Top 7 Mistakes That Promoters Commit During Contract Negotiation

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1. USING DOWNLOADED TEMPLATES[1]

When the parties randomly use downloaded templates that are generally available on the internet, then the negotiations are bound to take very long.

Example: A well-known IT company is sourcing cleaning solutions and equipments for its office. Naturally, the draft that is generally used for appointing software vendors cannot be used. As the intention in both the transactions is different and using the template created for some other purpose, just because it is available may be a blunder and may unreasonably delay the negotiation time, resulting into delay in closing contract.
In fact, Sale of Goods Act, 1930 in India specifically attaches a lot of importance to the intention of the parties and more than 15 sections which are subject to the intention of the parties. More information can be found here[2].

2. EYE WASH PROPOSALS

One must remember that a proposal is a key document to share with customers and must be elaborate enough to cover key commercial points in order to avoid misunderstandings later.

For instance, as a distributor, if one is keen on a minimum term then the proposal could mention the same. If a Software Developer is going to use certain third-party components, then the proposal should disclose the same. Intellectual property rights are very crucial and third-party intellectual property rights cannot be transferred without having necessary rights to sub-license.

3. REVIEW OF AGREEMENT ONLY FROM TAX ANGLE

Agreement is a bundle of multiple rights and obligations. If the agreement is simply reviewed from the tax angle only while disregarding obligations and other risks, then naturally the expectations of the parties are different. With mismatch in expectations, either party is likely to be dissatisfied which may lead the arrangement to be dispute prone or end up in litigation.

[1]The article reflects the general work of the authors and the views expressed are personal. No reader should act on any statement contained herein without seeking detailed professional advice.
[2]Microsoft Word - 5-Intention of Parties_Sale of Goods Act Article 4.docx (ynzgroup.co.in)

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4. INITIATING TRANSACTION WITHOUT DOCUMENTATION

Sometimes, the entire transaction is initiated without proper documentation. Thereafter, the contract becomes necessary for the parties to ensure proper payment and audit purposes. In such cases, the parties have acted on their own accord, but the documentation may contain representations and warranties which may seem difficult for a party to agree.

Example: A Supply Agreement may need the supplier to obtain prior consent from the customer for all its raw material manufacturers. Now, if the parties have commenced the transaction and the customer is not willing to consent to the raw material supplier of the vendor, it could be an issue. As the transaction has commenced, it may lead to a deadlock situation as the supplier may not be in a position to change the raw material vendor and customer is not willing to accept such vendor due to other issues like improper compliance documentation etc. This may well be beyond their ZOPA: ZONE OF POSSIBLE AGREEMENT[3] .

5. ORAL COMMITMENTS

Oral commitments are always a barrier to a proper contract and create confusions. Sometimes, parties give oral commitments that the agreement should be signed as it is without negotiations and harsh provisions will not be pressed in reality.

Example: Parties are negotiating a Services Agreement, specifically on a clause related to the customer's right to conduct a financial audit. Looking at resistance, the customer may orally commit that he/she will not enforce his/her rights of conducting such financial audit, but the vendor should agree to the clause being a mandatory clause. Relying on such oral commitments during negotiations, makes one tread on unsure arenas, especially if the same are not made from the appropriate stakeholders. It is always advisable to modify the agreement suitably during negotiations to reflect the true understanding.

[3]Zone Of Possible Agreement (ZOPA): Definition in Negotiating (investopedia.com)

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6. ADOPTING A COMPETITIVE APPRAOCH RATHER THAN WIN-WIN APPROACH

Negotiations can be successful only if the parties actually adopt a win-win approach instead of pushing the interest of each organization forward only. Of course, each contract has certain key elements for each party which will naturally favor one party. However, on certain clauses collaborative approach instead of competitive approach can be adopted. Like in a software license agreement, parties could insist on an absolute intellectual property warranty but agree on a mutual confidentiality or data protection clause.

Example: A vendor is negotiating a Receivable Purchase Agreement with a bank. Considering the nature of the arrangement, the Bank insists that each invoice from the vendor must contain a specific notification to mention Bank's charge on the receivables from such invoices. While the Vendor agrees on the aspect of inclusion of the notification, the vendor may want certain language edits and also negotiate on the exact placement of such notification on the invoice.
The Bank could consider the format and language edits.

7. IDENTIFYING THE BREAKING POINT

Typically, contracts provide a good faith negotiation before either party goes for litigation or arbitration. While parties commence negotiation, it is important to identify the breaking point or the impasse.

Breaking point is defined by the Supreme Court in a judgment delivered on 18th May 2023, M/S B AND T AG versus MINISTRY OF DEFENCE, ARBITRATION PETITION (C) NO. 13 OF 2023; MAY 18, 2023, as the date at which the cause of action arose for the purpose of limitation.
To understand this better, cause of action is a set of facts that entitle one party to sue another.

The Supreme Court decided over a dispute under which, the Ministry of Defence had awarded a tender of procuring over 1568 Sub-Machine Guns through a fast track procedure to a Swiss Company. Thereafter, due to delays, the government invoked the bank guarantee and imposed liquidated damages in 2016. The company claimed that they were negotiating on this from 2016 till 2022 which was not accepted as the Supreme Court said the Parties were already at breaking point in 2016 itself and the action was rejected on the ground of limitation.

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"What is more important is the fact that the respondent on 26.09.2016, deducted the amount towards recovery of the liquidated damages. The requisite amount was credited into the Government account in accordance with the instructions contained in the letter dated 11.08.2016. This was the end of the matter. To say that even thereafter, the petitioner kept negotiating with the respondent in anticipation of some amicable settlement would not save the period of limitation.
Negotiations may continue even for a period of ten years or twenty years after the cause of action had arisen. Mere negotiations will not postpone the "cause of action" for the purpose of limitation. The Legislature has prescribed a limit of three years for the enforcement of a claim and this statutory time period cannot be defeated on the ground that the parties were negotiating."

For any feedback or response on this article, the authors can be reached on aarti.banerjee@ynzgroup.co.in and ashvini.kandalgaonkar@ynzgroup.co.in

Author: Aarti Banerjee

Aarti is a Partner - Corporate Legal Advisory:

Aarti is experienced in corporate legal matters having specialization in drafting, vetting and negotiation of agreements. By qualification she is an advocate and a solicitor.

Co-author: Ashvini Kandalgaonkar

Ashvini is a Partner- Corporate Legal Advisory, She is experienced in corporate litigation and non-litigation. She is experienced in Corporate litigation and non- litigation. She provides training required under POSH Act.

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