IACCM
International Association for
Contract & Commercial Management

Commercial Excellence: Ten Pitfalls To Avoid In Contracting

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Table of contents

Executive Summary

Of course you care about the bottom line. But do you have any sense of how much money you are losing each day through under-performing contracts?

Your contracts are core business assets, but unless you tackle the common sources of erosion, they are leaking value. On average, companies could be generating over 9%† improvement to their bottom line if they tackled the commercial issues that commonly undermine contract performance.

Contracts are of course just one element of commercial excellence – but quite a significant element when it comes to financial results. This brochure highlights ten pitfalls in your contracting process that are most likely to be costing you money – and damaging the quality of your customer and supplier relationships. The first step towards fixing them is awareness: by reading this, you have already started on the journey.

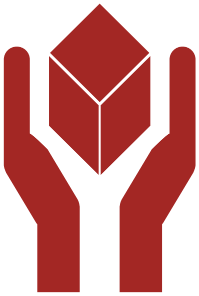
About IACCM

As the only global non-profit association focused on contract, commercial and relationship management, IACCM conducts and gathers extensive research to help member organizations improve results from their trading relationships. This brochure summarizes those findings and presents the case for investigating and improving the quality of your contract management.

† This statistic - and others in this brochure - is drawn from IACCM research with its global, cross-industry membership, representing more than 12,000 organizations.

The Ten Pitfalls

Pitfall 1: Lack of clear scope and goals



Research shows this is the most frequent source of claims, disputes and disrupted relationships, impacting around 40% of projects. It results from poor communications, unclear responsibilities and failure to update business requirements. IACCM is not alone in recognizing this problem; failure to fully define, agree or prioritize requirements is consistently cited as the main cause of troubled projects.

Pitfall 2: Commercial team involved late

There is a common belief that early involvement of commercial staff will cause delays and problems. Research shows the opposite: early engagement cuts cycle time to a signed contract by around 20% and results in around 25% less claims or disputes. Yet internal management and measurement systems often work against inclusive behavior, resulting in poorly defined relationships and the wrong commercial structure or terms.

What the research tells us

Less than 15% of organizations have an integrated approach to commercial excellence. So while trading relationships are core economic assets, more than 85% of executives lack data or insights on key performance criteria. With the commercial process having no clear ownership, there are repetitive errors and sources of value loss.

More than 85% of executives lack key data or insights on performance.

For example, the terms and conditions that attract most attention during negotiations relate to liabilities, indemnities, liquidated damages, intellectual property, data protection and price. Yet those that have the greatest impact on success (or failure) are scope and goals, responsibilities of the parties, change management and communications and reporting.

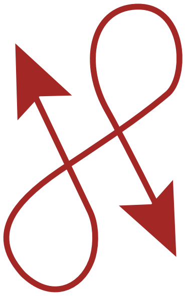
Because authority for commercial excellence is often dispersed across the business, less than 10% of organizations have consolidated data on performance, such as the most frequent sources of contract claim or dispute. This ensures that sources of weakness remain invisible and unresolved.

More than 9 out of 10 managers admit that they find contracts difficult to read or understand.

Although the purpose of a contract is to build a bridge between organizations, they are generally designed to reflect internal interests and perspectives. In more than 90% of organizations, contracts are viewed primarily as instruments for control and compliance, rather than as business enablers and tools for improved communication and understanding. A similar percentage admit that they find contracts hard to read or understand.

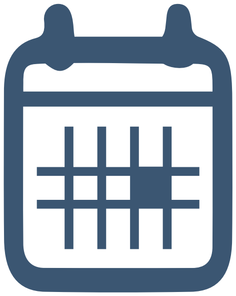
The Ten Pitfalls

Pitfall 3: Failure to engage stakeholders



Project or opportunity evaluation must include full analysis of stakeholders, internal and external. These are people or organizations on which success can depend and failure to engage and align them threatens results. Stakeholders often promote specific rules and policies, frequently reflected in rigid contract templates that are difficult to change and may be contrary to the required relationship. External stakeholders are frequently overlooked or their motivations are not adequately addressed. This creates misunderstanding, undermining the collaboration needed for value creation, innovation and trust.

Pitfall 4: Protracted negotiations



Inefficient stakeholder engagement and review processes extend the cycle time to reach agreement. Top quartile organizations close deals in one quarter the time it takes the bottom quartile. Delays result in competitive exposure, extended time to revenue and often hasty decisions imposed out of frustration or the need for urgency.

What the research tells us

92% of medium and large organizations seek to impose their standard contract templates onto their trading partners. While success rates vary, this approach causes inevitable contention, both internal and external. Forward-thinking organizations are adopting a 'principles-based' formula, enabling far greater flexibility and empowerment without jeopardizing business control.

Forward-thinking organizations are adopting a 'principles-based' approach to negotiation.

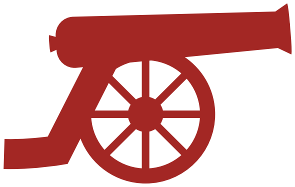
There has been a tendency over recent years for the economic basis of commercial decisions to become subordinate to legal and compliance concerns. This has resulted in an unbalanced approach to risk management, with fears over risk consequence dominating the process, to the exclusion of wider commercial considerations and assessment of risk likelihood. Many relationships therefore lack the mechanisms for proactive risk alerts and collaborative approaches to revision and change. This is a serious defect since, over the last 5 years, the need for significant revision or renegotiation of contracts during their execution phase has increased by almost 40%.

The need for significant revision of contracts during execution has increased by almost 40%.

At a time when business leaders are recognizing the need for more collaborative relationships and improved management of complex supply networks, many contracts are quite simply not 'fit for purpose'. New models are needed to support a world which requires agility, cooperation and delivery of shared value.

The Ten Pitfalls

Pitfall 5: Negotiations focus on risk allocation



The most frequently negotiated terms are indemnities and liabilities. A focus on protecting assets and avoiding loss creates an often adversarial environment, in which battles over risk allocation undermine the creativity and openness that support innovation and value. These defensive behaviors result in failure to tackle the sources of greatest risk likelihood.

Pitfall 6: Relationships lack flexibility, governance

Each year, the speed of change and market volatility increase, yet more than 80% of trading relationships remain traditional in their terms and structure. At senior levels, management encourages more collaborative, performance-based relationships, yet commercial practices are struggling to adapt. As a result, organizations are not effective in anticipating or enabling change and operational teams lack tools for managing performance.

What the research tells us

Given the time and effort expended on putting contracts in place, it makes sense to pay attention to their effectiveness. Yet without a focal point for commercial excellence, there is no point of accountability for the quality of contract relationships or their contribution to business outcomes. Best practice organizations – the top 20% - are designing contracts and systems that communicate effectively to the people responsible for their implementation and management. They are doing this through better structure, simpler language, the use of graphics and software.

Contract design: better structure, simpler language, the use of graphics and software.

Having simpler forms of contract not only reduces the time required for their interpretation, it dramatically reduces error rates – even among experts. As result, people are more ready to refer to the contract and mistakes are avoided.

Post-award contract management is fast becoming an area of major focus.

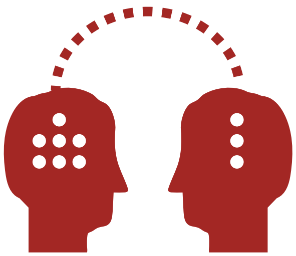
Post-award contract management is fast becoming an area of major focus. Historically seen as an administrative role, the duration, complexity and uncertainty surrounding many agreements has made their oversight increasingly important to business results. The transition phase from contract signature to implementation is viewed by many as critical to success.

The Ten Pitfalls

Pitfall 7: Contracts difficult to use or understand

Many people see contracts as having relevance only when there are problems. Yet in a world of longer term service and solution delivery, contracts contain critical rights, obligations and performance criteria. The complexity of their structure and language is not only unnecessary, but it is a source of risk.

Pitfall 8: Poor handover to implementation



Over 60% of project managers and implementation teams complain about the problems caused by handover from the bid team to the post-award execution team. Lack of engagement, communication and appropriate software tools often result in missed commitments or obligations. Frequently, there is no transition plan that engages personnel from both supplier and customer to ensure shared understanding.

What the research tells us

As networked technology and digitization transform the environment for trading relationships, the absence of robust and integrated commercial management technology is a severe gap in organizational capability. It leaves management relatively blind to key performance indicators and levels of risk, especially across major contract portfolios or interdependent supply networks. Only 14% of organizations even have plans to plug these data gaps through the adoption of advanced data management and analytics.

Only 14% of organizations have plans to plug contract management data gaps.

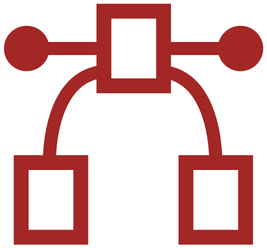
While software is important, it is only one element of the enhanced capability which tackles value loss. Commercial management is by its nature complicated. It involves a wide variety of stakeholders, internal and external, each of whom has valid interest in the content and the consequences of the contract. The sources of value erosion can only be tackled if there is a process which oversees and reconciles the varied perspectives and interests of the stakeholder community.

Stakeholders are reluctant for responsibility, but they resist it being assumed by others.

Stakeholders are typically reluctant to accept responsibility for contract outcomes, but they resist authority being given to others. That is why meaningful improvements in commercial management – and the bottom line benefits that flow from them – are achieved only by senior management intervention and sponsorship.

The Ten Pitfalls

Pitfall 9: Limited use of contract technology



Contract management is one of the least automated processes: over 60% of organizations lack a coherent application or have the wrong software. This results in inefficiency and weaknesses in performance oversight. It also explains the absence of management reporting and information.

Pitfall 10: Weak post-award process governance

Top performing organizations suffer contract value erosion of less than 4%. A distinguishing feature in all of these organizations is the investment they have made in post-award contract management capability. Through a combination of rigorous process, clearly defined roles, development of skills and supporting tools, they are eliminating repetitive issues and errors – and have made themselves more attractive and reliable trading partners.

Notes:

Who we are

IACCM is the world's only professional association for commercial management. We undertake research and benchmarking to provide global insights to best practice; we offer training and advisory services to support the development of organizational competence and capabilities; and we ensure that you have the knowledge you need to generate increased value from your trading relationships.

- More than 10,000 organizations represented in our membership
- Raising standards in over 150 countries

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