

Risk Research Bulletin

Improving Contracting on Campus

A Layperson's Guide to Understanding Contract Basics

Every year colleges and universities, through their administrators, faculty, and staff, enter into thousands of contracts for a variety of activities, including outside services and supplies, facilities use, construction, copyright, and research. Despite the prevalence of contracts on campus, many institutions have not educated staff or established a policy to guide employees responsible for contracting. The failure to understand contracts or a campus contracting policy can result in unexpected and sometimes serious liability for educational institutions and employees involved in a contracting process.

United Educators studied more than 2,000 pending claims related to contracting to identify the most preventable. Hundreds of these claims involved weak contracting practices, such as:

- Relying on an oral agreement when a written contract would have memorialized and clarified each party's rights and obligations

- Behaving in a way that implies a contract when none exists
- Using a written agreement that lacks detail or includes ambiguous terms
- Entering into an agreement that cannot be performed, or is onerous to perform, as written
- Signing a vendor's form contract that would put the institution at a disadvantage if a problem were to occur

Colleges and universities may avoid problems like these by helping staff gain an understanding of contracts and by reviewing their contracting practices to ensure sound processes are in place.

Understanding Contract Basics

What Is a Contract?

A contract is an exchange of promises that the law will enforce. To create a legally enforceable contract, a promise must be given in exchange for consideration. Consideration is a promise to give something of value, such as a monetary payment, goods, or services. For example:

- ✎ If the Rock Paper Scissors Company promises to provide XYZ University with 1,000 cases of paper, and in exchange XYZ promises to pay \$20,000 to Rock Paper Scissors, the two parties have created a contract. Each party's promise is given in exchange for consideration or something of value from the other party (\$20,000 in exchange for 1,000 cases of paper).

The document that reflects a contract can take different forms and be referred to by different terms. For example, a letter of agreement, a memorandum of understanding, a purchase order, and even an email can be a contract if it reflects the parties' mutual assent to exchange promises.

Does a Contract Have to Be in Writing?

Not always. To many people the word contract connotes a document with lots of fine print, but that is only one type of contract—a written contract. A written document is not always necessary to create a contractual relationship. A “handshake deal” can also be enforceable. Courts have enforced contracts based on an oral exchange of promises or have recognized implied contracts from the behavior of the parties. The key to determining whether parties have formed an oral or implied contract depends upon whether they can demonstrate a promise given in exchange for consideration.



An Exchange of Oral Promises

Consider the following example that highlights the problems involved with an oral contract and an implied contract:

Bernie Bridges, a representative of ABC College, tells the owner of Tip Top Trim, a local landscaping company, that the college will acquire property on Jan. 1 that will expand its campus by one-third. During this discussion, Bridges promises to pay Tip Top Trim one-third more for its services starting Jan. 1, and in exchange Tip Top Trim promises to perform the landscaping services for the entire campus through the end of the academic year.

On Dec. 22, Bridges is fired, and his replacement, unaware of the oral contract with Tip Top Trim, retains Over the Hedge to provide the landscaping services for the new portion of the campus. Tip Top Trim sues the college for breach of contract. The college refutes the existence of any contract, but Tip Top Trim produces statements from its owner and Bridges that confirm the oral agreement. The college has nothing to contradict Tip Top Trim's evidence.

Conclusion

Tip Top Trim has a good chance of proving it had formed an oral contract with the college based upon the promises exchanged by the owner and Bernie Bridges, the prior representative of the college.



Behavior That Implies a Contract

Consider the following example that highlights the problems involved with an oral contract and an implied contract:

For the last 10 years, ABC College has had a handshake deal with Tip Top Trim to provide landscaping services for the entire campus. The college's director of buildings and grounds tells Tip Top Trim's owner that the institution will be expanding its campus by nearly a third in the coming year.

Tip Top Trim hires new employees, purchases additional equipment, and after the campus expansion, provides landscaping services for the new sections of the campus. For nearly a year, the college continues to pay Tip Top Trim its original fee and does not increase its payments. Tip Top Trim sues the college for breach of contract and seeks payment for the additional services provided.

The company also seeks recovery of the costs required to hire employees and purchase equipment to service the entire campus in the event the college does not continue to retain Tip Top Trim's services.

Conclusion

Here, a court may determine that the college and Tip Top Trim had an implied contract. In trying to reach a fair result, a court can infer the existence of a contract from the parties' behavior. In doing so, it would consider the college's history of retaining the company without a written contract, the actions the company took in anticipation of the increased campus size, and the college's acceptance of Tip Top Trim's performance of landscaping services for the new portion of campus.

Although neither arrangement between the college and Tip Top Trim involves

a written exchange of promises, the college may be obligated as if a written contract exists. Also, because neither an oral nor an implied contract involves a written document, the specific terms are vulnerable to the subjective and often faded memories of the representatives who negotiate these contracts. If the representative has left the institution, those recollections would be even more tenuous and might be lost forever. Because the college has no record of these contractual agreements, it cannot point to a writing that clarifies or refutes another party's claims about the terms of the exchanged promises. Had the college required a written contract, the college's disputes with Tip Top Trim might have been avoided.

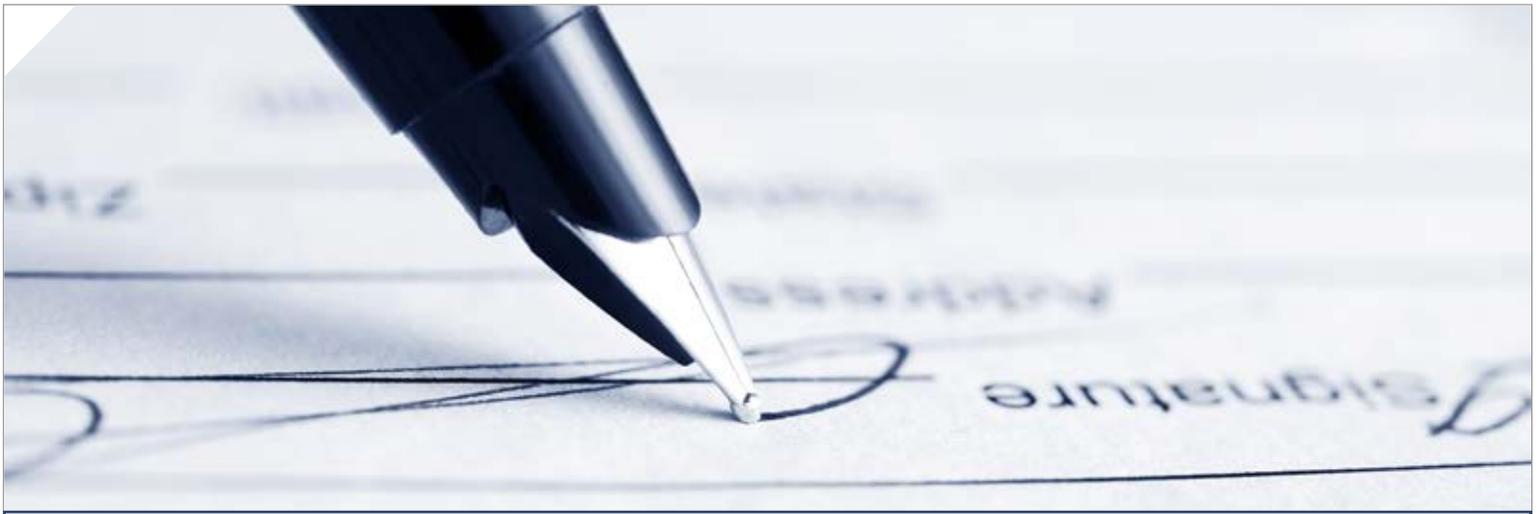
Is a Written Contract Preferable?

There's wisdom in the adage, "Get it in writing." A written contract has many advantages. It:

- Formalizes the promises exchanged between parties
- Details terms affecting the performance of each promise, such as start and end dates and payment schedules
- Ensures that each party understands what it is required to do under the contract
- Details each party's rights in the event one of them fails to perform, prematurely terminates, or otherwise breaches the contract
- Provides tangible proof of the parties' agreement

Because a well-drafted written contract provides clear guidance on all aspects of the parties' agreement, it can reduce and sometimes eliminate the need for parties to dispute or litigate the contract.

An informal handshake deal may seem less complicated and more trusting than a written contract. However, if a dispute arises between parties, that handshake will not provide any guidance on the exchanged promises or the rights and obligations of each party. A well-worded written contract saves an institution time, energy, and money that will be required to resolve misunderstandings about the terms or even the existence of a contract. When possible, an institution should strive to commit contractual agreements to writing.



Will a Written Contract Guarantee That There Will Be No Contract Disputes?

A dissatisfied party can always challenge the terms of a written contract. However, a well-drafted contract that accurately reflects the promises, rights, and obligations of each party provides the parties and, if necessary, a court with a road map for resolving these challenges.

When an institution enters into a poorly written contract, problems can ensue. Common problems with written contracts are that they lack detail, omit important terms, are ambiguous, or cannot be performed as written. These problems are compounded when the institutional representative does not review the contract before signing it, reviews the contract but does not fully understand its terms, or reviews and ignores questionable terms because of the perceived benefits the contract will bestow upon the institution.

Consider the following example. Professor Oscar Optimistic and Learning Adventures Inc., a well-reputed, national organization focused on outdoor leadership training, have been talking

about a joint venture by which the university would establish a leadership program and the company would provide the outdoor training component to enrolled students. Learning Adventures is interested in gaining exposure to a wider audience of trainees who can then promote the training to others. Optimistic and the university believe the program will successfully attract future leaders as students to the university and improve its reputation.

Adventure Learning presents the professor with a contract that requires the university to enroll a minimum of 150 students in the program annually. The contract provides that failing to meet this requirement will result in a \$15,000 penalty and the contract's termination. While initially concerned about the penalty, Optimistic quickly concludes that the positive appeal of the leadership program is likely to attract a large number of students and signs the contract. In the first year of the program, only 75 students enroll.

Learning Adventures terminates the contract and demands the \$15,000 penalty. The professor is shocked that the company would take this action. Optimistic claims, on behalf of the university, that he employed all reasonable efforts to meet the contract's enrollment minimum and refuses to pay the penalty.

Conclusion

In this case, Optimistic did not seriously consider how to best protect the university if the contract could not be performed. Rather, he placed undue emphasis on the likelihood that Learning Adventures' strong track record would attract students and improve the reputation of the university. To avoid entering into a contract that contains unfavorable terms, the institution's representative must ensure that the contract language conforms with prior discussions, ask about the terms that disadvantage the institution, and seek the assistance of legal counsel when the contract is difficult to understand or appears unfair.

Who Should Sign a Contract on Behalf of the Institution?

Generally, a written contract is not effective until the parties sign it. A signature indicates that the signing party agrees to and is bound by the contract's terms. When confronted with a contract dispute, courts routinely examine a contract for signatures and generally regard a party's signature as proof that the party understands and agrees to its terms even if the party did not actually read, understand, or fully agree with it.

As an entity, an educational institution cannot itself sign the contract. Rather, institutions are bound to written contracts when they are signed by an individual who has been authorized to act on its behalf. Typically, high-level administrators have that authorization. To increase the ease of doing business with outside contractors, top decision makers can also delegate that authority. Given the importance of this responsibility,



colleges and universities must balance the need to ensure that contracts receive the appropriate level of review against the need to be able to transact business in a timely and flexible manner. After carefully balancing these interests, each institution then needs to clearly identify those positions on campus authorized to sign contracts.



What If an Employee Signs a Contract Without Authority?

The results of an unauthorized signature on an agreement can have unfavorable consequences for both the institution and the signer.

Only those employees "with authority" should sign an institution's contracts. However, if an employee signs a contract without authority, in many instances the institution still will be bound to perform the agreement. If the other contracting party reasonably believes that the employee has authority to sign or enter into the contract, the employee's "apparent authority" will bind the institution. Consider the following:

After serving as an outside computer consultant, Charlie Cheatum was hired by the university to coordinate the updating of the university's computer system. In his new

role, Cheatum did not have authority to sign contracts. Nonetheless, he signed a contract that obligated the institution to purchase computer equipment from Farmer and the Dell Computers for a total cost of \$75,000. Cheatum regularly made similar purchases from Farmer and the Dell when he was an outside consultant for the university. The university has not issued a policy or any communication informing vendors, suppliers, and service providers such as the computer company that Cheatum was not authorized to sign the contract.

Conclusion

The college could be required to accept and pay for the computers if it was reasonable for Farmer and the Dell Computers to believe that Cheatum

had authority to sign the agreement. A contracting policy that is well publicized and clearly identifies those positions on campus authorized to sign contracts is one way to provide important information to potential contractors.

Even though a court may require the university to perform the contract, unauthorized signers act at their own peril. For example: Institutions can view employees' unauthorized actions as taken outside the scope of their job responsibilities and may even be able to hold employees personally liable. To provide clear guidance, an institution's contracting policy can address who has authority to sign agreements and the consequences for signing contracts without authority.

Improving Contracting Practices on Campus

Colleges and universities can take the following steps to improve contracting practices and reduce the likelihood of contract-related problems.

Establish a Contracting Policy

A policy that requires written contracts is of paramount importance to improving the contracting processes. The policy should also include a consistent practice of contract review and signing by authorized employees only.

Perform Contract Reviews

Campus policies typically require that every contract to which the institution is a party receive an appropriate level of review before it is signed. The employee who negotiates the contract may be the best person to perform the review because he or she can evaluate the accuracy of the promises contained in the contract. A contract review may also be reserved for higher level officials depending on the contract value or the type of business relationship that is contemplated. At the same time, it is important to understand that contracts involving small sums of money can present a large liability exposure for the institution. An institution may want to establish other criteria to trigger a heightened review of a contract. For example, an institution may require legal counsel to review all contracts that are nonroutine, extend over one year, or involve substantial complexity or liability exposure.

Many institutions find it helpful to use a checklist with a step-by-step guide for reviewing contracts. This can be particularly useful when two or more employees are responsible for reviewing and signing a contract. The completed checklist details the steps that the contract reviewer undertook before it goes to the authorized people for signing. The guidance provided by a campus contracting policy or a contract review checklist or both can ensure that agreements are reviewed by the most appropriate individuals before the institution agrees to them.

Establish Who Has Authority to Sign Contracts

Colleges and universities take different approaches when conferring contract signing authority upon employees. Institutions that want to promote a centralized approach will limit signature authority to a few people on campus, such as trustees, officers, or deans. However, that limitation can delay the signing process until after the small circle of signers completes other work priorities. To increase the speed of the contracting process and ease of doing business, institutions can expand the signing authority to a broader range of employees, including department heads and other lower level administrators, such as managers, directors, and supervisors. Institutions that employ the less-centralized approach may want to establish a tier of signers based on the contract's monetary value. For example, a policy could provide that supervisors can sign contracts involving an amount less than \$2,000, department heads can sign contracts up to \$5,000, and a trustee or officer must sign contracts involving amounts over \$5,000.

Develop Model Forms for Routine Contracts

Consider working with local or in-house counsel to develop form or model agreements for those types of contracts that are most common on your campus and then require the use of those forms. Examples of contracts for which educational institutions often develop forms include purchase orders, facilities use agreements, professional services or consulting contracts, and simple copyright licenses.

To increase the speed of the contracting process and ease of doing business, institutions can expand the signing authority to a broader range of employees, including department heads and other lower level administrators, such as managers, directors, and supervisors.



Create a Central Repository for Contracts

Institutions can manage their contractual commitments by developing a central repository for all agreements. Depending upon its size and the number of contracts, an institution could establish a single, central repository or a system of repositories broken down by college or department. Also, many institutions use contract management software to create and maintain a repository so that the institution can effectively track and monitor the performance, expiration, and renewal terms of its contracts. These programs can also house the contract document as well as related items, such as documents referenced in the contract, side agreements, and information about the employees who are responsible for a particular contract.

Depending on the number of pending contracts, some institutions find it useful to appoint a contract manager to oversee the repository and take responsibility for monitoring contract implementation. The manager can keep a watchful eye on both the institution's and the outside vendors' compliance with their respective obligations under the contract.

Educate Representatives About Contracts and Campus Policy

Educating institutional representatives involved in the contracting process about basic contract principles and the institution's policy is key to reducing contract-related claims. Many employees are intimidated by contracts and think, "I'm not a lawyer so I can't be expected to read or understand the language in a contract." Yet these employees often are the most knowledgeable about the contract's subject matter and core promises. Moreover, contracts are interpreted based on the plain meaning of the language used to describe the exchanged promises, rights, and obligations of each party. If institutions can demystify basic contracts for employees who negotiate, review, and sign contracts, and inform them about the guidance contained in the campus contracting policy, the quality of contracting process is likely to improve.

Ideally, institutional representatives who are closer to and better understand a contract's subject matter can supplement any specialized review performed by legal counsel or other experts. To educate employees on campus contracting, institutions can use online or in-person training, create a contracts section on the institution's website, or write and distribute articles outlining critical information for employees to understand about contracts and the campus policy.

A Final Word

Many claims and unexpected liabilities are avoidable through clear campus contracting policies and procedures. An institution that takes the time to implement good contracting practices is more likely to be bound to written contracts that have been reviewed for favorable language and the less likely to face contractual problems.



EduRisk™ provides education-specific risk management resources to colleges and schools, and is a benefit of membership with United Educators (UE) Insurance. As a member-owned company, UE is committed to helping educational institutions by offering stable pricing, targeted insurance coverage, extensive risk management resources, and exceptional claims handling.

To learn more, please visit www.UE.org.

Copyright © 2015 by United Educators Insurance, a Reciprocal Risk Retention Group. All rights reserved.

Contents of this document are for members of United Educators only. Permission to post this document electronically or to reprint must be obtained from United Educators.

UE-113162 12/15