deemed to have occurred is defined in the contract, often in a dispute resolution clause.

Many disagreements and disputes arise when the parties cannot agree on issues related to the interpretation of contract provisions, the definition of deliverables, meeting performance standards and/or the effect of unexpected events. These disagreements may be of a minor nature and can be readily resolved. It is important that any possibility of dispute or an actual dispute be recognised at an early stage and addressed as quickly as possible. Avoiding the escalation of disagreements can impact on the contract deliverables and reduce the costs to both parties.

**Where a dispute arises, the contract manager's role is to protect the Australian Government's interests in all cases.**

However, where a dispute arises, the contract manager's role is to protect the Australian Government's interests in all cases.

The forms of dispute resolution can include negotiation, arbitration, mediation, or litigation. These are discussed under separate headings below.

### **Negotiation**

As discussed, the need to negotiate may arise throughout the procurement cycle. The importance of negotiation skills was also discussed under the skills heading.

Negotiating between the acquiring entity and the contractor is the most common approach to resolving disagreements and disputes. At this stage of the procurement cycle, the intention of the negotiations is to reach a mutually acceptable solution, where both sides consider they have gained the best possible result in the circumstances. It is important that one party does not consider they have been unduly pressured to agree to a particular solution as a result of the negotiation, as this can lead to an escalation or reappearance of the dispute at a later stage.

**At the early stages of a potential dispute it is generally preferable to attempt to resolve the matter by first discussing the issues with the contractor.**

At the early stages of a potential dispute it is generally preferable to attempt to resolve the matter by first discussing the issues with the contractor. These discussions may take place in the course of regular meetings between the parties or as separate discussions. Such an approach may mean that it is possible to resolve any disagreements and prevent a formal dispute arising.

When these informal arrangements do not result in a resolution of the issue, invoking the dispute resolution provisions of the contract will need to be considered. When this step is taken, careful preparation and planning needs to be taken, including determining the need to obtain specialist advice and assistance.

Irrespective of the approach adopted, negotiations should be undertaken by a person(s) who has the appropriate authority and skills and care needs to be exercised to ensure the outcome does not contravene any legal or policy requirements. It is also important that the details of all discussions and negotiations are recorded and a record maintained of all the agreements reached.

### **Mediation**

Mediation involves the use of a neutral third party to assist in resolving the dispute. The mediator does not impose a decision on the parties in the way a court or arbitrator does, but instead seeks to help the parties to resolve the dispute themselves. Mediation is usually regarded as a faster, less formal and less costly process than court proceedings or arbitration. There are a number of commercial organisations who maintain registers of mediators, and who can be approached to appoint a mediator for a dispute.

### Arbitration

Arbitration is a formal dispute resolution process governed by legislation in which two or more parties refer their dispute to an independent third person (the arbitrator) for determination. The aim of arbitration is to obtain a final and enforceable result without the costs, delays and formalities of litigation. Arbitration proceedings are private and can be held at a mutually convenient time. The actual proceedings are less complex than litigation and the arbitrator can be a person who is able to provide technical expertise relevant to the contract.

It is, nevertheless, an adversarial procedure with the possibility that neither party will be satisfied with the outcome, nor it may be costly. Other possible drawbacks that should be considered before entering into arbitration include: the difficulty in selecting an agreed arbitrator; the expertise of the arbitrator for the particular case; uncertain appeal rights; and the lack of legal precedence.

### Litigation

Litigation is the act or process of contesting a lawsuit or seeking redress through the courts. It can be an expensive and time-consuming procedure and is generally taken when other avenues of dispute resolution have not been successful or are not available. Other approaches to resolving disputes or contractor defaults should therefore be considered prior to litigation. Appropriate legal and other professional advice should be obtained prior to considering and commencing litigation. The Legal Services Directions 2005 issued by the Attorney-General outline certain requirements that apply to FMA Act agencies and CAC Act bodies when considering or conducting litigation.

[http://www.anao.gov.au/html/Files/BPG%20HTML/Developing%20and%20Managing%20Contracts/5\\_12.html](http://www.anao.gov.au/html/Files/BPG%20HTML/Developing%20and%20Managing%20Contracts/5_12.html)

