

Contracts: The art of the deal



What *is* a contract? The law generally defines a contract as a “meeting of the minds” that the law enforces with binding effect. We’ve all experienced or heard of situations where someone was able to “get out of a contract,” or didn’t think they had a contract but were bound anyway. Many arrangements that appear to be contracts are not, and vice versa.

Contracts may be either express or implied. Contracts also may be written or unwritten, or even partially written. The “meeting of the minds” needed to form the contract can be by words, action or even inaction. But if there has been an “offer” and an “acceptance,” a binding contract has likely been formed. For example, if a vendor provides services to the township that the township needs and the township receives and uses the services without objection, a contract has likely been formed even though no contract document was ever signed.

Whether a contract will be enforced will often depend on the definiteness and certainty of the language used, and enforcement may be affected if the contract contains missing or vague terms. Formation of a contract also requires “consideration”—an exchange of value between the parties.

In some cases, a contract obligation may be avoided if a mutual mistake, fraud or duress can be demonstrated. Even though a contract may be executed and appear valid on its face, it is not enforceable if it is illegal because it is (1) in violation of specific statute or constitution; (2) against public

policy; or (3) made without authority. The township generally cannot waive illegality.

In a township, only the township board has authority to enter into binding contracts. Although it is possible for the board to delegate its authority to one of its officials, such delegations are strictly construed. For example, if a third party enters into a contract that is only approved by the township supervisor, and there is no clear record of the township board granting authority to the supervisor to enter into that contract, then a valid contract with the township likely does not exist.

Best practices for township contracts

A contract should be written in clear and unambiguous language. All terms should be set out in sufficient detail so that future misunderstandings will be avoided. A clear and unambiguous contract will discourage litigation in resolving a contract dispute.

In a dispute, if the contract language is clear, a court is required to interpret the contract based on its plain language. It is not permitted to look beyond the “four corners” of the contract to interpret the parties’ intent. A court cannot look at discussions during negotiations, or the personal opinions of one of the signing parties in interpreting the meaning of the contract.

If reasonable minds could differ on the meaning of a particular word or phrase in a contract, the clause is ambiguous, and only then may the court look beyond the plain language of the contract to interpret the parties’ intent. This means a court could consider any outside evidence to interpret the parties’ understanding of the particular clause or phrase.

Service contracts among municipalities

A township may lawfully enter into a contract with another local government or government agency to do virtually anything the township has authority to do on its own. Two Michigan constitutional provisions give wide authority for intergovernmental agreements. Article 3, § 5 provides authority for townships to enter into intergovernmental agreements and joint authorities. Article 7, § 28 allows townships to enter into contracts with other public entities for the joint administration of any of the functions or powers they would otherwise have the power to perform individually.

There are also some general statutes that implement the constitutional intent to allow broad intergovernmental contracting. These broad statutes include:

- The Urban Cooperation Act (Public Act 7 of 1967), which provides that public agencies (including townships, counties, cities, villages, school districts, single and multipurpose special districts, or single and multipurpose public authorities) may collaborate to exercise any power or authority that each party could exercise separately on its own. This includes providing a mutual exchange of services (without any payment other than the exchange of services).

Important contract clauses

Purpose: Explains why the parties are entering into a contract and what they hope to accomplish. Can help define a missing term or provide a reasonable interpretation of the contract if a dispute arises.

Authority: A municipal contract should set forth the source of authority for entering into the contract, and for the undertaking for which the contract is necessary to accomplish.

Term: The contract should specify a term during which the contract will be valid. In the absence of a defined period of time, the contract will be valid for “a reasonable time.”

Duties and rights: These set forth what each party’s obligations are under the contract and what each party’s rights are under the contract, so they should be explained in reasonable detail.

Terms of payment: If one party is expected to make periodic payments to another party, the terms must be specified; i.e., how much, how payment will be made, when payment will be made. A provision for “interest” or “costs of delay” should be included to account for late payments.

Termination: Provision should be made in the contract to specify when a party may unilaterally terminate the agreement, i.e., when one party fails to comply with other terms of the agreement or one party fails to perform their obligations within the time specified in the agreement.

Renewal: Normally a contract may be renewed upon the agreement of both parties. In some circumstances, it is advisable to provide for automatic renewal, or renewal at the option of one of the parties.

Indemnification: One contracting party agrees to protect another party against resulting lawsuits, liabilities and costs associated with the work performed pursuant to the contract.

Dispute resolution: The contract may provide for a method by which the contracting parties will resolve disputes, short of court litigation. Litigation is costly. Requiring mediation or arbitration can sometimes provide a faster and less costly means of resolving a dispute.

Governing law: Each contract should specify which state’s laws will apply in governing the contract, and in which jurisdiction a legal action may be brought to resolve a dispute.

Assignment: Frequently such clauses prohibit the assignment of a contract by one party without the express consent of the other party.

Severability: This protects the enforceability of other clauses of a contract if one provision is found invalid.

Amendments: A contract should provide that amendments may be made only upon the written authorization of both parties. Some contracts may require periodic changes to contract terms, and the procedure for making these amendments should be specified in the contract.

Remedies: Each contract should provide the specific type of relief a party may receive if the other party breaches or fails to perform its duties under the contract. Examples include automatic rescission of the contract, liquidated damages, attorney fees for enforcement, etc.

- PA 35 of 1951, which authorizes municipal corporations to enter into contracts with other municipal corporations for the operation of a facility, performance of a service or ownership of property.
- The Intergovernmental Transfers of Functions and Responsibilities Act (PA 8 of 1967), which authorizes townships to enter into contracts to transfer functions or responsibilities to other municipalities, other political subdivisions or combinations thereof.

Joint fire, police and ambulance arrangements

Single-township fire departments are becoming less common, and multi-unit departments are becoming standard. These multi-unit fire departments are governed by service contracts and/or joint authorities. There are many legal tools available to townships to provide shared fire service, allowing townships to choose the option(s) that best fit their needs, including:

- The Township Police and Fire Protection Act (PA 33 of 1951), which provides authority to adjoining townships, villages and qualified cities to jointly purchase fire protection vehicles, equipment and buildings, and to provide funding to maintain and operate fire, police and ambulance services. PA 33 also allows townships to contract with an adjoining municipality to obtain fire, police and ambulance service (or a non-adjoining municipality if no adjoining municipality provides such services). Each individual participating entity may also enact an ordinance to collect fees for providing fire protection services.
- The Municipal Emergency Services Act (PA 57 of 1988), which allows two or more municipalities (including townships) to incorporate an authority to provide emergency fire, police and ambulance services. A participating municipality may transfer its existing department employees, buildings and equipment to the authority. Contracts for fire, police and ambulance services with participating and non-participating municipalities are limited to a term of no longer than 30 years. However, contracts with non-participating municipalities may include higher fees.
- The Urban Cooperation Act (PA 7 of 1967), which is a broad enabling statute. It permits townships to enter into interlocal agreements for all or part of the township's fire, police or ambulance services. The participating municipalities may also contract for the mutual exchange of services without any other type of compensation.
- The Intergovernmental Contracts Act (PA 35 of 1951), another enabling statute that allows townships (and other municipal corporations) to contract or join with other municipal corporations for the operation

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Financing joint municipal services

When local units join together to provide a service to their combined populations, there are alternative ways to finance the cost of those services. There may be an area-wide tax in some cases, or each unit may choose its own method of raising its share of the service costs. Here are the main options:

Authority-wide millage: This requires special statutory authority, such as is contained in the Municipal Emergency Services Act.

Independent millages: When costs are divided among municipalities and each chooses different approaches to raising their share of the total costs, this may be an option.

Special assessments: This is more common when a portion of the township benefits from the joint service. Some statutes, such as the Township Police and Fire Protection Act, authorize township-wide special assessments for services.

Service rates: Typical for sewer and water systems, these rates must be based on cost of service. Questions remain regarding higher rates for some municipalities than others.

Fees for service: These are common for building inspection, fire and ambulance. Fees must reflect costs.

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or performance of fire, police or ambulance services, or any other services that either contracting municipal corporation would have the power to operate or perform individually. Since townships have the authority to operate fire departments, they may contract under PA 35 with any other municipal corporation to operate a fire department.

- Townships and other municipalities may enter into contracts to provide mutual police assistance to each other in emergency situations pursuant to MCL 123.811.

Joint water and sewer service arrangements

The Legislature has also provided many alternative means for joint contracts between townships and other municipalities to provide sewer or water service in a regional or multi-unit manner. These include:

- MCL 124.251, *et seq.*, which provides authority to two or more townships, cities or villages, or any combination thereof, to incorporate an authority to acquire, own, and/or operate a water supply system or systems.
- MCL 121.1, *et seq.*, allows two or more townships, cities or villages, or any combination thereof, to incorporate an authority for the purpose of acquiring, constructing, purchasing, operating, and maintaining a water supply and transmission system.
- MCL 124.282 provides authority for any two or more municipalities to incorporate an authority for the purpose of acquiring, owning, improving, enlarging, extending and operating a sewage disposal system, a water supply system, a solid waste management system, or any combination of those systems. As used in this act, the term “municipality” includes each county, township, city, or village.
- MCL 123.381, *et seq.* (specifically, MCL 123.382) authorizes townships, alone or in conjunction with other units of government, to construct, maintain and operate waste disposal systems and water supply systems through agreements with local units of government located in another state.

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How to negotiate a contract

Not everyone is a “born negotiator,” but with practice and care, almost anyone can learn to negotiate contracts effectively. A good negotiator is not a bully or a dictator. As is so often said, “you catch more flies with honey than vinegar.” The following skills are more effective and far more important than coercion or threats:

- **Begin with the end in mind.** Imagine what a successful agreement will look like. That will help you move discussions in that direction.
- **Listen to what the other side says.** We so often have misconceptions about what the other side really wants, or what is really bothering them. We can minimize this liability by listening.
- **Consider whether you can meet the other side’s expressed needs within the zone of your own needs.** Remember that the area where your needs and those of the other side meet is the only area where an agreement can be reached.
- **Building relationships is an essential negotiating skill.** People are naturally resistant to reaching deals with people they distrust or dislike.
- **Avoid attacking the other side.** Even if you think it might make you feel better, it will not further your cause and will surely set you back.
- **Avoid highly charged emotional arguments and responses,** like “that’s absurd,” “what a rip-off,” etc. But don’t be afraid to say that a particular proposal makes you “unhappy” or “unsatisfied.”
- **Appealing to “reason” is usually unproductive.** It comes across as condescending, and the other side will often have its own firm ideas of what is “reasonable.”
- **Ask questions about the other side’s proposal to clarify the proposed deal.** This will help you and the other side to understand all the consequences of the contemplated agreement.
- **Make a few alternative proposals.** If you let the other side know that your needs parameters are flexible, you will be more likely to find an area of common ground.
- **Seek continuous feedback from the other side** to be sure you are being heard and understood.
- **Be observant of nonverbal cues and certain phrases.** (For example, “to be honest” often precedes a statement that is not entirely true.) And be aware that your own nonverbal cues are being observed by the other side.
- **Never appear very eager for a deal.**
- **If the other side is not behaving well, don’t be afraid to walk away from the table that day.** But let the other side know that you are willing to continue negotiations when they can treat you civilly.
- **Frequently summarize points on which both sides agree.** Use a whiteboard to keep track of the progress of the negotiations, and what concessions each side has made.

- Pursuant to MCL 123.231, *et seq.*, townships may contract with any one or more political subdivisions for the joint ownerships, use and/or operation of sewers and/or sewage disposal facilities. Townships may also contract with any one or more political subdivisions regarding furnishing sewage disposal services by one (or more) of the participating entities. Such agreements must be approved by the legislative body of each participating entity and cannot exceed a term of 50 years.

Allocating costs of joint services among municipalities

Service agreements or joint authorities between two or more municipalities rarely involve completely equal partners. One unit may require a majority or a large percentage of the services, and others may not have a similar demand. Therefore, it is crucial to develop a method to divide up the cost of the services that is perceived by all the members as fair. Here are some options:

- **Formula for allocation:** Various formulas have been devised to allocate costs among municipalities. For example, data on population, state equalized value, and historical fire runs are often blended to determine the allocation of total costs of a joint fire authority.
- **Owner or renter:** Cost allocation may be different depending on if each municipality has made a capital investment in the authority or is just buying service.
- **Millage:** An authority-wide millage essentially results in dividing the costs among the municipalities according to taxable values.

See the sidebar on page 18 for more on financing joint services.

Control and governance of joint authorities

One way to provide joint services is to create a joint authority to provide services to all the members. A joint authority is a separate legal entity created specially as a service provider to its members. Instead of one municipality providing the services to others by contract, the authority is responsible for the services and for providing them to all the members. This can often take some of the “politics” out of local services, but it also involves some municipalities giving up the direct control they once had over the services. To optimize the operation of a joint board, consider some of these ideas:

- **Size of joint board:** If the joint board is too large, there is a potential for numerous differing opinions, making a final decision on an issue more difficult. However, remember that a larger board generally means that no one entity will dominate the decision-making process.
- **Representation on joint board:** Although most joint boards have equal representation from the participating entities, some boards apportion membership based on financial contributions or commitment.
- **Staggered terms:** Many joint services agreements will provide for staggered terms for board members. This helps ensure continuity and stability on the joint board.

- **Budget oversight:** Most “parent” boards want to retain the authority to adopt or approve a budget for the joint program. This is especially important where the governing bodies provide financing for the program.
- **Veto power:** Some joint authority agreements also vest veto power and/or ratification power in the member governing bodies. In such agreements, certain joint board actions would have to be reviewed and approved by the parent boards (by majority, supermajority or unanimous consent), and could be vetoed by one or more of the parent boards.

A tricky contracting decision

Few contracting decisions can be trickier than whether to hire an employee or an independent contractor to perform particular township services. There are different requirements and responsibilities for the township, depending on whether a person is an employee or independent contractor, including the person’s status under federal and state wage, hour and benefit laws, payroll reporting and withholding, workers’ compensation, and liability insurance coverage. There are also tax penalties if the township incorrectly classifies an employee as an independent contractor.

But how do you know if the person providing the services is an employee or an independent contractor? A contract is not enough. A simple label like “independent contractor” is not enough. Instead, the law requires you to use the “economic realities test,” which considers the totality of the circumstances surrounding the relationship between the parties. Under the economic realities test, the following factors are balanced to determine if an individual is an employee or an independent contractor:

- What liability, if any, does the employer incur if the individual is terminated at-will?
- Is the work being performed an integral part of the employer’s business that contributes to the accomplishment of a common objective?
- Is the position or job of such a nature that the individual primarily depends upon the income from the employer for payment of living expenses?
- Does the individual furnish his/her own equipment and materials?
- Does the individual hold himself/herself out to the public as ready and able to perform tasks of a given nature?
- Is the work or undertaking in question customarily performed by an independent contractor?
- Does the employer have the right to control the means by which the individual achieves the end result?

Good tips to follow

No single factor can determine whether a person doing a service for the township is an employee or an independent

contractor. But to increase the likelihood that the person will be found to be correctly classified an independent contractor, here are some good rules for townships to follow:

- Don't regulate the hours of the independent contractor. Someone in their own business sets their own hours.
- It would be ideal if the independent contractor had his or her own employees. This is not always practical in most real-world situations and is not mandatory.
- Payment should be by the job rather than by unit of time (i.e., an hourly wage).
- Repairs to tools should be paid for by the independent contractor.
- Don't supply liability and health insurance to your independent contractors.
- Don't pay the expenses of your independent contractors. If someone is in their own business, they should pay their own business expenses.
- A true independent contractor will often have his/her own office lease and office help.
- Don't have an independent contractor wear a uniform with your township's logo.
- The independent contractor should arrange for his/her own materials and do his/her own clean-up.
- You may control the ends but not the details of the work.

- That the independent contractor spent money on advertising is an excellent factor to have on your side.
- Independent contractors don't generally get bonuses.
- Your independent contractors should have any and all licenses that are needed to perform the work they are hired to perform. Construction is an area especially prone to the problem of work being done by unlicensed persons.

The art of the deal

Being knowledgeable of the authorizing statutes, and being proactive during contract negotiations, can allow townships to realize the exceptional services that their residents want—and deserve.



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Hear more from Fahey at "Living With Your Joint Service Agreement," on Wednesday, Jan. 29, from 2:45 to 4 p.m., at MTA's 2014 Annual Educational Conference at the Grand Traverse Resort, and learn how to work with difficulties you may be encountering in your current intergovernmental agreements.



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