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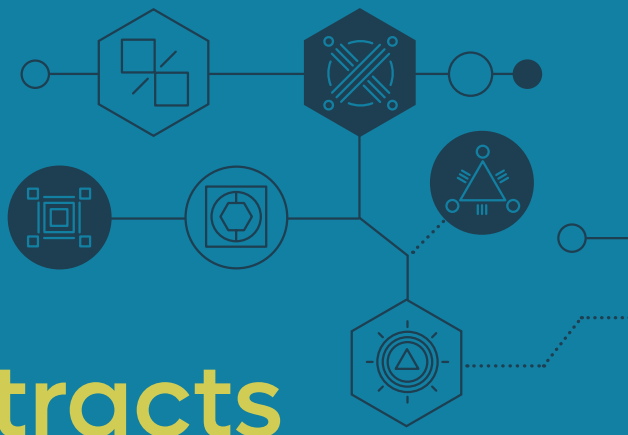

Negotiating Contracts

How to get them done quickly, and properly

Negotiating contracts can be a frustrating experience. You send your contract to the other side, and they return it with deleted clauses, amended clauses, new wording and a raft of tracked changes.

Not only does it take time to wade through the changes, but this sort of to-ing and fro-ing introduces a level of doubt into your process.

Which changes do you accept? What impact will that have on the business? Does the legal wording reflect the practical realities?

It takes a fair bit of experience to build confidence in negotiating contracts. Over time, you learn which points to concede and when to stand your ground. In the meantime, we've put together a few pointers to give you a steer.

Which points to concede in contract negotiations

In general terms, the points you can concede are any additions or changes which don't prejudice you. For example:

- **Clarification wording**
- **The addition of an obligation you're happy to carry out**
- **'Haggling' points: Do you really want to waste time arguing whether or not default interest rates should be 2% or 4% above base?**

The easy points to concede are those that are fairly immaterial to you.

But when it comes to changes that place more obligations on you, or increase your liability, what do you do then?

First, ask yourself if you can live with that change. Even if it is an extra obligation, there's no harm in agreeing to it if it's straightforward for you to take it on. If you can't agree to it, either reject it outright, or amend the wording.

Then think about what would happen if you were to breach the clause. Practically, what will the knock-on consequences be? Will that cause major issues for you or the other side? Remember that some breaches of contract will result in damages for the other side, and they may have the right to rescind the contract.

Once you've thought it through in those terms, you'll have a clearer view of whether to accept the change, reject it, or tweak the wording.

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When to stand your ground in contract negotiations

What are the changes that you really don't want to concede? Here are a few generic examples to think about:

Pricing

Is the proposed change to the price commercially viable for the business?

Payment

Changes to payment terms can have significant consequences for the business and its enterprise value. For example, if you're a SaaS business, you need to be wary of changes that can affect your ARR (Annual Recurring Revenue) metrics.

Term

Have you worked out the price based on a minimum term? If you change the term of the contract, will you need to make a corresponding change to the price? Might there also be ARR consequences?

Service levels

Your customer may request higher service levels than you first proposed. You can accept this if it is genuinely achievable for you. But consider the practicalities of having different service level agreements (SLAs) for different clients and also consider 'flow-down' – for example, you can't promise a better SLA than those provided by your suppliers (for example, hosting availability SLA).

Intellectual property

Customers will often try to seek ownership of your deliverables, particularly if they deem them to be bespoke. But don't give away your valuable assets. If the proposed change tries to claim ownership over your IP, it's wise to reject that change.

Fairness

If the issue is unfair, don't agree. Of course, 'fairness' can be subjective and what's fair to one party is totally unreasonable to another. Put simply, if it's unrealistic for you to achieve it, don't agree to the proposed change.

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Grey areas in contract negotiations

The nature of negotiation is give and take. Agreeing to changes in some clauses can give you leverage to make changes to other clauses that are more important to you. So some changes may be tactical.

The 'grey' areas are those clauses that can be amended, to a degree, if you have to. These are often quite 'legal' clauses where you may need a bit of interpretation from the lawyers. For example:

Limitations of liability

Customers will regularly request you take on higher levels of liability and even unlimited liability for certain things. There is a lot of accepted practice around what is and isn't reasonable and you should always consider these requests very carefully before agreeing anything. Taking on too much risk v reward can have serious consequences for the value of a contract and your business.

Warranties & Indemnities

Again, it's common for customers to request changes to warranties and indemnities, which are designed to give them more protection. The flipside for you is that these clauses increase your obligations and potential liability. It's that more risk v reward equation that we mentioned above.

There are certain warranties and indemnities that won't be appropriate for you to give and others may be appropriate with the corners knocked off. It's one of the points to bear in mind before you begin your negotiation.

With all that in mind, you can see that you can't negotiate in a vacuum. You need a strategy as a business, and you need to agree your 'red lines'. You also need to prepare your responses to certain common requests. For example, a stock response to customers could be: "our SLAs are standard. We don't deliver different SLAs to different customers."

The main thing to agree internally is your attitude to risk. As a business you need to fully understand where the main risk points are – where and to what extent could you cause problems for customers that could leave you liable to them? If you understand this, you can then work out where you can/can't take on more liability when customers request it. This helps you form an agreed approach to risk v reward which can be applied to negotiations.

Not all of your contracts hold the same weight for your business. Some contracts are more strategically significant than others. If the contract is especially important to the business, then you might take a more lenient approach to negotiation.

With every contract negotiation however, keep one eye on the long-term business goals. When it comes to selling your business, purchasers will review all of your contracts as part of the due diligence exercise. Any contract that carries with it too much risk or liability could be seen as a red flag for a buyer, or a reason to reduce the price they offer.

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How to find lawyers with a pragmatic approach

At some point, you might want to get lawyers on board, either to bounce ideas off, or to make sure you haven't overlooked a legal point. While you have a good understanding of the commercial issues, it's not always easy to translate these into the legal drafting.

If you want to keep costs down, and reduce any red tape and delays, you need lawyers that take a pragmatic approach.

But lots of lawyers will tell you that they are pragmatic. What should you be looking out for in a genuinely 'pragmatic' lawyer? Here are a few suggestions:

Experience

Brand new lawyers tend to be legally accurate, but haven't had the commercial experience to take a practical view. The more years' experience a lawyer has, the more rounded their understanding of business, commercial relationships, and impact of risks and liability.

Responsiveness

Slow responses often mean that there are layers of supervision at play in the law firm. Each and every email will be checked by a more senior lawyer. That means that each and every decision about the contract will have multiple lawyers' input, which ends up escalating costs.

Regularity

Regular reviews of your contracts make sure that they don't get out of date. Your lawyer should be suggesting at least an annual review of your contracts to capture any changes to the business over time.

Turning down work

This is an unusual one! But genuinely pragmatic lawyers will sometimes tell you that you don't need advice. A 'belt and braces' approach would nit-pick over every possible risk and scenario, but if it's a commercial decision at the end of the day, then you don't necessarily need to spend money on legal advice.

A tool to speed up contract negotiations

As you can see, there's a bit of groundwork to put in place before you're confident that you're negotiating contracts in line with the business strategy. You need some way of defining your appetite for risk, and assessing the obligations that you're willing to take on.

We try and make it a bit easier for our clients, helping with the risk assessment and giving you a 'playbook' to use for your contract negotiations. We call it our Contract Manager, and you can find out more about it **here**.

If this sounds like something that could speed up your contract negotiations, please get in touch. We're happy to have a chat about how it works, and how it could be used in your business.

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