



RETHINKING CONTRACT MANAGEMENT FOR A POST-COVID WORLD

Abstract

In the wake of the disruption unleashed by COVID-19 and the resulting increase in the invocations of force majeure clauses by suppliers, organizations are being compelled to rewrite their contracts. This paper examines how more effective contract management processes can help mitigate the risks of non-performance amidst the continuing uncertainties in the post-pandemic world.

A new relevance for contract management

Even a year after the sudden outbreak of COVID-19, organizations continue to search for ways to improve agility and build resilience, and the subject of contract management is assuming fresh importance. This is because several suppliers and service providers are yet to get to grips with operating in the new normal. While some were able early-on to utilize technology interventions such as adopting work from home and continue with operations, many others faced insurmountable challenges in doing the same.

These latter businesses having defaulted on their contractual obligations are seeking to evade the huge losses they face on this account through invoking omnipresent clauses such as force majeure. The force majeure clause — dealing with adverse ‘Act of God’ kind of forces beyond anyone’s control — has remained silent for long but has increasingly been invoked during the spread of the pandemic. Until April 2020, China alone had issued 7004 force majeure certificates to contracts worth \$98 billion¹. Similarly, Italy and Russia too have experiencing a surge in number of requests

for issuance of the certificates including from foreign companies².

In this context, it has become crucial for organizations to review their contracts and adjust force majeure and other similar clauses to accommodate the new uncertainties brought about by the global pandemic. With the strength of contractual relationships and their outcomes at stake, effective contract management will increasingly be used as a lever to ensure business continuity and competitive advantage in the post-COVID era.

Managing the nuts and the bolts of contracts

As the name suggests, contract management simply covers the entire process of managing a contract across its lifecycle – starting from its creation and right through its execution and governance, analysis, and renewal. However, in reality these processes are much more complex than commonly understood. They involve maximizing the operational performance of the business, reducing financial risks and costs, constantly ensuring compliance to realize

savings booked under the contract, and often resolutions of conflicts that arise during the course of the contract.

The process of contract management begins when two companies first join hands to work together. The terms and conditions — known as clauses — of the said association are then drafted on a document and are mutually agreed to by both the parties. These clauses aim at safeguarding the interests of both the

stakeholders while also facilitating greater profitability for both in the long term.

While effective contract management ensures thorough compliance of the clauses of the contract, it also helps avoid disputes and contradictions through sound contract implementation and structured governance, ensures satisfactory delivery of services, prompt response and cooperation from suppliers, and paves the way for financial benefits and returns.

Three aspects to managing contracts well

In this context, the keys to effective contract management lie in successful upstream and post-award activities. The entire concept of contract management can be divided under three aspects.

Collaboration/ Governance

1

The basis of any contract — and thus contract management — is collaboration between two parties. Two consenting parties verbally agreeing to work together provides the reason to build a contract. While all the clauses in the contract are necessarily agreed to by both stakeholders, this consensus is reached only after several

rounds of discussions and negotiations.

During these negotiations, each side presents its concerns with regards to pricing structures, terms and conditions, rights and obligations, warranty provisions, renewals, termination, and the like. The negotiation process also involves laying

down clear and relevant metrics and KPIs to measure performance. These discussions while helping to create transparency, also initiate a long-term relationship and synergy via a carefully structured contract governance approach with participation from both parties.

¹ <https://www.dlapiper.com/en/china/insights/publications/2020/04/force-majeure-certificates-in-a-global-context/>

² <https://conflictoflaws.net/2020/force-majeure-certificates-by-the-russian-chamber-of-commerce-and-industry/>

Compliance

2

Contract compliance is a vital area that focuses on conformance to the terms and conditions agreed to by both parties in the contract. It is quite often seen that the hard savings identified during sourcing dissipate during actual spending due to poor compliance. This is especially true for indirect spend categories where there could be multiple leakage points such as a global buyer base not having the visibility into the contract, the lack of clearly laid

out policies for preferred suppliers giving opportunities for non-preferred suppliers, or a lack of linkages of contract rates to downstream procure-to-pay (P2P) systems.

An effective contract compliance framework mechanism can go a long way in reducing such contract leakages or value erosion over the deal term. This involves mature contract processes, approach, and infrastructure which are key to determining

the opportunity size for realized savings.

As procurement teams are responsible for implementing cost reduction strategies and identifying saving opportunities, it is imperative that they also give due emphasis to monitoring compliances. As per an Aberdeen Group Research report³, clearly defined compliance processes have helped organizations achieve 80% more savings.

Renewal/ termination

3

When entering a long-term association, it is important to renew the contract after definite intervals of time to ensure that agreed terms remain valid throughout the period of association. Managing the

renewals of multiple contracts is difficult, and it is important to automate the process and set a reminder every time a contract reaches its date of termination. Missing contract renewals or continuing

with contracts that have passed their termination dates can result both in losses as well as in damaged relationships.



Journeying ahead to better contracts

Going forward, the role of effective contract management is only set to intensify as organizations continue to struggle with the lingering aftershocks of the pandemic. Apart from industry's renewed focus on efficiency and scalability to recover from the setbacks already suffered, there is also increasing pressure to sign new contracts with suppliers to avoid the challenges that could be brought about by future invocations of force majeure clauses and the resulting risks of non-performance. The evolving situation mandates frequent evaluation and amendments in terms of scope, rights, and obligations through incorporating contemporary post-pandemic strategies.

Typically, force majeure clauses in

the past did not mention in detail the inclusions or next level specifications and invoking the clause often rendered the supplier completely relieved from all contractual obligations. However, after now experiencing various undefined invocations of this clause, organizations will need to review contract terms and include specific clauses for widening the risk coverage, especially regarding emergency situations like the ones posed during the COVID-19 outbreak.

Next, procurement teams also need to explore the possibilities of including reasonable mitigation measures to be taken by suppliers as part of their business continuity planning — such as recovery plans, liability insurance, and the like —

while also mandating timely notices by suppliers for anticipated breakdowns.

Lastly, organizations will need to consider the inclusion of technology and automation solutions such as contract lifecycle management (CLM) systems and contract analysis tools. Apart from greatly reducing manual efforts and errors, these solutions will help identify and plug leakages as well as analyze inconsistencies in verbiage, thus ensuring that contract management processes are efficient and effective.

This moment in time favors those who are thorough with their contracts and their clauses. Undoubtedly therefore, the journey towards more effective contract management is one worth undertaking.

³ <https://www.industryweek.com/leadership/companies-executives/article/21933292/5-best-practices-toward-contract-compliance>

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