BEST PRACTICE

CONTRACT MANAGEMENT WITH CATS CM® VERSION 4

From working on contracts to contracts that work

Linda Tonkes
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Van Haren PUBLISHING

Contract management with CATS CM® version 4
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Foreword

You are looking at version 4 of the CATS CM methodology. CATS stands for Contract Administration and Tracking Scenarios. CATS CM offers a comprehensive contract management methodology that has the flexibility and scalability necessary to adjust its use to meet your organization's specific needs.

This first English version of the CATS CM methodology has been preceded by Dutch books on three earlier versions of the methodology. The methodology is continuously tested against interactions with contract management professionals in the field. In recent years, CATS CM has also been regularly tested based on the practical experiences of the authors as well as the professionals in related areas of expertise such as procurement, legal specializations, and auditing. This has also contributed to the further development of the methodology.

We believe that professional contract management will continue to develop and be further validated and structured into detailed best practices. We are proud that CATS CM – as a contract management application methodology – is playing a role in the development of these best practices.

Contracts give form and content to the collaboration between clients and suppliers. Wherever contracts are used, there is some form of contract management. Organizations that have not structured the management of those contracts can be sure of one thing: they will never get the most out of the intended added value of those contracts. Structuring contract management based on CATS CM can significantly improve this. It is also exactly why 'from working on contracts to contracts that work' is the subtitle of this fourth version of the methodology.

We have made an effort to use gender-neutral language in this book and, as we look at the field of contract management, we notice that the number of female contract managers is growing rapidly. The same is true for us, now that Linda Tonkes – who has been giving CATS CM training programs for many years and very successfully – has joined our ranks as a partner.

This book could not have been written without the support of several people who are close to us. They know that we thank them with all our hearts. Moreover, this book would have looked very different and would not have been so easy to read without the positive feedback and input of Arjen van Berkum and Richard Steketee.

We hope you will enjoy reading this book.

Linda Tonkes, Gert-Jan Vlasveld

June 2020

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Introduction

A constantly changing world

Change is nothing new. It is continuous and eternal. Technological and social changes rapidly follow one another, which is why revised policies and goals are coming out of corporate boardrooms at an increasingly faster pace. Even though long-term plans were commonplace in every sector when we published earlier versions of the CATS CM methodology, we now see that the strategy has changed from a comprehensive multi-year plan to a multi-year vision that focuses much more on the options for making additional and faster adjustments.

Nobody can and wants to do it alone

Responding adequately and timely to this fast-changing environment is crucial for the organization's operations and continuity. Moreover, in recent years both suppliers and clients have been involving more and more parties, resulting in new collaboration models to facilitate this. Both clients and suppliers have seen the number of contracts increase and/or have become part of complex contract chains. There is also an increasing awareness that an organization's overall contract portfolio has become an ecosystem rather than simply the sum of those contracts. As an ecosystem, the cohesive whole is aimed at delivering added value to the entire system. Consequently, the way the collaboration works towards a joint goal can be more important than the implementation of an objective linked to an individual contract. Creating value is a joint effort. Being open to external influences is essential for the proper functioning of the ecosystem. This requires flexibility and strong control measures on the overall contract portfolio within this ecosystem.

Changing times require different contractual relationships

The acceleration mentioned above also means that the relationship between client and supplier often needs to change as well. As the initial situation in which the contract was created remains the same for increasingly shorter periods, the need to allow for adjustments within the existing contract increases. This growing need for and frequency of change demands contracts that offer scope to do that. Moreover, the contract manager's input and expertise have only become more urgent during the phases before the finalized contract is signed, which is why this version of the CATS CM methodology describes the contract manager's role and involvement, in this pre-award phase, even more extensively.

Contract management has become a strategic necessity
Shareholders, legislators and supervising bodies all demand transparency. In public organizations, there is an ever-increasing call for a demonstrable structure of responsibilities. Besides, executive boards and directors in the public domain have gained a better understanding of the fact that entering into contracts can be a risky enterprise. Whereas financial risks used to be the main concern in contracts, today, aspects like continuity are increasingly often identified as a risk. In a society specialized to a large degree, outsourcing has become fundamental. The result of this specialization leads to contracts covering a much larger part of the process, while organizations no longer have the in-house expertise to adjust for any possible discrepancies. Suppliers almost always use contracts to structure their relationships with clients. Most of all, the rise of the customer-success function, which has an even more intense focus on delivery, indicates the increasing importance of the contract management function. The same applies to timely and adequate risk management. With the increased demand for transparency and responsibility, as well as the fact that timely and adequate contract risk management is quickly becoming more relevant, the importance of proactive contract management only grows, and is being added to the organizations' agendas on a strategic level.

In version 4 of the CATS CM methodology, which is significantly extended and offers many practical tools, we respond to the changes and issues in the market, for which we can draw upon our experiences with the many organizations that have allowed us to share our expertise on contract management in recent years.

PART I

A VISION ON PROACTIVE CONTRACT MANAGEMENT

■ INTRODUCTION

Companies are entering into a rapidly increasing number of contracts, driven in part by specializations and niche players in the market, as well as acceleration caused by technological developments. For quite some time now, the make-or-buy decision clients have to make is not being made based on an individual need that must be fulfilled. Ever more frequently, companies are choosing to make a strategic choice to 'buy'. Sometimes, this is even necessary because organizations no longer have in-house expertise in a broad range of areas.

It is not just the number of contracts that is increasing, but the form of collaboration is changing as well. Consequently, this increasingly results in the ecosystem described in the introduction to this book. That means that the relationship between client and supplier must be structured in a different way. As a result, this changed relationship requires contracts that are more flexible and more focused on value creation and the adjustment of contracts that do not yet offer that flexibility. Furthermore, contracts are increasingly contributing to the full implementation of processes. The effects of a possible discrepancy in the contract agreements increase and the response time to deal with them gets shorter. This is why contract management must become more proactive. Proactive contract management means: focused on activities linked to the execution and modification of a contract while concentrating on anticipating specific situations where possible or necessary.

Entrepreneurship is inextricably linked to having contracts. Contracting parties are increasingly aware that entering into contracts with due care is not sufficient to control the realization of the desired results, and it offers insufficient direction to the above-mentioned collaboration dynamics. This makes effective and efficient contract management crucial. The first chapter of this book explains what effective and efficient contract management entails and how CATS CM helps to achieve this. CATS stands for Contract Administration and Tracking Scenarios.

Our vision on proactive contract management is based on the idea of having effective and efficient contract management. Chapter 2 lists the most important definitions and explanations. Chapter 3 is a description of the determining factors for successful contract management and its implementation at a strategic, tactical and operational level. Last but not least, Chapter 4 describes the CATS contract life cycle, the role of contract management during those stages, and it delves deeper into the other processes that sustain this contract life cycle at an operational level.

1 Effective and efficient contract management

As soon as an organization enters into contracts, each one of those specific contracts requires specific actions. This is a form of contract management. So, it is not a question of whether or not organizations need to use contract management but how they can execute the already existing contract management more effectively and efficiently. Applying CATS CM results in effective and efficient contract management through optimizing realizing of the contract objectives, minimizing possible contract risks, achieving costs savings and avoiding unnecessary costs. This chapter explains the correlation between organizational goals and contract objectives, and the elements of effective and efficient contract management.

1.1 ORGANIZATIONAL GOALS AND CONTRACTS

Every organization has a mission and vision that determine its organizational goals. To realize those goals, the organization establishes a strategy that also takes laws and other regulations into account. Based on this strategy, the organization describes its goals for the short, medium and long term. When the organization enters into a contract with another party to realize its own organizational goals, these goals will also determine the contract objectives. The contract will describe how the objectives, for which the contract has been set up, are to be translated into performance. This performance can involve the delivery of both products and services. Figure 1.1 diagrams the relationship between organizational goals, contract objectives, and contract performance.

Every client uses suppliers, and therefore contracts, to carry out its activities to a lesser or greater extent, in order to realize its goals. Suppliers make choices when it comes to the products and services they offer and the markets in which they want to operate. Since the 1990s, the percentage of 'contributions from suppliers' relative to overall operations has been increasing significantly. Studies indicating that more than 70 percent of the total costs incurred by organizations can be attributed to the purchase or procurement of goods and services only confirm this. One of the main indicators that procurement has become even more important is the fact that Management Boards of both large and small organizations are choosing to appoint a Chief Procurement Officer (CPO), so that a solid embedding in the financial column is becoming the norm rather than the exception.

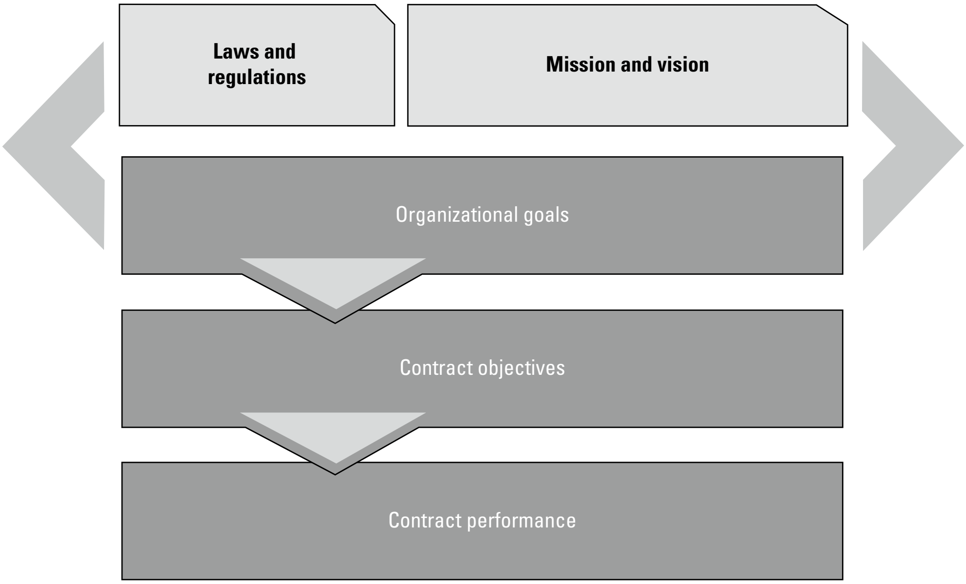

Figure 1.1 The relationship between organizational goals, contract objectives and contract performance

1.2 EFFECTIVENESS OF CONTRACT MANAGEMENT WITH CATS CM

As described above, contract objectives are derived from the organizational goals. Such a relationship can still be a perfect match at the time the contract is finalized, but this balance may shift over time. The organizational goals may change and, partly influenced by the rapidly changing environment, the way contracts are executed is also in constant flux. Relationships between contractual parties can change, the required technical solution may already have been outstripped by the market, and contracted volumes may no longer meet the need.

Effective contract management ensures that the contract realizes the intention, for the correct compensation, with acceptable risks, and with the efforts planned by the organization. Whenever an organization's needs change, effective contract management ensures that these changed needs lead to changes in the contract. The effects of good contract management contribute to achieving the contract objectives, the best possible relationship between contractual performance and contract value, as well as to savings and avoiding costs incurred by the organization in executing the contracts. The more contracts, and the more complex they are, the bigger the advantages of contract management.

1.2.1. Improved realization of contract objectives

The contract objectives describe what the organization wants to realize with the contract, and this applies to both purchaser and seller. Contract management following the CATS CM methodology is primarily focused on contract objectives and so it contributes substantially to achieving them. Sometimes, this contribution can be directly demonstrated in monetary terms, but there may also be a qualitative contribution.

A unique category of contract objectives are those related to compliance, meaning that the organization complies with laws and regulations. This is something every organization has to deal with. Even though there are many different areas in which laws and regulations are applied, there are some elements that apply to a broad range of laws and regulations to which good contract management contributes:

- Adequate documentation is very important.
- An organization is held responsible for structuring and implementing a quality system that guarantees compliance with laws and regulations.
- The compliance control measures carried out by the organization must be defined and their execution and conclusions must be visibly documented.
- Non-compliance has severe consequences (financial, reputation, continuity).

Considering these elements in advance, while the contract is being drafted, ensures that there is adequate focus on the completeness of the documentation, the control measures that must be implemented, and the assessment of these measures as soon as the contract comes into effect. This is even more applicable when some of the documentation or control measures have been outsourced as part of the contract.

Due to the abovementioned reasons, compliance officers and internal audit department staff are increasingly promoting contract management implementation.

1.2.2. Relationship between performance and contract value

The contract value is the sum of the client's budgeted expenditure based on the contract with the supplier. The contract value reflects the compensation for the deliverables. The supplier benefits from a higher compensation while a lower compensation is a financial advantage for the client. This might lead to the assumption that a supplier focuses exclusively on achieving the highest possible contract value and the client the lowest. However, things are not that simple. For suppliers who invoice their budgeted sales to the penny and achieve exactly the expected return, contract management does not seem to have gained them anything on paper. However, without proactive contract management, they might not have achieved the expected return. For the supplier, contract management can have a substantial impact in terms of client satisfaction, more efficient use of internal resources, or the opportunity to try new innovations.

A client who pays the agreed amount to the supplier while, at the same time receiving a modified service that still meets the changing user needs, does not save on expenses but