

# Commercial Perspectives on Long Term Contracting

*Selwyn D'Souza\**

## Key points

1. Planning is essential to a successful negotiation. While this may seem obvious, it is surprising how often useful negotiation concepts and tools are overlooked in practice. To minimise the risk of a sub-optimal agreement, a good negotiator will:
  - (a) recognise that the parties' predictions of the future are likely to be wrong;
  - (b) identify and analyse the sources of power, objectives and individual and organisational incentives surrounding the negotiation;
  - (c) use concepts such as ZOPA (zone of potential agreement) and BATNA (best alternative to a negotiated agreement) to guide the negotiation; and
  - (d) take the time to prepare for future uncertainties with tools like scenario analysis, war games, financial analysis, simulation modelling and risk analysis.
2. It is often the case that those responsible for negotiating a long term contract are not responsible for implementing the contract and so they may bring a short term perspective to the negotiations.

This essay seeks to provide some observations on complex negotiations of long term contracts and the inadequacy of many contracts in reflecting the unpredictability of the future or establishing suitable mechanisms for dealing with uncertainty.

Commercial contracts and the eventual outcomes are driven by the context of the negotiations, the motivations of the negotiating parties and the complexities of different industries. Preparation for contract negotiations is critical and it is important to recognise that prediction of the future

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