

Developing contracts

Session 1

Categories of procurements:
goods, services, capital items, goods for re-sale
The objectives of good procurement



Learning objectives

At the end of this session candidates will be able to:

- describe, using examples, the types of products and services typically purchased by organisations
- identify the categories of expenditure on goods and services
- explain the role of the procurement function in setting up agreements for purchased goods and services
- define the overall purchasing task
- formulate objectives that enable purchasing departments to realise overall strategy
- explain why specifications, performance measures and contractual terms are used in supply agreements.



Purchasing and procurement

Purchasing

Buying or obtaining goods or services which are paid for.

Procurement

Obtaining goods or services in any way including hiring, leasing, borrowing; and taking account of whole life costs.



Categories of procurements

- Capital equipment
- Production materials
- MRO supplies (Maintenance, Repair and Operation)
- Re-sale goods
- Services.



Expenditure

Capital

Infrequent purchase

Tend to be high specification and cost so consider life cycle costs and payback

Negotiations can be complex and lengthy.

Non-capital

Purchased more frequently

Lower cost and tend to be simpler specification

Negotiations not as complex.

Purchasing role

Depends on:

- type of goods or services
- frequency of purchase
- size of organisation
- level of experience.



Five rights of purchasing

- Quality
 - Quantity
 - Place
 - Time
 - Price.
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- An additional right is that of the right source.



Purchasing objectives

- Related to the organisational objectives
- Are sometimes in conflict
- If irreconcilable, then the importance of one must be compared with that of another.



Key issues

- Conformance to specifications
- Measuring supplier performance
- Clear contract (legally binding)



Developing contracts

Session 2

Achieving procurement objectives
Contract formation – the agreement



Learning objectives

At the end of this session candidates will be able to:

- explain the importance of specifications in achieving value for money
- explain, using examples, why performance measures and targets are used in agreements with suppliers
- summarise the differences between purchaser's and supplier's contractual terms
- define the term contract
- explain what an offer is and distinguish it from an invitation to treat
- identify and describe the ways in which an offer can terminate
- define acceptance and distinguish it from a counter offer
- explain the rules on communication of acceptance
- explain the distinction between framework and call off contracts.

Specifications

Clear and unambiguous specifications facilitate:

- communication between all involved, including purchaser and supplier
- comparison between bids.



Specifications

- Conformance specifications – strict technical specifications
- Performance specifications – identify what the requirement is expected to do or achieve.



Specifications

There are many different ways of specifying requirements and they vary in different environments. What methods do you use for your requirements?

Examples – brand name, physical properties, samples.



Supplier's performance indicators

- Price
- Quality
- Delivery
- Customer satisfaction.

Performance management systems can be complex and should include alerts when KPIs are not met.



Written contract

Benefits of a written contract include:

- accurate record of the agreement
- clarify purchaser's rights against the supplier
- clarify buyer's obligations to supplier and vice versa.



Invitation to treat

Provides information

Invites an offer, but is not itself an offer

Is not legally binding.



Offer

Often in response to an ITT

Provides details of the offer

Indicates willingness to enter into an agreement

Is legally binding.



Offer

- Offer must be communicated
(by the 'offerer' to the 'offeree')
- If it is not communicated it is incapable of being accepted
- May be made to the world at large, or just to an identified individual or company or group.



Termination of offer

- Rejection
- Acceptance
- Counter-offer
- Revocation
- Time.



Acceptance

- Unconditional acceptance leads to agreement
- Acceptance must be communicated verbally or in writing to the offerer
- If posted, acceptance is taken from the point of posting, otherwise when received.



Framework agreements

- Used for situations where parties anticipate doing business in the future but do not want to agree terms for the future
- Specifies detailed terms and conditions for future contracts
- Fixed term, fixed quantity or 'insurance'.



Call offs

- Purchase orders submitted by the purchaser against the framework agreement
- Relatively simple, so is often made by a junior member of staff
- If the offer is accepted a contract is formed (frameworks do not show contractual commitment).

Developing contracts

Session 3

Contract formation: – ‘consideration’ and ‘intent’;
‘The battle of the forms’



Learning objectives

At the end of this session candidates will be able to:

- define 'consideration' in the context of contract formation and explain its main principles
- identify the legal presumptions in intention and explain their application to the formation of contracts
- explain who has the right to sue on contracts
- explain the meaning of 'capacity' in the formation of contracts
- apply principles of contract formation to given situations
- explain what is meant by the 'Battle of the Forms'
- apply the legal principle in the Battle of the Forms in a given situation
- identify how the procurement function can avoid battle of the forms situations arising
- analyse the formation of e-contracts.

Consideration

- There is no contract if one party promises to do something but the other party promises nothing in return – no ‘bargain’ has been struck
- Consideration is something of value (in the eyes of the law) that is given or accepted in return for a promise
- Consideration must be sufficient but not necessarily adequate – the law is not concerned with how ‘good a deal has been done’.



Insufficient consideration

- If the consideration is insufficient there is no legally binding contract
- Consideration may be insufficient if the alleged consideration is something that the party is already obliged to do – such as carrying out an existing contractual or public duty, part payment of debt
- Consideration may not be related to past actions
- A contract can only be enforced by someone who provides the consideration.



Intent

- Both parties must intend to enter a legally binding contract
- In *social/domestic agreements* the law presumes that there is no intention to create a legally binding relationship unless there is very clear evidence to the contrary
- Whereas in all *business/commercial arrangements* the presumption is that the parties always do intend to create legally binding relationships.



Capacity

- Parties to a contract must be 'capable' within the legal definition such as over 18, not drunk or drugged, and not mentally unstable
- But the Law distinguishes between individuals and businesses – presumption is that if contracting on behalf of your employer, you are always 'capable' of making legally binding deals.

(And business would be impossible were it otherwise, and businesses could 'opt out' of deals after they were made)

The battle of the forms

- Occurs when both parties to a contract try to ensure that their own standard terms and conditions will govern that contract
- In a 'battle of the forms' situation, acceptance often takes place when the purchaser accepts the goods

Has your organisation been involved in a battle of forms?

What can be done to make sure your organisation always wins the battle?



Right to sue

- Only a party to a contract may sue to enforce that contract or be sued on it (doctrine of privity)
- Purchaser may not sue a subcontractor or third party if the contract is with the main contractor – a purchaser in a strong position may be able to insert a clause that holds main contractor liable for any breaches by a third party.

Contracts (Right of Third Parties) Act 1999



E-contracts

E-commerce – doing business electronically. More precisely it is conducting the exchange of information using a combination of structured messages (EDI), unstructured messages (email), Internet, data, databases and database access across the entire range.

E-contracts – contracts made using electronic communication on the Internet and email.

Developing contracts

Session 4

Forming contracts for International trade
standard model form contracts



Learning objectives

At the end of this session candidates will be able to:

- identify and outline the laws which are relevant for the formation of contracts in international trade
- describe the contents of bills of lading and explain their function
- describe the use of documentary credits
- describe the main provisions of the Vienna Convention
- explain what is meant by a 'standard model form contract'
- discuss why and how standard model form contracts are used
- identify examples of model form contracts and briefly describe some of their main provisions.



International trade

- Procurement activities must comply with the government obligations under the relevant EU Directives and the World Trade Organisation (WTO), formerly GATT
- The EU Procurement Directives set out the legal framework for public procurement. They apply when public authorities and utilities seek to acquire goods, services, civil engineering or building works. They set out procedures which must be followed before awarding a contract when its value exceeds set thresholds.

- Source: www.ogc.gov.uk



International trade

- Carriage of Goods by Sea Act 1951
- Hague-Visby Rules
- *What International contracts does your organisation currently operate?*



BOL – Bill of Lading

This is a receipt for goods shipped on board a vessel, signed by the person (or his or her agent) who contracts to carry them and states the condition in which the goods were delivered to the ship. This is the document of title to the goods without which the buyer will not be able to obtain delivery from the shipping company

Source: Export Practice and Management 4th edition, Alan Branch

Documentary credits

- Revocable letter of credit
- Irrevocable letter of credit
- Confirmed irrevocable credit.



Vienna Convention

- The Vienna Convention is a United Nations implemented agreement dealing with the sale of goods across International boundaries
- The Vienna Convention addresses risk management issues and should be considered by any organisation conducting International trade.



Model forms of contract

- Model forms of contract and conditions have been developed by professional and trade bodies
- For example, OGC, CIPS, the CBI, Association of Consultancy Engineers (ACE)



Developing contracts

Session 5

Effectiveness of supply agreements
classification of contract terms



Learning objectives

At the end of this session candidates will be able to:

- explain what is meant by a 'supply agreement'
- identify matters which affect the effectiveness of supply agreements
- evaluate the effectiveness of a supply agreement
- explain the classifications of statements and contractual terms
- identify and explain what is meant by a 'condition' and the effect this will have on breach of contract
- identify and explain what is meant by a 'warranty' and the effect this will have on breach of contract
- identify and explain what is meant by an 'innominate term' and the effect this will have on breach of contract.



Supply agreement

- Sets out the agreement between the seller and the buyer
- Includes customer identification details, billing information, terms and conditions
- Signed by both parties and is legally binding.



Contract terms

What is the difference between:

- express terms
- implied terms.



Conditions

- A condition is a term in a contract that relates to what the parties to the contract have agreed
- Breaching a condition entitles the other party to sue for damages and terminate the contract if they wish
- In some cases, the injured party might take the option of affirming the contract and claiming damages
- What experience have you of breach of contract?

Warranties

- A warranty is normally a promise that the goods and services will meet the required standard
- Regarded as a minor term relative to condition
- Breaching a warranty does not entitle the injured party to terminate the contract but there is entitlement to damages.



Innominate terms

- Terms are innominate if so stated in the contract or if the contract is silent as to what classification the terms falls into
- Breaching an innominate term has different consequences depending on how serious the consequences are on the contract at that time.



Developing contracts

Session 6

Implied terms

Express terms – key contract terms



Learning objectives

At the end of this session candidates will be able to:

- explain the circumstances when terms may be implied into contracts
- describe the terms implied in contracts by ss12-15 SGA 1979 (as amended)
- explain the effect of breach of the implied terms under ss 12-15 SGA 1979 (as amended) and identify any possible remedies
- identify whether terms implied in contracts under the SGA 1979 (as amended) can be excluded
- describe the terms implied in contracts by ss 2-5 SGSA 1982 (as amended)
- describe the effect of breach of the implied terms under ss 2-5 SGSA 1982 (as amended) together with any relevant remedies
- explain how the courts will treat contract terms
- identify suitable key terms to be used in different contract situations.



Legal framework

- Sale of Goods Act 1979
- Supply of Goods and Services Act 1982
- Sale and Supply of Goods Act 1994
- Data Protection Act 1998
- Fair Trading Act 1973
- Competition Act 1980
- Unfair Contract Terms Act 1977
- Limitation Act 1980.



Terms and conditions

- Express
 - Implied
 - Statutory
 - Unlawful.
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- Exclusion or limitation clauses
 - Retention of title clauses
 - Penalty clauses.



Core clauses

- Terms of payment
- Time of the essence
- Confidentiality and data protection
- Insolvency and bankruptcy
- *Force majeure*
- Dispute resolution
- Termination for breach.



Implied term

- A contract term that has not been expressly agreed, drafted and included in a contract
- It is 'implied in the contract' by law whether or not both parties agree or not
- If a contract is too detailed, courts will be reluctant to imply terms, too many gaps may lead to a contract being declared void!



Sale of Goods Act 1979 (as amended)

- Applies to goods that are sold – not hired or bartered
- ss12, 13 and 15 apply whether the transaction is private or business but s14 applies only to business transactions
- *What is the definition of 'goods'?*



Ss12-15 SGA 1979 (as amended)

- s12 Right to sell the goods
- s13 Description
- s14 Quality and fitness of goods
- s15 Sale by sample.



Supply of Goods and Services Act 1982

- Part I ss2 – 5 apply to contracts which are for the supply of goods:
 - s2 Title
 - s3 Description
 - s4 (2A) Quality
 - s4 (3) Fitness for purpose
 - s5 Sample.



Supply of Goods and Services Act 1982

- Part I ss7 – 10 apply to contracts which are for the hire of goods
- s7 Title
- s8 Description
- s9 (2A) Quality
- s9 (3) Fitness for purpose
- s10 Sample.



Supply of Goods and Services Act 1982

- Part II ss 13 – 15 apply to contracts which are for the supply of services
- s13 – reasonable skill and care
- s14 – within reasonable time
- s15 – reasonable price
- *What is a situation of bailment?*

Effect of breach

Breach of condition under SGA 1979 provides remedies for damages only:

- purchaser has accepted the goods
- purchaser does not wish to terminate the contract so breach is treated as breach of warranty
- breach is slight so termination is unreasonable
- otherwise remedies include termination and claim for damages.



Effect of breach

- Breach of condition under SGSA 1982 provides similar remedies to breach of SGA 1979
- Breach of ss3 – 5 and ss8 – 10 only allow claim for damages where:
 - purchaser/bailee is not a consumer
 - breach is so slight it would be unreasonable for the purchaser/bailee to seek termination.

Unfair Contract Terms Act 1977

- Imposes limits on the avoidance of civil liability for breach of contract or negligence by contract terms

- Two considerations whether express terms to exclude or limit liability:
 - status of purchaser
 - reasonableness of term.



Liquidated damages

- Compensation that must be “a genuine pre-estimate of loss”
- Often referred to as ‘penalty clauses’ (albeit mistakenly, as English Courts do not enforce an actual ‘penalty’, only a genuine loss that was pre-estimated)

TUPE

- Transfer of Undertakings (Protection of Employment) Regulations 1981 - regulations change frequently – ensure you keep up-to-date – free guide from www.dberr.gov.uk
- TUPE Regs provide safeguards for employees' rights where businesses change hands between employers and/or contractors change
- Employees rights, and years of service, should be 'transferred' with them to the new contractor.

Developing contracts

Session 7

Express terms – limitation/exclusion clauses

Express terms – amendments, change, review,
renewal



Learning objectives

At the end of this session candidates will be able to:

- identify clauses which are limitations of liability or exclusion clauses and explain how the courts will treat such clauses
- apply the incorporation test
- apply the interpretation test
- apply the reasonableness test to limitation/exclusion clauses
- identify suitable limitation/exclusion clauses to be used in contracts
- compare and contrast litigation and alternative dispute resolution
- identify suitable contract terms to deal with resolution of disputes, variation and termination of contracts.



Liability clause

- Should clearly state the maximum amount that one side will pay to the other in compensation in the event of a breach of contract
- The type or types of loss for which no compensation can be claimed
- Some clauses limit liability of both buyer and seller but more often clauses are drafted to limit the liability of the seller.



Liability clause

Buyer needs to consider:

- should buyer's liability be limited, as well as the supplier's?
- from which types of loss is the supplier trying to limit their liability?



Force majeure

Suppliers may try to claim '*force majeure*' in order to avoid responsibility for their failures.

- *Beware of FM clauses!*
- *What, precisely, might occur?*
- *What are the real risks?*
- *What can be done about those risks?*
- *Who is best placed to bear the risk?*

Incorporation

- An exclusion clause that one party seeks to rely on must form part of the contract
- An exclusion clause can be incorporated into a contract by signature, by notice, by a course of dealing.



Interpretation

- Once it is established that an exclusion clause is interpreted, the whole contract is construed (interpreted) to see whether the clause covers the breach that has taken place
- An exclusion clause that is ambiguous may be declared *contra proferentem*
- An exclusion clause must be consistent with the main purpose of the contract
- *How is fundamental breach of contract dealt with?*



Reasonableness

UCTA 1977 s11(1) states:

"the term shall have been a fair and reasonable one to be included having regard to the circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made."

Contract clauses

Clauses should be included to cover:

- variation of contract
- renewal of contract
- termination of contract
- dispute resolution.



Alternative Dispute Resolution (ADR)

- Informal procedure for resolving disputes about a contract without involving a court of law
- A more flexible and informal approach to dispute resolution
- Major disadvantage is that it will only work if there is willingness on both sides
- See www.acas.gov.uk and www.ogc.gov.uk



Governing law and disputes

- Clause should state what will happen in the event of a dispute – arbitration, ADR
- Ensure that the clause states what law should apply and which court will resolve disputes if appropriate.



Arbitration

- Both sides agree to appoint a nominated person to resolve their dispute and to abide by his/her decision
- Hearings are held in private and the arbitrator is often a person with relevant expertise
- May not be less costly than going to court!



Termination clause

- Sets out the right of the parties to terminate the contract in the event of a breach or insolvency of one of the signatories
- Should identify a notice period
- Buyer needs to consider what happens post termination if there is still 'unfinished business'.



Variation of contract

- This phrase means a change in the terms of the contract itself and must happen with the agreement of both parties
- The contract with the agreed change in terms becomes a new contract between the two parties.



Contract extension

- Often called contract renewal, it can arise for a number of reasons relating to the client
- Alternatively, the original contract may have provision for the term of the contract to be extended
- Should not be renewed more than once, otherwise it leads to exclusion of other potential contractors.



Developing contracts

Session 8

Standard contract terms for indemnities

International considerations for express terms

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Learning objectives

At the end of this session candidates should be able to:

- discuss standard terms for indemnities such as intellectual property rights, insurances, accidents and damage, third parties
- identify the reasons for including a contractual term in an international contract to specify choice of legal system
- outline issues which an arbitration clause could address in an international contract for the sale of goods or services
- compare and contrast different types of Incoterms.



Indemnity

- Promise by the supplier to compensate the buyer if there is breach of warranty
- Main advantage for the buyer is that he/she can usually claim more money when things go wrong
- The buyer may have to go to court if the supplier refuses to pay.



Intellectual Property Rights (IPR)

- Patents
- Copyright
- Designs (registered and unregistered)
- Trade marks (registered and unregistered).



Insurances

- Professional indemnity
- Public liability
- Products liability, products guarantee, products recall.



Risk and title

- Risk is important because it impacts on what insurances you, as a buyer, need to take out
- Generally risk and title pass to the buyer on delivery of the products
- Retention of title clauses prevents the buyer taking ownership of goods until they have been paid for.



Contracts (Rights of Third Parties) Act 1999

- This legislation allows a 'third party' (someone who is not a party to the contract) to sue one of the actual parties (signatories to the contract) for breach of contract
- If the parties do not want this to happen then they 'specifically exclude' the Act

What circumstances can you think of where, as the buyer, you would not want the Act to apply?

International purchasing protection

- Appointment of agents working overseas
- Bills for collection
- Letters of credit
- Incoterms (International Chamber of Commerce)
- Establishment of an overseas base.



Incoterms

Incoterms define:

- the precise place of delivery from the supplier
- the responsibility for freight costs, carriage and insurance of either the buyer or the seller
- the point at which the risk of the goods in transit passes from the seller to the buyer.



Incoterms

There are 13 Incoterms and they are used to help clarify misunderstandings about who should:

- be responsible for clearing goods through customs
- pay the costs of loading, transporting and final delivery of goods
- bear the risk of loss or damage to the goods in transit
- take out insurance against the above risks.



Developing contracts

Session 9

The tendering process
EU procurement objectives



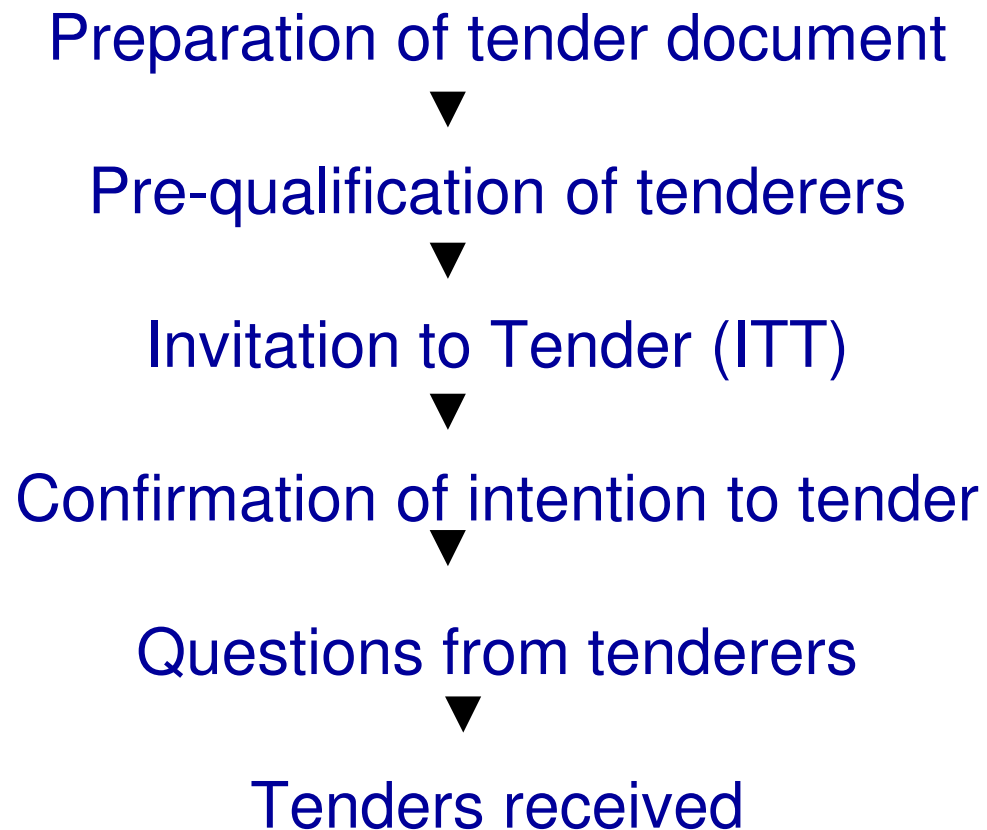
Learning objectives

At the end of this session candidates will be able to:

- describe the stages in the tendering process
- explain why pre-qualification and evaluation criteria are used
- explain when it would be appropriate to enter into post-tender negotiations
- explain what 'contract transitional arrangements' are
- state the objectives of the EU Procurement Directives
- explain how the EU Directives can be enforced to ensure compliance
- explain the relevance of threshold values
- identify and describe the different procurement procedures under the EU Directives
- describe the criteria used when awarding contracts under EU procedures
- explain the debriefing process under the EU procedures relating to procurement.



Tender process



Tender process

Evaluation of tenders



Short-listing of tenders



Post-Tender Negotiations (PTN)



Award of contract



Pre-qualification

- Process to determine acceptability of potential suppliers
- Criteria include the five rights – quality, quantity, place, time, cost
- Additional criteria are set to ensure the supplier can meet the requirements as specified by the purchasing organisation
- Effective pre-qualification should ensure suppliers can consistently meet requirements and will be placed on the ASL or PSL
- Pre-qualification is essential in situations of high risk and high spend.

Invitation to Tender (ITT)

- Instructions and deadline
- Objectives and scope
- Specification
- Explanation of award process
- Bill of quantities
- Pricing requirements
- Point of contact.



Supplier tender evaluation

- All suppliers must be treated equally
 - Set clear commercial, technical and financial criteria for evaluation
 - Evaluate fairly against commercial compliance
 - Evaluate fairly against ability to meet specifications on a technical basis
 - Evaluate fairly on the basis of costs
 - Analyse all tenders against objective criteria
-
- Tender evaluation is significantly impacted by the relationship between risk and spend.



Tender evaluation

- Commercial criteria
- Technical criteria
- Financial criteria
- *What specific criteria might be included under each heading?*



Post Tender Negotiation (PTN)

Be wary of PTN! It...

- *Might re-open the competition*
- *Might distort the competition*
- *Might invite challenge from unsuccessful bidders.*



Contract transitional arrangements

- To ensure smooth transition from one contract to a new contract
- To ensure there is no impact on service capacity and continuity
- To help manage investment costs
- Sets out review process and time scale.



EU Procurement Directives

Principle: EU public bodies **MUST** advertise **ALL** of their requirements.

Procedures: All needs must be advertised. In addition, when triggered by financial thresholds, public bodies must:

- advertise their requirements, and their contract awards, in the supplement to the Official Journal of the European Union (OJEU)
- obey time limits for bids and expressions of interest
- outline selection criteria clearly ('MEAT')
- show that they treat all suppliers equally
- use mandated processes.



EU procurement best practice

- Clear objectives
- Clear specification
- Knowledge and understanding of market and law
- Effective sourcing with all suppliers treated equally
- Sound, objective criteria for contract award
- Efficient contract management
- Strict monitoring of supplier performance.



Public Procurement Directives

- The EU Procurement Directives set out the legal framework for public procurement
- They apply when public authorities and utilities seek to acquire goods, services, civil engineering or building works
- Intended to guarantee fair and non-discriminatory international competition in bidding for goods, works and services above specified threshold values.



Procedures

The EU Procurement Directives provide for four different procedures. One of these **MUST** be followed, precisely, for all purchases above the thresholds:

- restricted procedure, whereby only invited suppliers may submit tenders
- open procedure, whereby all suppliers interested in the contract can subsequently be invited to submit tenders
- negotiated procedure, whereby purchasing bodies may negotiate the terms of a contract with one or more suppliers of their choice (this can only be used in special circumstances, but in certain cases may be used without first publishing a contract notice)
- competitive dialogue procedure, for complex and novel requirements only. see www.ogc.gov.uk

Debriefing suppliers

- Should offer all unsuccessful tenderers the option of a debriefing – full debriefing may be difficult to justify for minor contracts
- Unsuccessful tenderers have the right to know the reasons for rejection
- Assists suppliers in improving performance if the debriefing includes weaknesses of unsuccessful bid
- Assists buyer and purchasing organisation in establishing open and honest reputation.

Developing contracts

Session 10
Electronic tendering;
Contract review and improvement



Learning objectives

At the end of this session candidates will be able to:

- identify the uses of e-tendering
- outline the legal issues relating to e-tendering
- explain how contracts can be managed successfully
- identify what is meant by contract review
- identify how the contracting process can be improved.



Electronic tendering

Benefits include:

- quicker
- no paper
- easy access
- semi-automated
- easily secured
- instant audit trail.



Electronic tendering

Drawbacks include:

- costs of software
- suspicion by bidders
- no paper audit trail
- lack of access for unskilled bidders.

How does e-tendering differ from the 'traditional' tender process?



Review of contract

Many organisations have procedures in place to cover contract review, and to gather 'lessons learned' after each tendering exercise

Write a checklist to identify what should be checked when reviewing how well a contract was let.



Contract monitoring

Should reveal situations such as:

- unsatisfactory performance
- misunderstanding of requirements
- inadequate or ineffective communications
- poor data management
- changes to the contract brought about by unexpected altered requirements
- contractor insolvency.



Record keeping

- Both parties to a contract should keep timely and accurate records to help them review and improve process and maintain an audit trail
- Records should cover all activities including complaints, performance failures and recurring problems
- Records also inform vendor rating systems and monitor performance for payment purposes.



Post-project assessment

Following termination of contract it is good practice to review what went well and what did not to inform future activity. Evaluation should cover:

- conduct and outcome of the project
 - extent to which the project deliverables were achieved
 - total cost and variance
 - what has been learnt about systems, processes and procedures.
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- *How does your organisation ensure continuous improvement in contract management?*