## 

**CONTRACT RISKS AND CONTRACT CLAUSES:**

**A guide to help us manage our contract risks**

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**September 2014**

**Helping to manage your contract risks**

**INTRODUCTION**

In general a contract governs the rights and duties of the parties to the contract. Effective risk management includes having a good contract. This can limit USP’s exposure to liability, protect USP’s assets and staff and maximise benefits. It can also protect the other party.

Contracts in the university come in several formats. They include memoranda of understanding, research grant contracts, consultancy contracts, donor fund contracts and specialised contracts for capital works. There are many other types. All of them require us to look at the conditions and manage the delivery of the goods and services to reduce risk.

Good contracts build better relationships with the other party/ies. They can reduce manageable set-backs/difficulties that relate to costs, quality and timeliness. Good relationships also increase the opportunity to achieve better value for money. Contracts which are specific, clear and include concise language contribute towards good business relationships.

Good contract management during the contract period enables good lessons to be learned. These can help us improve our contracts over time. These improvements include better management of contract risks. This increases assurance that USP’s interests are better protected. Good record keeping and regular meetings during the contract period will greatly assist in this.

Good contract terms also help with our insurance claims. We need to be careful not to accept all the risks in a contract without questioning them. If we do, our insurers can say we were prepared to accept the risk ourselves. They might then deny any claims for costs or damages if we submit a claim. However, if we can show we’ve considered these matters before submitting a claim, we’re on much firmer ground. So it is important we protect ourselves and carefully consider contract risks.

We’ve prepared this guide with points to consider when reviewing your contract. It contains “helpful hints’ to assist you improve managing your contracts. You are encouraged to go over the relevant points before deciding to enter into a contact or signing the contract. There’s a short checklist at the end to help you with any assessments you make.

We’ve had a lot of help in putting this together. We’ve had suggestions from the Council Secretariat, Procurement and Marketing colleagues. Thanks to our colleagues for their considered input into our various drafts. We would encourage all colleagues to contact Procurement for their in-depth expertise in managing contract risks.

This is the first assessment in this area we have issued. We welcome your comments on it. We’ll issue other guidance as we identify issues about risk and contracts that may help you.

We hope you find the guide useful.

**Director of Assurance and Compliance**

**September 2014**

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| **Some definitions**:  A contract refers to any agreement between USP and other party.   1. **Where USP prepares a contract:** Examples are contracts for goods, services & construction, consultancy agreements and USP -tenancy agreements. 2. **Where another party prepares the contract:** Examples are services from an outside contractor, lease agreements for land, buildings and equipment. And rental agreements.   **Liability:** Legally broadly means a binding obligation to settle a debt. Being liable is being responsible for something, such as paying for services. This will be contained in a liability clause. Liability clauses can vary. Examples include exclusions (not liable for something), limitations (will cover up to a maximum amount) or restrictions (will cover specific types of loss or damage).    **Indemnity:** Broadly speaking, this is a provision in a contract where one party or both parties commits to meet the expenses of the other for any harm, liability or loss occurring in the contract. |

**SOME BASIC CONSIDERATIONS**

**BASIC POINTS ABOUT CONTRACTS**

When we enter into a legally binding contract need to ensure it:

* Adequately protects USP.
* Support USP’s strategic objectives.

Even documents with no specific obligations and not considered ‘legally binding’ such as an “agreement to agree” should be reviewed.

**BASIC POINTS ABOUT CONTRACT TERMS**

* When USP is given a contract by another party or company, it is their standard contract. The terms of the contract will benefit them. These contracts must be reviewed to ensure USP is adequately protected.
* Contract terms are usually negotiable. If there are terms which concern you, negotiate for more appropriate terms for USP.
* All adjustments must be included before the document is signed.
* The best decision may be not to enter into the contract. This might be because the contract terms impose too great an obligation or risk on USP.

**OUR MAIN POINTS OF GUIDANCE**

1. **Know your contracts (expired and active)**
   * Maintain a list of your contracts and agreements. These include the third party name, the value, a description of the contract and the contact expiry/renewal date.
   * Ensure meetings and concerns about larger contracts are kept. This is to ensure important points and risks are picked up if the contract is to be renewed.
   * Use this list to ensure the timely scheduling of contract reviews.
2. **Understand reason(s) for the contract. (I.e. objective/benefit)**
   * Ensure you have the current version of the full contract. For example, all appendices are included.
   * Both parties must invest time and read every line/word of the contract (including the fine print).
   * How will the contract benefit USP and meet our objectives?
3. **Written and oral contracts:**

Oral agreements to deliver goods and services **are contracts**. Avoid making these commitments. We have standard procurement terms and conditions that we must comply to. There is much more risk attached to oral agreements as there is a greater chance of ambiguity about what the other party needs to do.

A well written contract reduces misunderstandings. However, badly written clauses increase the risk of legal costs being incurred. They can also eventually cause financial loss and reputational damage.

**4. Allow adequate time to review and negotiate before signing**.

* + Do not sign contracts unless you understand the details. These include the liability and indemnity clauses.
  + Start reviewing contracts well in advance of signing or renewing them. Allow time for a thorough review.
  + Do not work in isolation. Involve other relevant departments to get assistance, advice and input.
  + If your contract is very large, complex or important, consider whether it needs some legal scrutiny. This will require SMT approval in compliance with our policy on accessing this service.

1. **Both parties must clearly understand all clauses in the contract and be able to fulfill their obligations.**
   * Contracts must specify what each party is responsible to do, by when, rights and duties, managing disagreements/termination conditions, contract end date, payments terms, handling changes etc.
   * Ensure a clause is included that says changes are not valid unless they are in writing and signed by both parties.
   * USP must work directly with the company unless USP approves involving a third party.
   * Clearly understand the country’s statutory laws/ regulations.
   * Ensure important USP policies, such as compliance to our OHS policies, are included.
   * Reduce the risk of confusion through ambiguous wordings.
     + They must be clear and precise.
     + Separate clauses by issue or category. This improves clarity.
     + Any insurance requirements and warranty periods are clear and acceptable to both parties.
     + Carefully examine any term that seems to guarantee something, such as, ‘ensure’, ‘insure’, ‘all’, ‘assure’ etc. Avoid this where possible.
     + Avoid general phrases words like ‘any loss’, ‘to your satisfaction’, ‘appropriate’ etc. For example, exclusion clauses should be more specific than just saying ‘any loss’.
   * Contracts are generally entered into in good faith. This assumes each party will uphold its part of the bargain. However, this does not always occur. Therefore, contracts may need to include dispute resolution and escalation clauses.
   * Is there any wording in the contract which makes USP responsible for consequential damage like loss of profit? We need to make sure these clauses are excluded or limited wherever possible.
   * Is there an all-important exit clause if the contract is deemed to be failing for either party? This can protect each party from the costs associated with non-delivery of goods and services. We should look to have these in longer-term contracts.
2. **Contracts often contain clauses protecting parties from the risk of losses:** Managing risk is an integral part of good management and should be an integral part in developing and managing contracts. The risk of losses can be transferred through insurance cover. Another way of managing this risk is by using disclaimers or specific conditions.

* Are there any potential financial implications, including long-term liabilities, being taken on? If there are, ensure USP or the other party can meet them.
* Are USP and the other party’s insurance cover adequate in scope and also in value? For example, if someone is providing a service for us, do they have professional indemnity cover? If a company leases us a building, do they have adequate business interruption arrangements if the building can’t be used?
* Are there any clauses such as: limit of liability, indemnity, disclaimer or conditions not to USP’s benefit? Should USP consider negotiations? We need to consider if such clauses are reasonable and acceptable. These considerations include:
  + Can the other party seek damages from USP if USP does not do something stated in the agreement?
  + Can USP seek damages from the other party if they do not meet contract terms/conditions?

1. **We need to take care when we are either asked or are asking other parties to take on responsibility for costs. We need to ask if this is either required or reasonable.**

* Is USP being requested to take on expenses/costs which the other party is liable for? What are the reasons and is this really required? In general USP should not agree to indemnity clauses that transfer financial risk from a liable party to the university.
* Is USP liable for any expenses due to contract terms?
  + - Is there a limit of liability clause such as party will only pay up to a certain amount for damages? For example, USP has a contract with a construction company. Their work causes damage to USP contents within the building they’re working on. USP can then only recover damages to contents up to the limit. We need to ask if such a clause is reasonable.
* Are we asking others to bear our costs and are we being reasonable in doing so?

1. **We need to ensure we manage contract risks during the currency of the contract:** This is a very big area. The main stages we’d emphasise from a risk perspective are the following:

**Managing relationships:**  An important element in any contract is the quality of the relationships between the parties. There is an obligation on both sides to establish and maintain a productive relationship. Having professional, constructive relationship with contractors is key to successful contract delivery.

* Is there a clear strategy for contract liaison meetings to reduce the risk of contracts failing?
  + - * Are there identified persons to deal with any matters requiring escalation?

**Defining contract deliverables clearly:** One of the critical aspects in any contract is clearly defining contract deliverables. Deliverables are often called a statement of work, a statement of requirement, specifications or other similar terms. These must explain the goods or services to be provided under the contract.

* Is there a clear statement of what is required from the contract to reduce the risk of contract disputes?
* Is there a clear timeline for delivering the goods and services to reduce the risk?

**Developing a contract management plan:** A contract management plan is a best practice approach to managing risks to successful contract delivery. It ensures risks relating to everyone’s obligations under the contract are not overlooked.

* Has a contract management plan been put in as a requirement of the contract?
* Are there clear KPIs to reduce contract delivery risks and risks of disputes?
* Is there an adequate risk assessment to support contract delivery and reduce the risk of disputes?
* Do we have appropriate risk treatments for each phase of the contract (where required) to reduce the risk of disputes?

**CONTRACT ASSESSMENT CHECKLIST**

The following short checklist will assist you covering the main points noted above. We’ve taken the main headings and put them into a series of questions. When you do your evaluation, refer back to the points we’ve made under each heading. This should help you note any actions you need to take to strengthen your processes and help manage your contract risks

This is a general guidance and when reviewing contacts. There may be other matters you need to consider for specific contracts. We would emphasise that you should speak to our Procurement team in cases of concern or doubt. The Risk and Insurance Unit will also provide advice on risk and insurance matters for you.

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| **GUIDANCE PART** | **Assessment questions:** | **Y** | **N** | **ACTION NOTES** |
| **1** | **Do you have an active contract register that can also be used to schedule timely contract reviews?** |  |  |  |
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| **2** | **Do you need all your contracts? If so, do you understand the reason for them and are all the clauses clear to you?** |  |  |  |
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| **3** | **Are there any oral agreements you have that you need to end?** |  |  |  |
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| **4** | **Have you identified all the persons you may need to help you with any contract review well in advance?** |  |  |  |

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| **GUIDANCE PART** | **Assessment questions:** | **Y** | **N** | **ACTION NOTES** |
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| **5** | **After reading the contract, are you clear what is expected of USP and the other party?** |  |  |  |
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| **6** | **Are you satisfied that the liability, indemnity and insurance clauses provide adequate protection to USP and that neither party is being put under unreasonable obligations?** |  |  |  |
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| **7** | **Are clauses in areas where either party is being asked to assume liabilities for costs or activities reasonable or not?** |  |  |  |
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| **8** | **Do we have adequate, documented processes to manage risks while the contract is being delivered?** |  |  |  |
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