CONTRACTS

What should go in (and what might sneak in)

Useful for: Business, Government, Local Government
Article looks at: Contractual Terms

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In Brief:

- Every legally binding contract should deal with these 6 pillars: Who, What, Where, When, How and How Much?
- Special clauses dealing with intellectual property rights and obligations, privacy/data protection/indemnities etc will be more or less relevant depending on the nature of the contract.
- Construction contracts, leases (and occupation licences) and employment/independent service providers contracts must be looked at from a different perspective as these areas are governed to a large degree by their own bodies of legislative and general law and the considerations can be quite different from other types of contracts.
- When entering into a contract always bear in mind that it may contain terms by operation of law that cannot be contracted out of. In particular, the Australian Consumer Law imposes certain consumer guarantees on all consumer contracts, and if it is a standard form contract, the unfair contract terms regime will also apply.

COMMON CONSIDERATIONS WHEN CONTRACTING

Every Contract should answer these 6 questions – Who, What, Where, When, How and How Much?

Who? Who am I actually dealing with here? Is the name on the contract a legal entity? Is this the right entity to contract with? Can this entity deliver what I want? If I am taking on risk by dealing with this entity (for example because it is a $2 company with no or few assets), should I require security for performance? Do your upfront due diligence (see related articles "**Due Diligence – Who are you getting into bed with?" and "Credit Control – Where's My Money?"**).

What? What am I getting? What do I have to do? What does the other side have to do? Do the obligations set out in the contract match my perception of what the "deal" is? Are service levels/key performance indicators relevant? If they are, ensure that the ramifications for failure of same are precisely set out in the contract to ensure there are no hidden unintended consequences of the breach.

Where? Where will the contract be performed? In my office? At the other party's place of business? In Africa? For supply contracts – where are the raw materials/goods being sourced from? What happens if there is a failure in the supply chain? What could be the impacts of dealing with a company located/incorporated in a foreign jurisdiction?

When? When do the parties' obligations need to be performed by? Milestones? Final completion date? Is the timeline clear and correct? What are the ramifications for late/failure of performance of a milestone or late completion of the contract?

How? How are the obligations to be performed by the parties? Are key personnel (certain people) required to do the work? Do I have the right resources and enough of them to perform and avoid penalties/damages being claimed by the other party? Does the other side actually have the capacity to perform their side of the deal? What are your rights if the owners of the counterparty change? If key personnel change?

How Much? What is it going to cost me/them? Don't forget to factor in GST and ensure there is an appropriate grossing up clause where the agreed price is exclusive of GST. When is the price payable? Will there be an upfront deposit payable? How will it be secured (ie. kept safe from a party going into liquidation) until completion of the contract? Will there be milestone payments? For Government bodies – follow the procurement rules - do I have the budget/appropriate approvals to proceed? For bodies that are using government funding to carry out the contract, am I in compliance with the funding agreement?

SPECIAL CONSIDERATIONS

Intellectual Property

A clause dealing with the IP rights of the parties is very important if the contract envisages that intellectual property rights will be used or created in the course of conduct of the contract, or if existing IP rights of one or more of the parties will be used by others either for the purpose of the contract, or ongoing into the future after the contract ends.

Assets in which intellectual property rights subsist include patents, copyright (including moral rights under the Copyright Act), rights in circuit layouts, registered designs, trademarks, Indigenous Cultural IP, and other rights. Intellectual property rights are each governed by their own laws and legislation (including UN Declarations/treaties), so it is very important not only to deal adequately with rights and obligations in each individual contract, but also to ensure your IP is properly protected under the specific relevant laws (which may require a registration process to be completed in order for ownership rights to arise).

Within the contract, the IP clause should deal with:

- Who owns what IP at the commencement of the contract.
- Grants of licences one to the other party or parties to use one's IP for the purposes of the contract (if you intend to grant rights that will live on after the particular contract is completed these are best dealt with in a separate agreement or deed).
- Terms of the licence – eg. royalty free? Nature of fee (if relevant)? Nature of licence – is it only for non-commercial use or can other parties commercialise? Publication and reproduction rights?
- Effects on third party IP rights – warranties that the grant of licenses will not infringe the rights of third parties.
- Who will own what IP at the conclusion of the contract and any ongoing rights/obligations of the parties.
- Do you need, or do other parties have, the right to sub-licence IP, and if so, on what terms?

Privacy/Data Protection

Will you or the other parties be handling personal information of individuals?

If the answer is yes, then ensure the contract deals with each party's obligations in relation to compliance with the Privacy Act, and, if the contracting parties (or any of them) operate

in or are connected with the EU (for example, an Australian company that handles personal information of customers in the EU), then compliance with the General Data Protection Regulation.

A privacy clause will also ideally contain details about:

- How personal information will be handled and protected by the contracting party (often expressed as an obligation on all parties to comply with the Privacy Act (and/or individual State and Territory Acts dealing with handling of information) or simply to comply with the Information Privacy Principles set out in the Act (see the privacy principles and common examples of personal information at the website of the Office of the Australian Information Commissioner), or for State and NT public sector organisations, the legislation in your own State or Territory dealing with the collection and use of personal information.
- An obligation on relevant parties to ensure their subcontractors comply with all relevant Privacy laws.
- Depending on the type of contract, indemnities to protect the parties from damage caused by privacy or data breaches by another party.
- Where data will be held (generally, State and Territory legislation will provide that personal information contained in government contracts must be held within the jurisdiction, or within Australia, unless otherwise stated by policy/the contract).
- How data will be secured (if relevant).

Government contracts are also likely to also contain a "Public Accountability" clause, which deals with the special responsibilities of government, for example under "Independent Commissioner against Corruption" legislation and enables government to pass through some of its obligations to its contractors, including but not limited to the obligation to identify and avoid improper conduct. Government contractors should familiarise themselves with the relevant legislation and ensure they understand the special responsibilities that may pass to them by virtue of the fact that they are government contractors.

For further information about Privacy see related article "**How Private is Private Enough?**".

Confidentiality/Publicity

These clauses deal with the circumstances under which some or all contractual terms can be disclosed to third parties and the terms that govern what parties can say about the contract and when. Confidentiality (or non-disclosure) agreements are often used in business relationships before contracting, during the life of a contract, and sometimes continuing after the contract is concluded. Such agreements or clauses protect your commercially sensitive information (including where relevant, your intellectual property) from becoming public, or falling into a competitor's hands.

Ensure you have a confidentiality clause in the contract if it contains sensitive commercial or financial information.

Confidentiality Obligations outside the contract

You may want to ensure that pre-contractual or stand-alone negotiations are kept confidential by use of a confidentiality (non-disclosure) agreement or deed separately up front, which will take you through to when the executed contract takes over but will continue in force to protect your commercial information even if you never enter a contract. Sometimes confidentiality issues are only relevant in pre-contractual negotiations, but often they carry through the life of the contract and beyond.

Examples of where a non-disclosure agreement will be useful on a "stand alone" basis are when you are disclosing information:

- To pitch to potential investors.
- To explore the feasibility of a project that will be carried out with others.
- Entering into employment and independent contractors' relationships, bringing on partners, shareholders or developing other business relationships;
- Looking at the suitability of potential service providers to your business.

Confidentiality agreements/deeds or provisions within a contract will usually provide that if there is a breach or anticipated breach, damages (money) will not be an adequate remedy and the injured party may seek an injunction from the court to stop disclosure (where it has not already occurred), in addition to orders preventing further or other disclosure where it has occurred and awarding damages in addition to those remedies.

In certain circumstances there is an action available for breach of confidence under the general law (meaning that a remedy will be available through the Courts notwithstanding

that there is no agreement or clause in a contract). It is however, far preferable to have these obligations protected contractually.

Warranties

A warranty is a statement about a certain state of affairs, and if breached, gives the other party a separate right to sue for breach of it, without that party having to prove a breach of the contract itself. Breach of the warranty may or may not also give rise to a right of termination, depending on whether the contract provides for it. A breach of warranty will not usually permit termination under the general law.

Warranties are generally given in respect of matters that the counterparty could not ascertain by making reasonable enquiry of public registers and authorities, and if the information turns out to be wrong, it would be reasonable to assume the party would not have entered into the contract.

Common examples of warranties are:

- that a party does not have a conflict of interest;
- that a company or business is not carrying debt or liabilities other than those disclosed or showing on the face of the financial documents of the company;
- that a Trustee has certain powers or authorities to deal with trust assets;
- that a purchaser has relied on its own enquiries and not on any statement or document produced by a vendor of property or shares in a company;
- that a party is not a foreign interest in a purchase of property;
- that plant and equipment is in working order on a sale of business;
- that the parties executing a document has full power and authority to enter into the contract;
- that a business is not insolvent.

Indemnities

An indemnity is an undertaking on the part of one contractual party to compensate, protect, or insure another person or entity against future financial loss, damage or liability.

The form, context and scope of protection of an indemnity varies depending on the nature of the contract and the risk profile of each party, therefore indemnity provisions shouldn't be glossed over as "standard", but require careful thought by the party being indemnified to ensure its risk is covered, and a thorough understanding by the party indemnifying of the

risk that party takes in giving the indemnity (including any ramifications on its business protection insurances).

An indemnity protects the indemnified party against loss that it actually sustains. It doesn't cover losses suffered by third parties. In practice, an indemnity clause will "ring fence" the types of losses that are indemnified. Common ones are losses sustained because of the indemnifying party's negligence, breach of contract, breach of specific laws or statutory duties, and/or arising out of the use or misuse of property.

In practical terms, an effective indemnity potentially saves the indemnified party from the time and expense involved in having to bring a court action for breach of contract or negligence and prove all the elements of the cause of action, before obtaining damages. Once the loss has actually been sustained, so long as the damage being claimed is within the scope of the indemnity, the indemnified person simply brings an action for recovery of that loss on the basis that it is a debt payable under the indemnity provision.

Indemnity provisions should always be drafted and/or advised on by lawyers, as the courts are notoriously inconsistent in the interpretation of the breadth and scope of indemnities, which are often not well thought out having regard to the particular circumstances.

Force Majeure/Suspension of Contract

Force majeure (i.e. unforeseeable circumstances that prevent a party performing a contract) is not a concept that is recognised at common law. This means that if parties wish to provide for what happens in circumstances where an event makes performance either temporarily or permanently impossible, they must include it in the contract.

In contracts that run for a significant period of time (eg. construction, period for ongoing works or services), or contracts that involve occupation of land (leases/licences) a force majeure clause may be beneficial.

Traditionally, force majeure events were limited to Acts of God, fire, storm, tempest, civil riot, industrial action and the like. Events may be widened to include pandemic, epidemic, and/or simply any event that is beyond the reasonable control of a party.

A properly drafted force majeure clause provides that where a relevant event occurs, the obligations of one or more parties to the contract will be suspended during the period that the effects of the event continue, provided that the party affected by the event takes reasonable measures to limit or stop the effects of the event on the contract and resumes

performance as soon as practicable. Generally, if the circumstances have not returned to normal within a certain period of time, there will be a right to terminate, either by the party not affected, or both/all parties. Be careful to ensure that obligation of parties to pay money suspend in line with the suspension of obligations to complete work.

In a lease or licence, you may see this clause expressed as "premises unfit for occupation" or similar, which essentially covers all practical circumstances occurring that make the premises unfit for occupation by a tenant, rather than focussing on what the event itself is. Typically, rent will be abated for the period that the premises continue to be unfit for occupation and provide for termination in due course should the premises not be restored by the landlord within a certain timeframe.

Insurances

Generally speaking, some level of insurance should be, or will be required to be carried by all parties to a contract. See related Article – "**Insurance – Back to Basics**" for information about different kinds of policies and what they cover.

GENERAL OR STANDARD CLAUSES (SOMETIMES CALLED "BOILER PLATE" CLAUSES)

Standard clauses are often glossed over and assumed to be meaningless "legalese". This isn't so – a well drafted boiler plate clause can provide a quick solution to all kinds of legal issues and avoid costly litigation.

Ensure you have at least, the following:

- A survival clause (this stops certain obligations from ceasing when the contract terminates or expires) – you will ordinarily want this to operate in respect of IP rights, confidentiality, privacy, warranties and indemnities, and depending on the nature of the contract other obligations may warrant continuation after the contract ends.
- A governing law clause – while nothing is foolproof, for the most part this ensures that there won't be significant argument over the court system that has jurisdiction to hear disputes in relation to the contract and is especially important in supply contracts where one or more parties are incorporated in, or located in, foreign jurisdictions.
- An "entire agreement" clause – states that the written contract contains the entire agreement of the parties and avoids arguments about whether verbal representations or ancillary documents form part of the contract or not. Again, not foolproof as this clause won't save you from the Australian Consumer laws (where applicable), but otherwise set the boundaries of the terms of the contract effectively.
- A "severance" clause – which provides that if a court decides that one or more clauses is void (not valid or legally binding), they may be removed from the contract and the balance will remain enforceable. This can save a contract from failure, but it depends on what the void provisions are. If the whole substance of the contract is void, then the contract will fail.

WARNING – SOME TERMS CAN SNEAK IN!

The Australian Consumer Law (ACL) imposes heavy restrictions on providers of goods and services from contracting out of their liability for the delivery of those goods and services. The Consumer Guarantees are a set of assumptions that the law makes about the delivery of goods and services to a consumer, and if they are not met then the consumer will have certain rights - to a refund, exchange and in some cases to wider damages. These laws cannot be contracted out of and will always override anything in the contract to the contrary.

The ACL also regulates the use of standard form contracts via the Unfair Contract Terms regime. These are contracts that are not negotiated between the parties, but instead given to the consumer to accept on a "take or leave" basis. Any unfair terms contained in the contract will be void (invalid/not legally binding), and the business will not be able to rely on them. Significant penalties for breach may be imposed as well as damages to injured consumers. See Related Article – "**Supplying Consumers – Tread Carefully as Laws Sharpen their Claws"**) for detailed information about the Australian Consumer Law and its effect on business transactions.

Important Note: This article is general in nature and is not intended to be a substitute for specific legal advice in relation to particular contracts or types of contracts. The requirements of contracts will differ according to what the commercial deal is. This is an outline of matters that virtually every contract will deal with along with some of the more common special clauses. You'll find other articles on this website that deal with matters relating to special clauses and ancillary laws like the Australian Consumer Law in more detail.