

Negotiating Commercial Contracts in Uncertain Markets: The In-house Counsel Perspective

Commercial and Contracts



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Cheat Sheet:

- **Build controlled flexibility into the contract.** Ensure the contract can adapt to market volatility through structured mechanisms (not open-ended discretion) to reduce breach and dispute risk.
- **Prioritize the risks that matter most.** Work closely with business colleagues to ensure focus on the high impact areas during the contract negotiation.
- **Employ “boilerplate” clauses as strategic risk management tools.** Avoid a "copy-paste" from precedent approach; review and negotiate force majeure, MAC, and change-in-law clauses as core protections, and also use tiered dispute resolution to address operational issues promptly.
- **Use pricing and structured exit mechanics to absorb shocks.** Include index-linked price adjustments, hardship and risk sharing in the contract to account for rapid cost fluctuations, and incorporate clear suspension and termination rights to facilitate orderly contract exit and/or handovers if necessary.

Recent years have seen pandemics, major conflicts and sometimes drastic regulatory changes that have led to significant economic volatility which has impacted business contracts. Even the most carefully negotiated agreements have been affected. A judge in the English High Court recently recognized, “the unpredictability of events is such that it is virtually impossible to draft a contract so as to cover any situation that might arise without leaving room for argument or doubt”. In-house counsel should support commercial stakeholders, not with the impossible aim to completely eliminate uncertainty, but negotiating contracts that remain viable and workable even in rapidly changing conditions.

This article seeks to provide guidance on moves that in-house counsel can deploy to support contract negotiations in an uncertain market.

Incorporating controlled flexibility into commercial contracts

Typically, when negotiating commercial contracts, the aspiration is to ensure certainty for the parties. Clear scoping of rights, defined delivery obligations, clarity on liability exposure, and pricing certainty have therefore been key features of business agreements. However, recent years have illuminated the importance of ensuring contracts can adapt. Rigid contracts that cannot adapt are more likely to be breached or renegotiated under pressure, often at significant cost. As a result, it is important for in-house counsel to ensure commercial contracts have built-in flexibility and structured mechanisms that enable the parties to respond to change without undermining (or having to revisit) the commercial agreement. This is not to suggest that contracts should contain discretionary obligations or excessive flexibility that creates ambiguity; rather, the focus should be on balancing certainty with pragmatic ways to address external pressures or change, reducing the likelihood of expensive and challenging disputes.

Part of the pursuit of that balance is recognition of the fact that not all risks are of equal standing and therefore do not need to be addressed in the same way. This recognition should be familiar to all in-house counsel. The focus should be on addressing critical contractual risks, with the objective of protecting the interests of the parties in the commercial deal. Some of the key risk areas include:

- delivery milestones;
- pricing volatility and fluctuations;
- security and continuity of supply;
- applicable law and regulatory changes; and
- financial viability and solvency of a contractual party.

Any successful negotiation relies on the reasoned and justified prioritization of specific points and areas from the outset. This enables focus and greater accuracy in approach, and consequently also buys credibility with the counterparty, enabling a more structured and ultimately more successful

process. Prioritizing key areas that have a bigger impact on the commercial position of the parties, and enable the mitigation of more significant financial impacts, provides more value and is therefore preferable.

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Revisit “boilerplate” clauses

Traditional boilerplate clauses have come under the spotlight in recent years, as global events have led parties to really consider how these provisions operate in practice and whether they provide sufficient protection to the commercial interests of the parties. In-house counsel should take time to review these in the context of the commercial objectives at hand, and negotiate these points as thoroughly as needed. These clauses should no longer be relegated to the final points to add after an extensive negotiation of other parts of a contract. Counsel should give greater thought to these points, drafting and negotiating them with focus, considering:

- whether force majeure clauses adequately cover events such as pandemics and epidemics, tariff changes, and trade restrictions;
- the consequences of prolonged disruptions and the potential use of material adverse change (MAC) clauses, common in M&A contexts, in other industry areas including infrastructure and energy contracts; and
- change in law provisions which protect parties from sudden and unforeseen changes due to regulatory volatility. For example, where a new product regulation is introduced that requires additional compliance, the contract can clarify the party that would bear such costs, the acceptable time impact, and the approval process.

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Typically, these clauses are now heavily negotiated, but counsel should persevere to ensure that these boilerplate clauses provide structure to the parties and enables them to address potentially significant changes in the regulatory and economic environment. A commonly less challenged proposal, but significantly of use in uncertain markets, are tiered dispute resolution provisions that enable the prompt and agile resolution of issues that may arise. Operational

disputes, such as whether particular performance milestones have been reached, can be escalated from account/contract managers to executives within defined time limits, pushing for a prompter resolution and avoiding a formal dispute.

Alignment with key internal stakeholders on approach here is essential, but the inclusion of such provisions can be commercially and financially beneficial to contract parties.



Use pricing mechanics to avoid renegotiation under pressure

Whilst parties may consider pricing certainty to be attractive, this is often not the case particularly where market dynamics are uncertain. This lack of certainty can have an impact on the contract, with parties facing significant increases in financial obligations. Even when changes may have a favourable impact on one party, the impact on the other party could be substantial and threaten its viability, which could ultimately lead to attempts at price renegotiation, suspension of performance or could even threaten the viability of that party. This undermines the partnership model that should be at the centre of business contracts.

Counsel should consider what insurance requirements or forms of security are necessary under the contract to provide some financial protection against risk during such uncertain periods. In addition, in-house counsel should advise commercial stakeholders to ensure the insertion of pricing models that provide flexibility and build realism into the contract. This can include:

- price adjustment mechanisms linked to independent rates or indices can ensure the contract price is tracked to a published index avoiding the need for ad hoc renegotiations;

- hardship clauses which enable structured renegotiation through a formal process if, for example, delivery costs move beyond an agreed threshold;

- risk sharing by parties to account for cost increases; and
- adjustable pricing (using service credits or fee adjustments) linked to party performance thresholds in the contract.

Such an approach is not completely without risk, and it is the role of in-house counsel to properly advise the business of these potential scenarios during the negotiation process. This should be accompanied by an understanding of the risk tolerance of the business, whilst working with other key internal stakeholders such as Finance, to properly map risk and scenario plan.

Planning and designing exits

Counsel should advise businesses of the importance of including appropriate exit provisions within a contract, to provide a pressure valve that can release some of the commercial, operational, or financial pressures that can build during the performance of a contract in periods of uncertainty and change.

- Adjustable delivery dates based on fault determination, with a transparent mechanism for extensions.
- Suspension rights tied to acknowledged risk factors, such as the failure to make milestone payments or meet agreed operational completion deadlines, with make good periods.
- Distinct step-in rights to protect continuity of critical deliverables, with scope for reasonable and agreed alternative sourcing.
- Termination for convenience rights with a process for assigning costs.
- Requirement for orderly termination or handover.

The inclusion of such rights can establish a basis for the negotiations during the life of the contract when unexpected events or pressures arise, and set out the steps for an orderly exit.

Business coordination

Working effectively within a team is a key requirement for any in-house counsel, and this internal alignment is even more critical in uncertain environments. Sales, Finance, Procurement, the Project Management Office, and business leaders are all essential in defining the risk threshold of an organization. They help confirm the non-negotiable positions of the business, and provide

confirmation as to how realistic and workable the terms being negotiated into the contract are. This coordination is essential, and in-house counsel should drive engagement from these essential stakeholders to support the negotiation process.

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Conclusion

This period of uncertainty has reinforced the perspective that contracts should no longer be viewed as documents that determine the final risk for parties solely at the outset. As the now Lord Legatt of the UK Supreme Court previously acknowledged, “it can be crucial to the long-term success of a joint venture that parties are able to adapt their bargain when circumstances change substantially.” Contracts should, in practice, be viewed as frameworks with scope for change and evolution as market conditions change, in order to effectively support the ongoing business relationship between the parties. This requires a shift in perception and mindset for in-house counsel. The objective is not absolute fluidity in contrast to absolute rigidity. Rather in-house counsel should look to ensure that contracts have enough flexibility to absorb market shocks and commercially protect the business.

There should be less focus on black letter law and literal drafting, and more focus on:

- developing clear and effective mechanisms in the contract;
- adaptability to changes; and
- alignment with business requirements and objectives.

The reality appears to be that uncertainty is likely to continue, at least in the near term. Ongoing geopolitical instability may continue and cyber disruption and climate change will impact businesses operating in an interconnected global economy. In-house counsel that focus on contracting with clear and controlled flexibility built in, as well as with commercial awareness, will be best placed to help businesses successfully navigate ongoing challenges.

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Febechi Chukwu



Corporate Counsel

Cummins Inc.

Febechi Chukwu is corporate counsel at Cummins, a global leader in power solutions, where he leads legal support for the European Distribution Business. He is a commercial lawyer, with experience negotiating and advising on high value commercial contracts, procurement, compliance, risk management, and governance. Chukwu has worked as in-house counsel for large multinational energy and infrastructure companies for the last decade, and prior to that worked in private practice in London. He also serves as a board member of a housing charity supporting young professionals, particularly key workers, with accommodation.