

Commercial Insights

Dangers in negotiating commercial agreements

Commercial agreements vary in complexity, the length of time parties are involved in negotiations, and importantly, in the level of formality the parties employ as they ‘thrash out’ the terms. For these reasons, it is sometimes difficult to work out when the negotiations have reached a point where the law would regard the parties as having reached a binding and enforceable agreement.

It is not uncommon for people to assume that they can enter into a negotiation and will not be bound to any agreement reached with the other party, unless and until the agreement is documented and signed. However, this is not the case, except in some cases where the law requires a written agreement. An agreement can be found by a combination of written evidence (email communications for example), oral discussions (including for example verbal representations), and the conduct of the parties (the actions that are taken).

In broad terms, the courts have categorised the effect of negotiations between the parties as falling into one of the following four categories:

1. The parties have negotiated the terms of their agreement, are in agreement and intend to be bound, but wish for the terms to be outlined as they are in a formal contract document. In this circumstance, the parties are bound by their agreement notwithstanding that it has not been fully documented and signed.
2. The parties have negotiated the terms of their agreement, are in agreement and intend to be bound, but wish for the performance of those terms to be conditional upon their execution and exchange of a formal contract document. In this circumstance, the parties have an obligation to ensure that the agreement that has been reached is documented and are bound by that agreement.
3. The parties do not intend to make an agreement at all until a formal contract document is executed. In this circumstance, the parties are not bound by what they have negotiated unless and until the agreement is documented and signed.
4. The parties have negotiated the terms of the agreement, are in agreement and intend to be bound, but expect to make a further contract in substitution for the first agreement which contains additional terms, yet to be agreed. In this circumstance, the parties may be bound by what they have agreed notwithstanding the fact that the agreement may not yet be documented. Whether or not the parties are bound will depend upon the importance of the additional terms not yet agreed to the operation of the agreement.

The above summary highlights that parties need to be careful about the language used when negotiating agreements. When negotiating an agreement it is important to make it clear to the other party, whether or not you intend to be bound by the negotiated terms, when those terms may not have yet been documented.

Confusion, ambiguity and uncertainty can arise when one or more parties have not clearly indicated whether they have reached a point in the negotiation where they intend the terms to be binding on them. It is also understandable for comments made during a contract negotiation to have an unintended consequence, especially when parties have not made it clear whether or not they intend to be bound to the negotiated terms.

Meridian Lawyers' Commercial and Corporate team frequently advises clients during contract negotiations and helps clients navigate the sometimes dangerous waters that exist between a robust contract negotiation and a concluded and enforceable agreement. Our Dispute Resolution team works with clients in resolving disputes that have resulted from misinterpretations of language in commercial agreements and misunderstanding parties intentions. This note serves as a timely reminder of the need to take care during contract negotiations so that there is no uncertainty about the status and legal effect of the negotiations at any given point in time.

This article was written by Lawyer, Alexander Hughes. If you have any questions about commercial agreements, please contact Meridian's Commercial Disputes team.



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