



COVID-19 QUICK HELP GUIDE

## CONTRACTS & SUPPLY CHAIN

Practical steps to help  
navigate the COVID-19 crisis

IDEAS | PEOPLE | TRUST



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# CONTRACTS & SUPPLY CHAIN

## Helping you respond to the evolving COVID-19 crisis

### Background (as at 7th April 2020)

- ▶ The COVID-19 crisis has engulfed us all at an alarming rate - not least the way it has escalated over the last three weeks here in the UK
- ▶ An IACCM survey issued on the 6th March found that only 7% of respondents said COVID-19 was having a severe impact on suppliers and/or their ability to perform their customer contract obligations - by 19th March this had risen to 14%, with a further 45% reporting moderate disruption and over 60% are reviewing contractual T&Cs. By the time you read this, these percentages will have undoubtedly increased → **this is driving greater reliance on robust, continuous contract management with a spike in emergency renegotiations which companies must be prepared for**
- ▶ For a long time, thought leadership focused on supply chain issues resulting from relationships with suppliers based in China. Suddenly, companies are trying to understand the new reality that this is no longer an issue of supply chain disruption in a particular geography, but a fundamental question of whether your business obligations are actually now deliverable - impacting both key customers and supplier contracts
- ▶ The real risk is that this descends into legal/adversarial conflict at a time where society is looking to business to do all it can to sustain production and restore economic stability
- ▶ There is an unprecedented opportunity for players across the value chain to open-up and collaborate, adapting to the ever-changing environment, keep businesses going and preserve the supply chain as much as possible for when we emerge the other side

### Purpose of this document

- ▶ **This guide is intended to support quick, practical actions for organisations to help establish what this crisis means for them (focusing on customer and supplier contracts), what their exposures are and inform critical decision-making over the days and weeks ahead**
- ▶ As the crisis develops, your priorities and focus will evolve. We will issue updated guidance as the situation progresses, based upon what we are hearing from our clients and wider industry

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# CUSTOMER CONTRACTS

## What we are seeing and key actions

Many organisations are scrambling to understand what the latest COVID-19 developments mean for their business - a significant proportion will be seriously concerned for their survival. **Decisions made now will have profound knock-on effects, so it is vital they are taken with the best, most relevant information available.** This guide focuses on high-priority issues relating to customer and supplier contract portfolios. It is intended to be a practical guide (not an exhaustive framework) to help businesses rapidly establish their position and act quickly with their third parties to preserve output as far as possible.

### Critical activities

1. Rank and prioritise key customer contracts
2. Establish your exposure in these agreements
3. Open communication channels to understand changing customer demands and requirements
4. Prepare for emergency re-negotiations

### 1. Rank and prioritise key customer contracts

Focus on business-critical customers initially (do not neglect the others):

- ▶ Who are our key customers?
  - List out customers by size, profitability using available data (e.g. CRM, AR reports, financial performance reporting)
  - Prioritise customers and assign teams to action
    - Review of your contractual obligations
    - Understand outstanding payments and agree cash collection approach
    - Identify communication channels and stakeholder engagement plan
    - Link delivery to your supplier contracts and feed in known supply chain issues/risks (refer to Supplier Contracts section below)
    - Prepare negotiation plan should your ability to deliver obligations fall short and/or where your cost base materially changes

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# CUSTOMER CONTRACTS

## Key actions

### 2. Establish your exposure

Understand contractual obligations and provisions across key contracts:

- ▶ Establish your major delivery obligations
- ▶ Identify what obligations are at risk
- ▶ Set out penalties for non-delivery
- ▶ Force Majeure / frustration clauses
  - What do your contracts say and is there alignment across customer and supplier agreements?
  - What claims may be put forward? For whole contract or particular elements of the goods/services delivered?
  - What are the implications - deferral, adjustment or termination?
  - What provisions are there for the recovery of costs?
- ▶ Termination rights on both sides (and associated penalties)
- ▶ Link delivery to your supply chain
  - What additional considerations/risks are there for your customer contracts based on emerging supplier issues?
  - Discuss emerging issues and needs with Procurement teams to support their alternative supply/supply chain management activities

### 3. Open communication channels

Understanding your contractual requirements is vital, but good communications and trusted relationships will help avoid adversarial discussions from the outset.

- ▶ Open up free-flowing discussions with decision-makers at key customers:
  - Understand how COVID-19 is affecting their business
  - Determine whether your services are business critical to them to feed into your negotiation approach
  - If you anticipate issues in delivering contractual obligations, communicate these early and work with them to understand what elements are of most importance to them
  - Discuss how delivery methods and timing of delivery can flex to optimize what is possible in the near term
- ▶ Not all customers will be collaborative, some will take a more adversarial stance, however:
  - Be empathetic, demonstrate willingness to help everyone get to a good outcome - we are all in the same boat
  - Know your own position (see negotiation section)
  - Take the opportunity to build further trust between parties with a view of the longer term

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# CUSTOMER CONTRACTS

## Key actions

### 4. Prepare for emergency renegotiations

Businesses are seeing an increase in negotiated changes with customers and suppliers alike as everyone adapts to the emerging situation.

Those who are prepared and fully understand their own position and the negotiating levers available to them will realise the benefit.



Get a structured negotiating plan in place:

- ▶ Identify how to build trust, empathy and collaboration with key stakeholders
- ▶ Know your contractual position
- ▶ Feed in your known exposures
  - What is deliverable and what is not?
  - Supply chain constraints/capabilities
- ▶ Set out your customer's likely negotiating position in terms of:
  - Ongoing service requirements
  - Commercial
- ▶ Work out commercial parameters
  - What are your cost drivers?
  - How will service changes impact profitability and cash flow?
  - What are you prepared to change?
  - What impact will termination, delay, deferral, force majeure etc. have on your business?
- ▶ Be ready to agree and embed Emergency Performance Indicators to temporarily replace KPIs
- ▶ Be prepared to move towards adaptive contracting - providing a framework for customers and suppliers to be flexible in the evolving environment

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# SUPPLIER CONTRACTS

## What we are seeing and key actions

Actions to assess the supply chain and the impact on your business must be taken hand-in-hand with ongoing business continuity as well as key customer contract management. According to the latest IACCM survey (as at 19th March 2020):

- ▶ 59% of businesses are experiencing either moderate or severe disruption to supply chains and their ability to deliver customer contracts
- ▶ 61% are reviewing T&Cs across their contract portfolios
- ▶ 26% are already exploring near-shore/domestic alternatives
- ▶ 19% are working to reduce their exposure in low-cost markets
- ▶ 17% are considering in-sourcing options

Procurement, Supply Chain and Contract Management teams are under significant strain to gather the right information quickly, to enable better decision-making under the circumstances. This guide is by no means exhaustive, but can be used to help drive a rapid response in the short term.

### Critical activities

- ▶ Identify high priority supply chain requirements
- ▶ Review requirements against known supply chain constraints & analyse financial resilience of key suppliers
- ▶ Assess emerging supply chain risk profile - in key markets, territories and existing suppliers and consider alternative supply options
- ▶ For existing key suppliers, set-out contractual levers available to manage fluctuations in demand and any recourse for non-delivery to your customers up-chain
- ▶ Engage key supplier stakeholders to understand changing supplier capacity and capabilities - evaluate what is at risk
- ▶ Plan emergency re-negotiations with existing suppliers and negotiations with new suppliers (where relevant)
- ▶ Tailor contract management approach to the new environment

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# SUPPLIER CONTRACTS

## Key actions

### 1. Identify high priority supply chain requirements

Determine your business critical supply requirements relating to:

- ▶ Your general business operations
- ▶ Delivering against your customer obligations

Rank requirements to focus on high-priority supply considerations in order

### 2. Review requirements against known supply chain constraints

Map your supply requirements against the current status of your supply chain

- ▶ Identify what supply is at risk through discussions with supplier
- ▶ Analyse key supplier resilience including:
  - Financial indicators throughout the corporate family structure
  - Contractual clauses including step-in rights and any parent company guarantees
  - Intelligence gathering: sector, geopolitical, company specific issues, past behaviours etc.

### 3. Assess emerging supply chain risk profile

Review Tier 1 (and if possible Tier 2) profile to identify risk areas including:

- ▶ Consolidation risk by limiting supply to a small pool of suppliers
- ▶ Market/geographic risk of supply (how those territories are impacted and what restrictions on delivery will affect your operations)
- ▶ Known single points of vulnerability - scarcity of parts/resources; shipment risk etc.
- ▶ Which suppliers have known issues/high risk of service non-delivery (note previous step)?
- ▶ Keep an eye on long term supply chain strategy (what will the future supply chain model look like? How do we want to be perceived by the market and what impact will that have on our immediate response?)

Consider alternative sources of supply where the above identifies unacceptable risk

### 4. Set out contractual position/options on existing supplier agreements

Starting with key supplier contracts:

- ▶ Identify force majeure provisions and the potential impact on continuity and extent of supply. Map these to major customer obligations
- ▶ What options are there for the deferral, adjustment or termination of contracts?
- ▶ What mechanisms are there to address increases/decreases in costs resulting from such variations?

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# SUPPLIER CONTRACTS

## Key actions

### 5. Open communication channels

Engage decision-makers at key suppliers:

- ▶ Evaluate the impact of the crisis on their operations
- ▶ Seek representations from suppliers on their ability to deliver; work with them to identify what is possible under the current circumstances
- ▶ Understand their own supply chain profile and any known or perceived risks impacting their ability to provide goods/services as contracted

Supplier discussions must be coordinated with customer management activities set out above

### 6. Plan emergency negotiations with existing and/or new suppliers

Your negotiation plans for suppliers broadly need to reflect your key customer negotiation approach, as repetitions with the customer section above illustrate. Following a standardised approach will support decision-making that mirrors changes in customer demands and your supply chain capabilities:

Set out your negotiating approach:

- ▶ Identify how to build trust, empathy and collaboration with key supplier stakeholders

- ▶ Know your contractual position, where an agreement is in place
- ▶ Feed in your known requirements
  - What is essential and what can be deferred or changed?
  - Business-critical customer obligations
- ▶ Set out your supplier's likely negotiating position in terms of:
  - Your ongoing supply needs
  - Commercial
- ▶ Establish your commercial negotiating position
  - What are the cost drivers?
  - How will supply changes impact your profitability and cash flow?
  - What are your red lines and what changes can you accept?
  - What impact will termination, delay, deferral, force majeure etc. have on your business?
- ▶ Be ready to agree and embed Emergency Performance Indicators to temporarily replace KPIs
- ▶ Be open to adaptive contracting to facilitate cooperation and flexibility. This will better enable you to manage situational developments across both customers and suppliers

# SUPPLIER CONTRACTS

## Key actions

### 7. Tailor contract management approach

A new, flexible way of working with suppliers will require a contract management approach to match. Revisit your supplier and contract management functions in, but not limited to, the following areas:

- ▶ Increase dialogue with key suppliers
  - Understand how the evolving situation is impacting them
  - Identify any areas of the contract/agreement that will require adaptation, should circumstances deteriorate or improve
  - Implement collaborative, no-surprises relationship management
  - Make best use of available technology - avoid management via email
- ▶ Capture variances to the contract formally
  - Adaptive contracting requires sufficient sign off and audit trail so all parties keep track of the evolving nature of the relationship
  - Emergency Performance Indicators are likely to temporarily replace KPIs where delivery against original obligations is unachievable and force majeure claims are unavailable/avoided
- ▶ Link supplier contract management activity to customer management
  - Changes within both the supply chain and customer portfolios will require close monitoring and coordination across the two groups to facilitate your ability to adapt

- ▶ Keep a close eye on your commercial position overall
  - Know your cost drivers and levers impacting profitability and cash flow across both customer and supplier contracts
  - Be ready to make informed, quick decisions to adapt contracts/change the nature of agreements that are based upon sound understanding of the likely commercial implications



This guide is intended to act as a practical guide support organisations as they respond to the COVID-19 crisis. We will be issuing further guidance as the situation evolves. If, however, you would benefit from a further discussion please contact:

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