

# Integrated Contract Governance for Sustainable Supplier Performance: A Literature Review and Future Research Agenda

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## Abstract

Effective contract governance mechanisms are crucial for developing and sustaining meaningful partnerships between customers and suppliers. While the literature has extensively studied supplier partnerships, it has not provided enough coverage regarding contract governance and agency theory. However, understanding agency theory in detail could shed light on why certain partnerships fail and others succeed, and provide a better understanding of contract governance. The economic costs associated with transactions have a significant impact on contract governance, and a thorough understanding of this theory will help identify opportunities to make more informed decisions about the type of contract governance required for asset-specific or non-contractible investment. The theoretical framework for institutional and organizational analysis of contractual governance suggests studying institutional and organizational structures in detail that impact contract governance. This framework emphasizes transaction costs, which are influenced by factors such as legal systems, cultural norms, trust monitoring mechanisms, asymmetries in power, opportunism, uncertainty, and its impact on contractual relationships. To build the best contractual governance and relationships, suggested research includes market-based governance, hybrid governance, and network governance. In the context of supply chain contracts, research recommends considering context-specific factors when selecting between output-based and behaviour-based contracts. For example, output-based contracts are effective when the supplier has more control over the production process and there is less uncertainty in the market, whereas behaviour-based contracts are best when the supplier has less control over the production process and there is greater uncertainty in the market. All these observations identify gaps that call for a detailed study of the identification of contract governance mechanisms for the ITES industry and the design of a governance mechanism that is effective and yet sustainable.

**Keywords:** Behaviour-based contract, Output-based contract, Conflict, Legal enforceability, Unilateral government support, Institution theory, transaction cost theory

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## INTRODUCTION

India is the world's largest outsourcing destination for IT and ITES services, with the industry contributing 8% to the country's GDP in 2021. The National Association of Software and Service Companies (NASSCOM) says that the Indian IT industry is likely to make \$227 billion in the financial year 2022, which is more than the \$196 billion it made in the previous financial year, 2021. Due to its dominance in the universal offshore ITES market, Despite the benefits of outsourcing, organizations face significant challenges while executing outsourcing contracts, such as revenue leakage, regulatory compliance, information security risks, business performance defaults, lack of trust, and effective communication between the two parties. Such challenges often lead to cancellations and disputes of multi-million-dollar revenue outsourcing contracts. Global outsourcing contracts bind the entire revenue, risk, and business outcomes to be delivered by the service providers to the customers. As a result, companies spend between 2% to 3% of the contract value to ensure vendor management teams are established to monitor and control contract execution. In an organization while the focus to achieve reducing risk remains, managing vendor contracts means creating, signing, and studying contracts to make sure a business runs well and makes the most money possible.

### Conceptual background of the review

Output-based contracts v/s behaviour-based contracts According to (Bai et al., 2015) study identifies how different ways of managing contracts, either by focusing on the results or on how people behave, can affect conflicts between buyers and suppliers in a supply chain. In an alternative scenario, we observe a contrasting dynamic where the effectiveness of output-based contracts exhibits a negative correlation with buyer-supplier conflict. Conversely, contracts based on behaviour demonstrate a positive association with mitigating buyer-supplier conflict. The contractual impact was influenced by two key institutional factors:

the legal accomplishment of the agreement and one-way support provided by the government. The examination of hypotheses involved employing hierarchical moderated regression analysis

Exploring how contractual governance practices influence supplier performance yields: A study on how state-owned companies in Uganda handle contracts and buying things found that there is a good connection between how well they manage contracts and procurement performance. The relationship is positive and strong, with a value of  $r=0.653$ . The research showed that for every small positive improvement of 1%, there was almost a 60% improvement in the prediction of procurement performance in state-owned companies. In simpler terms, better contract management was linked to an increase in how well these companies performed in procurement. Furthermore, the performance associated with procurement demonstrated a positive correlation with contract objectives, contracting capabilities, and operational procedures. State-owned companies that follow good contract processes tend to do better in their procurement activities, and the opposite is true as well, as mentioned by Masaba et al., (2015).

Supplier Performance and Governance Structure: (Basheka et al., 2013), This sentence is about how the way public purchasing is managed affects governance structures was analysed along with values, processes, and mechanisms to determine administrative efficiency in Uganda's public sector, the discoveries find relevance in diverse political contexts. The findings showed that good management of public purchasing was likely to lead to a 45% improvement in administrative efficiency. This is a significant percentage, especially when comparing it to the various tasks performed by public organizations.

#### **Contract Management Teams and Supplier Performance**

A study by Shiwa et al., (2014), a brief mention of oil and gas companies in Tanzania, established that contract management teams indeed had a relationship that was directly related to HSE (health, safety and environment) performance; on average an increased unit of contract management team had a 0.5-unit increase in health, safety and environment performance. Basheka et al., (2013), observed that among the pivotal determinants of effective contract management are precise clarity of roles and diverse contract management understanding of the contract management team. Kingoo et al., (2013) indicated the need to have skilled and competent contract management group assigned to oversee the contractor's work. Shiwa et al., 2014 additionally confirmed that the strength of a statement of work (SOW) is weak or robust based on the expertise, proficiency, and understanding of the contract manager. Despite the aforementioned, Basheka et al. (2013), observed contract management as the company's ability to supervise the contractor's work is influenced by having skilled employees, good people, and an effective management system, (Kemunto et al., 2014). yet, disagreed on the necessity for hiring and keeping contract management staff with better skills, experience, and qualifications and supervising the contractor's work. A Combination of methods was well-suited for a mixed-methods approach as it involved using qualitative data to complement quantitative data, thereby gaining more profound insights into the research. On average, participants concurred that their contracts align with their organization's objectives (mean=3.95, SD=0.97). The objectives of the contracts aim for the highest quality of goods and services, and this information is conveyed to suppliers (mean=3.67, SD=1.01). Additionally, there is an emphasis on exercising due diligence in drafting procurement contracts to align with these goals (mean=3.96, SD=0.90). The research also found that, on average, participants agreed that they only initiate contracts for specific amounts of money. Furthermore, their contract specifications allow them to track the entire contract process (mean=4.27, SD=0.94), They made sure to reach an agreement on contract specifications with the supplier before finalizing the contract (mean=3.95, SD=0.84). Furthermore, the study found that by reaching consensus on contract specifications with their suppliers, the respondents have successfully averted legal issues, as evidenced by a mean of 3.71 and a standard deviation of 0.94. Multiple regression analysis established the fact that contract specification, contract governance structure, skilled, qualified contract management teams predict the supplier performance of state corporations in Nakuru county. The R Square value of 0.805 suggests that contract specification, contract governance structure, and contract management teams, taken together, explain 80.5% of the variation in supplier performance.

Governing Interfirm Relationships for Social Sustainability: A study by Awan et al., (2018) The research suggests that the efficacy of contract governance might experience a boost with heightened firm cultural intelligence capabilities. Information obtained through surveys was collected from 239 manufacturing firms engaged in export activities across diverse industries.

The "Transaction Cost Economics" (TCE) theory is used to see if working together on contracts is a good idea. When we look at how contracts work, there are two main groups of ideas. One group looks at the duties and rights of the people making the deal. They use contracts, rules, and terms to protect the

relationship and plan for future transactions. The second group uses shared expectations about behaviour to guide exchanges. This helps with control and understanding between the people involved. The collaboration inclination of a firm is positively influenced by contract governance. Taking a TCE perspective, it was expected that firms with greater administrative efficiency in contract governance would have a positive effect on collaboration when facing different exchange partnerships. In terms of how well a company does socially, Sancha et al., (2016) suggested that when buyers and suppliers work together on sustainability issues, it directly connects to better knowledge for both of them. This, in turn, helps improve the company's social performance. When people work together, it usually leads to better social performance. Looking at how cultural intelligence (CQ) affects the connection between contract governance and collaboration. Definition of CQ by Ang et al., 2008. CQ has four parts: understanding, thinking about your own thinking, behaviour, and motivation. Williamson et al., 1996.

How does the collaboration of distributors impact contract governance in marketing channels? (Zhuang et al., 2020). This study found a few important things. First, when distributors' networks are strong, manufacturers and distributors tend to have detailed contracts. Second, having detailed contracts helps in lowering conflicts in the distribution channels. Lastly, when a distributor is very central in the network, the positive effect of a strong network on detailed contracts is not as strong. This research not only talks about the limitations of studying one-on-one relationships in distribution but also helps manufacturers understand and deal with how distributors work together.

#### **Contractual Governance-Institutional and Organizational Analysis**

This paper explores how contracts can be more adaptable, drawing on responsive regulation theories. It shows that how contracts work depends on government policies and laws. The paper also creates a way to measure the quality of relationships by looking at how well contracts connect with relationship norms. The government plays a crucial role in making sure that, through flexible rules, the right conditions are in place for contracts that focus on relationships in money transactions (Jones et al., 2000).

### **RESULTS AND DISCUSSION**

Output-based contracts are negatively related to buyer and supplier conflict. Contracts that are behaviour-based are related positively to buyer-supplier conflict. Contractual effects are balanced through the legal ability to enforce and support from the government acting alone. Contract governance and supplier performance: Contract specifications have a strong positive relationship with procurement performance in state-owned enterprises in Uganda. Enhancements in governance of public procurement through legal enforceability and one-sided government backing. has the potential to result in a 45% enhancement in administrative efficiency in public organizations. Contract management teams have a direct relationship with HSE (Health, Safety, and Environment) performance.

Accurate definition of roles and diverse contract management knowledge are major determinants of effective contract management. Contract specifications, the way contracts are managed and the teams handling contracts together account for 80.5% of the differences in how well suppliers perform. in state corporations in Nakuru county. Working together on contracts is better when a company is really good at understanding different cultures. This makes contract management more effective. Understanding different cultures is really important when managing relationships between different cultures in supply chains. Having good contract rules makes a company more likely to work well with others.

When distributors work closely together, it helps manufacturers and distributors have more detailed contracts. Thorough contracts can help reduce channel conflict. The centrality of network weakens when there are a lot of connections in a network, it makes detailed contracts more likely. Contractual governance, responsive regulation, and government policy: Contractual governance's responsive outcomes depend on government policy and legal regulation.

The state plays a central role in facilitating the development of relational contracting in monetized exchanges through responsive regulatory policy. These results provide insights into how contracts are managed, supplier performance, cooperation and cultural intelligence when dealing with relationships between buyers and suppliers. They also highlight influence of government policy on contract governance. The findings shed light on the critical dynamics of contract governance and its impact on various aspects of supplier relationships and organizational performance. The difference between contracts based on results and contracts based on behaviour shows how important it is to create contracts that help handle conflicts between buyers and suppliers. Output-based contracts, which emphasize performance outcomes, are associated with reduced conflict, whereas behaviour-based contracts, focusing on conduct, can lead to increased conflicts. Moreover, the influence of contracts on these outcomes is not uniform and affected

by the legal capacity to enforce and one-sided government backing, highlighting the importance of the broader institutional context. In terms of supplier performance, the research reveals that clear contract specifications play a pivotal role in enhancing procurement performance, particularly in state-owned enterprises in Uganda. Additionally, improving public procurement governance is shown to be a significant driver of administrative efficiency, with a potential 45% improvement. This underscores the need for robust contract governance practices to achieve better organizational performance. The role of contract management teams in supplier performance is underlined, with a direct relationship established between these teams and Health, Safety, and Environment (HSE) performance. The study highlights the significance of accurately defining roles and cultivating diverse contract management knowledge within these teams to ensure effective contract management, consistent with the research findings. We look at how contracts and working together are connected. Reiterating importance of cultural intelligence (CQ). Results suggest that Companies that understand different cultures better can make contract governance more effective. Moreover, cultural intelligence plays a pivotal role in managing relationships between different cultures in supply chains, further highlighting the role of soft skills and understanding in contract management. The findings concerning distributors' network intensity and contract governance illustrate the nuanced nature of contract relationships in marketing channels. Distributors' networking can positively impact comprehensive agreements and reduce channel conflict. However, centrality of network effect can temper how many connections in a network affect these contracts. underscoring the complexities of distributor interactions in contractual governance. Lastly, the study delves into how contracts can be flexible and responsive in a regulatory context, indicating that outcomes depend on rules made by the government and laws The state's role in fostering relational contracting and its influence on monetized exchanges is emphasized, suggesting that government policies can significantly shape the landscape of contract governance. Overall, these findings provide valuable insights into the multifaceted world of contract governance, offering valuable guidance for organizations seeking to enhance supplier performance, reduce conflicts, and navigate the intricate web of buyer-supplier relationships in various contexts. Additionally, they underscore the significance of cultural intelligence and responsive regulation in the evolving landscape of contractual governance.

### **Practical implementation**

**Lack of Specific Contract Governance Framework:** While the text highlights the relationship between contract types (output-based and behaviour-based) and their impact on buyer-supplier conflicts, it does not provide a specific framework for structuring these contracts or guidance on selecting the most appropriate contract type for different situations. Organizations may face challenges in implementing these findings without a comprehensive contract governance framework.

**Limited Guidance on Enhancing Contract Management Teams:** Emphasizes the importance of contract management teams in relation to HSE performance and overall supplier performance. However, it does not provide detailed recommendations on how organizations can enhance the effectiveness of these teams. Specific strategies or best practices for recruiting, training, and managing contract management teams are not discussed.

**Insufficient Focus on Measuring Cultural Intelligence:** The text recognizes how being culturally smart helps make contracts and working together better. Still, it does not provide a clear methodology for measuring or assessing CQ levels within an organization. Without a practical approach for evaluating and enhancing cultural intelligence, organizations may struggle to leverage this aspect effectively.

**Lack of Guidance on Responsive Regulatory Policies:** While the text highlights the influence of government policies on contract governance, it does not delve into specific recommendations or examples of responsive regulatory policies that can foster relational contracting. Guidance on aligning an organization's contract governance practices with relevant government policies is missing.

**Absence of a Comprehensive Integration Strategy:** The text discusses various aspects of contract governance, supplier performance, collaboration, and cultural intelligence. However, it does not provide a clear strategy for integrating these elements into a cohesive contract governance framework. Organizations may find it challenging to create a holistic approach to contract governance based on the presented findings.

**Limited Discussion on Mitigating Network Centrality Effects:** The text highlights how being too central in a network might make detailed contracts not work as well. in the context of distributor relationships. Still, it does not offer strategies or tactics to mitigate this effect. Organizations may need guidance on how to manage network centrality in their contract governance efforts effectively. In conclusion, the text offers valuable insights looking at how contracts, how well suppliers do, working together, and understanding different cultures are all connected. However, it leaves several strategic integrated contract governance mechanism gaps that organizations should consider when implementing these findings. Addressing these

gaps would require further research and the development of comprehensive strategies and frameworks to enhance integrated contract governance practices.

## CONCLUSION

Based on the review of literature, the focus is on the importance of understanding contract governance mechanisms and agency theory to develop and sustain meaningful partnerships between customers and suppliers, there is also an emphasis on economic costs associated with transactions that impact contract governance, additionally, it's important to consider specific factors when designing and selecting between contracts that are output based and behaviour based. The major determinant to effective Contract Management is a clear understanding of each person's job and the varied knowledge of the team managing the contract, the need to have skilled and competent contract management team to monitor supplier's performance, by clearly stating what they want in the contract in collaboration with their suppliers. The people surveyed, managed to prevent legal complications. Explaining 80.5% of the differences in how well suppliers perform is because of the contract details. When buyers and suppliers work together on sustainability, it helps them learn more, with the goal of making the company more socially responsible. When a company manages contracts well, it makes them more likely to work well with others. Working together in a positive way is connected to making the company socially better. First, when distributors work closely together, it helps manufacturers and distributors have more detailed contracts. Second, having detailed contracts helps in lowering conflicts in the distribution channels. Lastly, when a distributor is very central in the network, the positive effect of a strong network on detailed contracts is not as strong. In organizations, how contracts work depends on how the company is divided between its different parts and between public and private sectors. The government's economic and competition policies also play a role in how these divisions are determined or influenced. The government plays a crucial role in making the right conditions for relational contracts to happen in money transactions by using responsive rules and policies.

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