



# Contract Management Guide

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## Introduction and scope

This guide is intended to cover all those activities associated with contract management from the establishment of the business case and the confirmation of need, through contract administration and relationship management to the review of contract performance. The activities themselves are divided into two distinct but interdependent phases, upstream and downstream of the award of the contract.

The guide is generic in that its principles are intended to be applicable to all contracts from a simple order, through framework contracts to complex construction or service contracts, and it should be seen as equally applicable to contracts in the private as well as the public sector.

## Definition

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”.<sup>1</sup>

There are a number of other definitions of contract management, the majority of which refer to post-award activities. Successful contract management, however, is most effective if upstream or pre-award activities are properly carried out.

## 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.<sup>2</sup>

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.

<sup>1</sup>(Aberdeen Group)

<sup>2</sup>(Aberdeen Group)

## Activities

The foundations for effective and successful post-award contract management rely upon careful, comprehensive and thorough implementation of the upstream or pre-award activities. During the pre-award stages, the emphasis should be focused on why the contract is being established and on whether the supplier will be able to deliver in service and technical terms. However, careful consideration must be given to how the contract will work once it has been awarded. The organisation's high-level requirements should be carefully researched so that there is clarity of purpose from the outset. This will help to ensure clarity in all aspects of the procurement process.

Management of contracts, particularly partnerships, requires flexibility on both sides and a willingness to adapt the terms of the contract to reflect changing circumstances. It is important to recognise that problems are bound to arise which could not be foreseen when the contract was awarded.

Finally, it may not be necessary to follow every activity for every contract - particularly in the case of small, simple orders - but it is advisable to read the whole guide and to apply the advice provided under each stage as appropriate to the particular contractual circumstances.

## Upstream or pre-award activities

### a) Preparing the business case and securing management approval

All contracts are predicated on the need to obtain management commitment and approval at the appropriate level. This involves the formulation of a sound business case aligned to the organisation's corporate and functional strategies.

The business case sets out the policy, business and contract objectives and the issues that affect the decision and the investment. It should seek to establish that the proposed contract will meet the need, that it is achievable and affordable, and it should address the following issues:

- the outcome(s) of the contract
- critical success factors
- the possible alternatives, including existing contracts
- the risks including the extent and where they may fall
- identification of any contingent needs and ramifications of proceeding
- timescale.

The business case should be prepared with the involvement of the stakeholders, including where and if possible, the end users.

It should be signed off by the sponsor or patron.

The business case is a working document and should form the basis of the post-implementation review and used as a management tool to ensure that the original outcomes and benefits have been achieved.<sup>3</sup>

<sup>3</sup> (OGC Contract Management)

If the project is large, complex and in particular, innovative in nature, the market should be approached concurrently with the preparation of the business case, firstly to alert them to the potential need and secondly to take soundings on such issues as feasibility, capacity, capability, approach and level of interest.<sup>4</sup>

### **b) 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 internally and externally.

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.

These aspects are beyond the scope of this guide, but it is considered advisable to devote time to studying the many books available on the topics of motivation, leadership, power, influence and group working, particularly if the size, timescale and complexity of the procurement project are significant.<sup>5</sup>

### **c) Developing contract strategy**

The strategy relating to a particular contract should accord with the organisation's overall procurement strategy.

The development of a contract strategy is designed to establish the form of the procurement and provide assistance in determining the formulation and award of the contract and the style and type of

<sup>4</sup> (OGC Contract Management)

<sup>5</sup> (For example see Handy Understanding Organisations)

management to be adopted for the subsequent service delivery, relationship management and contract administration.

There are many references these days to ‘partner’ rather than suppliers – should this be captured here?

The latter aims can be characterised by the need to address understanding, measurement and communication post-contract award. A successful contract management strategy should achieve benefits by:

- managing the organisation’s own responsibilities during the contract
- ensuring the supplier meets the minimum performance criteria, such as compliance
- allowing the achievement of both short and long term supplier performance improvement through developing effective supplier relationships.

In developing the contract strategy, the following issues need to be addressed:

- nature, scale and significance of the need to the organisation
- value of need
- type of specification - input or output
- complexity of the need including innovation level
- attractiveness to the market
- market capacity
- timescale and phasing
- level of understanding of the need by stakeholders and potential suppliers.

The use of supplier positioning matrices will also assist in determining the contract strategy, the nature of any negotiations that may need to be

conducted and the form of the supplier relationship following the award of contract. Possible supplier relationship types range from the spot buy through call-off contracts, fixed contracts and strategic alliances, to long term partnerships. Issues of relationship style such as adversarial, partnership, hands-on or pro-active should also be considered.<sup>6</sup>

Concurrently with determining the contract strategy, consideration should be given to the evaluation strategy which sets the direction for the overall evaluation of suppliers and the associated tender process. It covers such considerations as:

- business aims
- critical success factors
- relative priorities of the requirement
- communication plans
- criteria for determining quantifiable and non-quantifiable items
- overall evaluation procedures including assessment methodology
- personnel involved in the evaluation
- supplier selection criteria including guidance on interpretation and marking of replies.

Another important consideration in establishing contract strategy is whether to utilise Service Level Agreements (SLA). SLAs are negotiated agreements designed to create a common understanding about services, priorities and responsibilities and are applicable in two situations. Firstly, internally used and provided specialist support services and secondly when outsourcing.

<sup>6</sup> (CIPS study guide Legal & Procurement Processes)

Internal SLAs are not intended to have legal consequences since the customer and the supplier are part of the same legal entity which cannot sue itself, and normally there will be no direct financial compensation. External SLAs such as those for bought-in or outsourced services may have contractual implications. They are generally a schedule or part of a schedule to the buy-in or outsource agreement. It should also be remembered that EC Procurement Directives may apply to organisations using SLAs.

The purpose of SLAs and setting service levels is to enable the customer to monitor and control the performance of the service received from the supplier against agreed standards. It should be understood that service levels should be agreed and benchmarked for both customers and suppliers and should be:

- established at a reasonable level; if they are set too they will attract additional charges from the supplier
- prioritised by the customer in order of importance and on an agreed scale for example critical, major, urgent, important, minor, easily monitored, such as objective, tangible and quantifiable
- unambiguous and understandable by all parties
- open to re-negotiation at any time.

There are advantages and disadvantages in using SLAs. Among the advantages are:

- the service providers and the customers are clearly identified
- attention is focused on what a service actually does as opposed to a belief about the service

- customers have a greater awareness of the services received and the additional services that can be provided
- customers' real needs are identified and the associated costs are made clear
- services and service levels adding value can be more easily identified and distinguished
- greater awareness of costs/benefits of services and levels
- service level monitoring is facilitated
- failure reports enable improvements to be readily introduced
- understanding and trust is created between customer and supplier.

Disadvantages include:

- joint drafting of SLAs, negotiation and measurement processes can be costly
- potential increase in bureaucracy
- internal providers are seen as suppliers and not colleagues
- time wasted if clear goals and objectives are not set out initially, this leads to unrealistic expectations and acrimonious relationships, as well as giving the setting up of SLAs a bad reputation
- training needed to overcome resistance to the introduction of SLAs.<sup>7</sup>

#### **d) Risk assessment**

Risk can be defined as “the probability of an unwanted outcome happening”.

Risk assessment should be viewed in the overall context of risk management and seen as one of the three key activities – risk analysis, risk assessment and risk mitigation - which facilitate the taking of

<sup>7</sup> (For more information on SLAs and their successful implementation see *Service Level Agreements in the CIPS How to series*)

decisions and actions to control risk appropriately.

Risk analysis is the process of identifying all the potential issues that can go wrong with an activity and then estimating the probability of each happening. It should form part of any significant contract management process and is a fundamental part of determining the contract strategy. The process can range from a simple listing of risks on an informal, intuitive basis to a formal process involving set procedures and working with other professional disciplines in brainstorming and technically and financially evaluating potential risks. A more formal process may involve the establishment of a risk register for each tenderer and, following contract award, the transfer of the register of the successful tenderer to the contract management team for use in risk assessment; see section 5).

In addressing the fundamentally important issue of risk in contract management, the purchasing professional should adopt a continuous “what if” mentality throughout the procurement of products and services. Risk management requires a professional who possesses knowledge of techniques, an analytical mind set, objectivity and a knowledge and thorough understanding of their organisation’s business and the market. It is advisable to seek to mitigate and remove risk whenever possible before contract award.

Risk assessment is the process of assessing the likely impact of a risk on the organisation. Highly predictable risks

may have low impact and it is possibly not worth taking action to control or avoid such risks. Conversely, low probability risks may have a significant impact demanding action to be taken to avoid or mitigate the risk.

Other issues for consideration in risk assessment:

- the costs of identifying, controlling or avoiding the risk
- the need for insurance for risk not readily managed or avoided
- the need for “sensitivity analysis” on risks of an unknown level or magnitude
- identifying compensating behaviour practices
- the impact of time, external factors and project actions on risk and the need for assessment to be iterative
- the impact of product life cycle including disposal and obsolescence.

Having assessed the risks and identified those requiring action, responsibility for managing and mitigating them should be allocated. This allocation should be dependent on the assessment of the likelihood and consequence of the risk.

Other issues to be considered in risk mitigation:

- identifying the most appropriate body to manage or control the risk in terms of expertise, time and/or resource
- establishing a fair and reasonable reimbursement mechanism
- insurance
- risk transfer to suppliers including issues of appropriate level, “trade off” and supplier contingency.<sup>8</sup>

<sup>8</sup> (CIPS POP Risk management in P & SM)



A further issue, usefully classified under a consideration of risk in contract management is fraud. The need to address potential areas for fraud in buyer/supplier relationships and measures to mitigate their impact should be considered at this early stage in upstream activities, particularly contract formulation.

The adoption of a continuous “what if” mentality – a similar approach to that used when assessing risk - is advisable when considering areas for potential fraud. The CIPS Knowledge paper on Fraud provides useful guidance on areas of weakness and counter measures and gives answers answers to some frequently asked questions.

#### **e) Developing contract exit strategy**

A contract will conclude when both parties have satisfactorily fulfilled their responsibilities under the terms of the contract. This, for example, will occur when the goods or services have been supplied and payment made and/or at the end of a pre-agreed period of time. This situation, however, does not remove the need to develop a contract exit strategy as part of the process of risk identification and reduction, and reinforces the importance of establishing the foundations of sound contract management.

It is important to identify the circumstances under which early contract exit may be required or indeed desired. The following is merely a list of examples and is certainly not an exhaustive list:

- major default by your organisation; this may include contractual breaches or changed circumstances - market, political ,economic, funding resulting in major procurement need changes, financial resulting in non-payment of supplier's invoices
- major default by the supplier; this may include breaches, technical inability, capacity, and so on
- frustration of the contract.

Whilst many of these sets of circumstances are generally predictable, and “standard” terms and conditions are widely included in contracts today, it does not detract from the need to carry out this aspect of risk assessment and to ensure that clear and comprehensive terms and conditions are drawn up which address the identified circumstances and the rights and responsibilities of the parties and the means by which any damages or costs may be mitigated are set out. This latter should include the method by which the goods or services may continue to be provided and, if possible, seamlessly transferred to another supplier or contractor to ensure business continuity. It is also important to clarify any notice period to be given and any timescale constraints associated with the exit process itself.

#### **f) Developing a contract management plan**

During pre-contract award stages, it is normal for time to be devoted to the preparation of the business case, drafting specifications and tender documents selecting potential suppliers, and so on.

However, time and effort must also be spent on determining how the contract will work once it has been awarded. The importance of contract management has already been mentioned and it is vital that a contract management plan is drawn up in advance of contract award. This should set out how the obligations of all the parties should be carried out effectively and efficiently.

Contract management success factors, the conditions that should be met if a contract is to be managed successfully, are:

- the arrangements for service delivery continue to be satisfactory to both customer and provider
- expected business benefits and value for money are being realised
- the provider is co-operative and responsive
- the customer knows its obligations under the contract
- there are no disputes
- there are no surprises
- satisfactory delivery progress is demonstrable.

In addition to these success conditions, it is worthwhile noting the foundations of successful contract management and the need for preparing a management plan:

- the need for flexibility by the contracting parties, particularly in partnership agreements
- a willingness to adapt the terms of the contract to reflect change and unforeseen problems. Although the risk assessment process mentioned earlier may be carried out thoroughly and professionally, problems are still likely to arise during the contract period

- the need for the buying organisation to have clear business objectives, coupled with a clear understanding of why the contract will contribute to them
- the need to understand the provider's business objectives and drivers
- the ability to recognise and obtain senior management agreement to the need for the service provider to achieve their objectives and to make a reasonable margin
- the need for people with the right commercial, interpersonal and management skills to manage these relationships on a peer-to-peer basis and at multiple levels in the organisation.
- to recognise that all parties need managers who can manage upwards in their organisation and persuade their boards to make decisions for the benefit of the relationship.

Other issues to be addressed and appropriate processes and procedures set out in the contract management plan include:

- the processes for managing the contract which provide the level of control you need, such as contract governance
- the retention of sufficient expertise to understand the technical direction in which the provider is taking your organisation and to retain the ability to enter into effective dialogue with the supplier
- to ensure as far as is possible that the supplier is able to provide sufficient skilled resources, given the risk that another customer's account might take priority

- the possibility of the supplier team changing after award of contract, leading to a lack of continuity
- to set down how the members of any supplier consortium handle a variety of different types of issues so as to ensure that problems are resolved quickly and constructively
- to set down how members of a supplier consortium should share common quality management systems and escalation procedures
- to set down the timescale and methods by which the provider's level of knowledge and understanding of your business can be gained and transferred to the supplier's successive team members
- roles and responsibilities of individuals of the parties to the contract; this includes issues such as:
  - adopting the principles of good communication, awareness of new demands in partnership arrangements, leadership, appropriateness and capability of existing management structures, understanding the responsibilities of the various parties, clear understanding of what is expected and effective ways of reporting progress, having a framework defining responsibilities, reporting arrangements and policies
  - establishing the performance measures to cover all aspects of the service such as:
    - cost and value obtained
    - performance and customer satisfaction
    - delivery improvement and added value
    - delivery capability
    - benefits realised
    - relationship strength and responsiveness
- It is important that the performance measures selected and set out in the contract offer clear and demonstrable evidence of the success (or otherwise) of the relationship. Once chosen, the requirements underpinning the performance measures should be the primary focus for contract management. They should provide the framework around which provider information requirements and flows, contract management teams, skills, processes and activities are developed.<sup>10</sup>

#### **g) Drafting specifications and requirements**

A specification is a statement of needs and its purpose is to present to potential suppliers a clear, accurate and comprehensive statement of the organisation's needs in order that they can propose solutions to those needs. At the same time, the specification should enable the organisation to readily evaluate offers, provide the basis for performance measurement and be a record of evidence in any dispute.

A specification is also known as an operational requirement or a statement of requirement. It can take the form of a conformance specification – where the organisation sets out how the supplier should meet its needs - or a performance or output-based specification where the supplier is given scope to propose solutions to an expected and known end result?

<sup>10</sup> (OGC Contract Management)

Although the drawing up of specifications in the majority of large organisations is not the responsibility solely of the buyer, nevertheless it should be emphasised that the successful drafting of specifications is one of the most important responsibilities of a professional purchasing officer.

The starting point for the preparation of the specification, particularly in the case of large and complex projects, is the business case. The drafting process is concerned with breaking down the overall scope set out in the business case into more detail and then, progressively and iteratively, refining into schedules of detailed requirements.

All contracts are different and the following process is not intended to be prescriptive but to act as a checklist for issues that should usefully be considered when preparing the specification:

- define in detail the scope of the need including the essential or core requirement, optional and “desirable” needs
- establish sources of information about the need from:
  - business owners
  - customers and users
  - other stakeholders
  - technicians
  - the supply market
- gather information on:
  - background to the need
  - future developments
  - detailed requirements
  - metrics required for performance measurement
- decide the type of specification to be used and then prepare draft. In large, complex contracts to be performed over a long period of time, the document could include the following:
  - introduction
  - scope of the requirement
  - background to the requirement
  - detailed description of the functional requirements, classified as essential, optional and desirable
  - description of the performance requirements including input and output details
  - timescale/timetable
  - performance measurement requirements, for example volume, accuracy, availability, including damages and incentives/ service credit details
  - other requirements, for example security, access, standards, training, personnel, disaster recovery, data archiving, data protection
  - constraints, for example, time, interface with other parties, IT issues
  - contract management requirements, for example management information, project management and risk management methodology, and processes
  - contractual requirements, for examples terms and conditions, roles and responsibilities of personnel, opportunities for submitting alternative proposals

- procurement procedures including timetable, evaluation and acceptance criteria and process, contact information, format and content of responses. Public sector organisations subject to the EU Procurement Directives must ensure that this information is also included in the notice placed in the OJ
- appendices providing background data, statistics, organisational information.

The process of preparing the specification should also include the drafting of the evaluation model and criteria. It is important to ensure that:

- all the information needed for evaluation has been requested from potential suppliers
- the evaluation covers all the organisation's needs
- the responses are in a format that enables an effective, clear and fair evaluation of offers to be carried out.

A successful specification should:

- set out the requirement fully, clearly, logically and unambiguously
- focus on the outputs and how they are to be met
- contain sufficient information for potential suppliers to submit credible and realistic offers
- ensure that all information needed for effective evaluation is requested
- permit offers to be evaluated against the declared criteria
- set out the acceptance criteria
- provide a fair opportunity for all potential suppliers to submit offers
- not discriminate against or be biased towards any supplier.

The specification document should be reviewed and signed off by a person with the necessary knowledge, experience and authority. The review should ensure that the specification:

- is complete and accurate
- meets stakeholders' needs
- addresses future requirements
- addresses identified risks
- complies with and addresses the issues identified by the original business case
- is capable of being met by the market
- complies with EU Procurement Directives (Public sector organisations only).<sup>11</sup>

#### **h) Establishing the form of contract**

Contracts can range from a single, ad hoc agreement for the provision of a product or service of relatively low monetary value, requiring little more than a short term, formal relationship, or an overarching framework agreement, through contracts for long term product or service contracts, to a series of contracts for large, complex construction or leading edge research and development contracts with multi-million pound values requiring the establishment of strategic partnerships and alliances.

Commercial or mercantile law includes agency agreements contracts for the sale of goods and services, insurance, negotiable instruments, carriage by air, sea and land and electronic trading, and there are extensive examples of forms of contract in all these areas.

<sup>11</sup> (OGC Contract Management, CIPS Study guide Legal & Procurement Processes, Lysons CIPS EU Procurement Directive Guides)

Clearly, however, a “one size fits all” approach to the form of contract is unsatisfactory and will be ineffective. It is therefore extremely important that the appropriate form of contract is drawn up that not only reflects the size, nature, value and complexity of the need but also the relationship required with the potential supplier(s).

Post-award management of longer term, high value and complex contracts can be categorised as service delivery management, relationship management and administration. The form and content of the contract document should therefore also be determined by the balance and significance required by each of these aspects of the post-award management.

It is worth reiterating that the foundations for successful contract management post-contract award are laid down in these stages and thus the aspects of clarity and comprehensiveness are extremely important in determining the form and content of the contract document.

#### **i) Establishing the pre-qualification, qualification & tendering procedures**

Evaluating the suitability of potential suppliers to meet the commercial requirements of the organisation is normally undertaken via a pre-qualification system. This is the most efficient method of assessing suitability to meet the required criteria and is carried out prior to inviting them to tender. In large, complex contracts of long duration it is important to

determine firstly, whether or not the organisation will adopt a pre-qualification system, determine the qualifications or criteria and concurrently decide the tendering procedures.

Public sector organisations must comply (if the procurement itself is applicable) with the requirements of the EU Procurement Directives. These cover all aspects of the procurement of works, goods and service requirements and govern consideration of the tendering procedures to be adopted by the buying organisation. The Directives also set out the rules covering the procurement procedure to be followed and the permitted criteria for selecting (or excluding) suppliers invited to tender under the restricted and negotiated procedures and the contract award criteria. The Competitive Dialogue process has now been introduced – should this also be referred to here.

*“The EU Procurement Directives also set out rules covering particularly complex contracts in which a Competitive Dialogue process can be employed. Thus consideration of the tendering procedure to be followed should also have regard to the contract’s complexity.”*

The regulations limit the scope of the Selection Stage to three key areas of questioning relevant to the subject areas of the contract:

- eligibility in terms of insolvency, grave misconduct, and so on.
- economic and financial standing
- capability and capacity for the project and track record in providing similar services.

Buying organisations not subject to the EU Procurement Directives should also, however, give full consideration to the procedures by which they seek potential suppliers, evaluate and award contracts.

The pre-qualification or selection of potential suppliers is a critical stage in the overall evaluation and award process. It should be seen as distinct from the contract award but as a process which informs and assists the contract award decision.

The pre-qualification requirements should accord with the overall evaluation strategy drawn up concurrently with the procurement and contract strategy referred to in section C.

The key to success at the pre-qualification or selection stage is to strike a balance between the creation of a shorter list of potential suppliers from the list of suppliers indicating an interest, which can be the subject of in-depth evaluation, and a list sufficiently large to ensure that suitable suppliers are actually selected and proceed to the tender invitation or ITT stage.

Information on supplier capability and capacity can be sought through a number of routes, formally and informally. In the case of complex requirements, it is advisable to indicate in any advert (including for Public sector organisations, any notice placed in the OJ) that a Pre-qualification questionnaire (PQQ) will be issued to those expressing interest.

The PQQ should seek the following general information:

- organisation, including ultimate parent details, identity and ownership, background
- principal activities (past and present)
- organisational chart
- contractor/sub-contracting approach
- professional/commercial affiliations
- legal
- financial
- capability
- quality management systems
- experience and track record.

The PQQ should also make it clear that references may be sought from selected current customers.

It is important that PQQ questions ‘make sense’ to the supplier, that they deal with topics, processes and services that they can readily understand, that the PQQ does not ask for inappropriate information (or the right information in an inappropriate way) and the suppliers have scope to question, suggest and possibly adapt your needs.

The dividing line between the information needed for selection and that which is obtained later (at evaluation or during negotiations) is not always clear-cut. In some areas, it may differ in degree of detail rather than in nature. Some areas may require expansion or clarification later on, possibly through site visits. It is important to avoid putting suppliers to extra work that adds no value. Therefore, only ask for information which will actually be used in assessment, avoid scoring systems based on questions

requiring only "yes" or "no" answers, consider, where appropriate, using standardised formats and word limits to level the playing field and reduce bid costs and evaluation timescales, and seek information from participating suppliers on likely bid costs and ways to reduce them.

A variety of pre-qualification questionnaires are available from CIPS which can be tailored to your own particular requirements. Construction line provides a PQQ database covering most of the construction industry. Consideration should be given to allowing suppliers to refer to this as their response to the PQQ.

Supplier appraisal starts formally with an assessment of those suppliers who have completed the PQQ. The objectives of this stage are to establish whether any suppliers should be excluded from further consideration because they fail to meet the criteria and reject them, and to create the manageable shortlist of realistic candidates mentioned above who qualify by meeting the criteria and who will be asked to proceed to the next stage (tendering, entering into negotiations, for example) to identify any points that need to be clarified with selected suppliers through meetings, supplier visits and/or reference site visits at a later stage. (See section j) Appraising suppliers.)

In the same way that the PQQ should pose meaningful, relevant questions designed to inform the selection decision without placing unnecessary and costly burdens on potential suppliers in

responding, tenderers are entitled to expect that their offers will receive fair and full consideration and that their bids will remain confidential. It is important therefore that tenderers have confidence in the tendering procedures laid down by the buying organisation to ensure impartiality and confidentiality. In tendering to the public sector, confidence in impartial treatment is secured by adherence to the strict tendering rules set out in the EU Procurement Directives. The need for transparency in the public sector, however, limits confidentiality since the Directives require subsequent publication of price details.

The underlying principle is that the parties to the tendering process should retain confidence by strict and transparent adherence to a procedure which formalises the manner in which tenders are received, evaluated and awarded. The maxim that the system "is and seen to be" impartial is an important one. Attention should be given to such procedural issues as:

- the closing date and time for receipt of tenders
- late tenders are returned unopened
- tender documentation is securely held until the opening process
- the tender opening procedure is independently witnessed and tender price details recorded
- electronically submitted tenders are password controlled and possibly encoded
- evaluation and award criteria
- the format and content of responses including the manner in which they are submitted.

<sup>12</sup> (OGC Contract Management. CIPS ethical code)



The procedural matters should be communicated to potential tenderers both in the tender documentation and any advertisements.

Other issues to be considered when determining the tender procedures are:

- any post-tender negotiations (PTN) conducted do not undermine confidence or trust in the competitive system through unethical means, the use of buying or political power or the adoption of “Dutch auction” or “horse trading” techniques
- adherence to the buying organisation and/or the CIPS ethical code<sup>12</sup>.

#### **j) Appraising suppliers**

Supplier appraisal establishes (or otherwise) a potential supplier’s capability and capacity to deliver goods and services to your organisation now and in the future. The assessment process should establish the supplier’s capability to control quality, delivery, quantity, price and all the other factors contained in the contract. Following a successful appraisal, the supplier is placed on an approved list of suppliers.

CIPS produces guidance on Supplier Appraisal in its “How To” series, and it is not intended to replicate the booklet here but to summarise the issues surrounding supplier appraisal under the headings provided in that guidance of why, when, what, who and how.

#### **Why appraise?**

Supplier appraisal is an essential aspect of strategic sourcing, successful supplier

management and the achievement of competitive advantage in securing goods or services.

The process should commence when the requirement is known and, because it is not necessary to carry out the process for all needs, the requirement should be categorised according to whether it is standard or non-standard, of strategic or non-strategic importance and of high or low value. Assistance in assessing these latter two categories can be gained from the application of Kraljic’s matrix to assess the strategic importance of a requirement and the use of Pareto and ABC analysis techniques to assess value.

#### **When to appraise?**

The process is time consuming and costly and, as already mentioned, selectively carried out. There are, however, certain situations in which it is strongly advised to conduct appraisal and the following provides an indication of these situations but is not exhaustive:

- strategic, high profit, high risk, non-standard requirements
- capital requirements, construction and similar projects
- supplier development
- JIT arrangements
- use of supplier associations
- global sourcing
- e-procurement arrangements with long-term strategic suppliers
- negotiating TQM and quality in respect of high profit/risk items
- outsourcing contracts
- before agreeing sub-contracting by a main supplier
- service level agreements.

## What should be appraised?

There will be a range of factors to be appraised which are directly related to the particular requirement, but the following should act as a checklist of aspects to be assessed for the majority of contracts; the significance of each and thus the time devoted to the assessment will again vary according to the particular requirement:

- finance, including turnover, profit, assets, ROC, borrowings, debts, credit status takeover/merger possibilities, market positioning. The appraisal should employ the service of credit agencies such as Dunn and Bradstreet to provide supplier evaluation reports
- production capacity, including available productive capacity, scope for expansion, capacity utilisation percentage with and without your organisation's requirements
- production facilities related to the particular requirements including range, type, age and sophistication of plant and machinery, maintenance levels, housekeeping
- human resources, including staff numbers and employment, skills and qualifications, training policies, management/worker relationships, worker representation, industrial dispute record, attitudes and motivation, staff turnover
- quality, including the implementation of quality systems, for example ISO 9001:2000, ISO 14000, policies on TQM, inspection and testing procedures, statistical controls, quality control procedures for sub-contractors, guarantees
- performance, including information on past and current projects, features and

innovations introduced, references

- Corporate Social Responsibility (CSR) issues, including determining the policies on environment, human rights, equality and diversity, sustainability, ethics and ethical trading, biodiversity, corporate governance and impact on society<sup>13</sup>
- information technology, including the extent and the use made of current IT to support and report on business activities.

## Who should appraise

Apart from the procurement of standard or MRO products, appraisal should be carried out on a team basis and include the following:

- buyer
- users
- technical staff
- decision makers
- other stakeholders.<sup>14</sup>
- Third Party Appraisal  
This can be carried out by agencies including:
  - BSI
  - certification of major companies
  - supplier consortia
  - independent management consultants
  - UK Accreditation Service
  - UKSA accredits third party independent certification bodies, testing and calibration laboratory.

## How to appraise

Appraisal methods can be roughly classified under three categories desk: field or site visits and third party.

- Desk appraisal. This utilises published and unpublished information and is

<sup>13</sup> (CIPS Corporate Social Responsibility)

<sup>14</sup> (CIPS Supplier Appraisal. See also Lyons)

particularly appropriate for product and financial appraisals. Typical sources of information are catalogues, product data sheets, test reports, websites and trade journals. Desk research should precede field research since it will indicate what matters need to be investigated and help to assess the accuracy and veracity of the answers provided by potential suppliers. Questionnaires are the most economical method of obtaining information as a basis for supplier appraisals. They can be used either prior to visits to suppliers or as basis for supplier certification. They should provide assurances to the supplier of confidentiality, and the questions themselves should be as clear and concise as possible and designed to elicit the information required by avoiding “closed” questions. Assistance on the design of questionnaires can be found in the “How to” guide.

- Field appraisal. This involves visits to potential suppliers and other sites and should follow desk research and supplement the information gained from that process. It is particularly important to carry out this form of appraisal when evaluating suppliers of high risk/high value products and when long-term, collaborative relationships are under consideration and vital operational services are to be supplied from site. A checklist of matters to be investigated should be carefully prepared prior to the visit to ensure that no important questions are overlooked and to provide the evidence for decisions reached. The checklist will largely be based on the matters set out under what to appraise

above. It should be borne in mind that while some of the evidence gathered may be more subjective, some matters can be objectively assessed.

- The following are areas which warrant particular attention by staff involved in the appraisal visit:
  - personal attitudes of supplier's employees, providing an indication of likely service quality and dependability
  - adequacy and care of plant and machinery
  - technical knowledge of supervisory staff
  - quality control methods
  - housekeeping
  - competence of design, research and laboratory staff including knowledge of latest materials, tools and processes and industry developments
  - competence of management including commitment.

#### **k) Drafting ITT documents**

As with drafting specifications, great attention should be paid to ensuring that the contract document as a whole sets out clearly, comprehensively and unambiguously, the obligations of the parties to the agreement.

As already mentioned, all contracts are different, both in requirement as well as complexity and supplier relationship needs. The following schedule should therefore be seen as a checklist and not a prescribed list of matters to be considered for inclusion in every contract:

- form of agreement or form of tender setting out the contract period and spaces for signatures
  - specification of requirements including the levels of output to be achieved and the performance measurement methodology, relevant information to enable bids to be submitted
  - conditions of contract or articles of agreement. These should comprise definitions, general terms including changes, alterations and variations clause, notice clause, commercial terms setting out the rights and obligations of the parties, conditions, warranties, confidentiality, intellectual property, indemnity, exit management, data protection, dispute resolution/escalation and termination clauses and “standard “ clauses which should appear in all contracts covering such matters as liability, severability, waiver, force majeure and jurisdiction
  - pricing schedules - particular attention should be given to ensuring that potential suppliers are bidding on the same basis of output required
  - price variation mechanisms applicable to products, services and time-based requirements
  - invoicing and payment terms and methods, for example BACS, CHAPS cheque, and so on., invoice content requirements
  - pricing basis including milestone, incentivisation, payment reductions for non-compliance, retention, advance, interim
  - implementation and transition plans including knowledge transfer
  - testing methodology
  - acceptance strategy and procedures
  - award criteria
  - dispute resolution procedures including escalation process
  - sub-contractor information
  - contract change procedures arising from both internal or external sources and the consequential need for flexibility in contractual terms
  - contract management arrangements to ensure successful service delivery and the level of control your organisation requires during contract performance
  - communications including frequency, level, detail, content
  - exit/termination strategy and procedures
  - drawings
  - free issue materials schedule.
- This list of matters which are not exhaustive should be categorised and arranged clearly and logically into the tender document. Typically this may comprise the following sections:
- form of tender
  - conditions of contract
  - scope of work or technical specification
  - administrative and tender submission instructions
  - schedule of prices
  - drawings
  - schedule of free issue materials.
- An extremely useful model form of Contract for the Provision of Services together with guidance notes is available from CIPS and can be used or adapted as the basis of part of contract documentation.
- Contract documentation issued by public sector organisations will, in addition, need to comply with the tendering

procedures of the EU Procurement Directives, and it would be necessary for the purchasing officer to be familiar with those directives.

It is common practice for the enquiry inviting tenders to consist of:

- a covering letter explaining the invitation and re-iterating the date and time by which tenders must be returned
- re-iterating the instructions to tenderers about the manner in which the tender should be submitted
- the name and contact details of the responsible procurement person
- the procedure for raising queries and receiving clarification
- the tender document
- pre-printed labels for tender return.<sup>15</sup>

## **D) Evaluating tenders**

All tenders received by the appointed day and time should be recorded. This process can range from maintaining a simple clerical record of valid tenders received by the appointed time to the appointment of a tender opening board who record such issues as:

- who tendered
- the price quoted if a lump sum or bill of quantities bid
- the organisations which declined to submit
- rejected bids
- deviations or qualifications to offers
- programmes quoted
- the integrity of the tender procedure.

The formal opening procedure is followed by the tender evaluation process which, again, may range from a

simple straightforward process to one which is complex, involving many professional disciplines formed into an evaluation team and carried out over a period of time.

Tenders should be initially evaluated under the twin considerations of commercial and technical, the latter possibly carried out without price information, to ensure that the bids are brought to a comparable basis for more a thorough evaluation and study, without the influence of commercial considerations.

The criteria for tender evaluation should follow the award criteria set out in the tender documents and communicated to the potential suppliers. Public sector organisations are required under EU Procurement Directives to award tenders using only the criteria set out by the buying organisation in the OJEU advertisement. This can be either Lowest Price only or a range of criteria, linked to the subject matter of the contract, collectively known as contributing to the “most economically advantageous tender”. The relative weighting of each criteria, or their listing in descending order of importance, must be set out in the contract document and/or in the OJEU contract notice.

In principle, the evaluation process should include not only the analysis of the potential supplier's response to the main subject matter of the requirement set out in the ITT, such as price, delivery, quality, methodology, for example but also, most importantly, the quality of the bidder's offer.

<sup>15</sup> (CIPS Buying Goods and Services)

The evaluation process includes a clarification process whereby the buying organisation can seek further information in order to inform the decision making process. Clarification should not be seen as an opportunity to negotiate or change the basis of the decision, as this will only serve in the longer term to undermine the credibility, trustworthiness and standing of the buyer and the buying organisation. Additionally, public sector organisations must comply with EU Procurement Directive rules governing the clarification process.

#### **m) Negotiation**

It is not the intention of this guide to provide guidance on negotiation techniques. Information and further assistance can be found in the bibliography section of the guide and on the CIPS website. Negotiation is covered here in the context of the formal stages of contract management covered by this guide.

It is the aim of every purchasing professional to conclude the best deal for the organisation he or she represents. This is often achieved by post-tender negotiation (PTN) and is an activity to be considered and planned for in the formulation of the contract strategy.

CIPS defines PTN as “negotiation after receipt of formal tenders and before the letting of contracts with suppliers/contractors submitting the lowest acceptable tender with a view to obtaining an improvement in price,

delivery or content, in circumstances which do not put other tenderers at a disadvantage or affect adversely their confidence or trust in the competitive system”. PTN does not apply, for example, where

- there is no formal tendering process
- there is only one supplier
- there are discussions to clarify bids
- there is a need to correct problems arising from poor pre-contract preparation, or there are normal price adjustment requests or contract variations during the life of the contract by either party.

It is worth reiterating that any PTN should not undermine confidence or trust in the competitive system through unethical means, the use of buying or political power or the adoption of “Dutch auction” or “horse trading” techniques and should adhere to the buying organisation and/or the CIPS ethical code, as well as any tendering rules established.

When the buying organisation has decided that PTN will be conducted, the following matters should be considered:

- the criteria for conducting PTN
- contract value
- the balance between potential savings, the cost of carrying out PTN and the likely benefits
- time
- effect on the market
- the rules contained in the EU Procurement Directives for public sector organisations
- ethical issues.

The methodology and conduct in undertaking PTN is, in principle, the same as that for any negotiations outside the context of a formal tendering process, although the activity may possibly be less complex or drawn out. The following matters, however, should be considered in determining the negotiation strategy:

- the approach, such as adversarial or partnership (respectively a “win-lose” or “win-win” situation). There is no right or wrong approach - either may be appropriate. For example, an adversarial tactic may be the right course where no on-going relationship is contemplated and the purchase is a one-off or a simple resolution of a problem is sought. A partnership negotiation tactic may be appropriate where a long-term, stable relationship is contemplated and/or the approach is the only one likely to succeed in resolving complex, intricate problems
- identification of the implicit and explicit objectives of both parties
- the fall-back or Best Alternative to a Negotiated Agreement (BATNA) positions of both parties (as far as possible)
- the negotiation goals. Both the substance goals and the relationship goals are effectively concluded when the former have been resolved and when the latter have led to the preservation or enhancement of the working relationship
- the results of undertaking “what if” and sensitivity calculations on the tendered prices
- the negotiators – personalities needed, authority levels of the negotiator(s),

roles and responsibilities

- identifying the buyer's and the supplier's respective negotiation situations, strengths and weaknesses
- time and degree of urgency of the purchase. “Necessity never made a good buyer” – urgency is never a good negotiating position and time may in fact determine the negotiating tactics that have to be adopted.

Consideration must also be given to the negotiating process itself and issues such as:

Pre-negotiation stage:

- deciding upon a team or individual approach – if the former, allocating roles and ensuring the appropriate level of expertise will be present; the venue, information gathering including SWOT analysis and data presentation, determining the objectives, deciding the strategy and tactics at the actual negotiation stage including negotiation order, opening speakers, recesses, issues of concessions to be made, if any, linked issues, for examples price and quality, likely reactions to tactics of both parties, role plays and dummy runs

Actual negotiation stage:

- establishing the stages and procedural rules, agreeing the agenda, determining the issues to be resolved, agreeing common goals, removing barriers to achieving goals and final agreement and closure, adopting the appropriate behavioural tactics necessary, determining the ploys (if any) to be used

Post negotiation stage:

- drafting agreement statements, communicating the agreement to

stakeholders, implementing the agreement and monitoring the implementation

This is not intended to form an exhaustive check-list of the issues to be borne in mind when it is proposed to conduct post-tender negotiations, but will act as a prompt to the type and nature of the matters to be addressed.

Finally, it is worthwhile bearing in mind a number of general principles when considering negotiations, particularly in relation to large, high value contracts:

- avoid treating each negotiation as a separate event. This can be counterproductive when viewed from a strategic level through the agreement of advantageous terms on a particular contract at the expense of the long-term relationship with the supplier
- avoid negotiating each component of a single negotiation in isolation - a composite approach can often secure a better overall commercial solution
- broaden the evaluation of negotiator's performance beyond price and quality to measuring innovation and creative alternative solutions
- recognise the difference between deals and relationships. Concessions granted during deals can lead to an adversarial climate and mistrust and damage long-term relationships
- understand when to "walk away from a negotiation". Negotiators should be encouraged to make good choices, not merely to produce agreements which are mutually unsatisfactory.<sup>16</sup>

## n) Awarding the contract

Following tender evaluation and, where appropriate, negotiation, the project team will satisfy itself that an offer has been made which meets its requirements in all respects, including budgetary, and consider that it is in a position to accept an offer and award the contract to the tenderer who has made the most economically advantageous offer to the organisation. It may then move directly to the award stage or make a recommendation to higher authority levels within the organisation for acceptance.

The contract award stage comprises of a number of important aspects; communicating the award to the successful tenderer, notifying the unsuccessful tenderers, debriefing unsuccessful tenderers and, in the case of contracts awarded under EC Procurement Directives by public sector organisations, publishing a contract award in the OJEC. As will be seen, it is also useful for the procurement organisation to conduct a debriefing of the successful tenderer.

This stage should also include activities such as:

- ensuring that all relevant parties are aware of their roles and responsibilities in the immediate implementation and transition process
- checking that the agreed processes for contract management are in place by all the parties
- that knowledge transfer from the procurement or project team (which

<sup>16</sup> (Lysons)



may not have included members of the contracts management team) to the contracts management team takes place to ensure successful management of the contract

- that, where necessary, the continuity plans for the seamless transition of the service from one contractor to the new contractor will be carried out as agreed.

The method of informing the successful tenderer should follow the method set down in the tender documents (see section k). Whatever method of communication is adopted, it is essential that the notification is clear, unambiguous and sufficiently comprehensive to ensure that there is no possibility of doubt by either party about what has been accepted. Normally this should take the form of a counter-signed copy of the tender document incorporating all the agreed amendments made during the negotiation and clarifying stages. Notification should be made by the appropriate authority level within the organisation.

Concurrently, the unsuccessful tenderers should be advised of the non-acceptance of their offers and, in the case of contracts awarded under EC Procurement Directives, a contract award notice should be placed in the OJEC within the proscribed timescale and in accordance with the regulations relating to the content of the notice.

Some organisations from time to time make use of Letters of Intent to communicate instructions or requests to the potential supplier. These are used for

a variety of reasons, for example to smooth service transition, to speed up the start of a project or to secure more time to finalise contractual terms. A wide range of potentially serious problems can arise from the indiscriminate use of Letters of Intent and consequentially CIPS discourages their use and advocates establishing a separate contractual arrangement for the small amount of work that otherwise would be the subject of the Letter of Intent. If there is no alternative, great care should be given to the wording of the Letter of Intent to minimise the risk to the organisation and to ensure that the Letter is not binding on the organisation for anything other than the specific work set out in it. Equally, care should also be taken to avoid giving inadvertent instructions to supplier(s) to carry out work or indeed verbal comments which may be interpreted as instructions.<sup>17</sup>

As already mentioned, it is beneficial for the buying organisation to debrief the successful tenderer to gain their view of the procurement process recently undertaken, to gain better understanding of that market, to improve communications, to maintain good practice processes and to establish a good working relationship with the new supplier at the earliest opportunity.

It is equally beneficial to debrief unsuccessful tenderers. It assists suppliers to improve their competitive performance, not only with the buying organisation in the future but in markets elsewhere. In addition to the benefits gained from debriefing the successful tenderer, the organisation benefits by

<sup>17</sup> (For more information and a suggested Letter see CIPS POP Letters of Intent)

developing a potentially wider range of suppliers, thus increasing the potential for improved value for money, by receiving better quality bids in future and gaining useful market intelligence.

Debriefing should be constructive and as open as possible, not defensive and secretive. In general, it should be seen as helping to demonstrate procurement professionalism and establishing the organisation's reputation as a fair and ethical buyer with whom suppliers would want to do business.

Following selection and award, the communication advising tenderers of their success or otherwise should thank them for their participation in the tendering exercise and offer them a debriefing opportunity. If unsuccessful tenderers respond, requesting debriefing sessions, these should take place as soon as is conveniently and practically possible after award and, in the case of public sector organisations, in accordance with EU Procurement Directive regulations.

It is important that the debrief parameters are made clear, ideally confined to such topics as tenderer selection, tender award and tenderer withdrawal issues (where appropriate); it will not provide an opportunity to change any decisions and it will be confined to their own offer.

### **Downstream or post-award activities.**

Having carried out the pre-award activities associated with contract formulation and award, the process now

turns to post-award activities. These can be grouped into three general areas: the management of service delivery, the management of the relationship with the supplier and contract administration. The first is concerned with ensuring that the service is being delivered in accordance with the agreed performance and quality levels set out in the contract; the second is concerned with maintaining and developing an open and constructive relationship with the supplier and the last with the formal management of the contract.<sup>18</sup>

### **o) Changes within the contract**

Changes are almost inevitable during the period of a contract, particularly in the case of large, complex construction and service contracts. They should not necessarily be seen as causes for concern but, effectively managed, as opportunities to improve the contract outputs.

It is important to understand the implication of change for both parties. Changes of any significance will affect the scope and potentially the viability of the contract for either party. If a change results in a reduction in the value or scope of the contract, the organisation could be faced with claims for increases in charges and/or legal claims that there was, for example, misrepresentation in relation to the likely volumes required over the period of the contract. If the change results in a substantial increase in the value or scope, it is important that the organisation continues to ensure that value for money is secured. Public sector organisations should be additionally

<sup>18</sup> (OGC Contract Management

aware of the requirements of the EC Procurement Directives needing substantial changes during the contract period.

Change can be driven by a number of factors; amongst the more common are amendments to the strategies and objectives of the parties, the changing business needs of the organisation, market changes, developments in technology, economic trends which affect the viability of the contract and legislative change. These in turn can lead to changes in the service required, the metrics needed, service infrastructure and workload.

Changes are easier to manage when planned. Even the effects of an unexpected, externally driven change can often be mitigated through, for example, on-going effective risk assessment and the phasing-in of any implementation. Changes will require negotiation with the provider(s) and the introduction of amendments carefully scheduled to avoid workload peaks and year-end activities where possible. The implementation of the change should be effectively managed using change control procedures (see section r).

Particular care should be taken when making changes to construction, building and IT contracts. What are apparently quite small changes can have unexpected knock-on effects on other costs, particularly, for example, if a construction sequence is affected. Wherever possible, the outcome should be agreed with the supplier before instructing such a change.

## **p) Service delivery management**

This activity is concerned with the fundamental aspect of contract management, that of ensuring that the actual service provided by the supplier is in accordance with the agreed standards and prices. The ability to measure the performance of the supplier - sometimes called vendor rating - and to provide feedback is critical to successful contract management and supplier development.

Performance measures to cover all aspects of a contract should be designed to suit the requirements of a particular contract and should be set out in the contract documentation to ensure suppliers are fully aware of both the measures and the measurement methodology before any contract is awarded. It is important that the performance measures selected provide clear and demonstrable evidence of the success (or otherwise) of the relationship and, in principle, issues such as the following should be covered:

- cost and value obtained
- performance and customer satisfaction
- delivery improvement and added value
- delivery capability
- benefits realised
- relationship strength and responsiveness.

It is important to ensure that the actual metrics selected are not over-specified, that they are, as far as possible, readily obtained from the direct performance of the contract and that they are focused on issues such as those outlined above which impact most heavily on the organisation. It should be remembered that there are

costs attached to the production and maintenance of metrics by the supplier who will seek to pass them on in the form of higher prices or charges.

Once chosen, the requirements underpinning the performance measures should be the primary focus for contract management. They should form the framework on which information needs and flows and contract management teams, skills, processes and activities are developed and improved in conjunction with the supplier.

They should not be seen as a method of control, but as a proactive means of improving the performance of a supplier. Suppliers should always be requested to improve their performance, and incentives, used appropriately, should encourage improvement. Performance measurement results can be used to inform decisions on the type and extent of incentives.

There are a number of themes which could be used to measure supplier performance:

- product quality - Mean Time Between Failure (MTBF), Mean Time to Repair (MTTR), percentage of delivery rejects, warranty claims
- service quality using Service Level Agreements (SLA) – call-out time, customer service response time, performance against agreed delivery, lead times
- relationship Management (see section q) – accessibility and responsiveness of supplier management
- commercial – costs are maintained or reduced, service improved.

There are three aspects to performance measurement;

- gathering of factual, objective information from the supplier - usually obtained from IT systems
- gathering feedback from users about the service received – typically through questionnaires, surveys, telephone or face-to-face enquiry
- understanding the supplier's own experience of dealing with the organisation.

Performance measurement can be an expensive and time-consuming activity, and as such should be carried out on a selective and prioritised basis, proportionate to the value and importance of the contract to the organisation. This is particularly important when time and resources are very limited. Suppliers of high value, high risk goods and services should be closely monitored, possibly involving frequent regular meetings at the supplier's premises or on site. Security or bottleneck type goods and services of low value but of significant importance to the organisation may require less frequent but regular monitoring. High value or volume and low risk items may need only quarterly meetings to ensure satisfactory performance monitoring.

#### **q) Relationship management**

Contractual arrangements may commit the organisation to its supplier(s) for some time and to varying degrees of dependency. It is therefore important to make the relationship work effectively by developing mutual trust and understanding, creating an open and

constructive environment and contributing to the joint management of the contract delivery.

It is primarily through the development of mutual trust and confidence that the other elements for success are created. As the supplier gains greater understanding of the organisation's business needs and style and develops a level of confidence and trust, it will be more willing to be proactive and innovative in bringing forward improvements and savings to mutual benefit, more willing to share problems, plans and concerns, more willing to negotiate and more confident in investing for the longer term. The organisation benefits by gaining a greater understanding of the strengths and weaknesses of the supplier, enabling it to concentrate its management and development support in those areas.

Factors that can inhibit the development of a successful relationship include:

- frequent and rapid recourse to the formal contract to overcome problems
- clashes in cultures which are so disparate as to prevent the creation of the level of trust and confidence required
- reluctance by the supplier to co-operate in value for money or benchmarking tests conducted by the organisation
- commercial issues, for example lack of real competition resulting in uncompetitive, poor value for money terms from the supplier, or conversely that the organisation is critically dependent on one supplier leading to price rise vulnerability and/or

problems of management capability, resources or financial capitalisation

- too frequent demands for submission of competitive bids – reduces trust in the relationship.

It should be remembered, however, that such issues should have been identified and resolved at the pre-award appraisal stage.

In addition to the elements mentioned above, other factors that encourage the development of a successful relationship include:

- securing senior level support in both organisations
- recognising that actions and attitudes affect the tone of the relationship
- ensuring that the governance arrangements are fair
- ensuring that relationships between the parties are peer-to-peer as far as possible
- ensuring that roles and responsibilities are clearly understood by both parties and that the necessary authority levels have been ascribed
- ensuring that escalation routes are clear and understood but that problems are resolved as early as possible and as low down the management tree as possible
- separating strategic matters from the day-to-day service delivery issues
- ensuring that appropriate attitudes and behaviour are practised and displayed to assist the promotion of a positive and constructive relationship
- communicating and sharing information at the appropriate level between the organisation and the supplier, for example strategic,

business and operational levels and as openly as possible.

Performance monitoring of suppliers was covered in section p) in relation to the management of service delivery. It should be re-iterated, however, that it is equally important that the exercise should also cover the relationship between the organisation and the supplier, albeit that the measurements themselves may be somewhat more subjective. Such issues as the quality of the supplier's R & D department, their project management performance, the level of management responsiveness, flexibility and effort can be assessed as well as benchmarked.

#### **r) Contract administration**

This activity is concerned with the practicalities of the relationship between the organisation and the supplier and the operation of the routine administrative and clerical functions. The importance to the smooth running of post-award contract management should not be underestimated and it should be resourced appropriately. This is one of the primary responsibilities of a contract manager.

Whilst the level of significance and extent of the activity will vary according to the particular contract, one of the main areas critical to successful contract administration is contract maintenance and change control.

Changes will almost inevitably occur during the period of a contract and managing these changes is a particularly

important activity. As already mentioned, formal change control procedures should be designed and set out in the original contract documentation to avoid misunderstanding and ambiguity about roles, responsibilities and the actions to be taken in any given situation. These change control procedures should be initiated at the earliest opportunity, post-contract award. They should include procedures to keep all contract documentation up to date and consistent so that all parties have a common view of the agreed changes. For particularly large contracts or where there are a number of Service Level Agreements (SLA) in place, a formal document management system should be set up. The procedures need to be comprehensive but also flexible and straightforward and should cover such issues as:

- how to request changes including additional demands placed on the supplier
- assessing the impact including contractual implications
- prioritisation and authorisation levels
- agreement methodology
- controlling implementation
- documenting changes.

Normal price variations in the contract often fall outside change control procedures and have their own method of proposal, assessment, evaluation and agreement.

A formal framework, defining responsibilities and reporting arrangements should have been designed and set out clearly in the contract documentation. The information

called for may range from a complete suite of performance measurement reports to exception reporting. The design of reports should reflect the need for flexibility in the type and detail of the information required during the contract period and the recipients' possible need for access to greater detail. In addition, regular reporting – monthly or quarterly – may also be required.

Under the contract administration activity, and if the nature of the contract concerns the use of the organisation's assets, there will be a responsibility to ensure that the organisation's asset register is kept up to date, the use of assets by a third party is recorded and upgrades and replacements are planned and budgeted. The contract manager will be responsible for liaison with the provider on administration and maintenance of assets.

Other areas covered by contract administration and forming part of the responsibility of the contract manager are charges and cost monitoring, ordering and payment procedures, budget procedures, resource management and planning.<sup>19</sup>

### **s) Assessment of risk**

The importance of risk assessment to successful contract management has already been mentioned (see section d) and the likelihood of changes arising during long term contracts has also been highlighted. It can be seen therefore that there is a need to conduct continuous risk analysis and assessment throughout the period of the contract in order effectively to manage the risks that arise.

Whilst the issue of change during the contract should prompt a risk analysis activity, the need continually to assess risk in large, complex long-term contracts cannot be overemphasised. The techniques for conducting such analysis and assessment are set out in section d).

Risk management during the contract period comprises those activities associated with identifying and controlling the risks that may potentially affect the successful fulfilment of the contract. Risks to the contract include such issues as:

- lack of capacity of the supplier, particularly if there are significant increases in demand
- reduction in demand leading to higher unit costs borne by the supplier
- an event which causes an increase in the total of the price to the purchaser
- an event which causes a programme delay
- supplier staff changes
- changes to the supplier's business objectives
- deterioration in the supplier's financial standing
- demand changes that cannot be met by the supplier
- deterioration of quality
- force majeure issues
- market fluctuations for commodities.

When a risk is anticipated or perceived, its management involves the parties working together to identify where the responsibility for it lies, methods of minimising it and how the risk will be managed. Issues to consider for effective management to succeed include:

<sup>19</sup> (OGC Contract Management

- establishing a binding process to encourage early warning of issues such as those mentioned above, as soon as either a supplier or the purchaser becomes aware of them
- identifying the party best able to control the situation leading to the risk occurring
- identifying the party best able to control the risk itself - this may include the organisation
- identifying who should be responsible if the risk cannot be controlled
- establishing whether, if the risk is transferred to the supplier, the cost to the organisation will fall, whether new risks will arise and transfer to the organisation, and the legal position of any transfer.

It should be remembered that risks transferred to the supplier still require managing by the organisation and that suppliers will seek to obtain payment for any transferred risk not identified and incorporated into the original contract. Care should also be taken to ensure, in any long-term partnership based on openness and trust where the supplier is responsible for risk management, that the supplier fulfils its obligations effectively and comprehensively. Furthermore, the organisation should ensure that risk is not transferred back to the organisation as a result of a level of co-operation exceeding the scope of the contractual requirements by the organisation's own representatives.

Finally, it should be remembered that business risk cannot be transferred to the supplier and that the ultimate responsibility will always remain with

the organisation for any failure in fulfilment of the contract.

#### **t) Purchasing organisation's performance and effectiveness review**

Reference has been made to the necessity to measure the supplier's performance throughout the period of the contract. Equally important, and another downstream activity, is the measurement of the purchasing organisation's performance effectiveness and efficiency.

It is not the intention of this guide to cover the wider issue of performance appraisal, which should be conducted in an organisation as part of its normal management practice, but to focus on the review of purchasing in relation to the upstream and downstream activities of a particular procurement. Both practices will contribute to the development and training of professional purchasing staff.

Briefly, effectiveness is concerned with the ability to accomplish a given goal or purpose, and efficiency is concerned with the ability to maximise productivity with the least amount of effort, money or resources. In other words, effectiveness means "doing the right thing" whereas efficiency means "doing things right".

The aims of performance measurement of the purchasing department are to:

- ensure consensus between individual, functional and corporate aims
- compare actual results with planned performance
- identify reasons for substandard

<sup>20</sup> (Lysons)



performance and the basis for improvement

- improve decision making
- identify the contribution purchasing can make to the organisation
- motivate and encourage staff.<sup>20</sup>

A range of traditional purchasing performance measurements can be gathered from the on-going management of a contract, including metrics such as:

- savings on the purchase price
- reduced inventory levels
- incoming defects
- on-time deliveries
- procurement cycle time
- cost of change
- cost of placing orders.

These can be considered as quantitative questions which are readily monitored and measured. They are often considered to be basic, minimum performance standards today; nevertheless, they are extremely important.

At a higher level, effective measurement of purchasing will be concerned with establishing the need, managing internal and external relationships, managing contracts and performance, managing change, customer support, infrastructure issues, business continuity and transition.

In relation to a particular contract, these issues can be addressed by raising questions, although more qualitative and subjective in nature than those set out above, that are concerned with the upstream and downstream management processes and relationship issues. Mention has already been made in earlier stages of a number of the metrics

that may be gathered but they should include such broad issues as:

- documentation – clarity, understanding and comprehensiveness
- pre-award contract processes, understanding and timetables
- change control procedures – ease, understanding, comprehensiveness
- communication - suppliers, customers and other stakeholders
- risk - identification and management
- contractual relationships - smoothness, conflicts
- customer satisfaction
- business continuity and transition issues.

Each topic will suggest a range of questions related to the particular procurement as the measurement drills down to obtain data which will make a meaningful contribution to the assessment of performance. Responses may be measured in terms of extent, for example “not at all”, “partially”, “largely” or “fully”.

In addition to conducting an internal review of the project and documenting the findings, valuable information on the performance of the purchasing department can be gathered from suppliers during performance review meetings.

It should be recognised that some information can only be properly and usefully gathered following completion or closure of the contract, whilst it may be critical that other information is gathered before closure in order to implement process improvement changes for future procurement

contracts, including the possible re-letting of the current contract.

## u) Contract closure

This stage concerns the activities associated with closing the project down, whether in accordance with the contract or as a result of early termination. Different activities of course are associated with the different forms that contract termination can take.

In the case of more complex, long-term or construction contracts ending in accordance with the original contract plan, best practice requires the need for evidence that the contract has been completed to the satisfaction of all parties. This is normally carried out in two stages; firstly, to ascertain internally that there are no outstanding matters and, secondly, to secure agreement from supplier(s) that, apart from agreed on-going liabilities, the contract(s) has ended.

The aim of the closure procedure is to provide a mechanism for managing the closure of the contract following the end of any retention or guarantee periods and the resolution of all other outstanding matters. The procedure is designed (where and if applicable) to:

- ensure completion of all administrative matters
- record that all technical issues have been completed
- determine the extent of any liquidated damages to be deducted from the contract price
- record the end of the retention and guarantee periods and the date of the

final inspection carried out

- record the date of release of retention and/or bank guarantees
- to agree a statement of specific limits on continuing contractual obligations after completion of work and any on-going obligations following the end of guarantees or maintenance periods
- record any materials reconciliation
- transfer any assets, including data and intellectual property, and any loan items
- transfer operational systems to the successful supplier
- record the process of final contract payments and a summary of the financial payments and received
- summarise claims made against or received from the supplier
- ensure the retention of records relating to the contract to counter any subsequent claims that may be brought. The Limitation Act 1980 sets out the general periods – six years or twelve years according to the type of contract - within which an action maybe brought.

On completion of this activity, agreement should have been reached on all technical and commercial aspects of the contract. The agreement should require the signature of the parties to a document which records the acceptance of the work or service, the obligations fulfilled and the price paid or to be paid.

Another issue relating to the “normal” end of a contract, which should have been considered during the pre-contract award stages, but worthwhile repeating here, is the renewal or extension of the contract (if appropriate). The terms and

procedures for such eventualities should be incorporated into the original contract documentation and should include the period for negotiation of terms in order to ensure business continuity, together with a deadline for agreement. This deadline should allow for risk of failure to agree and a period of time for the contract to be re-let in order to ensure the smooth transition of the work or service from the old contract to the new contract. This period could be extensive and organisations in the public sector are reminded that they are required to adhere to the EC Procurement Directives and that it is unlikely that an accelerated contract award process for a new contract will be acceptable if the justification is the failure to agree terms in accordance with the deadline set out in the old contract.

There are many reasons why a contract may not be satisfactorily fulfilled in accordance with the contract, and it is not the intention of this stage to describe all the circumstances that may arise and the associated activities that may be pursued and remedies sought for breach in each case. The important factor to remember, as already mentioned in stage d), is the need to conduct risk assessment pre-contract award. As part of that activity, the possibilities for performance failure and consequential early termination should have been made and appropriate counter-measures considered and set out in the contract documentation. With complex, high

value contracts, the overriding consideration is the need to ensure business continuity and the maintenance of a service.

Remedies for breach will include recourse to adjudication, mediation, conciliation, and arbitration and if these methods fail – litigation. Resolution can take long periods of time extending to years in the case of serious disputes. Focus should therefore be on activating plans for securing the smooth transition of the work or service from alternative sources.

Another important activity conducted at this stage, particularly in the case of high value, large contracts, is the preparation of a post-contract project report. This may follow a formal post-contract review, undertaken to assess the business benefits – or losses - from carrying out the procurement, how those benefits may be furthered enhanced and/or costs and risks reduced and how the losses can be recouped and turned to benefits. The review should also gather the lessons that can be learnt from the management processes and procedures followed during the contract and implemented in the future. The review should include the views of all stakeholders and the report should relate to the costs and benefits set out in the original business case.<sup>21</sup>

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<sup>21</sup> (OGC Contract Management

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