

Companies Should Not Overlook the Importance of Their Contract Terms and Conditions

Article

November 16, 2020

Sales are negotiated and consummated between companies every day. What can often get overlooked in transactions are the terms and conditions within the variety of documents being exchanged between the contracting companies. At minimum, a purchase order and a sales order are likely to be exchanged and typically include terms and conditions. However, if you do not have detailed, product-specific, terms and conditions, these generic or “standardized” terms may come back to haunt you should a dispute subsequently arise.

In this era of supply chain interruptions stemming from labor shortages, pandemic shutdowns, heightened financial constraints, and other circumstances, the risk for dispute has never been higher. It is critically important to have terms and conditions that were specifically drafted for the product or service you sell. Pre-COVID-19, it was much more likely for services to be provided, or goods to be manufactured, shipped, accepted and paid for without any issues arising. Unfortunately, the pandemic has brought about many business disruptions, some of which lead to disputes. Once a conflict arises and litigation appears imminent, failure to review or understand either party’s terms and conditions can significantly impact the outcome of the dispute. Likewise, even if both parties aim to settle their disagreement in advance of litigation, having service/product-specific terms and conditions in place is vital toward tipping the leverage in your favor.

Below is a non-exhaustive sample of a few important terms and conditions that should be tailor-made for your product or service:

Warranty Provisions

- It is important to explicitly define what you are and are not warranting relative to your product or service. Having a well-thought out warranty provision can help limit your potential liability should a dispute arise.

Indemnification Provisions

PROFESSIONALS

Aaron E. Hall
Partner

RELATED SERVICES

Corporate & Securities

- An indemnification provision is used to shift a loss to your contracting partner. In other words, by including an indemnification you can ensure your contracting partner will compensate you for any harm or loss that you suffer in connection with the other party's product, services, or actions (or failure to act). Indemnification provisions should include a duty to defend clause requiring your contracting partner to compensate you for any attorney's fees and costs that you incur as a result of the other party's product, services, or actions.

Remedies for Breach of Contract

- Direct damages v. Consequential damages – if a product fails, it is important to spell-out whether the seller/manufacturer is only required to replace the product or pay the cost of replacement (direct damages) or whether the damaged party also entitled to lost profits, damages relating to business interruption, or damage to its business reputation (consequential damages).

Dispute Resolution Provisions

- Choice of Law and Venue
 - These provisions dictate which state's law will govern the dispute and which court (in which county and state) can hear a dispute between the parties.
- Attorney's Fees Provision
 - Provides that should a dispute arise between the companies, the losing party is responsible for paying the attorney's fees of the prevailing party.

Provisions Regarding Payment Breaches

- Should your customer breach its payment obligations to you, it is important to include language that allows your company to recover its costs of collection, including actual attorney's fees and cost incurred in trying to collect amounts owed under the contract, which includes filing a collection lawsuit. You should also clearly spell-out that you are entitled to interest, at rate certain, on unpaid balances owed from the date the payment was due.

What sometimes transpires in commercial transactions is that buyer and sellers exchange documents containing terms and conditions that directly conflict. For instance, the buyers' terms and conditions may contain express warranty and indemnification provisions, while the seller/supplier's terms may contain conflicting disclaimers of express or implied warranties. The parties' terms and conditions may also have conflicting provisions as to which state's law would govern any dispute or the venue in which disputes are to be litigated. One parties' terms may have a liquidated damages provision while the other party's terms may limit damages to replacement or a refund. In these scenarios, after a dispute arises and the parties find themselves in court, the question becomes whose terms and conditions control?

Companies
Should Not
Overlook
the
Importance
of Their
Contract
Terms and
Conditions

The determination as to which conflicting terms and conditions will govern a commercial transaction is referred to amongst lawyers as the “battle of the forms.” As to transactions involving the sale of goods, as opposed to services, the resolution of such conflicts is resolved under the Uniform Commercial Code (UCC) section 2-207 (In Wisconsin, the applicable UCC section is Wis. Stat. § 402.207). Under § 2-207, once a court concludes that a contract was formed (despite the exchange of conflicting terms and conditions), the court determines which party’s terms and conditions govern the transaction and any dispute arising thereunder. This is a fact-intensive inquiry that focuses on the actual documents exchanged, as well as the manner and order in which they were exchanged. If the court finds that the neither party accepted or agreed with the other parties’ conflicting terms, it will conclude that the conflicting terms are “knocked out” of the parties’ agreement. In this scenario, the “knocked-out” material terms of the agreement are replaced by the standard UCC provisions that govern the commercial sale of goods. These substitute terms and conditions are often referred to as “gap fillers.” While “gap fillers” may be better than forced adoption of your opponent’s terms and conditions, they are widely considered to be pro-buyer.

There are many complex, fact-intensive issues that can arise in battle of the forms scenarios. Far too many to list here. Despite the inherent complexity, there are a few takeaways that are important for all companies to consider when regularly contracting for the purchase and sale of goods:

- You must have terms and conditions that are customized to your business.
- Assume that your contracting partner’s terms and conditions will not be favorable to you.
- Be sure to provide your contracting partner with your terms and conditions.
- Try to have your contracting partner sign the document (quote, purchase order, sales order, etc.) containing your terms and conditions. This may avoid a “battle of the forms” situation completely.
- Do not sign your contracting partner’s forms containing its terms and conditions.
- Try to position yourself as the initial offering party, because under the “battle of the forms” analysis there are advantages to having your form(s) constitute the original “offer.”
- Make your offer (typically a purchase order or possibly a quote) expressly conditioned upon acceptance of your terms and conditions. Also, include an affirmative rejection of any conflicting terms and conditions that may be contained in the offeree’s documents that follow.
- If you are the offeree/buyer, make sure that your acceptance (usually in the form of a sales order or order acknowledgment) is conditioned on the offeror’s/seller’s agreeing to any additional terms and conditions contained within the documents you provided.

Companies
Should Not
Overlook
the
Importance
of Their
Contract
Terms and
Conditions

While the ultimate goal should be to avoid litigation due to the uncertainty that results, companies are well advised to factor everything they can to have strong, product-specific terms and conditions, that will govern its transactions with its contracting partners. With a little planning on the front end, companies can craft their terms and conditions to avoid or at least mitigate many of the pitfalls that could befall them if they should find themselves in a dispute.

Companies
Should Not
Overlook
the
Importance
of Their
Contract
Terms and
Conditions