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BUSINESS COOPERATION AGREEMENT: LEGAL RISKS YOU SHOULD KNOW

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BUSINESS COOPERATION AGREEMENT: LEGAL RISKS YOU SHOULD KNOW

Business cooperation activities often arise from relationships between parties who are familiar with each other. As a result, business partnerships are typically established based on mutual trust. At the initial stage, most parties maintain good relations, and conflicts have not yet occurred because the parties have not yet directly carried out the tasks outlined in the cooperation agreement. However, when entering the implementation phase of the cooperation agreement, many issues may arise, but the parties may not reach an agreement. This can occur when one party fails to comply with any prior commitments, and there is no enforcement mechanism or binding terms to compel one party to fulfill the contract. These situations often lead to the breakdown of previously established cooperative relationships. Typically, in a business cooperation relationship, we can list some common causes as follows:

1. THE BUSINESS COOPERATION OBJECTIVES ARE NOT CLEARLY DEFINED

In a business cooperation agreement, this is sometimes recorded in a vague or incomplete manner, failing to reflect the expectations or goals that each party has in the cooperative relationship. In practice, when any conflicts arise, in order to reach a mutual understanding on any issue, the parties will revisit the original objectives each party had in mind. This helps them come together with goodwill to resolve any remaining disagreements.

2. THE CONTRIBUTIONS OF EACH PARTY ARE NOT CLEARLY DEFINED

In a business cooperation agreement, failing to clearly and specifically outline each party's obligations and contributions is one of the main causes of disputes and disruptions in business activities. If the agreements regarding these aspects are not clarified, the parties are more likely to experience disagreements and find it difficult to resolve issues when they arise.

Failure to clearly define contributions, if the agreement does not specify what each party will contribute (such as assets, capital, effort, technology, or other resources), this can lead to misunderstandings about each party's responsibilities.

This not only causes conflicts over interests but also affects the feasibility of the planned business activities. The failure to establish a timeline for contributions, such as capital or assets, is critical, as the timing of these contributions ensures the business activities progress as planned. Without clear deadlines and contribution plans, delays from one party will directly impact the joint project, causing disruptions or financial losses for the other parties.

Lack of penalties for breaching parties, a contract that does not specify penalties for parties who delay or fail to fulfill their contribution obligations will lead to a lack of mechanisms to address violations. This weakens the ability to protect the rights of the other parties, creating an imbalance in the cooperation relationship.

To avoid the risks mentioned above, the contract should clearly outline each party's contributions, including the form of contribution (cash, assets, technology, human resources, etc.) and specific measurable values. The contract should also specify the deadlines by which each party must complete their contributions, along with milestones to check progress. It should establish clear penalties, including provisions for financial penalties, reducing profit shares or benefits, or even the right to unilaterally terminate the contract if a party fails to meet the obligations on time.

3. UNCLEAR DEFINITION OF MANAGEMENT AND OPERATIONAL ROLES

Business cooperation agreements often face with significant risks in management and operations if the roles and responsibilities are not clearly and transparently defined. One major issue is unclear delegation of authority, which can lead to conflicts over power or a lack of accountability, reducing the overall business effectiveness. Additionally, differences in management styles between the parties, especially when they come from different cultures or business models, can create tension and delays in decision-making.

The risk of abuse of power is also a common issue, where one party may exploit their authority to make decisions that disadvantage the other party, thereby eroding the cooperative relationship. Finally, a lack of transparency in operations, such as concealing information or failing to fully share details about activities and finances, will diminish trust and lead to unresolved disagreements. To mitigate this risk, the contract should clearly define the roles, responsibilities, and powers of each party, establish mechanisms for mutual oversight, and ensure transparency through regular meetings. This not only helps to strengthen trust but also creates alignment in management operations, contributing to the development of a sustainable cooperative relationship.

4. LACK OF FINANCIAL TRANSPARENCY AND CONTROL MECHANISMS

Financial risks are one of the major challenges in business cooperation agreements, especially when there is a lack of transparency and effective management mechanisms. The absence of transparency in financial reporting can cause doubts between the parties if there is no independent and transparent auditing process in place. Another serious risk is the failure to fulfill financial obligations on time, which occurs when one party delays or fails to fully meet their capital commitments. This leads to disruptions in the joint business activities, affecting the progress and effectiveness of the project.

Ineffective debt management is also a potential challenge, particularly when the cooperation involves borrowing funds or incurring debt. Without strict control measures, this financial pressure can directly impact the stability and sustainability of the joint project.

Therefore, the contract should be drafted with detailed provisions, including the financial obligations of each party, independent financial auditing and reporting mechanisms, and measures for addressing financial violations. Additionally, a contingency fund should be established to mitigate the impact of unexpected costs. This will help ensure transparency, strengthen trust, and maintain stability in the cooperation.

5. PROFIT DISTRIBUTION METHOD NOT DEFINED

Profit distribution is a sensitive issue in business cooperation agreements and can lead to disputes if there is no clear consensus. Disagreements about the method of profit sharing are a common risk, especially when the parties have different views on how profits should be calculated. Some may want to base the distribution on capital contributions, while others may prioritize effort or non-financial contributions, leading to conflicts.

Additionally, unclear priorities for profit allocation can also lead to disputes. If the contract does not clearly specify how profits will be distributed (reinvestment, debt repayment, or direct distribution), the distribution process may be delayed or lead to disagreements. Lack of consensus on contribution disparities is a potential issue, especially if one party feels that the share of profits they receive does not correspond to the level of investment or effort they have put in. To mitigate this risk, the contract should clearly outline the calculation method, profit-sharing ratio, priority order of profit use, and payment deadlines. Furthermore, a dispute resolution mechanism should be included to address disagreements quickly and fairly.

In business cooperation, identifying and managing risks such as contribution obligations, profit distribution, operational management, and dispute resolution mechanisms are key factors determining the success and sustainability of the partnership. A well-drafted, transparent, and comprehensive contract not only helps the parties avoid unnecessary disputes but also provides a solid legal foundation to navigate fluctuations in the business environment.

The article contains general information which is of reference value, in case you want to receive legal opinions on issues you need clarification on, please get in touch with our Lawyer at info@cdlaf.vn

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