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Legal advice can be obtained from Mr. Ende in his capacity as Managing Partner of Technology Law Group.

Effectively Negotiating Telecom Agreements

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Carrier agreements are intended to set forth the terms and conditions under which resellers purchase the essential commodity of their business: telecommunications services. Sadly, however, it is the rare instance when resellers have read or truly understand the essential terms and conditions of their agreements or negotiate the terms of their agreements effectively as a matter of tactic or strategy. Even more troubling is the fact that few resellers use their agreements to facilitate their business interests and to protect themselves against undue risk. As a result, rather than being a roadmap to success and a shield against risk, carrier agreements often become minefields through which resellers unwittingly wander until the inevitable misstep is made and the damage is done.

The white paper is the first in a series addressing key issues in telecom agreements. Future white papers will address the process of drafting telecom agreements (including a discussion of some of the most critical terms) as well as agreement implementation, dispute resolution and litigation issues. We hope that you find them of value.

The Value of "Showing Up"

There is much truth in the saying that "showing up is half the battle." With respect to the negotiation of telecom agreements we would argue both that "showing up" is well more than half the battle and, regrettably, that resellers and agents rarely "show up" in a capable manner.

We firmly believe that there is substantial value in the process of negotiating telecom agreements even if it does not result in terms and conditions that meet

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all your substantive objectives in the negotiation process. If you show up prepared and make it clear that you take your agreements seriously, it sends a signal to the carrier that you expect no less from them. Indeed, we have found that the process of negotiating, standing alone, has very substantial benefits—both in terms of the client's understanding of the risks and rewards it faces and in terms of its understanding of its specific obligations under the agreement—even if the ultimate document does contain all the terms that it seeks.

A properly managed negotiation process will serve you well, both in the negotiation stage and in future interactions. Indeed, while we litigate many carrier agreements, we rarely litigate ones in which we have been involved in the drafting process, both because those agreements are generally more balanced, but also because the carrier understands that the client has both the interest and ability to enforce its rights.

Understand The Risks and Rewards of Your Agreement

Agreements are, first and foremost, allocations of obligation and risk. The first step in negotiating an agreement, therefore, must be to take the time to understand the obligations each party is and/or should be undertaking, the risks associated with those obligations and in the agreement as a whole.

This process is best understood by example. Many telecom agreements include minimum take commitments (generally taking the form of a monthly or annual Minimum Revenue Commitment), which are theoretically justified on the basis of preferential pricing. For the supplier, the risk being addressed is that the customer will not purchase a sufficient quantity of service to allow the supplier to cover its costs and make its desired return. This is a legitimate concern. However, the manner in which most of these provisions are drafted, and associated with other terms of the agreement, often shifts more of the risk to the

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customer than can possibly be justified by the actual risk the supplier is undertaking.

Indeed, because these provisions generally require the customer to pay the full cost of service, even if no service is provided, they can result in a substantial windfall to the supplier. The opportunity to achieve this substantial windfall can create an incentive for the supplier to establish conditions (or to allow conditions to arise) under which the customer is more likely to default on this obligation. These conditions include changes in the rates applicable to the service, terms and conditions of service, provisioning practices and/or quality of service—all of which are entirely beyond the customer's control—but which can make it difficult or impossible to sell the service and to meet the commitment. Yet, it is the rare agreement that places any meaningful limitations or parameters on the supplier's ability to make unilateral changes in these essential terms or, more importantly, that the agreement associates the customer's obligation to meet its commitment, in any way, to the supplier's conduct.

Needless to say, terms of this nature create a materially unbalanced risk reward scenario for customers. Yet, we are endlessly astonished that virtually all agreements contain these types of naked MRC provisions in favor of suppliers without imposing any corresponding obligations on them.

The above scenario is but one of many found in telecom agreements where the risks and rewards are totally out of balance. We will address numerous others in upcoming white papers. For the purposes of the negotiation process, however, the good news is that each of these scenarios can be identified through the application of proper expertise and scrutiny and there are numerous alternative terms and conditions that can be drafted into the agreement to establish a more proper balance of risk.

Establish Realistic Objectives

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In addition to understanding the risks and rewards that you face, it is also critical to establish realistic objectives as to which terms and conditions which are truly essential to your business plan. For example, if your business plan is such that your customer base may be unstable, thus raising significant concerns with an MRC, then your negotiating objective must be either to have the MRC removed or, if that is not possible, to offer a viable alternative. In offering an alternative, it is essential that it addresses the supplier's rationale for insisting on the term, even if you believe it to be a false rationale. For example, in the MRC circumstance, if it cannot be removed in its entirety terms can be added limiting the scope of the MRC to the term of the underlying carrier agreement, reducing the amount of the payment to an amount which reflects the supplier's cost, controlling the circumstances in which it is applied and/or establishing a ladders rate scheme. The key is to craft alternative approaches which address both the claimed rationale and your business need. Experienced businessmen, working with experienced and creative telecom counsel, can generally craft such provisions to meet any scenario that arises.

Don't Sell Yourself Short

The corollary to the axiom that "showing up is half the battle" is that you need to show up with conviction. Much of the negotiation game is won and lost in the dynamics of the process. A key element of these dynamics is the conviction that you bring and the manner in which that conviction is presented. If you give up before you start, you appear to be willing to give up, or you show up unprepared or without adequate conviction, you will most certainly lose.

This reality is dramatically clear in the manner in which many carriers commence the "negotiation" process. How many times have you heard from a carrier that contract terms are "not negotiable", or that their attorneys do not allow any changes in the language of the agreement? These are negotiation tactics, pure and simple. Do not be deterred. If you are bringing valuable business to a carrier, they have a substantial economic incentive to work with you. Indeed, contrary to

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the mythology encouraged by carriers, we have found, in our decades of negotiating telecom agreements, that negotiation is generally possible and that most carriers will, in fact, make changes in their agreements to incorporate properly crafted terms.

Be Patient

The negotiation process can be a war of attrition. Carriers rely on the fact that their customers will simply cave in if the process becomes extended or difficult and that they do not have the staying power required to achieve a fair result. Do not fall into this trap. Even if you have limited resources and a limited time horizon, it is essential that you never reveal this fact and that you structure the negotiation process in a way that maximizes the chance for an outcome that meets your time and budgetary requirements. It can be done.

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Agreements are the foundation of your business and a well implemented negotiation strategy is the cornerstone of that foundation. While it never is possible to eliminate all risk, it is possible to understand where that risk lies, to limit its scope and effect and to structure your business operations to reduce the likelihood that a risk causing event will occur.