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How Companies Use Contracts in Interorganizational Exchange Relations

Anna Hurmerinta-Haanpää

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University of Turku

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ABSTRACT

Contracts are fundamental for today's networked business practices. Various professionals plan, design, and implement contracts, yet many of them find contracts difficult or even impossible to understand. Furthermore, contracts are mostly designed to safeguard parties' rights—not to support collaboration.

In this dissertation, I argue that many counterproductive contracting practices stem from traditional economic and legal theories. Drawing on alternative approaches to contracting, such as transaction cost economics, the relational view, functional contracting, the relational contract theory, and proactive contracting, I explore how organizations use contracts in their interorganizational exchange relations and how these different uses affect relational governance, for example, trust and social norms, and relationship performance. The methodological standpoint of the dissertation is American New Legal Realism (ANLR).

The dissertation consists of a summary and four Publications. The first and second Publication rely on an action research case study and explore how the functional contracting approach could facilitate a business model transition which is often plagued by a number of barriers. The third Publication draws on an expert interview study of 24 contracting professionals. It examines how companies use contracts and how these uses affect relational governance and exchange performance. Finally, the fourth Publication examines how companies utilize the various functions of contracts and frame their purchase contract documents.

Overall, this study found that in addition to the three established functions—safeguarding, adaptation and coordination—contracts are used to serve at least four additional functions: codification, internal management, collaboration, and policy. Even though organizations use all these functions, safeguarding seems to be the most common. Overemphasis of the safeguarding function has negative impacts on both theory development and contracting practice. Thus, I urge both academics and practitioners to adopt the functional contracting approach to design contracts that comprehensively meet the specifics of the exchange and enhance business success.

KEYWORDS: functional contracting, relational governance, relational contract theory, proactive contracting, contract design, contract framing, American New Legal Realism, empirical studies of contracts

TURUN YLIOPISTO
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TIIVISTELMÄ

Sopimukset ovat välttämättömyys nykypäivän verkostoituneessa liike-elämässä. Niitä suunnittelevat ja käyttävät eri alojen ammattilaiset. Silti monilla on vaikeuksia ymmärtää vaikeaselkoista sopimuskieltä. Lisäksi sopimukset laaditaan usein turvaamistarkoituksessa eikä tukemaan osapuolten välistä yhteistyötä.

Esitän väitöskirjassani, että useat haitalliset sopimuskäytännöt juontavat juurensa perinteisistä taloustieteellisistä ja oikeustieteellisistä teorioista. Tukeudun tutkimuksessani näille vaihtoehtoisiin teorioihin, kuten transaktiokustannusteoriaan, relationaaliseen sopimusteoriaan, proaktiiviseen sopimiseen sekä funktionaaliseen sopimiseen, ja tutkin, miten yritykset käyttävät sopimuksia liikesuhteissaan. Selvitän myös, millaisia vaikutuksia niillä on liikesuhteen muille hallinnan muodoille, kuten luottamukselle, sekä liikesuhteen toiminnalle. Tutkimuksen metodologisena viitekehyksenä toimii amerikkalainen uusi oikeusrealismi.

Väitöskirja koostuu yhteenvedosta ja neljästä osajulkaisusta. Toimintatutkimukseen perustuvissa ensimmäisessä ja toisessa julkaisussa tutkitaan, miten funktionaalinen sopimisprosessi voi tukea liiketoimintamallin muutosta, johon liittyy usein monia haasteita. Kolmas julkaisu perustuu 24 sopimusasiantuntijan haastattelututkimukseen. Siinä selvitetään, miten haastateltavien edustamat yritykset käyttävät sopimuksia liikesuhteissaan ja millaisia vaikutuksia niillä on suhteen muille hallinnan muodoille ja toiminnalle. Neljännessä julkaisussa analysoin yritysten ostosopimusasiakirjoja selvittääkseni, mitä funktioita niissä hyödynnetään ja miten ne on kehystetty.

Tutkimuksen tulokset osoittavat, että jo tunnistettujen funktioiden eli turvaamisen, mukauttamisen ja koordinoinnin lisäksi sopimuksia voidaan käyttää ainakin kodifiointiin, sisäiseen johtamiseen, yhteistyön johtamiseen sekä menettelytapojen ohjaamiseen. Vaikuttaa kuitenkin siltä, että sopimuksia käytetään yhä eniten turvaamistarkoituksessa. Turvaamisfunktion ylikorostamisella voi olla negatiivisia vaikutuksia sekä sopimusteorioiden kehittämisen että käytännön sopimustoiminnan näkökulmasta. Kannustankin tutkijoita ja käytännön toimijoita omaksumaan funktionaalisen sopimuskäsityksen ja muotoilemaan sopimuksia, jotka vastaavat parhaiten kunkin liikesuhteen erityispiirteitä ja tukevat niissä onnistumista.

ASIASANAT: funktionaalinen sopiminen, relationaalinen hallinta, relationaalinen sopimusteoria, proaktiivinen sopiminen, sopimusmuotoilu, sopimusten kehystäminen, amerikkalainen uusi oikeusrealismi, empiirinen sopimustutkimus

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What a journey! Little did I know what was ahead of me when my future supervisor, Professor Emeritus Ari Saarnilehto called me one Friday afternoon in January 2013. I still remember his words. He said he needed a researcher for an industrial management project run by a research team at the Åbo Akademi University. He described the project very briefly and said: "Don't worry, you have time to think this through. I don't need to know your answer until Monday." To be honest, I didn't need the weekend to make up my mind. I felt that if I was being offered this kind of once-in-a-lifetime opportunity, I had to take it. And I'm happy I did!

This project has been long and challenging, but rewarding. First I struggled with the subject, because it was totally new to me. I also had difficulties learning "the rules of the academic game", to borrow the words of a dear fellow doctoral student. The reason I survived is that I'm very good at surrounding myself with wonderful people. And now it's time to thank you all.

First, I wish to thank my first supervisor, Professor Emeritus Ari Saarnilehto. You always believed in me, even when I doubted myself. Also, you made sure I had financial support for my research. I've always been able to discuss things with you, not only research, but everything. We've had some very good laughs, too!

As I said, I like to surround myself with as much support as possible. So, I didn't settle for only one supervisor. My second supervisor, Associate Professor Mika Viljanen, offered me the most help with the subject matter of the thesis. We've worked together on research projects and co-written two articles. It was you who taught me to write in academic English. Moreover, I feel that we've had a rather informal supervisor-supervisee relationship which has allowed me to share my deepest thoughts, both professional and personal. Thank you Mika, for our inspiring and thought-provoking discussions!

My third supervisor, Professor Anne Alvesalo-Kuusi, supported me in the empirical work of this dissertation in particular. Anne, you have always commented on my work thoroughly, without unnecessary sugar-coating. One important comment of yours is etched into my mind. I'll get back to this later, perhaps at the "karonkka". You took me into your Sociology of Law research team, the Lokalahti group, and introduced me to the Finnish Association for Legal and Social Sciences

(OYY). I am deeply grateful to you for this – I have made lifelong friendships in these groups.

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Two of the Publications that form part of this dissertation were co-written with Associate Professor Mika Viljanen, Research Director Magnus Gustafsson, Johanna Liinamaa, Hanna Luotola, and Maria Ivanova-Gongne. The third Publication was co-written with Sampo Viding. Thank you Johanna, for initiating our co-writing process and thank you, all my co-writers at Åbo Akademi University, for your collaboration during the action research project and the article writing process. Sampo, thank you for planning and carrying out the survey and the interview study and writing the article with me.

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I also wish to thank the Faculty's writing group and its facilitator Carol Kiriakos for teaching me how to write a PhD. When I started in the writing group sometime in 2015, Carol said something that at first upset me. It was during a round in which everyone in the group shared their thoughts on their progress and possible writing problems. After my turn, Carol commented "No one is forcing you to write the thesis, right? It's up to you whether you want to write the thesis or not." Before Carol's comment, I had blamed everyone and everything else for not being able to write my thesis. Sometime after the comment, I took responsibility for my own work. Thank you Carol, for being so honest. I am grateful to the entire writing group for teaching

me how to plan my work and for supporting me all these years, and a special mention goes to Reijo Salo, Emma Holkeri, Johanna Sammalmaa, Johanna Vanto, Maija Helminen, Mira Turpeinen, Susanna Lundell, Anniina Jokinen, and Kirsi White.

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Finally, it's time to thank friends and family. First, the Kanteletar of D00m wants to thank all members of the WoA-Group for all the laughter and good times! Also, thank you my dear colleagues and friends Mira, Maija, Jutta, Emma, and Johanna. Our conversations have been immeasurably valuable to me, especially during the hardships of Covid-19. Thank you Emilia, for our 25-year friendship, and for helping me through difficult times. Thank you Kristiina, for your support over the past one-and-a-half years. Thank you my dear mother, for always believing in me and being there whenever I needed you. Thank you Rauli and Tiina, for your support and for taking care of Lumilla during the final steps of this research project.

Lastly, I want to thank my Higher Power for giving me the best time of my life with my husband Aarne and the best gift in the world: Lumilla. She has taught me to seize the moment—or a microphone if it's time to sing or rap—and to wonder at the miracles of life, over and over again.

I am deeply grateful to have such wonderful people in my life!

Akaa, April 15, 2021
Anna Hurmerinta-Haanpää

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List of Original Publications

This dissertation is based on the following original Publications, which are referred to in the text by their Roman numerals:

I Liinamaa, Johanna, Mika Viljanen, Anna Hurmerinta, Maria Ivanova-Gongne, Hanna Luotola & Magnus Gustafsson. Performance-Based and Functional Contracting in Value-Based Solution Selling. *Industrial Marketing Management*, 2016; 59: 37–49.

II Viljanen, Mika, Anna Hurmerinta, Johanna Liinamaa, Maria Ivanova-Gongne, Hanna Luotola & Magnus Gustafsson. Functional Contracting for Network Creation and Governance. In Vesalainen, Jukka, Katri Valkokari & Magnus Hellström (eds). *Practices for Network Management: In Search of Collaborative Advantage*, 2017; Palgrave Macmillan: 79–90.

III Hurmerinta-Haanpää, Anna & Sampo Viding. The Functions of Contracts in Interorganizational Relationships: A Contract Experts' Perspective. *Journal of Strategic Contracting and Negotiation*, 2018; 1–2: 98–118.

IV Hurmerinta-Haanpää, Anna. The Functional Contracting Framework: Assessing the Impacts of Contract Functions, Framing, and Regulatory Focus. In Corrales Compagnucci, Marcelo, Helena Haapio & Mark Fenwick (eds). *Research Handbook on Contract Design*, forthcoming; Edward Elgar Publishing: xx–xx.

1 Introduction

1.1 The need to change the traditional view of contracts

> "Contracts are often completely useless in practice, and very often unreasonable. I feel like I'm wasting my time with contracts".
>
> "Sometimes when I'm finalizing the contract with the buyer, neither of us exactly understands what we are agreeing to in the document. It might be a great paper when a dispute arises, but perhaps we should also understand what we are signing".

These comments were made by a CEO during an interview that I conducted as part of this research project. He is not alone in his views. The quotes illustrate two current problems related to contracts and contracting.

First, contracts are often drafted *by lawyers for lawyers* (Berger-Walliser et al. 2011: 56). This is still the case even though research shows that nearly 80% of the content of a contract is about business and financial terms and not about legal terms such as liabilities, indemnities and intellectual property (Cummins 2003: 4). In practice, professionals from various fields, such as engineering, procurement, finance, and law, use business-to-business (B2B) contracts in their everyday work. Yet lawyers are often in charge of contract drafting, which makes contracts difficult or impossible to understand for 88% of business users (WorldCC 2016; Vitasek 2017).

Second, the focus of contract negotiations, as well as of the contract document itself, is very often on *safeguarding* the interest of the party that has the most bargaining power. The result is that contracts create and support arms'-length[1] or adversarial relationships, which are known to create a spiral of opportunism and underperformance (e.g. Ghoshal & Moran 1996; Moeller et al. 2006; Frydlinger et al. 2016; Schilke & Lumineau 2018). Oftentimes these counterproductive practices are justified by referring to the rules of the game: Everyone must understand that "It's not

1 Arm's-length relationships are based on the idea that contracting parties are adversaries and compete with each other (Moeller et al. 2006: 70).

personal, it's just business" (Weber & Mayer 2011: 61; Frydlinger et al. 2016: 13). However, in today's fragmented and decentralized economy, organizations are dependent on their global network of suppliers and business partners, and value is created through collaboration with network members (WTO 2019).[2] Thus, instead of creating and supporting adversarial relationships, contracts should take into account the relationship-specific aspects of exchanges, promote the creation of trust, and encourage communication and collaboration (Frydlinger et al. 2016; Passera 2017).

Where do these counterproductive customs stem from? Along with many other researchers, I believe that the conceptualization of contracts by traditional economic and legal theories still influence contracting practices (e.g. Nystén-Haarala 1998; Haapio 2013; Passera 2017). Specifically, the *classical contract law* system that prevailed in the late nineteenth and early twentieth centuries in the US reflected the *neoclassical economic model's* ideas of spot market contracts and rational decision-makers (Gordon 1985; Smith & King 2009).[3] Thus, the system was formalistic, favored specific planning, ignored the relationship-specific aspects of contracts and opposed contractual flexibility (Macneil 1978). It is a long time ago since the neoclassical economic model and the system of classical contract law were complemented by legal and economic theories—such as the relational contract theory and transaction cost economics (TCE)—that took into account the relationship-specific aspects of exchanges, but these traditional models still affect the ways in which we understand contracts, their purposes, and their uses.

Indeed, in the legal field, the so called relationalists, Stewart Macaulay and Ian R. Macneil, followed the traditions of legal realists and called for a contract law system that would take into account the relational aspects of exchanges (e.g. Gordon 1985; Feinman 2000). In the field of economics, Oliver E. Williamson, who believed that humans are only boundedly rational and inherently opportunistic, presented similar ideas. Williamson claimed that because of the inherent opportunism of humans, transactions that differ in their attributes[4] need to be governed by various governance structures[5], which in turn are supported by the classical, neoclassical or relational contract law system (Williamson 1979, 1985, 1991, 2014).

2 Indeed, according to the World Trade Organization (WTO), two-thirds of world trade occurs through value chains and networks. See WTO 2019: 1.

3 For more about neoclassical economics and classical contract law, see Sub-chapter 2.1.

4 According to TCE, the variety of transactions is mainly explained by different *transactional attributes*. Williamson claims that the main transactional attributes are asset specificity, uncertainty and frequency. For more about transactional attributes, see Sub-chapter 2.2.

5 A governance structure refers to "the institutional framework within which the integrity of a transaction is decided" (Williamson 1979: 235). For more about the governance structures under study by TCE, see Sub-chapter 2.2.

A number of researchers have since elevated the ideas of the relationalists and transaction cost economists. Specifically in the field of organizational and management studies, research has shifted toward a broader view of contracts by focusing on their various functions and their interplay with relational governance. Relational governance refers to informal governance mechanisms, such as trust, flexibility and solidarity, which arise from the values and agreed-upon processes within a relationship and rely on self-enforcement by the contracting parties (e.g. Poppo & Zenger 2002: 709–710). This research criticizes TCE's excessively narrow focus on opportunism and safeguarding, and highlights that in addition to safeguarding, contracts can, for example, *coordinate* and *adapt* the exchange relationship. Moreover, it argues that while formal governance (i.e. contracts) and relational governance complement each other, the different functions of contracts have distinct effects on relational governance. Finally, the two governance mechanisms have mutual effects on exchange relationships (Schepker et al. 2014).[6]

The work of the relationalists and the transaction cost economists has also influenced the work of many legal scholars. Macaulay's work in particular has inspired many law and economics scholars (sometimes referred to as economic relationalists[7]), who, like researchers of organizational and management studies, have found that at least in the context of innovations, the relationship between contracts and relational governance is more complicated than formerly believed. Scholars have suggested that contracts *braid* formal and informal enforcement mechanisms[8], thereby facilitating transparency in information exchange, helping to screen for opportunistic counterparties and increasing switching costs—costs related to switching contracting partners (Gilson et al. 2009, 2010, 2013, 2014). Similarly, Hadfield & Bozovic (2016) suggest that contracts function as *scaffolding,* helping organizations first determine whether the behaviors of the parties comply with the contract, and second guide the decision of whether to use informal enforcement, such as early termination, in cases of a contract breach.

Another school of thought informed by the relationalists is the proactive contracting approach, which was founded in the Nordic countries in the late 1990s

6 For more about the functional approach to contracting, see Sub-chapter 2.5.

7 Legal research following the traditions of Macaulay and Macneil has split into two schools, which are often called "economic relationalism" and "socio-relationalism". Although I myself relate more to the socio-relationalist school, I will limit further comparison between these schools because of the constraints related to the focus of this study. For more about the differences between the two schools, see Scott 2013. See also Tan 2019: 100–103.

8 Formal enforcement refers to enforcement by third parties such as courts. Informal enforcement, in turn, refers to the means that the parties themselves can use to safeguard performance in cases of a contract breach. Examples of informal enforcement mechanisms are early termination of the relationship and reputational sanctions. See e.g. Gilson et al. 2010: 1379.

and early 2000s (e.g. Pohjonen 2002; Siedel & Haapio 2010; Berger-Walliser 2012). Unlike law and economics scholarship, the proactive contracting approach underlines the promotive, *ex ante* use of contracts and the legal *and* managerial functions of contracts (e.g. Nystén-Haarala 1998; Pohjonen 2002; Berger-Walliser 2012; Haapio 2013). Gradually, the proactive contracting approach has grown into a multidisciplinary research stream that uses versatile methods to study contracts and contracting (Nystén-Haarala 2017). More recently, advocates of the approach have applied design-based methods such as experimenting, prototyping and user-testing to explore, for example, how to design contracts that can be used for organizations' competitive advantage and how choices relating to contract design affect parties' attitudes, behavior and the exchange relationship (e.g. Haapio & Hagan 2016; Passera 2017; Passera et al. forthcoming).

Indeed, some of the studies of the proactive contracting approach proponents also form part of the emerging discussions on the social and psycho-cognitive effects of *contract framing.* Framing refers to heuristics that guide decision-making by drawing the reader's attention to particular messages or events and by dismissing other elements (Tversky & Kahneman 1981: 453; Bertrandias et al. 2010: 2; Weber 2017: 747). In the context of contracts, researchers have been interested in the connections between contract framing and *regulatory focus,* which refers to the different strategic means that people and organizations use to obtain desirable outcomes and avoid negative outcomes. According to the regulatory focus theory (RFT) introduced by professor of psychology and business Tory Higgins, two regulatory focuses affect people's emotions and thus drive behavior: *preventive* and *promotive*. Preventively focused people see goals as minimal targets that must be met. Consequently, if the goal is not met, a person with preventive regulatory focus experiences high-intensity negative emotions. Conversely, if the person attains the goal, they experience low-intensity positive emotions. Promotive regulatory focus, in turn, leads to the interpretation of a goal as maximal. Thus, people with promotive regulatory focus experience low-intensity negative emotions if the goal is not met and high-intensity positive emotions if it is (e.g. Higgins 1997; Higgins et al. 1997).[9] Research on contract framing suggests that framing influences the creation and development of interorganizational trust (Mayer & Weber 2009; Bertrandias et al. 2010; Weber & Mayer 2011; Weber & Bauman 2019), and that a contractual frame must be selected on the basis of transaction attributes, task characteristics and the type of relationship desired (Weber & Mayer 2011).

Despite these advances in research, the traditional view of contracts endorsed by the neoclassical economic model and the classical contract law system seems to

[9] For more about RFT in the context of contract framing research, see Sub-chapter 2.8.

dominate the mainstream studies of contracts and contracting practice. One reason for this might be that while acknowledging the relational aspects of exchanges, many current approaches to contracts, such as TCE and economic relationalism, highlight the safeguarding and legal enforcement roles of contracts and understate contracts' abilities to create, sustain and develop collaboration. Moreover, research that underlines the business potential of contracts, the various functions of contracts, and the relationship between contracts and relational norms, has developed under distinct research streams that barely recognize each other. Hence, there is clearly a need to combine the insights of these different theories to gain a comprehensive understanding of the various uses of contracts.

1.2 Objectives, research questions and data

The aim of this dissertation is, by drawing on the above-mentioned theories, to examine the various uses of contracts in B2B exchange relations. Thus, the main research question of this dissertation asks:

> What are the functions by which companies use contracts in their interorganizational exchange relations, and what is the relationship between contract functions and relational governance in these relations?

By interorganizational exchange relations, I refer to transactions that are conducted between two (or more) companies and the relationship that envelopes these transactions.[10] Thus, the words *exchange* and *transaction* are used as synonyms in this dissertation. The research was limited to B2B exchanges for two reasons. First, the empirical data used in this dissertation were collected in liaison with the DIMECC REBUS research program, which focused on B2B relationships.[11] Second, both business-to-consumer (B2C) exchanges as well as business-to-government (B2G) exchanges are highly regulated and thus, the freedom of contract in these

[10] The definition of exchange relation is borrowed from Macneil. He defines a contract as "relations among people who have exchanged, are exchanging, or expect to be exchanging in the future – in other words, exchange relations" (Macneil 2000: 878).

[11] The DIMECC REBUS research program aimed to develop new relational business practices for network governance. Altogether 22 companies and seven research institutions participated in the research program, which ran from 2014 to 2017. The program was managed by DIMECC (a strategic center for research in the Finnish digital, internet, materials & engineering industries) and funded by private companies, public research institutions, and Tekes (The Finnish Funding Agency for Innovation). For more about the research program, see DIMECC 2016.

fields is limited. However, the results may also be at least partly applicable to these types of exchanges.

The main research question is addressed throughout this summary and in the four Publications. In addition, each of the Publications have specific contexts and objectives and operationalize the main research question in slightly different ways. Table 1 summarizes the Publications' research questions, data and method of analysis.

Table 1. Research questions, data and method of analysis used in Publications.

Publication	Research Questions	Data	Method of Analysis
I Performance-Based and Functional Contracting in Value-Based Solution Selling	How can an industrial solution seller commercialize its solution with value-based selling techniques when using a highly advanced performance-based contract as the pricing device?	Data from explorative and collaborative action research[12]: Material from 14 monthly review meetings, 50 solution productization meetings, 47 sales process development meetings, 4 solution sales training workshops, 16 sales progress follow-up meetings, 6 MoU[13] development meetings, 7 external stakeholder workshops, 8 financing model meetings, and approx. 880 emails.	Data analysis was conducted throughout data collection by following the two last phases of action research described by Susman & Evered (1978): evaluating and specifying learning.
II Functional Contracting for Network Creation and Governance	How can the functional contracting approach be utilized in the creation and governance of a business network?	Same as in Publication I.	Same as in Publication I.
III The Functions of Contracts in Interorganizational Relationships: A Contract Expert's Perspective	What are the functions by which companies use contracts to govern interorganizational relationships? How does a contract and its different functions affect relational governance (or vice versa) and interorganizational relationship performance?	Interviews with 24 contracting professionals.	Thematic analysis (Braun & Clarke 2006).
IV The Functional Contracting Framework: Assessing the Impacts of Contract Functions, Framing, and Regulatory Focus	How can the functional contracting approach be used as a contract design framework?	Ten purchase contract documents of companies that participated in a survey and interview study conducted as part of the DIMECC REBUS research program.[14]	Concept-driven qualitative content analysis (Schreier 2012, 2014)

12 For more about explorative and collaborative action research, see Sub-chapter 3.2.1.
13 MoU refers to a Memorandum of Understanding. See also Sub-chapter 3.2.1.
14 See also Note 11.

The first and second Publications explore how the functional contracting approach could facilitate business network creation and governance in the context of business model transformation. The Publications draw on an action research case study in which the case company wanted to develop a new business model using value-based selling[15] techniques and performance-based contracts[16] but faced serious challenges when trying to implement the model. Our task was to identify the challenges and their root causes and to explore solutions to them.

The third Publication discusses the functions by which companies use contracts to govern their interorganizational exchange relations. It also focuses on the relationships among relational governance, contracts and interorganizational relationship performance. The empirical data of the study consisted of 23 interviews of 24 contract experts.

Finally, the fourth Publication explores how companies utilize the various functions of contracts and frame their purchase contract documents. It analyzes ten purchase contract documents and illustrates how the different functions of contracts appear in contracting practice and how the distribution among the functions and the framing, and the possible mismatches between the different functions, or between the functions and the framing, influence the buyer-supplier relationship that is created through the contract.

1.3 Structure of the dissertation

The dissertation consists of this summary and four Publications, which have been published (or have been accepted for publication) in peer-reviewed journals or in edited books. The Publications are presented in full at the end of this summary. The summary broadens the theoretical background of the research project and re-examines the results of the Publications in relation to the main research question. It is structured as follows.

In Chapter 2, I present the theoretical bases of the research. First, I describe the neoclassical economic model and the systems of classical and neoclassical contract law that TCE and the relationalists critiqued. Second, I familiarize the reader with TCE, a neoinstitutional economic theory that studies different forms of governance comparatively. After this, I introduce some of the basic ideas of the relational

[15] "In value-based selling, sellers seek to understand and influence their customers' desire for value, quantify and communicate the value of their offerings to the customer, and devise a value-based pricing method to capture some of the value offered to the customer" (Publication I: 37).

[16] A performance-based contract refers to a contract in which "at least a portion of a contractor's compensation is tied to the achievement of specific and measurable performance standards and requirements" (Publication I: 37).

contract theory, review the literature of the two fathers of the approach, and discuss the impact of relationalism on subsequent research. Then I present more recent research streams which, although based on TCE, criticize its excessively narrow focus on formal safeguards and opportunism, and underline the interlinkages between formal and relational governance: the relational view and the functional approach to contracting. Thereafter, I introduce the proactive contracting approach, which shares similar ideas with relational contract theory, the functional contracting approach and the relational view. Finally, I review the literature on contract design and contract framing. Chapter 2 concludes by summarizing the theoretical approaches, by combining the common denominators of the theories, and by stating the entry point of my research. In Chapter 3, I first introduce my methodological standpoint, American New Legal Realism (ANLR), and then describe the research designs of the Publications along with their methods, data and analysis processes. Finally, I present some ethical reflections on my research. Chapter 4 summarizes the findings of the Publications and Chapter 5 re-examines these findings in light of the main research question. Chapter 5 also summarizes the implications of the research for contract theory, research, teaching, and managerial practice; considers its limitations; and provides directions for future research. Finally, Chapter 6 summarizes the objectives and contributions of this work.

2 From neoclassical economics and classical contract law to the functional use of contracts

2.1 The neoclassical economic model and the systems of classical and neoclassical contract law

In the US, the laissez faire era was dominated by the neoclassical economic model[17] which adhered to Hobbesian individualism, according to which all humans are self-interested utility-maximizers and thus, law was needed to coerce them to honor obligations toward others (Macneil 1978: 862–865; Macaulay 1985: 466–471; Gordon 1985: 568–569). The model also disregarded what Arrow (1969) called the "costs of running the economic system" (Arrow 1969: 48). Likewise, the system of classical contract law embraced the neoclassical economic model by resting on a set of general principles, such as the freedom of contract and *pacta sunt servanda*, from which the rules governing specific cases could be derived. In essence, the system of classical contract law was based on the idea of two opposing contracting parties that acted out of self-interest but committed to a one-off market exchange by expressing their consent and free will in a contract. Thus, the system enhanced discreteness and presentiation[18], favored specific planning, ignored the social or relational dimensions of the exchange, and opposed contractual flexibility (Macneil 1978: 863–864; Smith & King 2009: 5).

The system of classical contract law was criticized mainly by American legal realists such as Arthur Corbin and Karl Llewellyn, who demanded that contract law

[17] For more about neoclassical economics, see Macneil 1981. The main point of the article is that both the neoclassical economic theory and TCE fail to accurately describe real-world contracting. Macneil concludes that current economic theories are insufficient for useful economic analyses of all contractual relations. For more about TCE, see Sub-chapter 2.2.

[18] Presentiation refers to bringing the effects of the future into present. In discrete, one-off market transactions, the future is brought into the present by restricting the expected future effects of the transactions to those defined in the present. See Macneil 1978: 863.

should also consider social values.[19] As a result, these values were written into the American contract law doctrine by the publications of the Uniform Commercial Code (UCC)[20] in the early 1950s and the Restatement (Second) of Contracts in the late 1970s (Macneil 1981: 1050, Note 81; Feinman 2000: 738; Macaulay 2003: 48; Smith & King 2009: 6–7). Even though this new contract law system, conceptualized as the neoclassical contract law system, introduced many adjustments to the classical contract law, it was still based on the assumptions that parties acted out of self-interest and only wanted to commit to one-off, discrete transactions. Thus, while the neoclassical contract law system enabled contractual flexibility through doctrines of, for example, unconscionability, the duty of good faith, and the inclusion of trade usage; and by techniques such as standards, third-party determination of performance, one-party control of terms, and agreements to agree, it still enhanced discreteness and presentiation (Macneil 1978: 865–886; Smith & King 2009: 6–7).[21]

The neoclassical economic model, together with the systems of classical and neoclassical contract law, was gradually challenged by TCE in the field of economics and by the relational contract theory in the field of law. Next, I discuss these theories in greater detail, starting with TCE.

2.2 Transaction cost economics

Transaction cost economics was developed as a counterweight to the neoclassical economic models of markets and the firm. Ronald H. Coase was the first scholar to challenge the prevailing view but only after two decades did the transaction costs gain attention in mainstream economics (Williamson 2014: 7).[22]

19 This study embraces American New Legal Realism (ANLR), which developed from the American Legal Realist (ALR) movement. For more about ALR and ANLR, see Sub-chapter 3.1.

20 The UCC is an American model code for commercial transactions created and revised by the American Law Institute (ALI) and the National Conference of Commissioners on Uniform State Laws (NCCUSL). In order to have a force of law, the UCC must be adopted by an individual state. By now, all US states and the District of Columbia have adopted at least part of the UCC. For more about the UCC, see Georgetown University Law Library 2020.

21 For the history of the American systems of classical contract law and neoclassical contract law, see Macneil 1978, 1981; Gordon 1985; Macaulay 1985, 2003. The American system of classical contract law is similar to what Finnish scholars usually call liberalist contract law. The neoclassical contract law system, in turn, can be compared to the Finnish discussion on the law of the welfare state. The Finnish and US contexts are, however, quite different. See Nystén-Haarala 1998: 5, Note 7, with references.

22 Indeed, Coase discussed transaction costs already in his 1937 article. See Coase 1937. See also Coase 1960.

The most famous theorist associated with TCE is Oliver E. Williamson, who described the firm and contract as governance structures to be examined comparatively. Essentially, Williamson argues that governance structures, such as markets, hybrids and hierarchies, differ in their coordination, adaptation and safeguarding abilities[23], and are supported and defined by a distinctive type of contract law system, based on Macneil's classification of classical, neoclassical and relational contract law (Williamson 1979; 247–253; Williamson 1991: 271–276). Moreover, Williamson includes behavioral aspects, namely opportunism[24] and bounded rationality[25] in the theory and argues that the threat of opportunism always exists in business, and should be managed by binding the cooperating parties together. The objectives of the different governance mechanisms are thus, first, to safeguard the interest of the transaction parties because of the inherent opportunism of humans, and second, to adapt the relationship to changing circumstances (Williamson 1979: 258).

TCE hypothesizes that because the main issue to be solved by an organization is that of adaption and because the main purpose of an organization is economizing[26], organizations must align transactions, which differ in their attributes with governance structures, which differ in their costs and competencies, in a discriminating (mainly, transaction-cost-economizing) way (Williamson 1979: 234; Williamson 1991: 277; Williamson 2014: 8). The main transactional attributes that influence the choice of a most suitable governance structure are:

- Asset specificity: the degree to which an asset can be redeployed for alternative uses by alternative users without sacrificing productive value. Asset specificity is further divided into six classes (1) site specificity, (2) physical asset specificity, (3) human asset specificity, (4) brand name

23 Even though TCE acknowledges the adaptation and the coordination functions of different governance mechanisms, these only "matter to the extent they affect the comparative governance choice" (Schepker et al. 2014: 205). For more about the critique of TCE, see Sub-chapters 2.4 and 2.5.

24 Opportunism extends simple self-interest seeking (adopted by neoclassical economics) to include self-interest seeking with guile, i.e. cheating, lying, deceit, and giving distorted information. Williamson's central argument is that while most people keep their promises, some outliers will always act opportunistically, and that because these outliers cannot be ascertained *ex ante*, safeguards are needed to mitigate opportunism (Williamson 1979: 234, Note 3; Williamson 1985: 64; Williamson 2014: 8).

25 The concept of bounded rationality is adopted from Herbert A. Simon and refers to humans' limited ability to behave rationally as opposed to the intention of behaving rationally. See e.g. Simon 1947; Nystén-Haarala 1998: 222–223; Williamson 2014: 8.

26 According to Williamson, economizing has two parts: economizing on production expense and economizing on transaction costs. The objective is to economize on the sum of production and transaction costs. See Williamson 1979: 245.

capital, (5) dedicated assets, and (6) temporal specificity (Williamson 1991: 281);

- Uncertainty: the lack of information regarding changes in circumstances. Uncertainty can be further divided into primary uncertainty, which is state contingent; secondary uncertainty, which arises from a lack of communication; and tertiary, behavioral uncertainty, which refers to strategic nondisclosure, disguise or distortion of information (Williamson 1996: 60)
- Frequency: the frequency by which transactions occur: one-time, occasionally, or recurrently (Williamson 1979: 246). [27]

The central thesis of TCE is that when transactions become uncertain and involve high asset specificity, they create exchange hazards[28], thereby increasing the risk of opportunism. In these situations, markets give way to hybrids or hierarchies, because they provide more effective safeguards to deter opportunistic behavior (Williamson 1979; Williamson 1991; Williamson 2014). In other words, TCE aims to recognize potential exchange hazards in advance and to invent governance structures to prevent or vitiate them (Nystén-Haarala 1998: 208).

In summary, TCE combines insights from microeconomics, organization theory and contract law theory by identifying the critical dimensions of the transactions that determine the most effective governance structure with its underlying contract law system (Williamson 1979: 239, 261). Compared to neoclassical economics, TCE adopts a more microanalytical view, as it focuses in detail on transactional attributes on the one hand and on the governance modes and their specific features on the other (Williamson 2014: 8).

Even though TCE departs from the neoclassical economic model, it has been criticized for its focus on opportunism and the safeguarding function of a contract (Ghosal & Moran 1996; Smith & King 2009). Even Macneil has criticized the theory

27 Schepker et al. (2014: 195–197) identify two more transactional attributes from the TCE-related literature: complexity and bilateral interdependence.

28 Examples of exchange hazards include: 1) Adverse selection, referring to the selection of an inappropriate contracting partner due to the organization's difficulty in assessing the contract partner's capability and intentions (e.g. Smith & King 2009: 14; Schepker et al. 2014: 196); 2) Moral hazards, such as shirking and cheating, which result from imperfect monitoring and/or enforcement in contracting (e.g. Smith & King 2009; 13–14; Schepker et al. 2014: 196); and 3) The hold-up problem, in which a party abuses its power to extract benefits at the expense of the other. Anticipation of the hold-up problem is said to motivate the structure of contractual relationships (e.g. Smith & King 2009: 17–18; Schepker et al. 2014: 196)). The term hold-up is sometimes used as a synonym to opportunism (e.g. Smith & King 2009: 18, Note 100). In my opinion, the hold-up problem is one manifestation of opportunistic behavior.

for its failure to accurately describe most contractual relations despite its other merits (Macneil 1981). Next, I discuss Macneil's relational contract theory and the "relational school" in greater detail.

2.3 Relational contract theory

The two founders of the relationalist approach, Stewart Macaulay and Ian R. Macneil, continued the work of the legal realists by arguing that the systems of classical and neoclassical contract law covered only a fraction of real-world exchanges. They claimed that both economics and law should take into account the social context of exchanges (e.g. Macneil 1978, 1983, 1985; Macaulay 1985; Gordon 1985; Feinman 2000; Smith & King 2009). Both understood law in broad terms: Macneil in Fullerian terms, as "the purposive enterprise of subjecting men to the guidance of rules" (Macneil 1983: 368, Note 73), and Macaulay as the living law according to Eugen Ehrlich (Macaulay 2005; Macaulay 2006).[29]

As to the relevance of formal contract law, Macaulay and Macneil argued that most exchange relations are governed by norms deriving from social structures that are often not affected by official contract law at all (e.g. Gordon 1985; Macaulay 1985). Thus, they emphasized the discontinuity and marginality of official contract law in the governance of contractual relations and argued for a system of relational contract law that would emphasize cooperation, trust, mutual responsibility and connection in exchange relationships (e.g. Gordon 1985; Feinman 2000). Consequently, according to Macaulay and Macneil, a system of relational contract law that would rest on standards rather than rules would better reflect the contracting reality and be justifiable for all exchange relations.

Apart from these similarities, however, Macaulay and Macneil have followed different research paths: Macaulay has focused on studying the empirical reality of contracts, and Macneil has focused on conceptualizing and theorizing the relational view (Gordon 1985; Braucher & Whitford 2013).[30] Next I discuss these two distinct but interrelated viewpoints.

29 For more about the living law in the context of ANLR, see Sub-chapter 3.1.

30 While Macaulay embraces sociolegal studies and ANLR (for more on ANLR see Sub-chapter 3.1), Macneil is more of a conceptual theorist and denies belonging to either the "sociological" or the "critical" school (Macneil 1983: 384, Note 132).

2.3.1 Macaulay and the empirical study of relational contracting

Stewart Macaulay's most famous study is that reported in his 1963 article dealing with the use and non-use of contracts in business (Macaulay 1963).[31] More specifically, he studied the use of contracts for creating a business relationship, adjusting the relationship and sanctioning default, by interviewing 68 sales managers, purchase managers and lawyers from 43 manufacturing companies and six law firms. He also studied the reasons behind the use and non-use of contracts.

Macaulay found that, first, commercial experts in particular, such as procurement managers and sales managers, avoided the use of contracts and relied instead on relational governance[32], such as trust and gentlemen's agreements. He found that great effort is put into planning exchange performance, while planning for contingencies, non-performance and legal sanctions was not the focus of businesspeople (Macaulay 1963: 56–60). Second, businesspeople seldom used legal sanctions to adjust relationships or settle disputes. Lawyers and financial experts, in turn, were more prone to using contracts for planning and for referring to in cases of a change in circumstances or a dispute (Macaulay 1963: 60–62, 66).

Regarding the non-use of contracts, Macaulay found that, in most cases, contracts were not needed, because other devices, such as careful planning of the primary obligation, industry customs, risk mitigation through securities, insurance, multi-sourcing supplier strategies, and effective non-legal sanctions[33] served the functions of a contract (Macaulay 1963: 63). He also found that sometimes the use of contracts had detrimental consequences. Some of the interviewees felt that detailed negotiation could hinder the creation of a good, trusting relationship, especially if the focus of negotiation was on remote and unlikely contingencies. This could result in only getting to the letter of a contract without room for flexibility to adjust to actual circumstances (Macaulay 1963: 64). Thus, oftentimes, detailed contract negotiations were replaced by more flexible alternatives. Finally, relational governance was used more often than contracts and litigation to govern adjustments of exchanges. This was because contracting and litigation (or the threat of it) incur

31 A full list of Macaulay's publications can be found in Braucher et al. 2013.

32 For more about relational governance mechanisms and their interplay with formal governance, see Sub-chapter 2.4.

33 Examples of non-legal sanctions are an organization's internal sanctions and reputational harms in cases of default (see Macaulay 1963: 63). See also Note 8 on informal enforcement means.

both monetary and non-monetary costs[34] that often outweigh the anticipated gains (Macaulay 1963: 64–65).

As for the use of contracts, Macaulay found that exchanges were contractually planned when it was believed that planning and a potential legal sanction would be more advantageous than disadvantageous (Macaulay 1963: 65). The second reason for contractual planning was the need of an organization involved in a business exchange to use the contract as an internal communication device (Macaulay 1963: 65). Thirdly, contracts were used when it was likely that problems would occur (Macaulay 1963: 65). Finally, the last resort was to use or threaten to use legal sanctions to settle disputes when other devices did not work and when the gains were thought to outweigh the costs, or just to use legal sanctions to "get even", even though the benefits did not necessarily outweigh the costs (Macaulay 1963: 66).

After his seminal work in 1963, Macaulay has continued to study contractual reality and its implications for contract law and adjudication in his works on automobile manufacturers (e.g. Macaulay 1965, 1966a, 1973), consumer issues (e.g. Macaulay 1966b, 1979, 1989), and the real deal versus the paper deal (Macaulay 2003).[35] In addition, he has devoted a great deal of time to developing law school teaching and is well known for his work on law and society studies and ANLR[36] (e.g. Braucher & Whitford 2013: xi–xii). In conclusion, Macaulay has shown, through his empirical work on contracts, that although contracts play an important role in governing business relationships, relational factors are also important. This does not, as some researchers have concluded, mean that contracts are unimportant to Macaulay, or that he would favor a neoformalistic contract law system or textualist adjudication.[37] Rather, Macaulay feels that *the classical and neoclassical academic models of contract and contract law* do not reflect reality and calls for empirical research that is interested in the living law of contracts (Macaulay 1985: 466).

34 Monetary costs include the costs of litigation, whereas non-monetary costs refer to, for example, the discontinuance of the exchange relationship, which is likely after a dispute (Macaulay 1963: 64–65).

35 Macaulay's 2003 article is probably his second most famous article. In it, he presents the ever-ongoing debate between the formalist contract law approach with textual interpretation and the rules-based contract law system and the realist approach with contextual interpretation and the standards-based contract law system. He argues that the real deal (the real exchange) is always more than just a paper deal (what is written in the formal contract document). Thus, he thinks that contract law should rest on standards rather than on rules, and interpretation should be based on contextual factors. According to Macaulay, a formalistic approach would be too simplistic for problems that occur in contractual disputes.

36 For more about ANLR, see Sub-chapter 3.1.

37 Macaulay is said to be the Lord High Executioner of the Contract is Dead Movement by Gilmore (for the Contract is Dead Movement, see Gilmore 1974). Macaulay himself refused the "honor". See Macaulay 1985: 465–466. See also Smith & King 2009: 8.

2.3.2 Macneil and the relational contract theory

The scholar most associated with the relational contract theory is Ian R. Macneil, who started to develop the theory already in the 1960s but only published his first articles on the subject in 1974.[38] Over the years, Macneil has developed the theory to contain four main ideas.

First, he argues that all transactions are embedded in complex relations, and that understanding any transaction requires understanding all the essential elements of these relations. Consequently, he calls for contextual analysis of transactions, both in economics and in contract law (Macneil 2000).

Second, Macneil situates all transactions on an axis on which as-if-discrete transactions represent one end of the spectrum and relational transactions the other. Figure 1 places Williamson's transactional attributes on the as-if-discrete—relational ends of Macneil's spectrum and provides examples of such contracts.

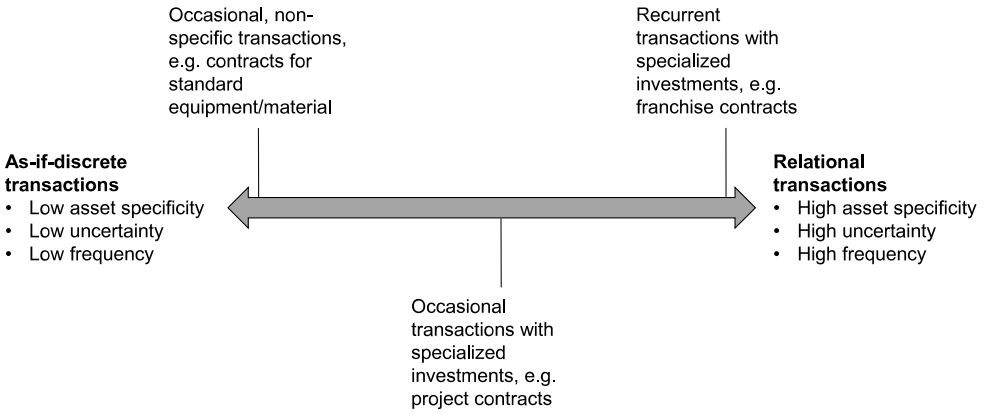

Figure 1. As-if-discrete—relational spectrum with examples of contracts.

Since purely discrete transactions are an oxymoron, Macneil uses the term as-if-discrete transactions to refer to exchanges without many past, present or future social ties. These exchanges are abstract, presentiated statements of obligations with no focus on context (e.g. Macneil 2000: 895–896; Macaulay 2003: 64–65). In the context of this study, occasional purchase contracts for standard equipment/material are an example of a fairly discrete transaction. According to Williamson, these kinds of transactions are best governed by what Macneil describes as the system of classical contract law (Williamson 1979: 248–249).

[38] See Macneil 1974a, 1974b.

According to Macneil, although as-if-discrete transactions do exist, most exchanges are relational. These exchanges are typically not specific or precise allocations of risk but involve complex transactions and span across undefined time frames. They are agreements to cooperate to achieve mutually desired goals, include flexible adjustment possibilities in cases of changes in circumstances, and emphasize solidarity and reciprocity (Macaulay 2003: 64–65). Depending on, for example, the duration of the transaction as well as on the investments required by the transaction, these transactions would be best governed by either the system of neoclassical contract law (as is the case with the project contracts in Figure 1) or by the relational contract law system (Williamson 1979: 249–253). In Figure 1, franchise contracts represent these kinds of relational contracts.

Third, Macneil believes that general principles—*common contract behavioral patterns and norms*—are present in every contract law system. These norms are:

1. Role integrity: The pattern of behavior expected from a contracting party. Role integrity requires consistency and involves internal conflict between self-interest and contractual solidarity. Roles are often multiple and thus, complex.
2. Reciprocity or mutuality: The principle of getting something back for something given.
3. Implementation of planning: Planning the substance of exchange or the processes that structure exchange relations, for example.
4. Effectuation of consent: The exercise of choice in a contract by giving a contracting party the power to limit the other party's future choices.
5. Flexibility: Capacity for change, either by processes within the transaction or by deliberately limiting the scope of the transaction.
6. Contractual solidarity: The norm of holding exchanges together. The sources of contractual solidarity are both internal—the complex webs of interdependence created by the relation itself—and external—the laws and customs created by the society surrounding the exchange relations.
7. The restitution, reliance and expectation interests ("linking norms"): A collection of principles that link the other norms to the rules of the contract and the contract damages.
8. The creation and restraint of power: Capacity to create, restrain and change power relations by contract. Power relations can be legal, political, social, or economic.
9. Propriety of means: Norms concerning how things are done.

10. Harmonization with the social matrix: The idea that the norms of society (supracontract norms) must at least partially become the norms of the exchange relations occurring within that society.[39]

Although all exchanges are situated somewhere on the as-if-discrete—relational axis, the ten behavioral patterns and norms occur all along the spectrum. Some norms are, however, more appropriate for as-if-discrete transactions and others to relational transactions. For example, while the norms of implementation of planning and effectuation of consent may be more visible in as-if-discrete deals, role integrity and harmonization with the social matrix can be more important in relational transactions.[40] However, if the common contract norms are inadequately served, exchange relations of any kind will fall apart (e.g. Macneil 1974b, 1983, 2000).

Finally, Macneil calls for a reunification of contract law that would be based on the common contract norms. He regards this kind of relational contract law system as more effective than the neoclassical contract law system for implementing contract justice (Macneil 1974b, 2000).

For quite some time, Macneil's relational contract theory only had a limited visible impact on adjudication and contract law doctrine.[41] It was criticized for being both an overly abstract and unnecessarily detailed account of groups of contracts that require contextualization. Beyond identifying a subgroup of relational contracts, the theory had no real use for contract doctrine (e.g. Feinman 2000: 737–740).

[39] Originally, Macneil presented five common contract behavioral patterns and norms in Macneil 1974b: 809. Later, he added new norms and patterns that are present in all contracts and contract law systems. See Macneil 1978, 1980, 1983. For more about the common contract norms, see Macneil 1980: 39–59; Macneil 1983.

[40] In addition to the common contract norms, Macneil (1980) presents a *discrete norm* that the as-if-discrete transactions follow, and *relational norms* that are exercised in relational contracts. The discrete norm is an intensification of two common contract behaviors—the implementation of planning and the effectuation of consent. It enhances discreteness and presentiation. Relational norms are role integrity, the preservation of the relation, the harmonization of relational conflict, and supracontract norms. Relational norms are intensifications of three common contract norms in particular—role integrity, contractual solidarity, and harmonization with the social matrix. See Macneil 1980: 59–70. See also Macneil 2000: 896–897.

[41] Tan (2019) deals with relational contract theory's *potential* doctrinal impact and argues that the theory has the potential to influence the doctrine on three levels, which he describes as follows: "(i) re-interpretive relationalism, a smaller-scale intervention which works by altering normative meaning without performing any surgery on the explicit face of concepts and rules; (ii) re-orientative relationalism, which is more visible and involves making explicit salience and additive changes to the content, structure and priority of rules and standards within a doctrine; and (iii) reconstructive relationalism, which involves larger-scale changes at the level of doctrinal categories and taxonomies." (Tan 2019: 119). Although Tan sees potential in relational contract theory's call for contextualist interpretation, he also points to the challenges of the theory's suggestions.

Gradually, however, the relational approach has sneaked into common law courts[42], contract law scholarship[43], and even contracting practice[44]. Next, I discuss law and economics research that is especially inspired by Macaulay's work and is relevant to my research.

2.3.3 Relationalism in law and economics

After its initial awkwardness, Macaulay's and Macneil's work has inspired many scholars in the field of law, economics and organizational and management

42 For example, English courts have started to refer to relational contracts, especially after the seminal case of Yam Seng Pte Ltd v International Trade Corp Ltd [2013] EWHC 111 (QB). In many of the cases, however, relational contract is conceptualized differently from the academic conceptualization of relational contract. Amey Birmingham Highways Ltd v Birmingham City Council [2018] EWCA Civ 264 was a game changer in this respect, bringing English case law conception closer to the academic conception of relational contract. Following this development, in Bates v Post Office Ltd (no 3) [2019] EWHC 606 (QB), the court listed nine non-exhaustive, indicative characteristics of relational contracts. It also mentioned factors that are not relevant to determining whether the contract in question is relational or not. The court ruled that in the case of a relational contract, there is an implied, overriding duty of good faith. This departs from English contract law, in which, contrary to the US and many civil law jurisdictions, no general duty of good faith exists. Examples of more recent cases include UTB LLC v Sheffield United & Ors [2019] EWHC 914 (Ch), Taqa Bratani Ltd & Ors v Rockrose UKCS8 LLC [2020] EWHC 58 (Comm), Essex County Council v UBB Waste (Essex) Ltd (Rev 1) [2020] EWHC 1581 (TCC), and Cathay Pacific Airways Ltd v Lufthansa Technik AG [2020] EWHC 1789 (Ch). For more about the UK case law on relational contracts, see Tan 2019.

43 For American contract law scholarship inspired by the relationalists, see Sub-chapter 2.3.3. In Finland, a number of contract law scholars have studied and conceptualized contracts similarly to the relationalists, and their influence is also shown in contract law teaching and adjudication. For example, Pöyhönen has conceptualized the contract as a process, which means that contractual duties neither emerge nor become fulfilled at a certain moment. Thus, the analysis of contractual rights and duties has to consider the substantial dimension, the time dimension, and the personal dimension of the exchange. See e.g. Pöyhönen 1988: 211–231; Pöyhönen 2003: 144–152. Soili Nystén-Haarala (1998) shares the process view in her dissertation on long-term contracts which focuses on the two different worlds of, first, contract law, and second, contracting. According to Nystén-Haarala, "the purpose is to emphasize that designing good contracts and governing them efficiently is so important that it should be understood as a part of contract law thinking" (Nystén-Haarala 1998: 15–16). Similarly to Nystén-Haarala, Macneil "include[s] contract-itself-in-action within the realm of law, as it is the foundation on which doctrines and formal legal processes are based, and from which they cannot be sensibly separated" (Macneil 1981: 1060, Note 120). Nystén-Haarala is a proponent of the proactive contracting approach, which is also inspired by the works of Macaulay and Macneil. The proactive contracting approach was initiated by Finnish contract law scholar and practitioner Helena Haapio. For more about the proactive contracting approach, see Sub-chapter 2.6.

studies.[45] In the legal field, Macaulay's work in particular has inspired law and economics scholars who have been interested in, for example, the relationships between public contract law and private ordering, the relationships between legal sanctions and non-legal, reputational-based sanctions, and the question of contract law system that best meets the expectations of the contracting parties. Essentially, these so called economic relationalists call for a neoformalistic contract law system and methods of adjudication (Tan 2019:100–102), but some law and economics scholars call for a combination of formalist and contextualist adjudication (e.g. Badawi 2009; Jennejohn 2010, 2016).

For my research, three theories that have been developed within the realm of law and economics studies are especially important.[46] All of them relate to the interaction between formal and informal governance in the context of innovation relationships that are subject to pervasive uncertainty (Hadfield & Bozovic 2016).

First, building on their earlier work on the relationship between formal and informal enforcement, Gilson et al. (2009, 2010, 2013, 2014) introduced the theory of a braided contract that combines elements from both informal and formal governance. Essentially, in braided agreements[47], parties agree on the processes of information exchange and collaboration, thereby complementing informal governance and endogenizing trust. According to Gilson et al. (2009), these techniques facilitate transparency in information exchange, help screen for

44 In contracting practice, the professional association for Commercial and Contract Management, World Commerce and Contracting (WorldCC, formerly known as the International Association for Contract & Commercial Management, IACCM), encourages organizations to use formal relational contracts in strategic and complex commercial exchanges. A white paper by the WorldCC, the University of Tennessee and the Lindahl Law Firm, introduces a model of a formal relational contract together with a five-step contracting process. See Frydlinger et al. 2016. This model is based on research carried out at the University of Tennessee, and a number of organizations have adopted it with good results. See e.g. Frydlinger et al. 2019; Frydlinger et al. 2020. Recently, the model has drawn wider attention in economics. See Frydlinger & Hart 2020, which discusses the merits of the model and explains in economic terms why it works.

45 Studies in the fields of organizational and management studies will be discussed in detail, especially in Sub-chapters 2.4 and 2.5.

46 I do not, however, consider myself an economic relationalist, nor do I agree with economic relationalists' assumptions that rational choice directs the behavior of commercial parties (Scott 2013: 118). Jennejohn's (2016, 2020) and Gilson et al.'s (2009, 2010, 2013, 2014) theories in particular seem to be based on the ideas of rational decision-makers that design contracts purely on the basis of different kinds of exchange hazards. Both theories seem to overlook the human and cultural factors that influence contract design choices.

47 Gilson et al. (2009, 2010) use the term "contract for innovation" to refer to a braided agreement.

opportunistic counterparties, and increase the switching costs—the costs incurred by switching a contracting partner. In their papers, they examine the braiding phenomenon in a variety of contexts, using many examples from real contracting practice. Moreover, they argue that since braiding is only one approach to harnessing opportunism, uncertainty and the scale of the markets in a specific exchange will determine whether or not braiding is used (Gilson et al. 2014). They also claim that courts should use low-powered sanctions in cases of breached braided agreements, because a high-powered sanction would crowd out the informal governance and vitiate the whole purpose of the braided contract.[48]

Second, Jennejohn (2016, 2020) continues the work of Gilson et al. (2009, 2010, 2013, 2014) in his two empirical papers but challenges the braiding thesis in part. First, he criticizes Gilson et al.'s argument of uncertainty and the scale of the markets that determine whether or not braiding is used. Jennejohn (2016, 2020) argues that in addition to market uncertainty and scale, alternative types of exchange hazards (such as technology spillovers and coordination problems) and different network types[49] can influence contract design choices. Consequently, he argues that a *multivalent approach* explains certain aspects of innovation contracts' designs better than the braiding thesis. According to Jennejohn (2016), multivalence can be in relation to both the exchange hazards that characterize innovation exchanges and the governance tools that respond to these multiple hazards. This also means that contract provisions that address a specific exchange hazard, such as the hold-up problem[50], might either conflict or support other contract provisions, mitigating another exchange hazard. He concludes that since different *formal* governance mechanisms can either substitute or complement each other, the relationship between *formal* and *informal* governance must be even more complex. Moreover, he speculates that the multivalent approach probably also extends to informal

48 Low-powered sanctions refer to reliance damages as opposed to expectation damages. See Gilson et al. 2010: 1399, Note 60.

49 Bernstein (2015) also explores the influence of networks – "a set of connections between individuals or between organizations" (Bernstein 2015: 599) – in the governance of Original Equipment Manufacturer (OEM) procurement contracts. According to her, network governance reinforces the influences of governance mechanisms used in individual buyer-supplier relationships by, for example, broadening the self-enforcing range of contractual obligations and expanding the types of behavior that can be sanctioned through informal enforcement. She also suggests that in addition to transaction costs, network-related factors, such as the network structure, the network position of suppliers, and innovation needs, influence firms' make-or-buy decisions.

50 For the definition of the hold-up problem, see Note 28.

governance: For example, informal governance will likely affect not only hold-up problems, but also other types of exchange hazards.[51]

Finally, in an interview study of high-level executives in non-innovation- and innovation-oriented companies, Hadfield & Bozovic (2016) found that in innovation-oriented exchanges, contracts were used as scaffolding. When a contract works as scaffolding, it "bridge[s] gaps and provide[s] just enough support for work on the underlying edifice to move forward" (Hadfield & Bozovic 2016: 1010). In this way, a contract serves as a classification institution, which refers to a set of rules that the practitioners can use to decide whether or not a contracting party's concrete conduct is a breach. The classification institution relieves the parties of the need to specify a complex plan *ex ante*, because it provides rules that will guide the parties to determine *ex post* whether specific behavior is in accordance with the contract. If the behavior is classified as a breach, it triggers the imposition of informal enforcement mechanisms, such as early termination and reputational harm.

All these three theories resemble the debate that has been ongoing in management studies for about two decades—the discussion of whether formal governance and relational governance substitute or complement each other. Despite this clear resemblance, the two research streams barely refer to one another.[52] One reason for this might be that research in management studies, conceptualized as *the relational view*, criticizes TCE's focus on opportunism and formal safeguards, which is exactly the approach that most law and economics studies take. Moreover, the focus of these legal studies is on governance by contract, whereas the focus of management scholars is on the informal governance mechanisms of exchanges. Next, I discuss this research in more depth.

2.4 The relational view——contracts and relational governance as substitutes or complements?

As discussed in Sub-chapter 2.2, according to the logic of TCE, the governance mode of an exchange should be chosen on the basis of the transactional attributes that

[51] In addition to his papers discussed in detail here, Jennejohn has also developed a theory of generative contracting (see Jennejohn 2008). Building on Helper et al. (2000) in particular, Jennejohn argues that in situations in which firms embark on joint innovation that is characterized by unique, endogenous, and pervasive uncertainty, collaborators use generative contracts to institutionalize a learning process that consist of benchmarking, error detection/correction mechanisms and simultaneous engineering. These kinds of contracts, according to Jennejohn, "establish routines for uncovering problems, cooperatively fashioning solutions in real time, and, in so doing, further defining their [the contracting parties'] respective self-interests"(Jennejohn 2016: 322, Note 199).

[52] For exceptions, see e.g. Gilson et al. 2009; Jennejohn 2016.

create exchange hazards and give rise to opportunistic behavior. The more exchange hazards there are, the more formal safeguards are needed to prevent exploitation by a less principled (more opportunistic) party. In fact, according to Williamson, although trust is needed in exchanges, it can never totally exclude opportunism (e.g. Williamson 1985: 64–65).

The relational view criticizes TCE's focus on opportunism and formal safeguards[53] and posits that in addition to formal safeguarding and control mechanisms, emphasis should be placed on the relational governance mechanisms that arise from the values and agreed-upon processes within a relationship and govern interorganizational relationships and their performance. These mechanisms rely on the contracting parties' informal structures and self-enforcement. Trust, solidarity and flexibility are examples of relational norms and governance methods (Poppo & Zenger 2002: 709–710; Lioliou et al. 2014: 505; Cao & Lumineau 2015: 17).

Initially, the relational view challenged the perspective of TCE, which regards contracts and the safeguards they create as having a *positive* impact on exchanges because they allow them to occur and continue on a long-term basis despite exchange hazards (Rich et al. forthcoming: 6). In effect, researchers who supported the so-called *substitution view* suggested that contracts have a *negative* impact on exchanges and exchange relationships, and that relational governance is the most effective way to minimize transaction costs and add value. As a result, relational governance, rather than contracts, should be used to govern exchanges (e.g. Gulati 1995; Ghosal & Moran 1996; Dyer 1997; Uzzi 1997; Dyer & Singh 1998). The proponents of the substitution view went as far as to claim that the combined use of relational governance and formal governance is fundamentally problematic, and that formal governance can even hinder the proper, functional use of relational governance and undermine the development of trust (e.g. Dyer & Singh 1998).

In 2002, Laura Poppo and Todd Zenger published an article that contrasted sharply with the substitution view (Poppo & Zenger 2002). For example, they found a positive correlation between increased contractual complexity, increased relational governance, and exchange performance. Thus, they argued that formal governance and relational governance work as complements rather than substitutes. They observed that, especially in the early phases of collaboration, contracts facilitate the development of trust by narrowing the domain around which parties can be opportunistic. Likewise, relational governance complements contracts when their limits are met, in the case of a conflict, for example (Poppo & Zenger 2002: 721–

[53] Research on behavioral economics partly supports this critique. For example, the famous ultimatum game indicates that while humans are opportunistic, they are also fair. See e.g. Kahneman 2011: 305–308.

722). In these situations, relational governance directs parties to behave flexibly and collaboratively rather than in a self-maximizing way (Schepker et al. 2014: 201).

After Poppo and Zenger's seminal work, the complementarity role of contracts and relational governance has been supported by a number of other studies (e.g. Mayer & Argyres 2004; Ryall & Sampson 2009; Li et al. 2010; Mellewigt et al. 2012; Cao & Lumineau 2015; Lumineau 2017; Shen et al. 2019).[54] Proponents of the complementary view see the two governance mechanisms as enabling mechanisms on the one hand and compensating mechanisms on the other. For example, as enablers, clear contracts facilitate the development of relational governance by increasing mutual confidence, reducing information asymmetry, improving mutual understanding, and supporting trust. As compensators, contracts also compensate for the limitations of relational governance (Huber et al. 2013).

Even though the relational view has a more comprehensive understanding of organizational governance mechanisms than TCE, it has been criticized for being one dimensional (e.g. Schepker et al. 2014: 218). Moreover, like TCE, the relational view assumes that contracts are only used for safeguarding—for preventing negative events from occurring (Rich et al. forthcoming: 7). According to recent research, these limitations have resulted in the dichotomous debate of the substitution and the complementary roles of the two governance mechanisms even though this relationship seems to be more complicated (Ryall & Sampson 2009; Bertrandias et al. 2010; Huber et al. 2013; Cao & Lumineau 2015; Weber & Bauman 2019).

For example, Huber et al. (2013) argue that the relationship between contractual and relational governance oscillates between complementarity and substitution. Poppo & Chen (2018) corroborate this in the context of classical and neoclassical contracting by arguing that although trust supports the development of contracts and vice versa, and although contracts and trust positively relate to performance in neoclassical contracting, the situation is less consistent in classical contracting. This is because of the different levels of risk involved in classical and neoclassical contracting; a classical, complete contract has little economic risk and thus, relational governance may substitute the contract. With neoclassical contracts—and here uncertainty enters the picture—if one party harms the other by failing to deliver the agreed-upon deal, the economic risk is significant. Thus, if trust substitutes a neoclassical contract, it means that parties forgo crafting a more complex contract that puts in place processes to resolve adjustments and disputes.

In connection to this, Cao & Lumineau (2015: 19) argue that different types of contracts can have distinct effects on relational governance: i.e. controlling contracts can have negative impacts on it, whereas coordinative contracts can facilitate its

[54] For comprehensive meta-analyses, see Poppo & Cheng 2018 and Cao & Lumineau 2015.

development.[55] In effect, research has begun to take notice of the different *functions of contracts* and their interplay with relational governance and exchange performance (Schepker et al. 2014; Cao & Lumineau 2015). This research is discussed next.

2.5 The manifold functions of contracts

The functional approach to contracting grew from the relational view and its critique of TCE's structural view of contracts and its focus on the safeguarding function. It was first conceptualized by Schepker et al. (2014), although the core elements of the approach emerged already at the beginning of the 2000s. The approach underlines, first, that there are other reasons to choose a specific governance structure than transaction costs or the threat of opportunism, and that various issues affect this decision (Schepker et al. 2014: 201–204). Second, the functional approach emphasizes other coexisting functionalities of contracts, such as coordination and adaptation, together with the safeguarding function[56] (Reuer & Ariño 2007; Lumineau & Malhotra 2011; Mellewigt et al. 2012; Schepker et al. 2014; Lumineau 2017; Chen et al. 2018; Schilke & Lumineau 2018). Coordinative clauses organize the relationship of the parties, tasks and communication throughout the contract's life and include provisions for communication and monitoring (Mellewigt et al. 2012: 850–851; Schepker et al. 2014: 211–212). The adaptation function, in turn, refers to contractual techniques such as a single contract clause or a combination of various clauses, which are used to adapt the relationship in response to possible endogenous or exogenous changes in the transaction. Examples of adaptive terms are price adjustment clauses, change management clauses, force majeure clauses, and contract termination clauses (Mellewigt et al. 2012: 852–853; Schepker et al., 2014: 212–213; Chen et al. 2018: 475–476).

[55] In the legal field, contract types refer to the classification of contracts according to their distinct characteristics, e.g. their parties, i.e. business-to-business (B2B) contracts, business-to-government (B2G) contracts, business-to-consumer (B2C) contracts, and consumer-to-consumer (C2C) contracts. Contracts can also be classified by their content. A sale of goods contract, a lease, and an employment contract are examples of different types of contracts classified by their content. Moreover, contracts can be classified by their term (a one-time or a short-term contract vs. a long-term contract). For the different contract types in the Finnish context, see Saarnilehto & Annola 2018: 12–15 and Halila & Hemmo (2008). In organizational and management studies that I refer to in this dissertation, different types of contracts refer to the different functions of contracts. For the different functions of contracts, see Sub-chapter 2.5.

[56] Instead of using the term contractual safeguard, some researchers refer to a contract's control dimension or function. See e.g. Lumineau & Malhotra 2011; Malhotra & Lumineau 2011; Cao & Lumineau 2015; Lumineau 2017.

Researchers have studied the relationship between organizational learning and the use of different contractual functions (Mayer & Argyres 2004; Mellewigt et al. 2012), and the relationship between transaction attributes, contractual function, and organizations' contract design capabilities (Argyres & Mayer 2007; Shen et al. 2019). Studies have also examined the effects of various contractual functions on trust and distrust (Malhotra & Lumineau 2011; Lumineau 2017; Shen et al. 2019) and on the level of conflict in alliance relationships (Schilke & Lumineau 2018). In addition, studies have focused on the relationship between contract detail, contract function, and the selection of a rights-based vs. interests-based approach to dispute resolution (Lumineau & Malhotra 2011). Finally, researchers have been interested in how prior ties influence the use of various contract functions, finding that prior relationships have a stabilizing or a slightly positive effect on the level of safeguarding clauses (Mayer & Argyres 2004; Reuer & Ariño 2007; Ryall & Sampson 2009; Mellewigt et al. 2012). The results concerning the relationship between prior ties and the use of adaptive and coordinative contract clauses are, in contrast, conflicting (Mayer & Argyres 2004; Reuer & Ariño 2007; Ryall & Sampson 2009; Mellewigt et al. 2012; Cao & Lumineau 2015; Wang et al. 2017). For example, Reuer and Ariño (2007) found that prior ties decreased the use of coordinative clauses but not the use of safeguarding clauses. In contrast, Wang et al. (2017), focusing on the distinct effects of the various contractual functions on cooperative behavior and on the relationship between prior interactions and the functions, found that although prior interactions increased the use of coordinative contract clauses, they did not affect the use of contractual controls and adaptation clauses.

The functional approach to contracting has attracted scholars in management studies, but has only recently gained attention in contract law scholarship (e.g. Nystén-Haarala et al. 2010; Viljanen et al. 2018a; Viljanen et al. 2018b; Viljanen et al. 2020; Huovinen forthcoming; Laurikainen-Klami forthcoming). Most of these studies embrace *the proactive contracting approach* that was founded in the Nordic countries in the late 1990s and early 2000s (e.g. Pohjonen 2002; Berger-Walliser 2012). The proactive contracting approach shares similar ideas with the relational contract theory but is more practice oriented and offers concrete tools for operationalizing the ideas of the relationalists in the context of contract design. I next discuss this approach in more detail.

2.6 The proactive contracting approach

The proactive contracting approach was initiated by legal scholar and practitioner Helena Haapio in her 1998 publication "Quality Improvement through Proactive Contracting: Contracts are too Important to be left to Lawyers!". After this, a handful

of Finnish scholars and practitioners joined forces and published the first book on proactive contracting.[57] They also founded the Nordic School of Proactive Law and the Proactive ThinkTank (Haapio 2013: 39).[58] Conferences on the proactive approach have been held since 2003, and have resulted in the publication of proceedings, including three books.[59]

According to Haapio (1998), proactive contracting refers to:

> "…recognizing and making use of contracts and contracting processes as planning tools to guide and support the success of your business. It provides the support needed to identify opportunities in time to take advantage of them—and potential problems in time to take preventive action. Proactive contracting provides tools and techniques for the early detection of gaps, traps and problems and the prevention of negative surprises" (Haapio 1998: 246).

Although the proactive contracting approach was initiated and developed mainly by legal scholars, it has grown into a multidisciplinary, practice-oriented research approach that is interested in the ways in which contracts can be used to promote business success (e.g. Haapio 2013; Kujala et al. 2015; Nuottila et al. 2016). Thus, its focus is not, as in conventional contract law scholarship or even in the many works of law and economics scholars, on interpreting contracts or contract law *ex post*, in cases of disputes.[60] On the contrary, the proactive contracting approach focuses on the *ex ante* use of contracts in business (e.g. Haapio 2013). In fact, as described by Soile Pohjonen, a co-founder of the proactive contracting approach, the goal of proactive contracting is that "the contracting parties achieve the goal of their collaboration in accordance with their will. This requires, above all, a careful investigation of their goal and will, and the skill to create a clear and legally robust framework for their implementation" (Pohjonen 2002: v, translation by Haapio 2013: 39).

The proactive contracting approach has two dimensions: preventive and promotive.[61] In the context of law, the preventive dimension is based on Preventive

57 See Pohjonen 2002.

58 See Nordic School of Proactive Law.

59 See Wahlgren 2006; Haapio 2008; Berger-Walliser & Østergaard 2012. For a comprehensive history of the proactive contracting approach, see Berger-Walliser 2012, with references.

60 According to Kujala et al. (2015), this limitation of conventional contract law scholarship stems from legal centralism, "which approaches every problem from the point of view of courts or legislation." (Kujala et al. 2015: 95). See also Nystén-Haarala 1998: 204.

61 The preventive and promotive dimensions are grounded in RFT (Siedel & Haapio 2010: 660–661). For more about RFT in the context of contract framing research, see Sub-chapter 2.8.

Law, introduced by US attorney and law professor Louis M. Brown in 1950 (Brown 1950). In the same way as the proactive contracting approach, the focus of the preventive law movement is on the future, and the goal is to use the law to prevent problems and disputes from occurring (e.g. Haapio 2013: 38–39). However, the proactive contracting approach adds a proactive dimension to Preventive Law, thereby focusing on enabling success and enhancing opportunities through law and contracts. Being proactive "involves acting in anticipation, taking control and self-initiation" (Rekola & Haapio 2011: 382).

In the proactive approach, the role of a contract expands from being merely a legal instrument to also covering *the managerial* functions of a contract. Legal and managerial functions are intertwined and strive for the same goal—that the parties achieve the benefit of their bargain (Haapio 2013: 30). In other words, like the functional approach to contracting and unlike conventional contract law scholarship, which focuses on the legal functions of contracts, the proactive contracting approach recognizes that contracts serve many functions. Researchers have conceptualized contracts as, for example, a process[62] (e.g. Nystén-Haarala 1998; Nystén-Haarala et al. 2010; Kujala et al. 2015); tools for planning and managing business, relationships and collaboration (e.g. Pohjonen & Visuri 2008; Berger-Walliser et al. 2011; Kujala et al. 2015; Nuottila et al. 2016; Nuottila & Nystén-Haarala 2019); blueprints; the visible scripts[63] and roadmaps of the deal (e.g. Haapio & Haavisto 2005; Rekola & Haapio 2011; Nuottila & Nystén-Haarala 2019); boundary objects (e.g. Passera et al. 2013; Passera & Haapio 2013; Pohjonen & Koskelainen 2012); and as a source of competitive advantage (e.g. Barton 2008; Siedel & Haapio 2010; Siedel & Haapio 2011; DiMatteo et al. 2012; Passera 2017). For instance, Haapio & Haavisto (2005) argue that good-quality contracts serve as visible scripts for the contracting parties and are instruments for:

1. Coordinating and managing business, projects and commitments;
2. Creating, allocating and protecting value, and realizing benefits;
3. Communication, motivation and control;

62 As discussed earlier in Note 43, the concept of the "contract as a process" also exists in Finnish contract law literature (see e.g. Pöyhönen 1988). However, the emphasis of the proactive contracting approach is not, as in the Finnish contract law literature, on the legally binding effect of a contract, which can both develop and fade away gradually, but on the contract as a managerial tool, throughout the exchange (Kujala et al. 2015: 96).

63 The contract as a script metaphor was introduced by Suchman (2003) who argues that contracts should be understood and studied as both technical and cultural social artifacts. The script metaphor also includes the technical and symbolic sides (Suchman 2003:114).

4. Sharing, minimizing and managing risks;
5. Preventing problems and controlling and resolving disputes. (Haapio & Haavisto 2005, translation by Haapio 2013: 29)

In addition to the legal-managerial functions of contracts, the proactive contract approach highlights the need for cross-professional collaboration in contract drafting. Haapio (2006a: 159; 2013: 37) uses the visual metaphor of a puzzle to refer to the different parts of contracts that must be consistent and coordinated throughout the contracting process, from planning through drafting to implementation. As can be seen in the following figure (Figure 2), the legal part is but one piece of the puzzle: The technical, implementation and financial parts are equally important pieces. This view changes the lawyer's job from that of a fighter in court or the drafter of a clear, enforceable legal contract that safeguards a company's interests against other contracting parties to a *designer* that needs to collaborate and communicate with multiple user groups and craft contracts for varying information needs (e.g. Haapio 2006b; Nystén-Haarala et al. 2010; Siedel & Haapio 2010; Haapio 2013; Kujala et al. 2015; Nuottila et al. 2016).

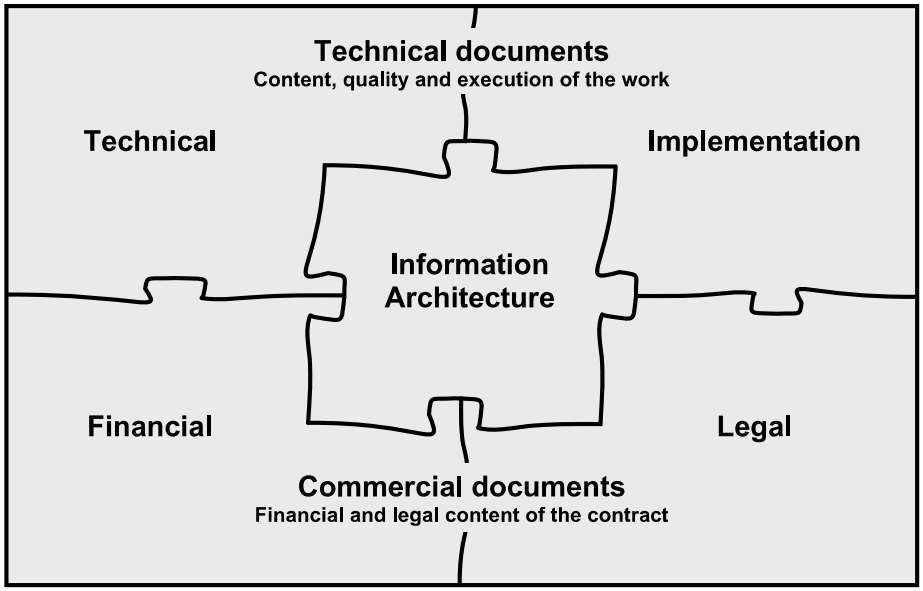

Figure 2. Contract Puzzle: Contract documents and their contents. © Helena Haapio. Used with permission.

Research on proactive contracting has focused on empirical studies of contracts-in-action, i.e. how contracts work in actual business practices. A number of researchers have adopted the approach when studying long-term contracts (Nystén-Haarala

1998), life-cycle contracting (Nystén-Haarala et al. 2010), contract simplification (e.g. Waller et al. 2016; Finnegan 2021), and contracts and contracting in project business (e.g. Kujala et al. 2015; Nuottila et al. 2016; Nuottila 2019; Nuottila & Nystén-Haarala 2019). Over time, the proactive approach has expanded to include not only contracts but also other fields of law, and today, the approach is applied in, for example, law for competitive advantage research and law and strategy research (e.g. Siedel & Haapio 2010; Berger-Walliser et al. 2011)[64], research on corporate social responsibility (CSR) (e.g. Pohjonen 2009; Park & Berger-Walliser 2015; Berger-Walliser et al. 2016; Berger-Walliser & Shrivastava 2015), and public procurement contracting research (Pohjonen & Koskelainen 2012). Notably, the approach has been endorsed by The European Economic and Social Committee (EESC) in relation to developing better regulation in the European Union (EU) (EESC 2009). Recently, the approach has been applied particularly in the context of contract design research.[65] This research, with its special focus on contract visualization and contract framing, is discussed next.

2.7 Contract design research

Contract design research, as understood in this study, is informed by the proactive contracting approach on the one hand and by design research and methodologies on the other.[66] Consequently, contract design research uses design-based methods, such as experimenting, prototyping, and user testing, to study contracting and contract documents. Moreover, it focuses on the entire contract document, including content,

64 The law for competitive advantage/law and strategy movements in the US share many similarities with the proactive contracting approach. In fact, the proactive contracting approach can be considered an integral part of astute legal strategy. For law and strategy/law for competitive advantage research, see e.g. Bird 2008; Bird 2011; Bird & Orozco 2014; Orozco 2020. For a comparison of the European proactive law movement and the American law for competitive advantage/law and strategy movement, see Siedel & Haapio 2010.

65 In addition to research on contract design, the proactive contracting approach has recently been applied in, for example, research on legal design in the context of transparency design, content design, and proactive visualization. See e.g. Rossi & Haapio 2019; Haapio et al. forthcoming.

66 A number of distinguished law and economics scholars study contract design choices from the perspective of, for example, economic efficiency and transaction costs. See e.g. the studies referred to in Sub-chapter 2.3.3. Most scholars representing the TCE perspective, the relational view, and the functional approach to contracting are also interested in contract design issues. None of these scholars, however, employ the proactive contracting approach or use design-based methods in their research. In other words, the context of their studies is contract design but their theoretical approach, as well as their methods, differ from the theoretical framework and methods used in the contract design research that is discussed in this Sub-chapter.

structure, language, and presentation, as well as the design of the contracting process, from a user-centric perspective (e.g. Haapio 2013; Berger-Walliser et al. 2017; Passera 2017; Finnegan 2021). In the context of contract design, user-centricity means that the needs of the people who use contracts are the driving forces behind the contract design process (e.g. Passera & Haapio 2013: 40–43; Berger-Walliser et al. 2017: 356). This dissertation examines both the contracting process (specifically Publications I and II) and contract documents (specifically Publication IV) and focuses mainly on the design of contract content (the functions) and language (the framing).

The pioneers of contract design research[67] argue that current contracting practices and contract documents are dysfunctional because of the classical legal paradigm dominating both research and practice, which is reinforced by lawyers who draft contracts from old templates[68] (e.g. Haapio 2013; Passera 2017). Moreover, they believe that contract design is the key to improving contract clarity and functionality and enhancing collaboration among the contracting parties, their lawyers and those implementing the contract (e.g. Passera et al. forthcoming). Consequently, contract design research aims to find answers to questions such as how to help users better comprehend the framework of a complex contract or how to transfer the information included in contracts to facilitate collaborative knowledge work (e.g. Passera 2017).

Recently, contract design researchers have been interested in, for example, the impact of contract design on the legal community (Cummins forthcoming), the opportunities and challenges of contract design in the context of consumer (online) contracts (Waller forthcoming; Mik forthcoming) and standard contracts in banking and finance sectors (Kaave 2019a, 2019b, 2020). Another trending research area is the opportunities and challenges resulting from merging contract design with smart contracts and contract automation tools (Rich et al. forthcoming; White

67 Haapio and Passera are "partners in crime": They have co-authored a number of articles, book chapters, and conference papers, and worked together in various contract design jams and projects.

68 Haapio (2013: 49–52) argues that most contracts are compiled of old contract templates that are put together by lawyers who are trained to prepare for worst case scenarios, minimize liability exposure and maximize benefits when using the contract in court. Anderson (2020) also argues that attorneys use the precedent heuristic—the copying of past transactions—to economize on the cost of writing contracts. Moreover, as reading, processing and understanding the precedent documents involve costs, attorneys often rely on the perceived "wisdom of the crowd" embodied in a standardized document (the cognition constraint). Finally, as the search for an appropriate precedent incurs costs, attorneys search local rather than global precedents (local search bias). According to Anderson, these three elements result in a path-dependent contract drafting process and miscalibrated contracts.

forthcoming). Moreover, researchers have proposed practical and innovative solutions to enhance the usability and comprehension of contracts (Haapio & Hagan 2016; Passera 2017; Finnegan 2021; Henschel forthcoming; Jeyakodi & Gelting-Ros forthcoming; Passera et al. forthcoming). For example, Haapio & Hagan (2016), Passera (2017), and Passera et al. (forthcoming) propose a pattern approach—the use of "reusable models of a solution to a commonly occurring problem"[69] (Haapio & Hagan 2016: 381)—to build common interdisciplinary knowledge in the specialized field of contract design and to make contracts easier to understand (Haapio & Hagan 2016; Passera et al. forthcoming). Another example is the work of Milva Finnegan (2021), in which she proposes that organizations adopt three distinct contract design methods (a user-based building block approach to contract structure design, a controlled contract language, and contract visualizations) to reduce contract complexity and develop user-friendly contracts to support successful business outcomes.

Like Finnegan (2021), many contract design researchers suggest contract visualization— "the use of diagrams, images, and visually structured layouts to make contracts more searchable, readable, and understandable" (Passera 2017: 19)—as a tool to improve contract quality and user-experience and to enhance collaboration among the contracting parties. Initially, Haapio and her colleagues proposed using contracts as visible scripts (Haapio & Haavisto 2005) and as road maps of the deal, and productizing and visualizing them to facilitate communication and collaboration (Rekola & Haapio 2011). Since then, the pace of contract visualization research, as well as its attraction in practice, has increased tremendously. Recently, scholars have been interested in the specific opportunities and challenges related to the use of contract visualizations (Kohlmeier & Beelen forthcoming) and the ways in which traditional concepts of contract interpretation can be applied to images in contracts (Haapio et al. 2020; Annola et al. forthcoming). Moreover, contract visualization research has expanded from visualization *in* contracts (e.g. timelines and other visual aids) and visualization *about* contracts (contract handbooks) to visualization *as* contracts (e.g. comic contracts, see de Rooy 2018; Baasch Andersen & de Rooy forthcoming; Murray forthcoming) and visualization *for* contracts (visualization tools used in negotiations and contract design processes).

One study that has been particularly influential in my research is Passera's (2017) dissertation, which focuses on contract visualization and its impacts on contract

[69] Interestingly, in the context of learning theory and contracts, Smith & King (2009) consider contracts to be "routine solutions to common problems faced by organizations" (Smith & King 2009: 31). However, over time, contracts can become increasingly less optimal solutions to specific problems (Smith & King 2009: 33). This is especially the case with contract templates. See also Note 68 and Sub-chapter 5.4.

comprehension and user experience. In addition to concrete solutions[70] for better contract comprehension and effective contract design practices, her study addresses the questions of why and how to use contract visualizations, and what approaches facilitate the adoption of contract visualizations in organizations' everyday business.[71] In addition, Passera's study contributes to the emerging discussions on the social and psycho-cognitive effects of *contract framing* by providing evidence that contract creators deliberately seek to frame information in ways that are more likely to foster collaborative, open and value-maximizing relationships (Passera et al. 2016; Passera 2017: 162). Indeed, a growing number of researchers have become interested in contract framing and its influences on exchange relationships, most of them focusing specifically on the connections between contract framing and *regulatory focus*. Next, I expand on this research.

2.8 Contract framing research

Studies that apply RFT to contracting are interested in different contract frames, their relation to personal and organizational regulatory focus, and their role in shaping exchange partners' interpretations and behavior and the interorganizational relationship (Rich et al. forthcoming: 1).[72]

Regulatory focus refers to different strategic means that people use to approach pleasure and avoid pain.[73] The concept was introduced by professor of psychology and business, Tory Higgins. According to Higgins, people have two kinds of regulatory focuses: preventive and promotive. People with promotion focus are inclined to utilize *approach* strategic means in order to attain their goals, while people with prevention focus tend to use *avoidance* strategic means in order to attain their goals (e.g. Higgins et al. 2001: 4). Regulatory focus also influences the way in which people interpret their goals: a promotive regulatory focus leads to the interpretation of a goal as maximal (meeting it would be ideal), whereas a preventive

70 Passera proposes that organizations adopt a pattern approach to contracting. She also presents six visual patterns for contracts that are, according to her, the most distinctive, recurrent and widely applicable: timelines, flowcharts, tables, swimlanes, companion icons, and delivery diagrams. See e.g. Passera 2017: 124. See also Haapio & Passera forthcoming.

71 In particular, Passera encourages organizations to use design pattern libraries, visual templates, and/or automation tools to facilitate the adoption of contract visualizations. See Passera 2017: 160–161.

72 For a comprehensive review on research on the relationship between contract framing and regulatory focus, see Rich et al. forthcoming.

73 Peoples' motivation to approach pleasure and avoid pain is called *the hedonic principle*. For more about the hedonic principle and its application in psychology, see Higgins 1997: 1280.

regulatory focus leads to the interpretation of a goal as minimal (something that must be met). Consequently, people experience different feelings when meeting or not meeting their goals, depending on their regulatory focus: Promotive focus leads to low-intensity negative emotions such as disappointment if the goal is not met, and high-intensity positive emotions such as happiness if the goal is met. Preventive focus, in turn, induces high-intensity negative emotions such as agitation if the goal is not met, and low-intensity positive emotions such as calmness if the goal is met. Although people have a dispositional or chronic tendency to view the world from either a prevention or a promotion perspective, this tendency can be overridden by a situationally or contextually induced regulatory focus (e.g. Higgins et al. 1997; Higgins et al. 2001). This means that preventive-framed statements may induce a prevention focus and promotive-framed statements a promotion focus (e.g. Roney et al. 1995; Shah et al. 1998; Weber & Bauman 2019). Finally, organizations may have their own regulatory focus (e.g. Mayer & Weber 2009).

In relation to contracts, research indicates that even though individual contract clauses or the entire contract can be framed promotively, most of today's contracts play a prevention role. Moreover, the increasing use of contract automation tools is likely to further this bias (Rich et al. forthcoming). It also seems that regulatory focus can have an impact throughout the contract's lifecycle: negotiation, design, review, performance, and management (Rich et al. forthcoming: 4). For the purposes of my research, studies of contract frames' influence on contract negotiations, exchange relationships, exchange performance, and relational governance are of particular relevance.

First, in relation to contract negotiations, people with a promotion focus seem to achieve better outcomes than those with a prevention focus (Galinsky et al. 2005; Shalvi et al. 2013; Trötschel et al. 2013; Rich et al. forthcoming). Moreover, research suggests that a negotiator's regulatory focus differs by occupation, and this must be taken into account in negotiations. For example, lawyers are presumed to frame contracts preventively because of their university education and working life expectations.[74] Thus, a lawyer might be better at planning and negotiating preventive contract clauses but IT managers may be better suited to planning exploratory tasks that often require creative and flexible contract terms and would therefore benefit from a promotively framed contract (e.g. Mayer &Weber 2009: 14–16). Most

[74] Although this is only a presumption and probably an oversimplified generalization, it sounds plausible. Lawyers are trained to mitigate risks and to prevent their clients from assuming excessive liability in contracts. Moreover, according to previous studies, experts in occupations that require similar precision to that required by legal occupation, such as bookkeepers and accountants, seem to have a preventive regulatory focus. See Mayer & Weber 2009: 14, with references.

importantly, lawyers and other contracting professionals should be trained to recognize the different ways in which a contract can be framed and their own regulatory focus, and to understand how the framing influences the exchange relationship and performance (Argyres & Mayer 2007; Weber et al. 2011; Rich et al. forthcoming). Moreover, firms should align the framing of clauses that are not task-specific with their organizational regulatory focus. Developing this kind of contracting capability is presumed to lead to sustained competitive advantage because the process is complex and thus non-imitable (e.g. Weber & Mayer 2009).

Second, in relation to exchange performance and exchange relationships, researchers have argued that different contract framings can induce a situational regulatory focus. For instance, Weber & Bauman (2019) argue that "contracts that frame goals as obligations and describe safeguards in terms of penalties may induce a prevention focus, and contracts that frame goals as opportunities and describe safeguards in terms of rewards may induce a promotion focus" (Weber & Bauman 2019: 363). Consequently, contract frames can be exploited in exchanges requiring different behaviors: for example, preventive contracts are better suited to mission-critical exchanges in which the failure of a task has a significant negative impact on the exchange or on the exchange partners, and the performance of a specific transaction is more important than continuing the relationship between the organizations. However, if a task is considered to be exploratory, i.e. when the supplier is developing something new or using an untested technology to create new functionality, or the parties seek a collaborative, longer-term relationship, one should select a promotive contract, sometimes even when the framing contradicts the task type (Mayer & Weber 2009: 12–13; Weber et al. 2011: 196–198; Weber & Mayer 2011: 58–61). Promotion-framed contracts are also better suited when the supplier suspects in advance that it may not be able to meet the performance expectations during the exchange (Weber & Mayer 2011: 65). Finally, promotion-framed duration clauses[75] seem more appropriate than preventively framed duration clauses[76] in exchanges with great geographical distances, or when the quality of the delivery is hard to measure, prior projects have involved the same customer, and the technology can be reused in the future (Weber et al. 2011). In essence, research suggests that the optimal framing of a contract depends on transactional attributes and the desired type of interorganizational relationship. If the contract frame, the transactional attributes

[75] Promotion-framed duration clauses refer to provisions that allow a party to unilaterally renew a contract on the condition that the other party performs well (Weber et al. 2011: 183).

[76] Preventively framed duration clauses are early termination clauses that allow one party to unilaterally terminate the contract before its initial end date if the other party does not meet prespecified conditions or its performance is unsatisfactory (Weber et al. 2011: 183).

and the desired relationship type are aligned, contracts can positively impact both the exchange relationship and exchange performance (Weber & Mayer 2011: 73). However, if the clause framing does not match the transactional attributes and the desired type of relationship, the contract—be it promotively or preventively framed––may be detrimental to the ongoing relationship (Weber et al. 2011: 199).

Third, research on contract framing contributes to the ongoing discussion on the relationship between contracts and relational governance, presented in detail in Subchapter 2.4. Studies have been particularly interested in how contract framing influences the development of trust and other relational governance. Initially, Mayer & Weber (2009) and Weber & Mayer (2011) proposed that promotively framed contract clauses can induce trust and complement relational governance, whereas preventively framed contract terms substitute trust and relational governance. In the context of franchise contracts, Bertrandias et al. (2010) corroborated these suggestions and found that, first, promotion-oriented contracts induced a higher level of goodwill trust[77] in the franchisor than prevention contracts. Moreover, it seemed that in promotion-framed contracts, perceived completeness positively influenced trust while such influence was not found in prevention-framed contracts. Finally, they found that perceived franchisor control negatively affected trust in prevention contracts but had no influence in promotion contracts. More recently, Weber (2017) has theorized that different types of trust develop in repeated exchanges through learning, which is influenced by contract frame and other cognitive elements (such as intergroup attributional bias[78] and partner explanations of trust violations). This, in turn, has an influence on whether contracts act as complements or substitutes to specific types of trust (Weber 2017: 756). A recent study by Weber & Bauman (2019) empirically verified that promotively framed contracts induced more trust than preventively framed contracts, but also found that both contracts increased the level of trust in comparison to a no-contract situation, again providing proof of the complementary view.

Although the dichotomous division between promotion and prevention frames might be too simplistic in the context of contract framing—and more studies are

77 Organizational and management scholars have defined trust as "the willingness of a party to be vulnerable to the actions of another party based on the expectation that the other will perform a particular action important to the trustor, irrespective of the ability to monitor or control that other party" (Mayer et al. 1995: 712). The concept of trust has been further divided into competence trust, which refers to the partner's ability to perform according to agreement, and goodwill trust, that is, the partner's intention to perform according to the agreement (e.g. Nooteboom 1996: 990).

78 Intergroup attributional bias refers to group members' tendencies to make external attributions for their partner's positive behavior and internal attributions for their partner's negative behavior. This bias is very common in interorganizational exchanges (Weber 2017: 748).

needed to explore, first, the interaction between different framings in a single contract, and second, their mutual effects on exchange relationships—the research on contract framing underlines important and previously understudied issues in contract design. In sum, this research suggests that a negotiator's or organization's chronic regulatory focus influences the way in which contract negotiations proceed and contracts are designed. Thus, negotiators, as well as organizations, should be aware of their own regulatory focus and exploit this focus in negotiations and contract design processes. At times, they might need to adopt a contextually induced regulatory focus that best fits the exchange at hand and which might differ from their own regulatory focus. In addition, prevention and promotion frames should be used intentionally to match the requirements and expectations of the exchange relationship and exchange performance. The influences of contract frames on trust and other relational governance mechanisms should already be taken into consideration in the early phases of contracting to enable contracting professionals to use contract framing strategically (Weber & Bauman 2019: 379; Rich et al. forthcoming: 2). In fact, Rich et al. (forthcoming: 15–16) encourage organizations to develop a new job function of "relationship manager"; someone to actively manage negotiator and contract frames and to match them with exchange characteristics and the desired relationship type.

2.9 Section summary and my entry point

Contracting research has undergone many transformations over the last two centuries. The neoclassical economic model characterized by the artificial Leviathan idea of humans as rational decision-makers, *homo economicus*, and the system of classical contract law that was based on the idea of a discrete market exchange with no social ties between the exchange parties, was first complemented by the neoclassical contract law of legal realists and finally by the relational contract theory. In economics, the ideas of the relationalists were followed by the ideas of transaction cost economist Oliver E. Williamson, who was interested in the comparative study of different governance modes of exchange relations. Like relational contract theory, TCE is interested in the social contexts of transactions and offers normative guidance on how to choose an optimal governance model for a specific transaction. The basic argument of TCE is that because organizations (as well as the people within the organizations) are only boundedly rational, *homo psychologicus*, and often act out of self-interest or opportunism, and because specific transactional attributes form exchange hazards that enable opportunism, exchanges need to be governed by different governance modes, ranging from markets to the firm.

Although TCE is arguably one of the most influential economic theories of our time[79] and has been widely tested and applied in economics as well as in other disciplines, it does not account for all choices related to the governance of transactions. In this chapter, I have discussed research streams which, while building on relational contract theory and TCE, also further develop them and even criticize some parts of TCE.

To begin with, the relational view focuses on the interplay between relational governance, such as trust, and formal governance, such as contracts, and argues that formal governance is not sufficient for governing interorganizational relationships. Some have even claimed that it would be more beneficial for organizations to use only relational governance to guide exchanges. Most proponents of the relational view, however, call for the combined use of both governance mechanisms, because rather than substituting each other, formal and relational governance actually complement one another.

The functional approach to contracting also emphasizes other coexisting functionalities of contracts, such as coordination and adaptation, along with the safeguarding function, and is interested in the relationship between contractual functions and relational governance, and their mutual effects on the exchange relationship. In essence, these studies suggest that clauses that serve different functions have distinct effects on relational governance and the exchange relationship. For instance, coordinative contract clauses can support the development of trust whereas the excessive use of safeguarding clauses can erode trust.

Moreover, the proactive contracting approach underlines the positive, proactive dimensions of contracts by conceptualizing them as tools to promote business success, to foster collaboration, and to prevent problems. Recently, proponents of the proactive approach have applied design-based methods to study contracts and contracting, and have been particularly interested in questions such as how to design contracts that can be used for an organization's competitive advantage and how contract design choices affect exchange parties' attitudes, behavior and the exchange relationship.

Finally, recent studies have been particularly interested in different contract frames, their relation to personal and organizational regulatory focus, and their influence on shaping exchange partners' interpretations, behavior and interorganizational relationship. These studies suggest that the contractual frame must be selected on the basis of, for example, transaction attributes, task characteristics and the type of relationship desired.

79 Oliver E. Williamson was awarded the 2009 Nobel Memorial Prize in Economics for his work related to TCE. See Nobel Media AB 2021.

In sum, although the focus of both organizational and management studies, as well as contract law scholarship, has shifted from calculative neoclassical economics and formal, classical contract law toward relationally oriented theories that recognize humans' limited abilities and their desire for collaboration, and regard contracts as tools for supporting relational governance and collaboration, the different theoretical approaches have developed in their own foxholes. My aim is to find the common denominators of these theories in order to analyze how organizations use contracts in their interorganizational exchange relations. Figure 3 below depicts my understanding of the transactional attributes and contract design choices that characterize interorganizational exchange relations.

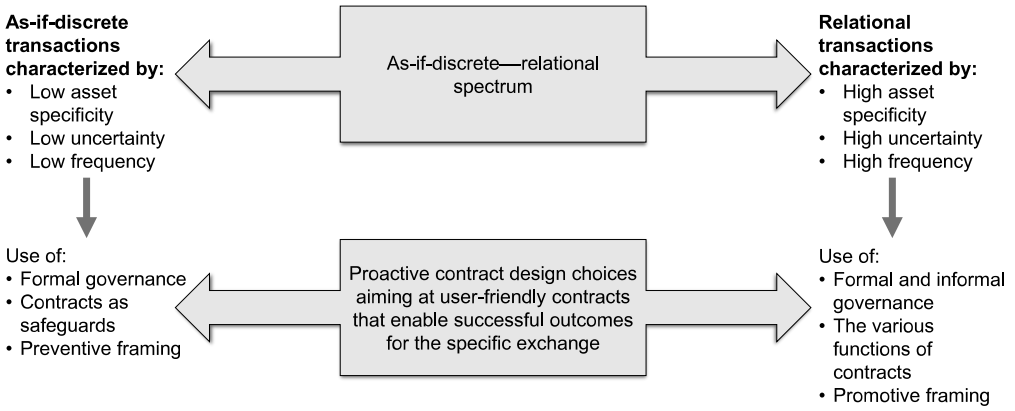

Figure 3. Characteristics and contract design choices of interorganizational exchange relations.

The figure draws on relational contract theory (the as-if-discrete—relational spectrum), TCE (the transactional attributes listed under the as-if-discrete and relational transactions), the proactive contracting approach, contract design research, the relational view, the functional approach to contracting, and RFT. It illustrates the different aspects that need to be taken into account when studying interorganizational exchange relations and their contract design choices. In my view, all interorganizational exchange relations are situated on the as-if-discrete—relational spectrum and are characterized by different transactional attributes. These are the macro-level theories that influence the contract design choices of interorganizational exchange relations. Depending on the transactional attributes on the one hand and on the location of the exchange in the transactional-relational spectrum on the other, user-friendly contract design choices should be guided by the proactive contracting approach. In transactions that fall closer to the as-if-discrete end of the spectrum, organizations may rely more on formal governance, use contracts as safeguards, and frame contracts preventively. In cases of relational exchanges, in turn, organizations

may use both formal and informal governance, utilize the various functions of contracts, and frame contracts promotively. This theoretical positioning guided my research process throughout the individual sub-studies reported in the Publications. Next, I move on to describe my methodological standpoint.

3 Research design

3.1 Research methodology: American New Legal Realism

Methodologically, this study embraces American New Legal Realism (ANLR), which emerged in the US at the turn of the 1990s and is rooted in "traditional" or "old" American Legal Realism (ALR)[80] (e.g. Alexander 2002; Erlanger et al. 2005; Nourse & Shaffer 2009; Suchman & Mertz 2010; Malminen 2016; Talesh et al. 2021; Poppe 2021). Consequently, following the work of, for example, Stewart Macaulay[81], I am committed to the following views that characterize ANLR research.[82]

[80] The golden days of ALR were in the late 1920s and 1930s in the Columbia Law School and Yale Law School (e.g. Alexander 2002; Malminen 2016). ALR can be seen as a continuation of early twentieth century progressivism (e.g. Alexander 2002; Nourse & Shaffer 2009; Poppe forthcoming; Talesh et al. 2021). For more on the rise and fall of ALR, see e.g. Schlegel 1979. For the history of ANLR, see e.g. Erlanger et al. 2005; Macaulay 2005; Nourse & Shaffer 2009. For a comparison between ALR and ANLR, see e.g. Macaulay 2005; Nourse & Shaffer 2009.

Europeans have also had their own realist movement, the Scandinavian legal realist movement, followed by the European New Legal Realist movement (ENLR). For a comparison of ALR and Scandinavian legal realism, see e.g. Alexander 2002. For the ENLR, especially in the context of international law, and the differences between ANLR and ENLR, see e.g. Holtermann & Madsen 2015; Holtermann & Madsen 2021. Scandinavian legal realism can be seen as a version of legal positivism and both European realistic movements are more concerned with philosophical and epistemological issues in legal science than their American counterparts. I identify myself with ANLR because of my empirical, pragmatic and limitedly positivistic research stance. For a critical perspective of both new realist movements, see Augsberg 2015.

[81] For more on the work of Macaulay, see Sub-chapter 2.3.1.

[82] For a recent volume on New Legal Realism, see Talesh et al. (eds) 2021. See also Mertz et al. (eds) 2016; Klug & Merry (eds) 2016.

I am primarily interested in the *living law*[83] or the *"private governments"* (Macaulay 2006: 1169) of contracting parties—in other words, the contracts and other governance mechanisms that actually direct the behavior of the parties in interorganizational exchange relations. However, despite my interest in the law-in-action approach[84], my purpose is not to deny the potential of doctrinal studies of contract law; it is to examine them critically (Erlanger et al. 2005: 345). The following reference from Macaulay (2016) reflects my stance on the potential and power of law and doctrinal studies:

> "Sometimes rules of law do work in a large percentage of situations. Sometimes they do not. New legal realism recognizes this and demands that we put doctrine in its place." (Macaulay 2016: 153)

Consequently, I chose to study the contracting practices of interorganizational exchange relationships empirically, using a bottom-up approach[85] embraced by ANLR. Moreover, I chose my research designs and methods *pragmatically*[86], based on the problems that needed solving and the questions in which I was interested. Finally, following ANLR's pluralistic view, my research is interdisciplinary and uses

83 Indeed, American New Legal Realists understand law as the living law referred to by Eugen Ehrlich as follows: "…law which is not imprisoned in rules of law, but which dominates life itself. The sources of its knowledge are above all the modern documents, and also immediate study of life itself, of commerce, of customs and usage, and of all sorts of organizations, including those which are recognized by the law, and, indeed, those which are disapproved by the law." (Page 1977: 39, quoting Ehrlich's description of the living law). Hence, the focus of ANLR is "on more relational, contingent, context-sensitive, or process-based understandings of law, where law is both dependent variable and independent variable" (McCann 2016: xv). Moreover, the law itself is recognized as power—"as language/discourse, as institutional practices, as aspirational ideals, as actual or potential enforcement by state violence, and so on…" (McCann 2016: xv). See also Talesh et al. 2021: 9.

84 The living law approach and the law-in-action approach are sometimes said to mean different things. For a discussion of the living law approach and the law-in-action approach in the context of ANLR, see Macaulay 2005.

85 Bottom-up approach means that the impacts of law and legal phenomena are studied empirically from the grass-root level. This approach provides voice for people affected by legal phenomena (e.g. Erlanger et al. 2005: 339–341). See also Nourse & Shaffer 2009; Suchman & Mertz 2010.

86 According to pragmatism, the best way to resolve a problem is to act (Erlanger et al. 2005: 356–357). For more about ANLR and pragmatism, see Erlanger et al. 2005; Nourse & Shaffer 2009; Suchman & Mertz 2010. For more about pragmatism in the context of contract design research, see Passera 2017: 100–101.

versatile methods to study contracts and contracting in "the real world" (e.g. Talesh et al. 2021: 14).[87]

Further, although I acknowledge that my own ideological views and beliefs have influenced the research themes I have decided to study, I have committed myself to limited positivism, according to which humans can, to some degree, see and understand in a positivist sense the physical world outside their own psyches, including human behavior and institutions (Macneil 1983: 408). In fact, unlike the proponents of some stricter forms of constructionism, I believe that it is possible to gain knowledge that is to some extent free of the researcher's own preferences and ideologies (Macneil 1983: 408). However, I also admit that situated knowledge underlines the role of the social scientist as a human and political being in shaping research outcomes, irrespective of the methods used in the study (e.g. Erlanger et al. 2005: 342–343).

Acknowledging these limitations that I face as a researcher and in order to secure the scientific rigor of my research, I critically reflected on my own motives and prejudices throughout the research process (e.g. Erlanger et al. 2005: 342–343). Consequently, having examined the contracting practices of a very limited number of organizations, mostly from the perspectives of relational, proactive and functional contracting, and by acquiring data from organizations through qualitative methods, I realize that I can provide only a tentative illustration of current contracting practices in certain fields of businesses. Reiterating Macaulay (2005: 396), I can only offer a provisional and qualified picture of the contracting realities of the companies I studied. Therefore, I hope that my findings will be tested, challenged and complemented. Ultimately, my aim is to answer to the call for more robust, theoretical, empirical, and multidisciplinary contract research (e.g Berger-Walliser 2012: 31; Haapio 2013: 88; Passera 2017: 172–174; Nystén-Haarala 2017: 1033; Nuottila 2019: 37–38).

3.2 Data collection and analysis

3.2.1 Collaborative and explorative action research (Publications I and II)

Publications I and II were co-authored by Magnus Gustafsson, Maria Ivanova-Gongne, Johanna Liinamaa, Hanna Luotola, and Mika Viljanen.[88] The aim of the

[87] ANLR scholars believe that it is the research questions that direct the choice of methods and thus, qualitative, quantitative and experimental methods are valued. See e.g. Suchman & Mertz 2010: 562.

[88] For my contributions to Publications I and II, see Annex 1.

research project reported in Publications I and II was, first, to explore the possible solutions to the challenges our case company faced when developing a new business model using value-based selling techniques[89] and performance-based contracts[90] (reported in Publication I); and second, to examine how the functional contracting approach could facilitate the creation and governance of a business network that was a prerequisite for the successful implementation of the new business model (reported in Publication II).

The research problem directed us to use *explorative action research* as our method of study and analysis (e.g. Lewin 1946; Susman & Evered 1978). Action research is rooted in American pragmatism and has been developed by social psychologist Kurt Lewin. He initiated the "Harwood studies", which focused on the problem of employee turnover in the Harwood Manufacturing Corporation (e.g. Lewin 1946, 1948; Burnes 2007).

Lewin (1946) characterized action research as "comparative research on the conditions and effects of various forms of social action, and research leading to social action" (Lewin 1946: 35). In other words, action research has dual objective: first, it aims to produce scientific knowledge on social action. Second, it aims to solve practical problems by social action (e.g. Clark 1980; 152; Heikkinen 2001: 170–171).

The research was conducted in a large team that consisted of researchers from fields such as law, industrial management, design, and marketing. Company representatives ranged from managers to sales personnel and from technical engineers to in-house counsels. In addition, consultants specialized in industrial investments and project business were part of the team. The research project started at the end of 2013 and lasted until June 2015. During the project, we held tens of meetings that dealt with the project in general and with the productization of the company's new business model. In addition, we organized trainings and followed up the sales cases. Figure 4 presents the most important events, meetings and data of the research project.

89 For the definition of value-based selling, see Note 15.
90 For the definition of performance-based contract, see Note 16.

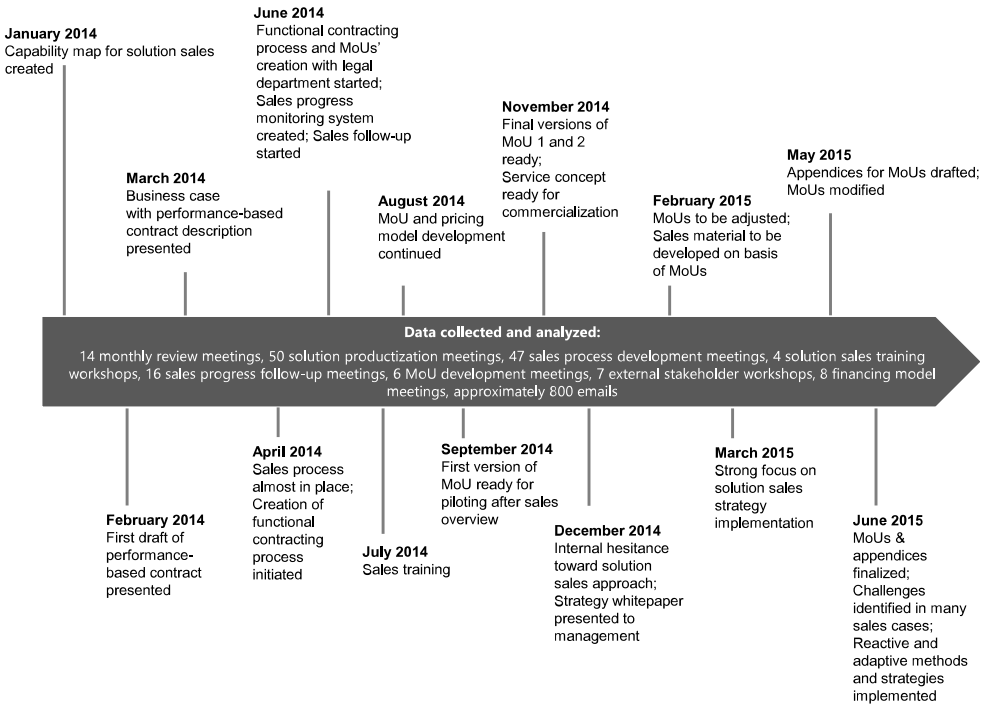

Figure 4. Most important events, meetings and data of research project. Adapted from Publication I. Used with permission.

The research project proceeded as a cyclical process, as we followed the five phases of action research described by Susman & Evered (1978): diagnosing, action planning, action taking, evaluating, and specifying learning (Figure 5).

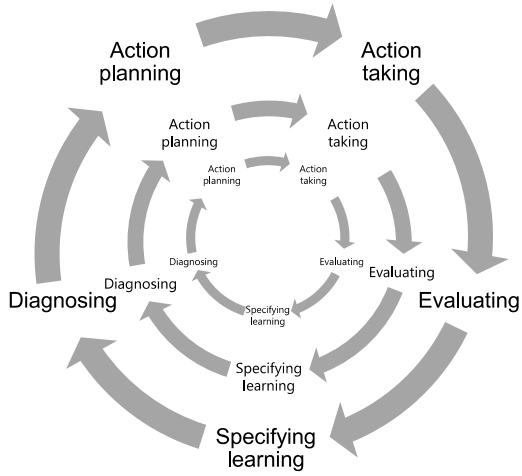

Figure 5. Cyclical action research process.

Data analysis was conducted throughout the research process. More specifically, in the diagnosis phase, the researchers held meetings and in-depth discussions with key representatives of the company and reviewed the relevant background documentation. In the action planning phase, the researchers reviewed the relevant literature on value-based sales, contracts and contracting, and interorganizational integration. The relevant literature was then presented and reviewed with company representatives to determine different possibilities for action. From this, the company chose to develop a value-based sales process and a functional contracting process to implement its new business model. We co-designed the sales and contracting processes together with the company representatives, participated in negotiations with selected customers, and provided sales training to the sales personnel of the company. In the last two phases of the process (evaluating and specifying learning), we analyzed the memos and feedback from business cases, reviewed the evolving sales training workshops, and revised the sales and the contracting processes with the organization's sales manager, solution designer, and legal department. The entire research team also discussed the commonalities of individual case findings. Finally, to disseminate and elaborate on the scientific findings of the research project, six researchers, including myself, wrote Publications I and II.

3.2.2 Expert interview study (Publication III)

Publication III, co-authored with Sampo Viding, focuses on the relationships among relational governance, contract functions, and interorganizational relationship performance.[91] In order to understand these phenomena, we designed a theory-generating expert interview study that comprised 23 interviews of 24 contract experts. We defined "contract expert" as a person who regularly works with contracts, for instance with contract drafting, contract negotiations, and contract execution. Thus, educational background or formal training was not of importance to us. Rather, we were interested in the knowledge that the interviewees had acquired through their concrete work with contracts (Korkea-aho & Leino 2019: 31).

We chose to conduct theory-generating expert interviews mainly for two reasons. First, we wanted to interview contract experts because we were interested in their interpretative knowledge of their organizations' contracting practices. Interpretative knowledge refers to the expert's subjective orientations, rules, viewpoints, and interpretations that influence the actions of other actors in the expert's field. In other words, the contract expert's interpretative knowledge affects the ways in which other contract experts and organizations use contracts (Bogner & Menz 2009: 53–55) and

[91] For my contribution to Publication III, see Annex 1.

thus, contract experts are also permitted to speak as representatives of their respective organizations (Littig 2011: 1344).

Second, our aim was to *theorize* on contract experts' views on contracts and their relationship among relational governance and interorganizational relationship performance (Bogner & Menz 2009: 48). The theory-generating interview method seemed to fit our research objectives because it "seeks to formulate a theoretically rich conceptualization of (implicit) stores of knowledge, conceptions of the world and routines, which the experts develop in their activities and which are constitutive for the functioning of social systems" (Bogner & Menz 2009: 48).

We selected the interviewees based on a survey study that we conducted in autumn 2016 with 65 contract experts working in companies that at some point had participated in DIMECC's (formerly FIMECC) research programs.[92] At the end of the survey, all the participants were asked to indicate whether they would be willing to participate in the interview study. We phoned those who had indicated their willingness and explained the purpose of the study and agreed on a date for a face-to-face interview. Before the interview, we emailed the interviewees the interview themes[93] and a unilateral confidentiality agreement[94]. Some of the participants wanted to amend the confidentiality agreement before the interview and we agreed to these amendments. Nine lawyers, two contract managers (one of whom was also a lawyer), five procurement professionals, four sales professionals, two chief executive officers (CEOs), and three other types of professionals who regularly dealt with contracts participated in the study.

The semi-structured interviews were conducted during autumn 2016 by myself and my colleague Sampo Viding. I was the sole interviewer in 12 interviews and my colleague in one interview. The rest of the interviews we conducted together. All the interviews except for one were individual interviews. One interview was a group interview with two interviewees. At the start of the interview, we introduced ourselves and the research project, went through the confidentiality agreement and explained the privacy and anonymity practices to the interviewee(s). All the interviews lasted approximately one hour, were conducted in Finnish, and were tape-recorded. After the interviews, the recordings were transcribed verbatim and the transcriptions were coded in NVivo 11.

92 FIMECC was a strategic center for research in the Finnish metals and engineering industries. In 2016, FIMECC merged with DIGILE, and the company changed its name to DIMECC. By 2016, 137 companies had participated in FIMECC's research programs.

93 On file with author in Finnish.

94 On file with author in Finnish.

The coding and the analysis process followed the six phases of thematic analysis of Braun & Clarke (2006: 86–93). Table 2 presents the phases of the coding and analysis process and the way in which we applied them in our study.

Table 2. Phases of thematic analysis applied in Publication III.

Phase	Actions taken in each phase of the study
1. Familiarizing yourself with your data	We read through the transcriptions, listened to the recordings, and corrected the transcriptions when necessary.
2. Generating initial codes	We designed the first coding scheme based on the interview themes that were theory driven. Thereafter, we wrote summaries of the interviews to ensure that the coding scheme reflected the contents of the interviews.
3. Searching for themes	We examined the data extracts from the codes that were relevant to our research questions and formed initial themes and sub-themes, as well as their descriptions.
4. Reviewing themes	We compared the themes with our data extracts and recoded the data, this time selectively, based on the themes and sub-themes identified in the previous phase. We also generated a thematic map that organized the themes hierarchically.
5. Defining and naming themes	We revised the themes, their names and their definitions.
6. Producing the report	We wrote Publication III.

3.2.3 Contract document analysis (Publication IV)

Publication IV describes the functions by which companies use contracts and the ways in which contracts are framed. In the study, I analyzed ten purchase contract documents of companies that participated in the interview study discussed in the previous sub-chapter.

I obtained the purchase contract documents by asking the interviewees to send me examples of their company's contract documents. Representatives of eight companies sent me a total of nine contract templates, one actual signed agreement, and eight standard terms and conditions (T&Cs). The contract templates ranged from research and development (R&D) contracts and cooperation agreements to service supply agreements and purchase agreements. For Publication IV, I chose to analyze the purchase contract templates and standard T&Cs. Ultimately, the analyzed

documents covered six purchase contract templates and four standard T&Cs. Two of the contracts were in Finnish and eight were in English.[95]

I began the analysis process by reading through the documents in order to develop an overview of the contracts. I then reread the contracts and concentrated on the specific clauses, their functions, and their relations to other clauses. My analysis was informed by concept-driven qualitative content analysis, in which the coding categories or themes are derived from previous knowledge, such as a theory, as was the case in my study (Schreier 2012: 84–87; Schreier 2014: 178).

Initially, the functional categories used in the analysis process were derived from the functional contracting approach and were the same as those identified in Publication III: safeguarding, codification, coordination, adaptation, internal management, and collaboration. However, as is usual in content analysis (Schreier 2012: 87; Schreier 2014: 178), the concept-driven categories were complemented by a new, data-driven category, which will be presented and discussed in greater detail in Sub-chapters 4.3 and 5.1. After the first coding, I recessed the analysis process for two months. Then, I recoded the contracts blindly. I also revised the new, data-driven category based on the feedback given by the anonymous reviewers, and adjusted the coding accordingly.

Finally, I analyzed the contracts in terms of their framing. Again, this analysis was concept driven as rested on two contract frames introduced by RFT: preventive and promotive.[96] However, I complemented these categories by data-driven categories and ultimately, I classified the framings as either preventive, promotive, collaborative, one-sided, or contradictory.

3.3 Ethical reflections and data management

In Finland, researchers in all disciplines are guided by general ethical principles, such as respect for the dignity and autonomy of human research participants, respect for material and immaterial cultural heritage and biodiversity, and commitment to conduct research in a way that does not cause significant risks, damage or harm to research participants, communities or other subjects of the research (TENK 3/2019: 8). Moreover, all scientific research in Finland must comply with the guidelines for the responsible conduct of research (TENK 2012) drawn up by the Finnish National Board on Research Integrity, TENK. Finally, all research on humans and human

[95] The analysis process only covered the express, visible terms of the contract documents and ignored the implied or invisible terms which are also part of the contract. For more about express and invisible terms and their relation to contract literacy, see e.g. DiMatteo et al. 2012: 72–73; Haapio 2013: 43–45; Annola et al. forthcoming: 2–3.

[96] For more about RFT in the context of contract framing research, see Sub-chapter 2.8.

behavior must follow the ethical principles of research with human participants (TENK 3/2019). The ethical principles require, for example, that participation in research is voluntary and that the participants give informed consent for their participation. Moreover, participants should receive understandable and truthful information about the research and the potential benefits, harms and risks related to it (TENK 3/2019: 10). In addition, the ethical principles guide the processing of personal data in research, the protection of privacy in research publications, and the openness of research data (TENK 3/2019: 12–16). Next, I describe the means that I, in collaboration with my research colleagues, used in the sub-studies to adhere to the guidelines and principles mentioned above.

In regard to the informed consent and the voluntary nature of research, the case company of Publications I and II participated in the DIMECC REBUS research program[97] voluntarily and signed a consortium agreement. In addition, the project team of the company was formed of voluntary employees. The team was fully aware of the research project, as it participated in the planning of the project in collaboration with the researchers.

As explained in Sub-chapter 3.2.2 in relation to Publication III, the interviewees volunteered to participate in the study by expressing their willingness to be interviewed at the end of the survey study. Before the interviews, we contacted the interviewees by phone and explained the purpose of our study and highlighted that participation would be fully voluntary and that the findings would be reported in a manner that individual respondents or the companies they represented could not be identified. Furthermore, the interviewees were given a unilateral confidentiality agreement before the interviews. Therefore, the participants gave their informed consent to participate in the study even though we did not ask them to sign a written informed consent form.

Regarding the rights of the participants to receive information on the content of the research, the processing of personal data and how the research is to be conducted in practice, in the case of Publications I and II, they received this information at the beginning of and during the research project, and in the case of Publications III and IV, during the phone call and again at the start of their interviews.

Furthermore, I aimed to respect the principles of avoiding harm in research and the principles related to the processing of personal data by first managing the data carefully. In regard to Publications I and II, all data were stored in the secured cloud service of Åbo Akademi (OwnCloud) and could not be accessed by any unauthorized persons. Regarding Publications III and IV, the interview recordings, transcripts, contract documents, and all analysis data were stored in the secured cloud service of

97 For more about the DIMECC REBUS research program, see Note 11.

the University of Turku (Seafile) and could not be accessed by any unauthorized persons. Moreover, in relation to Publications I and II, we only gathered and processed personal data to contact the participants and report on our findings. In the case of Publications III and IV, the interviewees, as well as the companies that they represented and the companies that provided us with the contract documents, were kept anonymous. I deleted all personal or confidential data as soon as it was reasonable in terms of the research. The transcribed interviews as well as the contract documents are still stored in the secured cloud service of the University of Turku (Seafile) where no unauthorized persons can access them. This is in case I am asked to verify the interviews or the contract documents. The transcribed interview data do not include any direct identifiers or personal information about the interviewees.

Second, I tried to analyze the data and report the findings in a way that respects the views of the research participants. In the case of Publications I and II, we also offered the participants the opportunity to comment on the draft articles before they were published. Moreover, in accordance with the DIMECC REBUS consortium agreement, we provided all consortium parties with the opportunity to object to the publication of Publications I and II. In the cases of Publications III and IV, my colleague Viding and I promised to send a report of the preliminary findings to the participants for comments before it was published. However, because of time constraints, we did not write a written report on the preliminary findings. Instead, we organized a seminar during which we discussed the findings orally. We invited all the participants to the seminar. Afterwards, we wrote Publication III, and I wrote Publication IV. In retrospect, in the case of Publication III, we could have offered the participants the opportunity to comment on the article before it was published. I did send the published article to each participant, along with a draft version of Publication IV.

To protect the privacy of the research participants (both the companies and their employees) in the Publications, we used a pseudonym for the case company in Publications I and II. In Publications III and IV, the extracts from the interviews, as well as the contract extracts, were modified when necessary, and the names of the interviewees and companies and the dates and places of the interviews were omitted.

Finally, in accordance with the DIMECC REBUS consortium agreement, no data used in this research are publicly available.

4 Summary of results

This chapter presents a summary of the findings reported in Publications I–IV. Throughout the chapter, I focus on the findings that directly relate to the main research question posed in this summary.

The results indicate that companies use contracts to serve various functions such as safeguarding, codification, adaptation, coordination, internal management, policy, and collaboration. They also show that these functions, as well as the framing of the contract clauses, have distinct effects on relational governance, satisfaction with the exchange relationship, and overall relationship performance. When contracts are designed and used intelligently, i.e. in the *proactive, functional frame*, they can facilitate precontractual integration, complement relational governance, and support the creation and governance of collaborative interorganizational exchange relations. Yet the findings suggest that today, organizations favor preventively framed contracts and focus mainly on safeguarding their own interests, sometimes at the expense of their contracting partners. This is alarming, because research shows that excessive use of safeguarding clauses and one-sided contracts can be destructive to the interorganizational relationship and the exchange as a whole.

4.1 Functional contracting for network creation and governance (Publications I and II)

Publication I explored the challenges faced in the implementation of a new business model that incorporated performance-based contracts and value-based selling techniques. Furthermore, it studied how the *functional contracting process* could facilitate the *precontractual integration* of the seller and buyer organizations that was required in order to overcome these challenges. In this context, integration referred to the coordination and adaptation of organizations' activities on several levels and with multiple tools, "bringing or joining together a number of distinct things so that they move, operate and function as a harmonious, optimal unit" (Kirsilä et al. 2007: 715). Publication II, in turn, examined the same phenomena on the level of business networks, i.e. how the functional contracting process could facilitate network creation and governance. Because the findings presented in both

Publications differ only slightly in regard to their context and focus, I will present them together.

To begin with, we discovered that a number of challenges must be overcome for the transition to a business model that includes performance-based contracts to be successful. Most of these challenges had already been identified in previous research (e.g. Töytäri & Rajala 2015; Töytäri et al. 2015). For example, like Töytäri et al. (2015), we found that network participants were resistant to the new pricing model included in the performance-based contract. This is because it disrupts the dominant, cost-plus pricing approach, which is based on discrete value-creation processes and requires deep collaboration between network members. Studies suggest that this kind of resistance can only be overcome in certain circumstances and by concerted, well-designed marketing efforts that are implemented consistently (e.g. Töytäri et al. 2015).

In particular, we identified *legal-technical contract design issues* as an important but previously unknown challenge to this kind of business model transition. Firstly, the performance-based contracts that were used to formalize the solution offering of our case company were complex and expensive to design. In fact, we discovered that the transaction costs of these contracts may actually prohibit the use of the new pricing model. In our case, for example, the key performance indicators (KPIs) that would be needed to calculate the increase in the financial performance of the customer proved to be complex to map and difficult to formalize into well-functioning contract clauses. Secondly, the introduction of this new, untested contract model triggered disinclination in legal departments, probably because they posed new kinds of risks, which most lawyers are trying to avoid or mitigate (e.g. Haapio 2013: 1). Moreover, performance-based contracts contradict the classical contract law structures adopted by most lawyers, which stress unambiguity, completeness, and certainty, and regard contracts as static allocations of rights and obligations (e.g. Macneil 1978: 862–865).

Furthermore, we found that because of the legal-technical challenges related to the new business model, the company had to convince the customer to accept the new pricing model along with its contract structure. Because the company had no established tools for this, the project team designed new sales and contracting processes to facilitate the precontractual integration and overcome the identified challenges. In particular, we deployed the idea that contracts can be used in the *functional frame* to allow network participants to align their sales and purchasing processes and to synchronize their value perceptions. This process would also help our case company present the benefits of the new value-sharing arrangement to the network participants. The end result was a value-based selling process and a functional contracting process, illustrated in Figure 6.

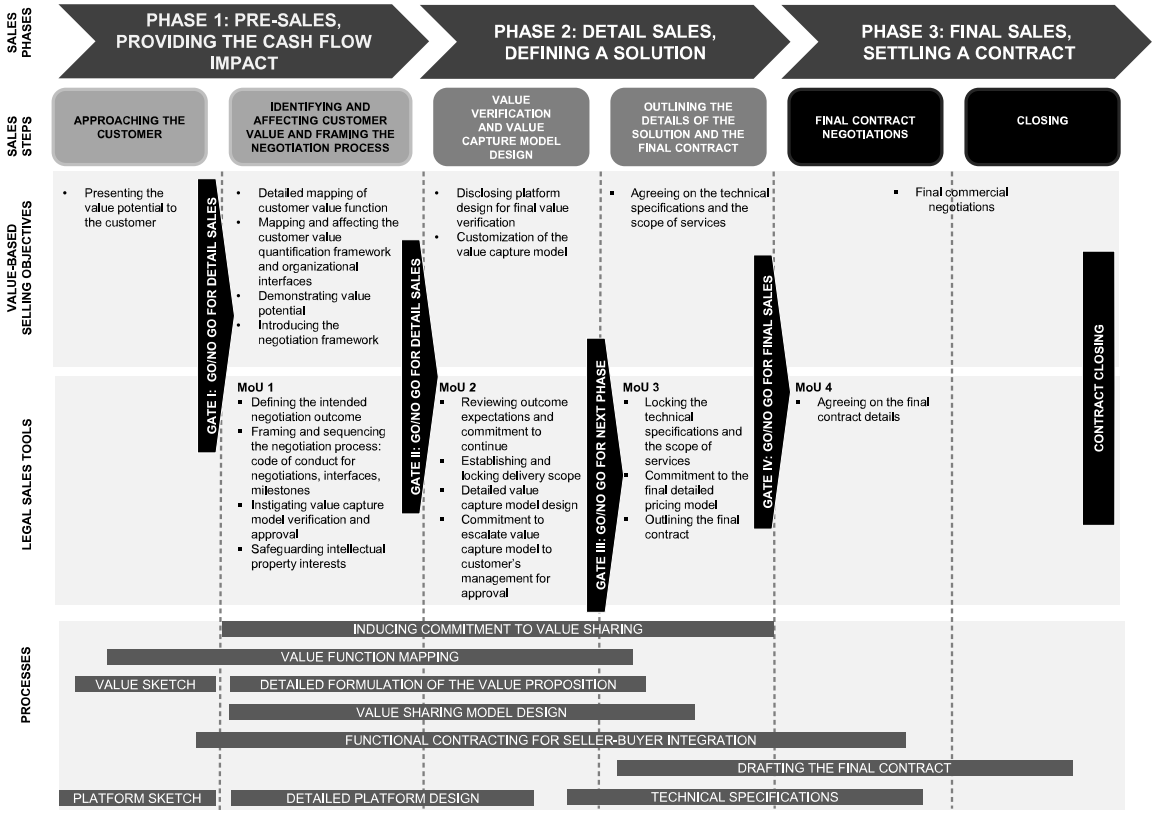

Figure 6. Value-based sales process and functional contracting process designed for case company. Adapted from Publication I. Used with permission.

The functional contracting process deploys safeguarding, adaptive, coordinative, and collaborative memoranda of understanding (MoUs), which break down the sales and negotiation processes into phases and allow the compartmentalization of the specific challenges the company expected to encounter during each phase. For example, MoU 1 sought to establish the new sales process within the case company and influence parties' behavior during negotiations, creating an honest negotiation space. MoUs 2 and 3, in turn, attempted to force a new customer interface by requiring the customer to commit to having their board approve the new pricing model. Furthermore, the MoUs aimed to eliminate opportunistic behavior by leveraging the contractual sanction mechanisms for unauthorized use of the case company's designs. In essence, the functional contracting process was designed to *complement* our case company's relational integration efforts and to increase trust between network participants. Moreover, it was targeted not only toward the customer's frontline employees, but also its executive-level decision-makers.

Based on the findings, we argue that the functional contracting process may be a key precontractual integration mechanism to overcome the challenges related to the introduction of a new business model that includes performance-based contracts. In essence, adopting a functional contracting process along with a value-based sales process changes negotiation tactics. They change from a win–lose game, in which the negotiating parties are viewed as adversaries and the contract is seen as a mere safeguarding tool, to a win–win situation, in which the parties strive for a mutually beneficial solution and the contract is a tool for coordination, adaptation and collaboration.

Finally, our findings indicate that the adoption of the functional contracting process requires not only interorganizational but also intraorganizational and cross professional collaboration. For example, legal, sales, procurement, execution, business, and product development professionals should be involved in the contracting process. More specifically, lawyers should proactively engage in the business and product development processes, taking on a forward-looking role in developing flexible and creative legal governance structures for emerging business models. In relation to this, business functions have to recognize that lawyers may substantively contribute to business development.

4.2 The various functions of contracts and their effects on relational governance and interorganizational relationship performance (Publication III)

Utilizing the interview data of 24 contract experts, Publication III focused on the relationships among relational governance, contracts and interorganizational relationship performance. More specifically, it aimed to answer the following research questions:

1. What are the functions by which companies use contracts to govern interorganizational relationships?
2. How does a contract and its different functions affect relational governance (or vice versa) and interorganizational relationship performance?

The functional contracting approach formed the theoretical basis of the study, as in Publications I and II. Thus, as my colleague and I analyzed the interview data, we expected to find that contracts were used in accordance with the functional approach—to safeguard parties' interests, to adapt the relationship to possible future changes, and to coordinate the information flows and roles and responsibilities of the parties. However, we discovered that in addition to these three established functions,

contracts were used to codify the deal, to manage the internal workflows of the organization, and to steer and support interorganizational collaboration beyond the ongoing exchange.

As expected, one of the most used contract functions was safeguarding, in which the focus is on protecting the contracting parties against any opportunistic behavior of the other party. The clauses used for safeguarding included liabilities, warranties, clauses on intellectual property rights (IPRs) and non-disclosure, clauses on supplier requirements and supervision, and clauses on conflict management and dispute resolution.

As for interorganizational relationship performance, the interviewees believed that in certain situations, safeguarding clauses could support this. For example, a non-disclosure agreement (NDA) could create and facilitate trust in the early phases of the transaction. However, the interviewees were of the opinion that clauses that safeguarded the parties but were one-sided hindered interorganizational relationship performance. These specific terms were intended to overprotect the seller and transfer excessive risk to the supplier. According to the interviewees, this attitude was often already evident during contract negotiations, as contract drafters focused on safeguarding their own interests at the expense of their suppliers.

In addition, the interviewees felt that lawyers sometimes hindered the creation of relational norms and collaboration. This was because the lawyers focused too much on safeguarding clauses and on irrelevant details without understanding "the big picture". In fact, contracts drafted by lawyers were regarded as excessively long, filled with unnecessary legalese, and generally written in complicated English. At worst, neither of the negotiating parties understood what they were agreeing to, and the drafting process was regarded as a waste of time. However, the lawyers themselves regarded their role as essential to assure that the required terms were included and written precisely. Legal terms in particular, such as IPR clauses, were considered to require legal expertise.

Further, even though the interviewees mentioned adaptive contract terms such as price adjustment clauses, clauses on buffer stock, clauses on change management, and clauses on contract termination, it seemed that often the formal, adaptive contract terms were complemented by relational governance. This was especially the case when contracts did not address a specific contingency or when things did not go as planned (e.g. Poppo & Zenger 2002: 713; Schepker et al. 2014: 201; Hadfield & Bozovic 2016: 993). For example, when the price of raw materials increased and the contract did not contain a price fluctuation clause, the parties were still prepared to change pricing terms. Moreover, the companies were willing to agree to minor scope changes without a formal amendment to the contract. Last, when changes occurred or things went wrong, the parties were flexible and did not follow the contract to the letter. Instead, they tried to settle issues amicably and avoid litigation

because they valued the relationship over the dispute (e.g. Macaulay 1963: 61; WorldCC 2014; Hadfield & Bozovic 2016: 998; Frydlinger et al. 2016: 15).

Another observation was that contracts were used to coordinate the parties' relationships, tasks, and communication for the duration of the contract. These types of clauses were especially used in project business, consortia, R&D agreements, and in businesses with a high degree of uncertainty (e.g. Chen et al. 2018). Clauses on project organization, steering group protocols, meeting protocols, schedule management, cost management, and change management were mentioned as being of special importance for project deliveries. Regarding the relationship between coordinative clauses and relational governance, the interviewees described how coordinative clauses were sometimes complemented by relational governance. For example, relational governance was used to agree on practical issues, such as daily communication. However, the formal contract was always in the background.

In addition to the three established contract functions—safeguarding, adaptation, and coordination—we found that contracts served several other functions. In particular, they were used to codify the deal, to manage the internal division of work and responsibilities inside an organization, and to strategically guide the present and future collaboration of the contracting parties.

The first additional function identified was the *codification function* of a contract. This refers to contractual techniques that put together and verbalize the deal for all the parties. Clauses that reflect the codification function include scope, roles and responsibilities, price, and delivery terms.

Clauses that reflect the codification function, especially those related to the contract's scope, were the most discussed in the interviews. The interviewees emphasized that contract scope, as well as the scope interfaces, needed to be clearly defined, and both parties had to have a mutual understanding of what the scope included. This also meant that contracts should be detailed, coherent, and not open to interpretation. If contracts were drafted clearly and understood by both parties, they enhanced trust and interorganizational exchange performance.

However, if contracts failed to codify the deal properly and did not correctly reflect the details of the specific agreement between the parties, they hindered exchange performance. There were various reasons for why the contract did not reflect the agreed to terms. First, some contracts were unfit from the start because they were copied from a prior contract or contract template from a different industry, had missing information or contained non-applicable terms. The second reason why contracts were unfit for purpose was that the people who drafted the contract were not those responsible for executing them. This caused a misalignment between the documented terms and how the project was to be executed in reality. Third, contracts could become unfit over time; clauses that had been originally designed to support

exchange performance could lead to the opposite, because they no longer reflected the relationship and practice.

The second additional function the interviewees described was the *internal management function* of a contract. When contracts were used for internal management, they aimed to communicate the objectives and scope of the deal not only to the people who had negotiated or drafted the contract but also to other internal personnel. An example of a clause that serves both the coordination function and the internal management function is a single point of contact clause, which is often used in relation to, for example, notices.

Although the internal management function is directed first and foremost toward intrafirm work, it has indirect implications for the governance and performance of interorganizational exchanges. For example, if internal ambiguities result in the misallocation of resources, this can affect the interorganizational exchange relationship and cause reputational harm, among other things.

Finally, companies used contracts to plan, promote and steer collaboration over the ongoing exchange. This function is referred to here as the *collaboration function* of a contract. Examples of clauses that were used by the participating companies and that served the collaboration function include pain and gain sharing clauses, open book clauses, clauses on licensing, options to extend or renew the contract, clauses that strategically coordinated the exchange relationship, and conflict management clauses that sought to resolve disputes amicably. Binding order forecasts, volume commitments, volume discounts, and supplier programs are also examples of collaborative clauses used by the participating companies in their supplier contracts.

As noted by previous studies (e.g. Frydlinger et al. 2016), the need for collaborative clauses was emphasized in complex and long-term contracts, in for example, R&D, construction and information technology projects. The maturity of relational governance also influenced the use of collaborative clauses. For instance, when the parties knew and trusted each other they were more likely to use contracts that were more complex and included collaborative clauses, such as gain and pain sharing clauses or open book clauses. In other cases, however, the familiarity of the parties resulted in the role of the contract becoming less important.

To summarize, the findings of Publication III contribute to and advance the theory of the functions of contracts. In essence, we found that in addition to safeguarding, adaptation and coordination, contracts were used to codify the deal, to manage internal workflows, and to strategically guide the interorganizational collaboration over the ongoing exchange. In other words, contracts were used in versatile ways, and these uses affected the development and utilization of relational governance as well as interorganizational exchange performance. Based on these results, we argue that considering the functions of a contract is fundamental to designing a contract that aims to complement relational governance and support

interorganizational exchange performance. If the relational dimensions of a contract, such as the collaboration function, are neglected, or the purpose and function of a specific contractual technique are not properly understood but implemented regardless of this, the contract can seriously hamper the development and use of relational governance and hinder exchange performance.

4.3 Assessing the impacts of contract functions, framing and regulatory focus (Publication IV)

Publication IV explores how the functional contracting approach can be used as a contract design framework to assess how organizations utilize the various contractual functions and how they frame their contracts. In the Publication, I present and discuss the results of a study in which I analyzed ten purchase contract documents of six companies that participated in the survey and the interview studies conducted as part of the DIMECC REBUS program.[98] The analysis illustrates how the different functions of contracts are present in the "real world"—in the actual contracting practices of particular companies. Moreover, it shows how the distribution among the functions, the framing, and the possible mismatches between the different functions or between the functions and the framing influence the buyer-supplier relationship that is created through the contract. In the following sections, I focus on the findings that are particularly relevant to the main research question posed in this summary.

Overall, the analysis revealed that the most used contractual function was the safeguarding function, and that the clauses that served the collaboration and the *policy*[99] functions were used the least. The analysis also showed that most of the contracts were framed preventively. Actually, only two contract clauses (one of which was optional) were framed promotively. This result is in line with those of previous studies and was unsurprising, as the contract documents generally supported arm's-length buyer-supplier relationships.

In relation to the first part of the main research question—What are the functions by which companies use contracts in their interorganizational exchange relations? – –I found that in addition to safeguarding, codification, coordination, adaptation, internal management, and collaboration, the analyzed contracts also served a seventh function: *policy*. Clauses that serve the policy function require contracting parties to conform to policies related to exchange performance itself or to broader societal values, such as CSR. In other words, the policies can range from internal "best

98 For more about the DIMECC REBUS research program, see Note 11. For more about the interview study, see Sub-chapter 3.2.2.

99 For more about the policy function, see next paragraph.

efforts" clauses and supplier codes of conduct to voluntary CSR initiatives[100] and multinational treaties, such as The OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.

All but one of the analyzed contracts included policy clauses. Below is an example of such a clause:

> The Supplier agrees that its actions are not contradictory to the Purchaser's code of conduct. The Supplier also agrees to comply with all other applicable laws, regulations, international agreements and treaties, including but not limited to those related to the use of child labor, environmental issues and human rights.

Regarding the relations between contract functions and their framing, the analysis revealed that although three of the analyzed contract templates claimed specifically to be based on the principles of long-term collaboration and mutual gains between the buyer and the supplier (Interview with a Procurement Manager of Company 11, reported in Publication III; Interview with a Procurement Manager of Company 15,), almost all the contracts contained inconsistencies in terms of (1) the functions the individual clauses were intended to serve, (2) the clause framings and the functions they were intended to serve, and (3), the general collaborative purpose of the contract and specific contract terms.

Most inconsistencies were found in clauses that served the collaboration function. The general observation was that clauses that were intended to serve collaboration were, in fact, designed in a manner that underlined the safeguarding function. Moreover, these clauses were often one-sided as they highlighted only the obligations of the supplier.

The following two examples illustrate the issues relating to the inconsistent use of contract functions and their framing. The first extract shows how a collaborative clause's intent is eroded by the addition of language that serves the safeguarding function:

[100] One example of a voluntary CSR initiative is the United Nations Global Compact, which was launched by former UN Secretary-General Kofi Annan in 2000. The Global Compact aims to mobilize a global movement of sustainable companies and stakeholders by helping companies conduct responsible business practices. According to the Global Compact, this can be achieved by aligning company strategies and operations with the Ten Principles on human rights, labor, environment and anti-corruption, and by taking strategic actions to advance broader societal goals, such as the UN Sustainable Development Goals. The Global Compact is signed by more than 13 000 companies and over 160 countries. See United Nations Global Compact 2021. Another example of a voluntary CSR initiative is the Global Reporting Initiative, see GRI 2021.

> The Buyer is entitled to demand technical changes for parts, and Supplier shall propose any technical changes it deems necessary or advisable. Upon written consent by the Buyer, the Supplier will execute these changes.
>
> The Supplier shall notify the Buyer without delay of additional costs and adjustments to delivery times that result from technical changes. The changes will be binding only after a written supplementary agreement has been concluded between the Parties concerning the additional costs and/or adjustments to delivery times.

In essence, even though the clause is presumably designed to support collaboration, the second paragraph focuses only on safeguarding the buyer's rights.

The second example illustrates how a similar (but not identical) clause is designed to support collaboration:

> If the Supplier notices any defect, discrepancy or inconsistency in the specifications, it shall notify the Buyer thereof without undue delay. The Buyer is liable for the correctness of the specifications and the information therein. The Supplier should, however, make its best efforts to detect possible defects, discrepancies and inconsistencies. In these circumstances, the delivery time will be adjusted accordingly.

Further, while the overall intent of the contract was collaborative, this intent was blurred because different functions and framings were used inconsistently. As an example, even if the contract was intended to be collaborative, only the buyer had the right to:

> …use names, brands, trademarks, commercial and other relations of the Buyer or the Buyer and the Supplier as well as names of the Buyer or the Buyer and the Supplier personnel for advertising, sales promotion or in any other way for commercial activities.

The supplier, in turn, needed written approval from the buyer to use this information.

In relation to the second part of the main research question—What is the relationship between contract functions and relational governance?—the results corroborate the findings of Publication III; the supplier agreements included an abundance of clauses that served the safeguarding function and were excessively one-sided. The most blatant example ruled that if the supplier did not send the invoice within 90 days of delivery, it could no longer claim payment for the delivered

items from the buyer. These kinds of clauses are overly safeguarding and, depending on jurisdiction, a court could even find them void.

Most of the clauses were not this extreme, but many of them either limited the liabilities of the buyer or granted rights solely to the buyer. Examples of such clauses included the right to postpone deliveries, the right to assign the contract, termination rights, the right to use the case as a reference, and rights to intellectual property. While the use of one-sided clauses may occasionally be justified in strategic terms, the excessive use of one-sided safeguarding can hinder overall exchange performance and decrease satisfaction with the exchange relationship. These are serious disadvantages for both the supplier and the buyer (e.g. Poppo & Zhou 2014).

In sum, the analysis revealed that contracts are still designed according to the logic of TCE, highlighting the need to safeguard one's own interests against the opportunistic behavior of the other contracting party. Although the approach is sometimes strategically justifiable, it can negatively affect overall satisfaction with the supplier-buyer relationship and hamper proper exchange performance, at least if applied to the extreme. Thus, I argue that organizations should consciously and critically assess the contracts that they use in their interorganizational exchange relationships. The functional contracting framework can help organizations assess the content and purpose of each contract clause and the main functions they are intended to serve. Furthermore, organizations can use the framework to assess the distribution of the contractual functions and whether there are inconsistencies between the individual clause functions and framings or, in general, in the functions, the framing, and the desired relationship type.

On a theoretical front, I argue that the use of the functional contracting framework can fundamentally change the manner in which we construct contracts and make sense of them. This may, in turn, diversify the theoretical understanding of and discussions on the purpose, functions, and influences of contracts. Next I discuss these theoretical contributions and their relation to previous research.

5 Toward a functional turn in contracting?

This chapter re-examines the findings of the Publications in relation to the main research question posed in this summary: What are the functions by which companies use contracts in their interorganizational exchange relations, and what is the relationship between contract functions and relational governance in these relations? It also links the findings to the different theoretical discussions and previous research presented in Chapter 2. I first discuss the findings concerning the functions by which companies use contracts in their interorganizational exchange relations. Essentially, the findings add to the functional contracting approach by introducing four additional functions of contracts: the codification function, the internal management function, the collaboration function, and the policy function. I then assess the findings that relate to the relationship between the contracts, contractual functions and relational governance, and suggest that when contracts are used functionally, they complement relational governance throughout the contract's lifecycle. Subsequently, I discuss the findings that relate to the contracting capabilities that are required to affect the shift toward the functional use of contracts. Thereafter, I elaborate on the findings that illustrated the weaknesses and the disadvantages of the traditional understanding of contracts and contracting. Finally, I discuss the implications of the functional contracting approach to contract theory, research, teaching and managerial practice. I conclude the chapter by considering the limitations of this study and by suggesting possible future avenues of research.

5.1 The seven functions of contracts

The traditional view of contracts held by both organizational and management scholars and legal scholars tends to underline the *legal safeguarding function* of a contract. However, scholars in both fields have gradually started to focus on functions other than safeguarding, and research has called for more detailed studies on how the various functions are represented and operationalized in contracting practice.

This dissertation draws on TCE, relational contract theory, the relational view, functional contracting, proactive contracting, contract design research, and contract framing research. It develops a holistic view of the different functions of a contract. Based on the findings presented in Publications I–IV, I argue that in addition to the three established functions conceptualized by the functional contracting approach—safeguarding, adaptation and coordination—contracts serve four additional functions: codification, internal management, collaboration, and policy. To summarize, the following table (Table 3) explains the seven functions of contracts and provides example clauses from the contract documents that formed the empirical data of Publication IV.

A contractual function refers to a contractual technique, such as a single contract clause or a combination of various clauses, which is used to affect certain actions in the exchange relationship. For example, clauses that codify the exchange aim to communicate the content of the deal to both contracting parties so that they have a mutual understanding of the expectations, scope and exchange relationship. Another example is clauses that aim to coordinate the roles and responsibilities and the workflow of the exchange.[101]

[101] One might argue that the word purpose would be better to describe the contractual techniques I refer to in this dissertation. However, I have decided to use the concept of "function" for several reasons. First, it is derived from the functional contracting approach, which specifically studies the various functions of contracts. Thus, the concept is well known, at least in this field of study. Second, the concept of the purpose of contract is widely used in contracting practice to describe the background and the context of the exchange relationship, the purpose of the exchange, and the general purpose and content of the contract. Finally, the word function refers to active doing, and I wish to highlight that contracts and contract clauses are actually capable of influencing and making things happen. Thus, I decided to refrain from using the word purpose in this work. As a side note, for me, value creation is the *main purpose of exchange relationships* (if the exchange does not create value there is no point in making the deal in the first place).

Table 3. Functions of contracts with explanations and example clauses. Adapted from Hurmerinta-Haanpää forthcoming. Used with permission.

Contract function	What does it do?	Example clause
Previously established functions		
Safeguarding	Safeguards the rights of one or both contracting parties either against the opportunism of the other party or one-sidedly.	In the event of all or part of the assignment being delayed past the agreed completion date or milestone date(s), the Supplier shall pay liquidated damages of X% of the order value as specified in the purchase order for each commencing week for which the assignment is delayed. The liquidated damages shall not, however, exceed X% of the order value.
Coordination	Organizes the responsibilities, tasks and communication of the parties throughout the contract's lifecycle.	The Parties shall set up a project organization to implement this agreement and to organize the cooperation between the Parties.
Adaptation	Adapts the relationship to possible endogenous or exogenous changes.	As a result of a significant decrease in the costs of labor, materials or other costs of manufacture, the Parties are obliged at the request of the Purchaser to negotiate a corresponding decrease in the price of the products. Should the result of such negotiations fail to reflect the decrease of the costs, the Purchaser has the right to terminate any orders without further liability to the Supplier.
Additional functions identified in this research		
Codification	Codifies, verbalizes, and communicates the deal to the contracting parties.	Pursuant to the terms and conditions of this contract, the Supplier agrees to manufacture and deliver parts to the Buyer, as listed in Annex 1, according to the data set for quality, logistics and delivery terms specified in this Contract.
Internal management	Helps manage the internal workflows, tasks, and responsibilities of an organization.	All orders are sent by the Buyer in writing. The Supplier may not accept orders by phone or otherwise orally unless they are later confirmed by a written order.
Collaboration	Organizes, promotes and steers both ongoing and future collaboration between the contracting parties.	Cooperation between the Parties shall be developed jointly. The Parties shall set annual goals for their cooperation, and the cooperation will be evaluated periodically. Both parties shall name their cooperation contact persons.
Policy	Requires the contracting parties to conform to policies related to exchange performance itself or to broader societal values.	The Supplier shall comply with the Buyer's Responsibility Framework and Policies, including the Buyer's Supplier Code, as amended from time to time.

It is important to understand that these functions can operate simultaneously, and that different contract clauses or bundles of clauses can reflect many functions. Moreover, the relevance of the different functions depends on the contract type and context. For instance, clauses that serve the coordination, adaptation and collaboration functions might be used more often in long-term contracts, whereas safeguarding clauses and codification clauses might be used more often in exchanges that are task specific and require technical precision. It might even be that collaborative contract clauses are unnecessary in simple, routine and short-term contracts.[102] Next, I move on to describe the functions identified during this research project in more detail.

First, the codification function of a contract refers to contractual techniques that codify, verbalize and communicate the deal to the contracting parties. Clauses that reflect the codification function include scope, roles and responsibilities, price, and delivery terms. This function seemed to be the most often referred to function in the interviews (Publication III) and the second most used contract function in the contract documents analyzed for Publication IV. Yet it has gained only limited attention in previous research. For example, in the field of organizational and management research, only a few studies have focused on this function. First, Lumineau et al. (2011: 22) found in their case study analysis that companies used a contract drafting process and detailed contracts to codify their goals and expectations and to grasp a better understanding of the overall deal. This way, contracts forced parties to carefully elaborate on each dimension of the exchange relationship. Second, Mayer & Argyres (2004) found in a case study of recurrent contracts between the same contracting parties that provisions were added to the recurrent contracts for the purpose of codifying the "lessons from previous experiences in the relationship" (Mayer & Argyres 2004: 404). In contract law scholarship, many scholars refer to similar uses of contracts but use a different word to describe this function. For example, Suchman (2003) uses the metaphor of a contract as a script, encouraging parties to elaborate on their expectations and roles before the final contract is signed. Similarly, proponents of the proactive contracting approach have conceptualized contracts as blueprints, visible scripts and roadmaps of the deal (Haapio & Haavisto 2005; Rekola & Haapio 2011; Nuottila & Nystén-Haarala 2019). Hadfield & Bozovic's (2016) interviewee also mentioned this function by describing how contracts are used as reference documents (Hadfield & Bozovic

[102] Frydlinger & Hart (2020: 5) come to a similar conclusion in the case of a formal relational contract. In particular, they consider that a traditional contract without the guiding principles of a formal relational contract is sufficient in routine situations in which unanticipated events are rare. For more about the formal relational contract, see Note 44.

2016: 1008) Finally, referring to Collins (1999: 15), Dietz (2012: 39) argues that the most important function of contracts is communication, "so that everyone knows what one talks about and what is expected" (Dietz 2012: 39, extract from G-IX interview). All these conceptualizations of legal scholars seem to combine elements from both the codification function and the coordination function of a contract.

Second, contracts served the internal management function by organizing intrafirm roles, responsibilities, and communication. Previous research on this function is limited. Mayer & Argyres (2004) and Macaulay (1963) prove exceptions by describing how contracts are used for internal planning, management and communication, thereby preventing customers' unwanted concessions by salesmen, delivery delays, misallocation of resources, and reputational harms (Macaulay 1963: 65; Mayer & Argyres 2004: 398–399, 404). Bernstein (2015) also discusses specific contractual techniques that serve the internal management function: supplier scorecards. According to Bernstein, these scorecards, along with regular supplier evaluation meetings, mitigate the risk of procurement managers favoring "certain suppliers out of feelings of friendship or loyalty, even when they are not the best suppliers available" (Bernstein 2015: 596).

Third, contracts were used to organize, promote and steer both ongoing and future collaboration between the contracting parties. In short, collaborative contract clauses aim to create a strategic collaborative relationship that spans beyond the individual exchange. Clauses that serve the collaboration function include strategic programs for collaboration, highlighting trust, communication, commitment, knowledge sharing, and information exchange (Schöttle et al. 2014: 1274–1275; Bernstein 2015; Frydlinger et al. 2016). While Macneil (1968) already recognized that contracts should be viewed as instruments for social cooperation, the historical burden of the neoclassical economic model—the arm's-length sourcing strategy that flourished until the 1980s—and overemphasis on opportunism led to a situation in which the social and relational dimensions of contracts were disregarded and contracts were seen to hinder the creation of trusting business relationships (Macaulay 1963; Gulati 1995; Ghosal & Moran 1996; Uzzi 1997; Dyer 1997; Dyer & Singh 1998; Frydlinger et al. 2016). In today's global economy in which two-thirds of production is organized in value chains and networks (WTO 2019: 1), the need for collaboration that is supported by not only relational governance but also by contracts is evident (e.g. Frydlinger et al. 2016: 10). Fortunately, recent publications by contract law scholars as well as practitioners have focused on contracts that include these social dimensions. For example, in Gilson et al.'s (2009, 2010, 2013, 2014) theory of braided agreements, formal contract terms that allow transparency, encourage information sharing and increase switching cost are used to support the development of relational governance in situations in which the parties are new to each other. Similarly, Jennejohn (2008) introduces the idea of generative contracts that act as learning devices and thereby limit

opportunism. More recently, Bernstein (2015) has explored a variety of contractual mechanisms that large American industrial buyers use to facilitate relational governance in highly cooperative procurement relationships. She concludes that the goals of these kinds of contracts include not only the safeguarding of contractual performance but also the creation of "a framework for an ongoing contracting relationship, a framework that is structured to build the types of relational and structural social capital that will enable the parties to identify and take advantage of future value-creating opportunities" (Bernstein 2015: 615). Finally, Frydlinger et al. (2016) urge companies to use formal relational contracts that are based on the idea of a partnership, and to establish a society of social norms to guide the behaviors of contracting parties. As with collaborative contract clauses, the focus of these formal relational contracts of Frydlinger et al. (2016) is on guiding the overarching exchange relationship.

Fourth, contracts served the policy function, which refers to contractual techniques that require contracting parties to conform to policies that can relate to exchange performance itself or to broader societal values, such as CSR. The policy requirements can be set either in the contract document itself or the contract document can include references to external policies, such as company codes of conduct, industry standards, or international self-governance tools. Examples of policies that relate directly to exchange performance are broad standards of performance, such as "best effort" clauses (e.g. Gilson et al. 2010), clauses requiring organizations to have a certain number of full-time employees working on the project, or clauses requiring organizations to assign employees with a certain qualification to work for the project (e.g. Schepker et al. 2014: 212). These types of clauses are common in exchanges in which the outcome is hard to determine ex ante, for example, innovation contracts (e.g. Gilson et al. 2010). In turn, an example of policy clauses that enforce broader societal values are clauses that require suppliers to follow voluntary CSR initiatives. These kinds of clauses have become popular quite recently[103] and today they are even cascaded down to the entire supply chain (e.g. Salminen 2019: 60–61 with references, 64). Although organizations sometimes

[103] For example, terms related to adherence to policies were the 20th most negotiated term in a survey by WorldCC in 2020. It is the first time in the 20 year-long history of the survey that these terms are on the list. See WorldCC 2020. Smith & King (2009) explain the phenomenon using institutional theory, suggesting that organizations seek legitimacy by adopting "certain contractual elements that conform to developing standards of rational organizational behavior" (Smith & King 2009: 37).

use these kinds of clauses for appearance only, they are generally meant to move industry practices in a more sustainable direction.[104]

To sum up, the functional contracting approach recognizes that contracts serve various functions: To start with, they can codify the agreed-to deal and verbalize it to the contracting parties. Moreover, contracts can coordinate parties' actions, and can be used to guide an organization's internal workflows and communication. Contracts can be also used to prepare for possible changes in circumstances by setting out procedures for adjustment and change management. Furthermore, although the functional contracting approach underlines the various functions of a contract, it also considers the possibility of opportunism in exchange relations. Thus, contracts also serve as safeguards to secure both parties' interests during the exchange and in cases of conflict. Contracts can be used to guide the parties to develop and deliver the deal in a way that shows commitment to best efforts and to sustainable business practices. Finally, and perhaps most importantly, contract clauses serving the collaboration function focus on the interorganizational exchange relationship by creating a fertile ground for collaboration and by supporting the development of trust and other forms of relational governance.

Next I address the possibilities of the functional understanding of contracts and the relationship between contract functions and relational governance.

5.2 The relationship between the functional contracting approach and relational governance

As argued and discussed in Publications I and II, the functional contracting process can be used as a precontractual integration tool to coordinate and guide the negotiation process, to align the expectations and value perceptions of network participants, and to implement changes in the network participants' attitudes and decision-making policies. In the words of Gilson et al. (2009, 2010, 2013, 2014), the functional contracting process introduced in Publications I and II *braids* the formal and informal governance mechanisms in a succession of MoUs to enable the parties

[104] For more about the historical developments of using private governance to promote the sustainability of transnational production, see Locke 2013. Unfortunately, as noted by Salminen (2017, 2019), voluntary private governance is not sufficient for addressing sustainability-related problems; private law liability and public regulation is also needed. In his doctoral dissertation, Salminen (2017) proposes a novel regime of production liability, in which lead firms would be liable not only for production-related contingencies toward users of goods but also toward other actors, such as labor and the environment. For current laws governing sustainability in contractually organized value chains, see Salminen 2019: 68–69. Moreover, the drafting of an international UN treaty to regulate transnational corporations and other business enterprises with respect to human rights is under way. See Business & Human Rights Resource Center 2020.

to examine whether the business case is worth pursuing. At the same time, it binds the parties to negotiate in good faith. Thereby, like the relational contracting process introduced by Frydlinger et al. (2016), formal MoUs attempt to build a fair contracting process, discourage opportunism and prohibit the unauthorized use of information disclosed during negotiations. In other words, the formal contract-like documents guide the processes that are usually governed by relational governance. In our case, the utilization of relational governance mechanisms was out of question because the parties were new to each other and trust had yet to develop. As previous research suggests, formal governance is especially used in the early phases of collaboration to convince the parties of their mutual engagement to the process, which in turn enables trust to develop (e.g. Mayer & Argyres 2004: 407; Gilson et al. 2010: 1415; Frydlinger et al. 2016: 25).

Along with promoting the development of trust and mitigating opportunism, the functional contracting process introduced in Publications I and II acts as a gesture that signifies commitment to negotiations. When parties put their thoughts into writing, the weight of commitment changes (e.g. Suchman 2003: 113; Hart & Moore 2008: 12–13; Viljanen et al. 2020: 19; Frydlinger & Hart 2020: 23) even though the legal enforceability of the MoUs may differ from the enforceability of traditional contracts (e.g. Gilson et al. 2010: 1415–1422; Hadfield & Bozovic 2016:1000; Viljanen et al. 2018b: 162; Viljanen et al. 2020: 18). For example, the breach of a soft contract obligation, such as the obligation to negotiate in good faith, may not result in the same remedy as the breach of a hard obligation (e.g. Gilson et al. 2010: 1415–1422). Nevertheless, codifying the framework for negotiations into the MoUs brings social norms to formal contract documents, thereby creating a paper trail of the negotiation process and bringing discipline to the relationship (Frydlinger et al. 2016: 4, 26).

In addition to complementing relational governance and facilitating precontractual integration during negotiations, contracts that utilize the various functions described in this dissertation complement relational governance throughout the exchange and even beyond. During negotiations, processing contract clauses that codify the deal enable parties to align their goals and expectations and gain information about the other party's intentions and motivations (e.g. Suchman 2003: 112–113; Gilson et al. 2009, 2010; Hadfield & Bozovic 2016: 1016). In the post-award phase[105], the codifying clauses, together with coordinative contract

[105] The term "post award" refers to phases that follow the contract signing and include, for example, contract execution and change management. "Pre-award" phases take place prior to contract signature. The terms are widely used in contract management practice and by contract management expert organizations, such as the WorldCC and the American National Contract Management Association (NCMA).

clauses, act as valuable roadmaps and scripts to guide the parties' performance (Suchman 2003; Haapio & Haavisto 2005; Haapio & Rekola 2011). In this way, contracts can enhance the development of trust and reduce misunderstandings related to scope and scope interfaces (Mayer & Argyres 2004: 401). Moreover, by bringing the social norms of the exchange relationship to the formal contract document, collaborative contract clauses aim to build a relationship that is based on fairness, even in situations in which a contract needs to be adjusted or interpreted in a new light (Poppo & Zhou 2014; Frydlinger et al. 2016).

Furthermore, when close attention is paid to contract framing, the contract reflects the desired exchange relationship and induces behavior that is desirable for that specific relationship. It is important to note that while neither preventive nor promotive contract framing is undesirable *per se*, the framing should always match the transactional attributes and the behavior that is desired for the successful performance of the exchange. Moreover, framing should be applied consistently throughout the contract and not only to a single contract clause (e.g. Weber et al. 2011: 199; Weber & Mayer 2011: 69). This ensures that a contract, together with relational governance, enables a well-functioning exchange relationship (e.g. Weber & Mayer 2011: 71).

The findings also suggest that the relationship between contracts and relational governance is bi-directional: relational governance complements contracts and vice versa. For example, the interviewees in Publication III described how coordinative contract clauses were complemented by relational governance when the parties agreed on practical issues such as daily communication. Moreover, as in previous studies, the interviewees indicated that relational governance was used to complement formal contracts in cases of changed circumstances (e.g. Macaulay 1963: 60–62; Poppo & Zenger 2002: 721; Hadfield & Bozovic 2016: 993–994). Relational governance also complemented collaborative contract terms: When relational governance developed over the course of the exchange relation, it encouraged the parties to use more complex and collaborative contract clauses. Some researchers have debated the question of whether experience gained from a prior relationship and the relational governance developed during that relationship leads to more or less contractual detail (e.g. Gulati 1995; Poppo & Zenger 2002; Mayer & Argyres 2004; Ryall & Sampson 2009), but I believe that the relationship between the two governance mechanisms is more complex. On the one hand, parties may rely more on relational governance in long-term relationships (e.g. Gulati 1995; Dyer 1997). On the other hand, an increased level of trust and the utilization of other relational governance mechanisms can also lead to more complex contracts (Mayer & Argyres 2004; Ryall & Sampson 2009; Mellewigt et al. 2012). Moreover, different contract functions also have a role to play here. It seems that prior relationships have a stabilizing or slightly positive effect on the level of safeguarding clauses (e.g.

Mayer & Argyres 2004; Reuer & Ariño 2007; Ryall & Sampson 2009; Mellewigt et al. 2012). They also seem to promote the increasing use of adaptive and coordinative contract clauses (e.g. Mayer & Argyres 2004; Ryall & Sampson 2009; Mellewigt et al. 2012; Cao & Lumineau 2015), although the findings related to the increased use of adaptive and coordinative contract clauses are somewhat inconsistent (Reuer & Ariño 2007).[106] The positive effect of prior ties on safeguarding clauses may seem counterintuitive, but the explanation might lie in the interplay between relational and formal governance: Partners who deal with each other repeatedly may find writing a detailed agreement worthwhile, not necessarily to be used in the case of a dispute in a court, but because it supports the relational governance between the parties (e.g. Ryall & Sampson 2009: 922–923).

Indeed, this study corroborates the findings of previous research, suggesting that even though contracts specify legal remedies in the case of disputes, they are not used very often. In cases of disputes, formal contracts are often put aside, and controversies are settled by informal means (e.g. Macaulay 1963: 61; WorldCC 2014; Hadfield & Bozovic 2016: 998; Frydlinger et al. 2016: 15). This raises the question of why parties write these clauses into the contracts in the first place. Like Cao & Lumineau (2015: 30), I believe that even though legal sanctions are not used, the fact that they are included in a written contract supports the development of relational governance, which in turn reduces opportunism.[107]

To sum up the findings concerning the relationship between contracts, contract functions and relational governance, it seems that contracts and relational governance are not substitutes, but that they complement each other. However, this result only holds for contracts that utilize the various functions of contracts. In essence, I argue that contracts that make each party's expectations, values and behaviors more observable, reduce information asymmetry and improve justice perception, have a positive effect on trust and strengthen the impacts of relational governance on satisfaction and relationship performance (e.g. Mayer & Argyres 2004: 407; Cao & Lumineau 2015: 30). However, if contracts are used in the traditional frame and mainly for safeguarding, it seems that they substitute rather than complement relational governance (e.g. Ghosal & Moran 1996; Cao & Lumineau 2015; Poppo & Cheng 2018).

As the results of Publications I and II in particular indicate, the shift toward the functional contracting approach in business practices will not be easy. This is

[106] Reuer &Ariño (2007) found that prior ties did not influence the level of safeguarding clauses that were used in subsequent exchanges. Instead, repeat collaborators were less likely to adopt coordinative provisions in their contracts.

[107] Interestingly, Cao & Lumineau (2015: 26) found that formal contracts did not themselves reduce the level of opportunism.

because the new approach disrupts current contracting practices and requires that different professionals who actually use contracts—such as lawyers, businesspeople, technical professionals, and financial professionals—change their attitudes toward contracts. In a word, they need to *collaborate* to create competitive advantage for their organizations (e.g. DiMatteo et al. 2012: 106; Haapio 2013: 82). Next, I elaborate on the findings concerning the contracting capabilities that are essential to drive this shift.

5.3 What does turning toward the functional use of contracts entail?

Turning toward the functional use of contracts requires that we reorient our understanding of contracts in various ways. First, we need to abandon the overemphasis on contracts as legal safeguards and to adopt a proactive view of them. This entails that contracts are understood as both promotive managerial tools that can be used to enable business success and to add to a company's competitive advantage and as preventive legal tools that prevent undesired risks from realizing (e.g. Haapio 1998; DiMatteo et al. 2012; Haapio 2013).

Second, contract design processes should be informed not only by TCE and relational contract theory, but also by the contract design research discussed in this study, including research on the various functions of contracts, the relationship between contracts and relational governance, and contract framing. In essence, contract design should result in user-friendly contracts that match the desired interorganizational relationship, support collaboration, and enable successful business outcomes (see also Figure 3).

Third, the results of this dissertation highlight the need for cross-professional collaboration when adopting the functional approach to contracting. They also point to the need for diverse contracting capabilities. Previous research on contracting capabilities suggests that some experts possess stronger contracting capabilities than others in relation to particular types of contracts, contract clauses or negotiations. For example, Argyres & Mayer (2007) suggest that managers and engineers are more suitable than lawyers for drafting clauses on roles and responsibilities, communication, and certain parts of contingency planning clauses, as these kinds of clauses require firm-specific and tacit knowledge. Lawyers, in turn, possess stronger contract design capabilities related to, for example, clauses on dispute resolution and IPR. Weber & Mayer (2006) also propose that, depending on the knowledge needed to complete the task of drafting a contract template or negotiating a deal, different stakeholders (internal counsel, external counsel, managers and engineers, and purchasing/sales agents) should be involved with distinct inputs (sole actor, team leader or team participant). In relation to contract framing, research suggests that

because of their plausible tendency toward prevention, lawyers may better frame contract clauses that deal with safeguarding and monitoring, while technical professionals might be better suited to negotiating contract clauses that require creativity and flexibility (Mayer & Weber 2009: 14–16; Weber & Mayer 2011: 73).

Indeed, the results of this study indicate that even though legal expertise is required when drafting legal terms such as IPR clauses, lawyers are sometimes seen as adversely impacting negotiations, contract drafting, and the development of relational governance. In line with previous research, the findings suggest that contract drafting should no longer be left solely to lawyers (e.g. Nuottila et al. 2016). Instead, it should be a cross-professional endeavor that recognizes and involves the various contract users, such as contract managers, business managers, sales professionals, procurement managers, in-house counsels, financial experts, and technical professionals. In addition, a mature contracting capability would focus on the manifold contexts of use and the goals of the different users: In other words, it would design more user-friendly contracts (e.g. Haapio 2013: 55, Table 9; Kujala et al. 2015: 101). Moreover, a mature contracting capability would utilize the knowledge on the antecedents and influences of contract framing (e.g. Weber et al. 2011: 199; Rich et al. forthcoming: 2). The shift toward cross-professional contracting capability requires, however, that lawyers welcome other professionals to plan contracting processes and contracts, and that managers start to see law as a potential source of competitive advantage, as opposed to the traditional view of law as a hindrance or a cost that only lawyers can manage (Bird & Orozco 2014; Orozco 2021).

5.4 Dangers of continuing on the traditional path

Like previous studies, I found that safeguarding was still one of the most used contractual functions (e.g. Argyres & Mayer 2004: 404; Nystén-Haarala et al. 2010: 471–472). This finding is understandable from a historical perspective: The neoclassical economic model of contracting and the system of classical contract law guided contract theory and contracting practice until the mid-20th century (e.g. Nystén-Haarala et al. 2010: 463). As Macaulay (1963) reported, many deals were completed without reference to the contract, and managers often felt that establishing a contract could "get in the way of creating good exchange relationships" (Macaulay 1963: 64). From the 1980s onwards, globalization and new business practices that were based on fragmented production changed the contracting environment: Local, long-term contracts were replaced by relationships in which the contracting parties did not know each other and even resided on the other side of the globe. This change resulted in the need to govern these uncertain exchange relations by complete contracts that safeguarded the parties against opportunism and were based on the

idea of an arm's-length relationship. Today, due to the interdependency of organizations along with a networked and hyper-competitive economy, these types of contract do not work (Frydlinger et al. 2016: 13). In fact, based on my research findings, these kinds of contracts negatively affect interorganizational exchange relationships.

To begin with, excessive use of (one-sided) safeguarding clauses can hinder the creation and development of relational governance and encourage conflict, thus negatively affecting exchange performance. Contracts that include a high number of safeguarding clauses can encourage the parties to vigilantly follow the contract to the letter and focus excessively on the partner's possible deviations from the contract. This creates a spiral of suspicion, pressure and retaliation, which in turn encourages opportunism and undermines collaboration and joint problem-solving (e.g. Ghoshal & Moran 1996; Moeller et al. 2006; Frydlinger et al. 2016; Schilke & Lumineau 2018). Further, a partner's assessment of the other party's task performance and satisfaction with the relationship declines if a contract focuses solely on safeguarding (Poppo & Zhou 2014). The quality of performance can also be endangered by overly constricted specifications and policing (Matthyssens & Van de Bulte 1994; Cova & Salle 2000; Moeller et al. 2006). Finally, these kinds of contracts (also referred to as power-based agreements) generate higher transaction costs than contracts that support relational governance (Willcocks & Cullen 2005) and are one reason for the value leakage of 9.15% in contractual relations (WorldCC 2012; Frydlinger et al. 2016: 11–14).[108]

Keeping up with old contract drafting traditions, such as leaving the lawyers to draft the contracts alone, can result in the contract not reflecting the actual content of the deal or the relationship of the parties. In the words of Macaulay (2003), the real deal does not translate into the paper deal. Moreover, excluding the actual users of the contract from the contract design process poses the real risk that, even if the lawyers are able to capture the real deal in the paper deal, the users will not comprehend its content because it is not user friendly, only lawyer friendly (e.g. Haapio 2013: 50–56; Haapio & Barton 2018). In these situations, the contract is left in a safe, while important decisions concerning the real deal are made informally. These practices create a spiral, which causes the contract document to be seen as an unimportant, rigid, inflexible legal tool unsuitable for managing, not to mention facilitating, collaboration (e.g. Kujala et al. 2015: 101).

[108] Indeed, WorldCC found in their 2012 survey that contracts underperform by approximately 9%. See WorldCC 2012. Although there are various reasons for this underperformance, the report suggests that the traditional, transactional approach to contracting explains much of the value leakage. See also Frydlinger et al. 2016: 11–14.

Previous research has discussed the various reasons behind the differences between the real deal and the paper deal. In relation to lawyers, one reason is the overutilization of contract templates, even in situations in which the templates do not fit the deal (e.g. Haapio 2013: 50–51; Anderson 2020: 569). In addition, research suggests that lawyers lack business intelligence: Although they seem to acknowledge the importance of business objectives, they struggle to address these issues in contracts (e.g. Nuottila et al. 2016; Nuottila 2019). Finally, lawyers' traditional training, which ignores the economic and managerial aspects of exchanges, influences their drafting habits (e.g. Nystén-Haarala 2006: 264; Siedel & Haapio 2010: 673–674; Haapio 2013: 51). Based on my research, I suggest two additional reasons for the prevailing contracting habits of lawyers: First, their self-indulgence, and second, the fear of what would happen if the entire contract drafting process, along with its end product (the contract document), was reoriented toward a functional framework. Simply put, keeping up with old habits is easier because there is no need to step out of one's comfort zone, and safer because everyone knows (or believes they know) what to expect from traditional contracts.

5.5 The implications of the functional contracting approach for contract theory, research and teaching

Adopting the functional approach to contracting brings about changes in the ways we understand contracts, their functions, and their effects on interorganizational exchange relations. It may also change the way we interpret contracts and develop general principles of contract law and contract law theory. Finally, it changes the ways in which legal scholars teach and study contracts.

To begin with, adopting the functional approach to contracts changes the way in which we understand contracts. The neoclassical economic model and the system of classical contract law presumes that contracts are legal safeguards of the deal into which the parties have voluntarily entered. TCE reorients this view by embracing the transactional-relational spectrum of Macneil and the adaptive and coordinative uses of contracts. However, it underlines the safeguarding function of a contract by focusing on ways to mitigate the opportunism that "plagues" all exchanges.

In contrast to TCE, the functional approach does not focus on the fact that opportunism exists in every exchange relation. On the contrary, it challenges the overemphasis of TCE on opportunism by emphasizing that in addition to economic and legal safeguards, contracts are managerial tools capable of coordinating and managing relationships and developing collaboration. Moreover, the functional contracting approach acknowledges that contracts are influenced by various societal phenomena, such as legal culture, managerial practices, social structures and

institutions, and research, and that contracts themselves influence these practices (e.g. Suchman 2003).

The functional approach challenges current contract law theories by introducing contractual techniques that these traditional theories do not recognize. Like adaptive contract clauses, such as agreements to agree, which were puzzling to common law courts some time ago[109], clauses that serve, for example, the coordination or the collaboration function might seem abstract and vague in a traditional, legal sense, as they do not necessarily fix specific, clear duties and rights.[110] Nonetheless, these kinds of clauses can have legal consequences. They might not be like the legal consequences of hard, traditional contracts (Gilson et al. 2009, 2010; Hadfield & Bozovic 2016): For example, a breach of the good faith negotiation obligation might not (and should not) result in expectation damages, but it can result in reliance damages. Thus, coordinative and collaborative contracting techniques extend the legal consequences of contracts to behavior that was formerly governed only by relational governance (Frydlinger et al. 2016). Perhaps even more importantly, however, the act of contracting the principles that govern collaboration can signify commitment to the relationship and add weight to these principles (Suchman 2003; Frydlinger et al. 2016). Agreeing on the principles of collaboration in the contract document brings them on a par with other, "harder" contractual rights and duties. This way, the functional approach to contracting multiplies the possible effectivity mechanisms of contracts. Moreover, by acknowledging that contracts can be used to bind not only the contracting parties, but also other members of the production network to adhere to policies related to, for example, CSR, the legal ramifications of contracts expand beyond contractual privity (e.g. Salminen 2017; Viljanen et al. 2018b; Salminen 2019; Viljanen et al. 2020).

In relation to contract law development and adjudication, the functional contracting approach could be a useful tool for operationalizing the ideas of the relational contract theory.[111] First, the different functions and their representation in a contract could provide inductive information when deciding whether and to what degree the parties have committed to the principles of good faith and fair dealing. If the contract contained, for example, a great deal of collaborative and coordinative contract clauses, it would indicate that the parties' purpose was to include relational

109 Essentially, agreements-to-agree clauses were seen as contrary to the certainty doctrine of common law. See e.g. Salminen 2011.

110 For more about the challenges related to the recognition of adaptive and coordinative contracting by contract law, see Viljanen et al. 2020: 12. In the context of formal relational contracts, Frydlinger & Hart (2020: 23) discuss the difficulty of enforcement.

111 Relational contract theory has been criticized, partly without justification, for its uselessness in guiding contract interpretation in adjudication (see e.g. Nystén-Haarala 1999: 205–206; Feinman 2000: 737–740). See also Notes 41 and 42.

aspects in the analysis of their relation. This way, courts could acknowledge and also enforce the relational elements of specific exchange relationships. On the other hand, a contract that included almost only preventively framed or even one-sided safeguarding clauses could indicate that the parties' intent was to deal with possible needs for adaptation and flexibility outside the realms of the contract. In this case, a court might prefer textual interpretation. As already pointed out, however, the representation of various functions in a disputed contract would be only indicative, and like today, the final decision on the doctrines to be applied in a particular case would depend on the specific facts of the case. Second, in relation to contract law development, it might be worth considering whether particular types of highly collaborative contracts, such as long-term alliance contracts and consortia, would benefit from a separate relational contract law system that would underline the more relational types of common contract norms (such as reciprocity, flexibility, and contractual solidarity). I restrict the further analysis of these questions in this work, but my intention is to address them in my future studies.

Adopting the functional approach in contract law research and teaching means, first of all, that law school students need to be taught with not only doctrinalist approaches to contract law (which are also important), but also with actual business and contracting practices and empirical studies of contracts (Nystén-Haarala 1998: 250).[112] This includes some basic knowledge of the economics of contracts as well as of the organizational, managerial, and psychological implications of contracts. Otherwise, students would only familiarize themselves with a fraction of contracting practices—the ones which end up in courts—and thus become estranged from most business and contracting reality. After all, most exchanges are completed without any conflicts, and if conflicts arise, they are usually settled without litigation (e.g. Macaulay 1963: 61; WorldCC 2014; Hadfield & Bozovic 2016: 998; Frydlinger et al. 2016: 15). Without a fuller picture of the contracting reality, it is impossible for law students to critically evaluate the existing contract law system and think of possible alternatives. On a more practical level, these students should gain knowledge and skills that are relevant to their future jobs. By studying actual contract practices and by adopting the functional contracting approach, they would gain the skills they need for drafting and managing contracts for interorganizational exchange relationships and solving problems arising from these relationships (Macaulay 1963:

[112] Many ANLR researchers have also called for a reform in legal education. For the latest call, see Poppe 2021, which argues for the reorientation of legal education to further the goals of ANLR. According to Poppe, this reform would: "(i) instill in students an appreciation for the value of empirical research; (ii) provide them with a framework for understanding the relationship between law and social science; and (iii) equip them with the knowledge necessary to engage critically with empirical data and analysis" (Poppe forthcoming: 201).

55, Note 2). If future lawyers were trained in this way, other professionals may start to see lawyers not only as legal professionals but also as business professionals (Haapio 2006b: 29–32; Nuottila 2019: 70–71).

At the moment, in Finland, empirical, multidisciplinary studies of contracts are in their infancy. Apart from myself, only a handful of legal scholars have engaged in empirical studies of contracts and contracting practices.[113] This is because traditionally, lawyers are not trained to conduct empirical research (Korkea-aho & Leino 2019: 18–19; Poppe 2021: 199).[114] If we wish to increase the level of studies that combine insights from, for instance, economics, sociology, organizational and management studies, design science, and law, and to utilize empirical methods to study contracts and contracting practices, we must start by training our future researchers to use empirical methods and to collaborate with researchers from other disciplines.

5.6 Managerial implications

This work offers a number of learning points that are relevant to managers. First, the results of Publications I and II indicate that transitioning to a new business model with performance-based contracts presents several challenges that need to be overcome. In the Publications, we propose that one way to overcome them is to engage in value-based selling and to introduce a functional contracting process. The functional contracting process works as a precontractual integration tool, as it helps: 1) align the expectations and interests of the network participants; 2) initiate and guide the development of appropriate organizational interfaces; 3) build trust; and 4) convince the network participants of the feasibility of the new business model.

Publications III and IV, in turn, underline the fact that contracting professionals need to be aware of the different functions of contracts and their relationship with relational governance. In essence, they need to acknowledge that contracts are not neutral codifications of exchanges; they can be used to align expectations and interest, to manage the exchange relation, and to push businesses toward more sustainable production practices. Moreover, contracts can be used to guide intrafirm work and communication. Finally, they can be used to build and develop long-term collaboration. If the different functions of contracts and their framing, as well as their influence on relational governance and exchange performance, are not taken into

[113] Examples of such scholars include, Helena Haapio, Piia Kaave, Soili Nystén-Haarala, Soile Pohjonen and Mika Viljanen. In the US, the situation is similar, although it has improved during the past ten years. For the US situation in 2000s, see Smith & King 2009: 19–24.

[114] At the moment, only two out of four law schools in Finland have sociology of law as a compulsory course for a law degree.

account, contracts can seriously hamper the creation and development of relational governance and have destructive effects on the exchange relation. Thus, I encourage organizations to critically assess their existing contracts and contracting practices, and to take corrective actions as needed. Publication IV even introduces a conceptual framework—the functional contracting framework—to help organizations in this endeavor. In addition to assessing an organization's current contract practices, the framework can be used as a classification tool and a checklist during the contract drafting and design process.

Recognizing that contracts can create a competitive advantage for the company is essential. Creating a competitive contracting capability calls for interorganizational and cross-professional collaboration throughout the contract's lifecycle and beyond, from negotiations to the continuous development of exchange relations. Lawyers need to change their drafting habits, challenge their beliefs regarding the purposes and the possible uses of contracts, and engage in a supportive role during contract negotiations and to a certain extent during contract drafting. Moreover, lawyers need to change their focus from risk mitigation and prevention to enabling business success, and designing flexible, creative legal governance structures that support other governance mechanisms, such as relational norms.

In addition to lawyers, changes are also required of other professionals. Stakeholders from outside the legal field need to become integral in the contract design process. This is because research shows that, in terms of clauses that require firm-specific and tacit knowledge, contracting capabilities reside outside the legal department (Argyres & Mayer 2007). Different professionals, involved in the exchange at different stages, are needed in the negotiation and design processes to ensure that the contract frame matches the transactional attributes and the desired relationship type, and that the contract does not contain provisions that are conflicting, purposeless or even hinder exchange performance. Instead, contracts should enable business success by being user-friendly, by reflecting the exchange as realistically as possible, supporting relational governance, and creating and supporting the desired relationship type. At best, contracts can be designed to encourage trust and make collaboration flourish.

Changing dominant business practices and attitudes toward contracts is not easy. For example, cross-professional collaboration in contracting requires that different professionals overcome the cross-professional knowledge gap, which is characterized by challenges related to coordinating different perspectives, ways of doing, and goals and priorities (Passera et al. 2016: 85). However, the effort is worthwhile, as developing the organization's contracting and legal capabilities creates a sustainable competitive advantage that is not easily imitable (e.g. Weber & Mayer 2006: 28; Mayer & Weber 2009: 7; DiMatteo et al. 2012: 106). This change

does not happen overnight, and further research on the value leakage of traditional contracting practices is essential to validate the need for change.

5.7 Limitations

Coming back to Macaulay's (2005: 396) words about the limitations of empirical research on contracts, I admit that this study has several limitations. Although the limitations related to following the ethical principles for research with human participants (TENK 3/2019) and data management are discussed in Sub-chapter 3.3, and the limitations related to the qualitative methods used in this dissertation are discussed in detail in the Publications (specifically in Publications I and III) and in Sub-chapter 3.2, I will briefly elaborate on some of them again. I also discuss limitations related to the entire research project.

The first limitation involves the nature of qualitative studies in general and especially the collaborative, explorative action research method. Qualitative research has been criticized because its quality is hard to assess and collaborative action research has been criticized for being biased and subjective (e.g. Werr & Greiner 2008: 98). The fact that all the Publications have passed peer-review evaluation indicates rather firm acceptance of the methodological appropriateness of the individual studies. I have further aided the reader in assessing the quality of my research by describing the research processes and reflecting on them in detail in each Publication, as well as in Sub-chapter 3.2. As regards the critique of collaborative action research, it is hard to deny that the organization that participated in the financing of the research program and in the research project itself had no influence on defining the research theme (e.g. Nystén-Haarala 2017: 1028). Within this framework, however, we were able to independently define our more specific research problems, to collect and analyze data, to conceptualize problems, to present our results, and to offer the case company feedback.

The second limitation is that the feasibility of the functional contracting tools (the functional contracting process and the functional contracting framework) were not tested in practice. This was because the company did not finalize any deal during the research project. In the case of the functional contracting framework presented in Publication IV, only ten purchase contract documents were evaluated. Future studies could focus on testing the tools in both qualitative and quantitative research settings.

The third limitation relates to the generalizability of the results. To begin with, the research reported in Publications I and II was from a case study. Moreover, the number of interviewees in the interview study reported in Publication III was small and the interviewees were not selected randomly. Finally, the number of analyzed contract documents in Publication IV was limited and I was not able to independently

choose them. Thus, instead of providing results that are generalizable across countries, industries and contract types, the findings only showcase some current problems in contracting in general. Through this study, my aim is to invoke discussion within and outside the legal profession and among researchers and practitioners, and to encourage further research on the topic.

The final limitation relates to the empirical nature of this work. As mentioned before, contract law scholars (especially in Finland) rarely conduct empirical research. Moreover, most of the few empirical studies that do exist are quantitative. Thus, a traditional contract law scholar may wonder what the legal implications of my work are. I have tried to translate my findings into legal language and for a legal audience (e.g. Erlanger et al. 2005; Suchman & Mertz 2010; Poppe 2021; Talesh et al. 2021), especially in Sub-chapter 5.5, but am aware of the limitations of this translation. However, I plan to engage in research of the legal implications of the functional contracting approach more thoroughly in my future work.

5.8 Future research

Drawing on various theories on contracts from economics, organizational and management studies, and law, this study offers several avenues for future research.

First, future studies could explore whether the seven functions of contracts are used in different industries and contract types. For example, it would be interesting to know whether more innovation-driven industries utilize different contractual techniques to those of more traditional industries. These studies could exploit both quantitative and qualitative methods: Quantitative studies could examine a large sample of contracts, while qualitative studies could investigate the motives and consequences of utilizing different functions. Both research settings would require a multidisciplinary research team, consisting of a minimum of legal scholars, economists and designers.

Second, future studies could test the feasibility of the functional contracting tools presented in this study and further develop them by means of contract design. This study focused on applying the functional contracting approach to designing a contracting process and assessing purchase contract documents, mainly from the perspectives of contract content and language. Future research projects in turn could apply insights from research on contract visualization, for example, to developing the tools. This kind of research project would require collaboration between researchers from various disciplines and companies. In my experience, the best way to structure this kind of collaboration would be in the form of a multidisciplinary research program, financed by public authorities, industry participants and research institutions. This type of research would yield benefits for both researchers and businesses.

Third, an important avenue for future research is the study of the relationships between contract functions, contract framing, and relational governance, and their mutual effects on the exchange relationship and exchange performance. Again, a combination of quantitative and qualitative studies would probably yield the best results in the examination of these relationships.

Fourth, it would be interesting to study in detail the implications of the functional contracting approach for adjudication and contract law. As noted in Sub-chapter 5.5, the different functions and their representation in a contract could provide inductive information for courts when pondering whether to apply textual or contextual methods of adjudication. Moreover, following in Macneil's footsteps, future research could develop general contract law principles for contracts, which include highly collaborative contract clauses, are generally highly collaborative in their nature, or otherwise require taking relational aspects into account.

Finally, in the advent of contract automation tools, it would be important to study the content and framing of the contracts that the contract automation tools use as references, to avoid the development of "garbage in, garbage out" contract automation systems (Haapio & Linna 2020). Moreover, future studies could focus on the parameters of contract automation tools to determine whether they are really likely to bias contract functions toward safeguarding, and contract frames toward prevention, as current research suggests (Rich et al. forthcoming).

6 Conclusions

The overall objective of this dissertation was to study the functions by which companies use contracts in their interorganizational exchange relations, and the relationship between contracts, contractual functions and relational governance. During the research project, I focused on three aspects: First, I studied the functional contracting process as a precontractual integration tool in a case in which a company tried to implement a new business model and introduce a new solution offering to its business network. Second, I examined the ways in which contracting experts used contracts and how they perceived the relationship between contracts and relational governance. Finally, I analyzed ten purchase contract documents to determine what contractual functions they included and how they were framed.

This study found that, in addition to the functions identified by previous research—safeguarding, adaptation and coordination—contracts serve codification, internal management, collaboration, and policy functions. In line with previous studies, I found that contracts were widely used for safeguarding the interests of one contracting party. Essentially, organizations seemed to be burdened by outdated power-based supplier strategies, as their contracts were full of preventively framed unreasonable risk transfers and one-sided clauses. In particular, the collaborative function and promotive framings of contracts were underutilized.

Based on my findings, I argue that current contracting practices and traditional contract theories that overemphasize opportunism are detrimental to today's network economy, which is characterized by rapid, unanticipated disruptions, such as the COVID-19 situation which began in 2020 and is still ongoing. Thus, I urge both academics and practitioners to adopt a functional understanding of contracts, which brings to the fore their managerial and relational uses, as well as contract design choices that underline the promotive, user-friendly aspects of contracts. This understanding draws on the ideas of the proactive contracting scholars who call for a broader understanding of the role and function of a contract and suggest that contracts should be designed from legal, technical, business, and relational perspectives. This means that although contracts are legal devices that manage risks and provide safeguards against possible problems in the business relationship, they are also tools for performance planning and communication, for facilitating proactive

coordination and flexibility to adapt to changing circumstances, and for designing and framing collaboration, business relationships and the interaction within them (e.g. Rekola & Haapio 2011; Haapio 2013; Kujala et al. 2015).

Moreover, like proactive contract scholars, the functional approach to contracting highlights the importance of the relationship between formal contracts and relational governance (e.g. Pohjonen & Visuri 2008; Nystén-Haarala et al. 2010; Nuottila et al. 2016; Passera 2017). In essence, I argue that contracts need to reflect the exchange relation and should not ignore, or even worse, contradict the relational norms of the exchange (e.g. Frydlinger et al. 2016). In other words, if parties want to create a collaborative exchange relation, the contract also needs to support collaboration by establishing governance mechanisms that enable open information exchange, joint learning and problem-solving. Moreover, contracts need to be framed in a manner that expresses trust and commitment to joint objectives (e.g. Nystén-Haarala et al. 2010; Nuottila & Nystén-Haarala 2019). This way, they support economic objectives while also shaping the parties' expectations, relationship and collaboration (e.g. Rekola & Haapio 2011; Passera 2017). Previous studies presented similar ideas of including the "soft" elements of exchanges in formal contracts, and now finally, these ideas have also gained momentum in economics (e.g. Frydlinger & Hart 2020).

I acknowledge that the transition toward the functional understanding of contracts is not easy. Organizations need tools to support them in this transition. This dissertation introduces such tools, two conceptual models—the functional contracting process and the functional contracting framework—to help organizations utilize the approach in their negotiation and contract design processes. These models can be tested and further developed by future studies. In addition to concrete tools, however, I argue that legal education must be reoriented toward the functional contracting approach and that students need to be taught empirical and practical skills. Only in this way can we legitimize the functional contracting approach as a relevant theory for contract law scholarship and contract law practice.

Abbreviations

ALI	The American Law Institute
ALR	American Legal Realism
ANLR	American New Legal Realism
B2B	Business-to-Business
B2C	Business-to-Consumer
B2G	Business-to-Government
CEO	Chief Executive Officer
CSR	Corporate Social Responsibility
C2C	Consumer-to-Consumer
DIMECC	A Strategic Center for Research in the Finnish Digital, Internet, Materials & Engineering Industries
EESC	The European Economic and Social Committee
EU	The European Union
FIMECC	Finnish Metals and Engineering Competence Cluster Ltd
GRI	Global Reporting Initiative
IPR	Intellectual Property Right
JFT	Tidskrift utgiven av Juridiska Föreningen i Finland
KPI	Key Performance Indicator
MoU	Memorandum of Understanding
NCCUSL	The National Conference of Commissioners on Uniform State Laws
NCMA	National Contract Management Association
NDA	Non-Disclosure Agreement
OECD	The Organisation for Economic Co-operation and Development
OEM	Original Equipment Manufacturer
RFT	Regulatory Focus Theory
R&D	Research and Development
TCE	Transaction Cost Economics
T&Cs	Terms and Conditions
TEKES	The Finnish Funding Agency for Innovation
TENK	The Finnish National Board on Research Integrity
UCC	Uniform Commercial Code

UN	United Nations
WorldCC	World Commerce & Contracting (formerly International Association for Contract and Commercial Management IACCM)
WTO	The World Trade Organization

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Annex 1: Division of work in co-authored Publications

Publication I

The initial idea for this Publication came from Johanna Liinamaa, and thus she was the corresponding author, leading and coordinating the writing process. I participated in the explorative, collaborative action research project that comprised the data of the Publication, by attending most of the monthly meetings, all the MoU development meetings, and occasionally other meetings. Together with Mika Viljanen and the company representatives, I was in charge of developing the functional contracting process. I took the main responsibility for writing sections 2.4 and 2.5, and I wrote most parts of sections 4 and 5 together with Mika Viljanen. I also contributed to other sections of the Publication and commented and edited the sections written by other my co-authors.

Publication II

Publication II is based on the same action research study reported in Publication I. In Publication II, Mika Viljanen and I were in charge of the entire writing process. We wrote all the sections together, while the other co-authors commented on and edited the writing.

Publication III

I was the corresponding author of this Publication and had more responsibility for analyzing the data as well as writing the Publication than my co-author Sampo Viding. Essentially, I wrote all the sections of the Publication, while my co-author commented on and edited the writing. However, we designed and conducted the interview study together.

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