

Risky Contracts

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Many people view a contract like a suit of armour. It is there to protect you against uncertainty, and the thicker it is then the better you are protected! But relying on a strong contract for protection can lead to unexpected problems. Most of these problems arise from the structure of the contract, as we can see by comparing it with armour:

- A suit of armour is made from solid metal plates linked together to cover the vulnerable parts of the body. In the same way, a contract is made up of clauses, terms and conditions, and these are designed to address areas that are perceived as risky. There is a basic design for the suit of armour, always including the same major pieces (breastplate, helmet, gauntlets). Contracts also have standard clauses, sometimes described as “boilerplate terms”.
- Armour changed over time, with extra parts being added when new threats arose. For example later types of armour included the *gorget* to cover the throat, and *greaves* to protect the legs. Contracts also evolve, with additional standard terms being developed to address new types of risk.
- Eventually the suit of armour covered the whole body, and the person wearing it was completely protected. But it was also very heavy, weighing up to 50 kg (110 pounds). This made it hard for the wearer to move quickly to react to new threats. Some contracts are so complex that they hinder us from responding when things change.
- Despite all the heavy protection provided by a suit of armour, the wearer could still be hurt by a well-aimed blow that penetrated the joints. While most attacks would fail as they struck the major pieces of the suit, there were weak spots between the plates of armour. Our contracts can also contain weak spots, where important risks are not tackled by standard clauses, and something might slip through the gaps.

So how can we improve our contracts to provide better protection against uncertainty?

- Review “boilerplate” terms and conditions. Only include contract clauses that are directly relevant to the situation of the contract. Aim to reduce restrictive terms that hinder flexibility and the ability to respond to change.
- Do not rely only on standard contract clauses for protection. Identify gaps where unforeseen risks might get through. Then develop specific contract terms to cover those areas.

- Include specific risks explicitly in the contract. Perform a joint risk identification with all parties, and price each risk, considering both the risk impact and the cost of response. Decide on who can manage each risk most effectively, and record this in the contract. Where the buyer carries a risk, the contract price can be reduced. If the supplier takes responsibility for a risk, then the cost of that risk should be added to the contract price.

Finally, if we think of the contract as a protective suit of armour, there is a danger that we view our contractual partners as “the enemy”. The contract does not exist only to protect the buyer. It is there to provide protection for all contracting parties against the effects of uncertainty. Instead of seeing the contract as defending “me” against “you”, we need to recognise that it offers a way for “us” to tackle risk effectively – together.

We must not be like the medieval knight who believed that his suit of armour offered complete protection, only to find himself defeated in battle by a fast-moving opponent who found gaps in his armour. Let’s be sure that our contracts are fit for purpose, covering our vulnerable areas, addressing risk effectively, and giving us the best possible chance of performing the contract successfully.

To provide feedback on this Briefing Note, or for more details on how to develop effective risk management, [contact the Risk Doctor \(info@risk-doctor.com\)](mailto:info@risk-doctor.com), or [visit the Risk Doctor website \(www.risk-doctor.com\)](http://www.risk-doctor.com).

About the Author



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Dr David Hillson CMgr FRSA FIRM FCMI HonFAPM PMI-Fellow is The Risk Doctor (www.risk-doctor.com). As an international risk consultant, David is recognised as a leading thinker and expert practitioner in risk management. He consults, writes and speaks widely on the topic and he has made several innovative contributions to the field. David's motto is "Understand profoundly so you can explain simply", ensuring that his work represents both sound thinking and practical application.

David Hillson has over 25 years' experience in risk consulting and he has worked in more than 40 countries, providing support to clients in every major industry sector, including construction, mining, telecommunications, pharmaceutical, financial services, transport, fast-moving consumer goods, energy, IT, defence and government. David's input includes strategic direction to organisations facing major risk challenges, as well as tactical advice on achieving value and competitive advantage from effectively managing risk.

David's contributions to the risk discipline over many years have been recognised by a range of awards, including "Risk Personality of the Year" in 2010-11. He received both the PMI Fellow award and the PMI Distinguished Contribution Award from the Project Management Institute (PMI®) for his work in developing risk management. He is also an Honorary Fellow of the UK Association for Project Management (APM), where he has actively led risk developments for nearly 20 years. David Hillson is an active Fellow of the Institute of Risk Management (IRM), and he was elected a Fellow of the Royal Society of Arts (RSA) to contribute to its Risk Commission. He is also a Chartered Fellow of the Chartered Management Institute (CMI) and a Member of the Institute of Directors (IOD).

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