

## **CONTRACT OR CONTRAP?**

by Stephen Toomey (Proprint Magazine - May 2005 issue)

Contracts are negotiated every day. Sometimes we underestimate their importance or are blasé about them. Often we fail to appreciate their commercial benefits, or the adverse consequences, which may flow from them.

Generally, contracts include any agreements that deal with the supply and acquisition of goods, the provision of services together with agreements relating to finance, hiring, employment, property (both real and personal, intellectual, tangible and intangible) and leases, to identify just some.

A contract should be written so that a person reading it, in good faith, can understand it. With the right provisions, it can add significant value to any business through reducing margins, increasing profits, reducing losses, deriving tax benefits and quarantining and limiting risk.

A contract with inappropriate provisions may lead to the parties to it not obtaining what they bargained for.

### ***Commercial contracts***

A good commercial contract should encourage cooperation. A contract that contains elements of mutuality is better than one that imposes requirements, which cannot be met or contains terms which discourage its proper performance.

Good contracts arise from careful negotiation. They arise from agreement being reached on the underlying subject of the contract and the development of provisions that reflect the agreement and the objectives of the agreement. To ensure a contract is drafted appropriately the parties should each be aware of each other's expectations with respect to what the contract is to deliver.

Properly drawn, a contract can achieve the desired commercial outcomes as well as minimising tax (including stamp duty), capping and quarantining risk, and protecting assets.

Good business practice calls for a commercial strategy to ensure an appropriate commercial contract. Such a strategy involves:

- Planning ahead;
- Ensuring the outcomes you envisage the contract is to deliver are consistent with your overall business strategy;

- Identifying the objects, objectives and desired outcomes of the contract;
- Identifying what is to be given and what is to be received;
- Developing objective criteria and making the procedures and standards to be adopted under the contract fair;
- Identifying the revenue and tax implications;
- Obtaining the benefit of good accounting and legal advice at the outset;
- Determining the correct entity to enter into the contract;
- Where possible, arranging to prepare the first draft (even if that results in an expense you could otherwise avoid);
- Ensuring that the warranties, representations and statements made in the negotiations by the other party find their way into the final formal contract.

### **Monitor Contractual Performance**

Often in the performance of a contract little regard is paid to the many obligations within it. Both intentional and unintentional breaches go unnoticed or unchallenged, often because the parties are not administering the contract with significant rigour or monitoring the manner in which it is being performed; the contract assumes a life of its own and the parties deal with each other without real reference to the contract and its terms. Frequently there will be miscommunications because the protocols within the contract are not observed.

Miscommunications are often the cause of disputes and claims.

Paying attention to the detail of the provisions of a contract and the continued scrutiny of the performance of the contract (both your own and the other party's) will afford benefits, as well as help to avoid disputes, unnecessary costs and the waste of resources.

### **The best contractual outcomes**

Never underestimate the benefit of properly negotiated contracts.

It's not a good idea to simply accept what is proffered. Generic contracts don't suit everyone and rarely suit anyone. They invariably need refining. Often there is opportunity to negotiate and that opportunity should always be taken. Be sure that the contract's terms are clear and concise, and deliver the desired outcomes.

Seek legal advice at the outset to establish the parameters of the contract before they are *commercially set in stone*.

Remember, it's much easier to establish the parameters of a contract in the initial stages, rather than undo them later on.

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