Contracts and the risk of unintended legal obligations

Like all organisations, charities have always dealt with contracts. Until relatively recently, contracts tended to be more important with respect to occupation of premises and employee relationships and broader supplies of services to the charity, rather than the delivery of services by the charities themselves. The increased focus on contracting of services from charities means that it is more important than ever for those in management positions to appreciate the basics of contract negotiation, and to be aware when and how legal obligations are formed.

When a contract arises

A contract generally arises when one party provides goods and services to another in return for either payment of money, or something else of value. Apart from this, all that is generally required is that the agreed terms of the contract should be clear enough to be capable of enforcement and that the parties intend that the agreement should be legally binding.

A contract, therefore, might arise in a wide range of circumstances.

Contracts in writing

Many contracts are intended to be entirely in writing. It is common, for example, that contracts for services from charities are written in a document based on a proforma provided by the commissioning body, often a local authority.

This type of contract will usually state that it includes all the terms agreed between the charity and the local authority and will provide particular mechanisms for further written agreements to vary the contract.

There is generally no legal right to renegotiate terms of a written contract once it has been signed. Signing the contract, whether the person signing it (or indeed anyone else) has read its contents, means that the organisation is bound by all of its terms.

Until the contract is signed, however, there is generally no obligation to continue discussions and either party can withdraw from the negotiations.

Documents are not always signed

Of course, it is often the case that the formal contract is never actually signed, for one reason or another, but the service that it relates to is still provided. Sometimes, services continue to be provided and paid for after the ending of a formal signed contract.

In these cases, there will be some kind of contract binding the parties, even though no formal document covering the arrangement is in place.

The contract which will often be regarded as incorporating many of the terms in draft agreements circulated between the parties, or previous signed agreements that have expired, but in the light of any recent activities by, or correspondence between the parties.

Contracts and pre-contract negotiations: the dangers

If formal draft documents have been circulated, a binding contract may arise even if no final version has been signed and even where no activities have been carried out or payment made by either party. Whether or not a binding contract is formed in such circumstances will depend on what was expressed in the communications between the parties and by their conduct. If there are mutual obligations, on the face of it the arrangements are apparently intended to be legally binding and if there is sufficient certainty of terms, a binding contract may arise which is as capable of enforcement as a signed formal written document.

In the case of *Proton Energy Group v Orlen Lietuva (2013)*, for example, one of the parties argued that their communications by email (which included a draft formal contract) did not conclude an agreement, but was an indication of the terms that they wished to be included in a formal binding contract, if one was finally agreed. Their view was that nothing was binding until the contract had been signed, and that they were free to end the negotiation.

The court held otherwise, and found them in breach of a completed contract.

Distinguishing between negotiations and contracts: "subject to contract"

It is well worth remembering therefore that when negotiating contracts, all correspondence should be marked "subject to contract" until the contract is signed.

Sometimes, in order to manage this risk, organisations include general disclaimers on their emails to confirm that all emails are "subject to contract" pending formal agreement. Care must still be taken however, as this policy may be counter-productive. If an organisation does intend to complete a binding contract by email (for example to order goods or services) and omits to say that the email disclaimer does not apply, the other party may use the statement to deny that there is any legal contract between them.

James McCallum
Partner
+44 (0)20 8394 6481
James.McCallum@russell-cooke.co.uk

Gareth Roy
Associate
+44 (0)20 8934 6493
Gareth.Roy@russell-cooke.co.uk