Drafting of Contracts

Dr. Ajar Rab

Partner, Rab & Rab Associates LLP

Professor of Practice, UPES

Distinguished Visiting Professor, NUJS, Kolkata

Visiting Professor, NLSIU

ajar@rabs.in

Do we need contracts?

- Think of a "Relationship Agreement"
  - Which behaviours are to be encouraged?
  - Which behaviour are forbidden?
  - Which behaviour(s) requires disclosure?
  - Conditional events and promises?
  - Wrongful behaviour is punished?
- Problem Anticipation and Solving

Why draft a contract?

- Efficiency – initial costs
- *Acquisition of 300 aircrafts by Indigo*
- Reduction in negotiation and disputes
- Understanding what parties really want
- What parties need to give up to get what they want
- Realistic expectations of risk and rewards

Why draft a contract?

- Consider the Business Deal, Contract is just a legal boilerplate
- Meeting of Two Minds – language to be interpreted *in exactly the same way*
- Ambiguity is the real enemy
- Ability to negotiate – litigation is to win
- Contracts are forward looking – expectation damages

Duties as a drafter

- Your job:
  - Help your company think about the deal
  - Understand the goal of your company
  - Walk your company through with issues beneath that goal
  - Spot issues
  - Protect your company's legal interest
  - Negotiate or help your company negotiate each issue and all additional issues
  - Negotiate with opp. Lawyers to reflect *your* company's understanding of the issues – not *yours!*
  - *Maximize the Deal!*

Drafting Styles

- Traditional
- Modern
- Contemporary Commercial Drafting
- If a risk is perceived, draft for it
- Drafting for litigators?

What is a well-drafted contract?

- *One that is never opened again after signing*
- Clear and unambiguous language
- Clear organization
- Easy to read
- Limited cross-referencing
- Short!!!
- Well formatted!

What is a well-drafted contract?

- Accurately memorialize the deal
- Pragmatic resolution of problems
- Specific about rights and obligations
- Flexible for changed circumstances
- Advance client goals
- Reduce risks
- "Good Deal"

Will and Shall

- "has an obligation to"
- Will – opinion or future representation
- Potential issue of authority of those representing the parties (certificate of incumbency, shareholder resolution, etc)

Recitals

- Record consideration
- American Law – literal and contextual approach to construction
- Reasonable Intent Standard
- Representations are possible
- *Contra Proferentem*
- CISG – Reasonable Business Person Standard (Art. 8(2))
- According to the circumstances (Art 8(3))
- Good faith standard of interpretation (Art 9)

Recitals

- Civil Law – broad terms and purposive approach
- Good faith standard
- Sanctity of contract (*pacta sund servanda*)
- Recitals are NOT BINDING!
- Use recitals for unenforceable clauses – Non Compete, Restraint of Trade

Definitions

- Expand or limit meaning
- Clarify meaning
- ‘Affiliate’ or ‘Control’ or ‘Applicable Laws’
- Never use ‘means’ and ‘includes’ – only either of them

Defined Terms

- Define terms that either relate to the party's role in the transaction or is a shorthand name for the individual or entity
- Avoid acronyms
- Do not use *mortgagor and mortgagee* etc.
- Number of parties – borrower and lender – more parties? – Schedule?
- Do not create two defined terms – IBM and Company

Action Section

- Clauses where the action is from client's perspective
- In action section, the parties
  - Agree to perform the main subject matter of the contract
  - Agree to pay financial consideration, if any
  - State the term, if any
  - State the closing date, if any
  - List the closing deliveries, if any

Subject Matter Performance Provisions

- Each side promises to the other that it will perform the main subject matter of the contract.
- Two types
  - Reciprocal covenants
  - Self –executing provision

Performance

- Executory Promises
- Payment Provisions – Follow the Cash – Who is paying, what, to whom, when, why and how
- Stub Period

Payment Provisions

- Sets out the financial consideration
- Value of the contract
- E.g. Purchase price, salary, royalties, rent
- Multiple ways to draft
  - Declaration + Covenant
  - Covenant

Term

- *One-off Deals* vs. Specific Term
- Termination for Cause
- Evergreen Provision – automatic renewal or parties to agree on a price increase at the time of renewal
- Agreement to agree are unenforceable
- Closing – should state place, date and time
- Closing vs. Time of the Essence – Rolling Closing Dates

Covenants

- Affirmative
- Negative/Restrictive
- Financial
- Credit Related Covenants – Veto List/Unanimous Consent/Shareholder Consent
- Representations v. Covenants – Facts v. Foresight
- Carveouts
- Baskets/Buckets – relevant for indemnity as well!

Covenants

- A promise to do or not to do something
- High Risk Covenants?
- Use shall in covenants to obligate a party to perform
- State the party's obligation rather that the right of the opposite party – right vs entitlement
- Using "agree" in covenants
- Use of "is responsible"
- Declarations – do remedies flow?

Elements of a covenant

- **Who** is obligated to whom?
- **What** is the obligation?
- By **when** must the obligation be performed?
- **Where** will the performance take place?
- **Why** must a party perform?
- **How** is the obligation performed?
- If performance involves money, **how much?**

Use of Representations

- Using either representation or warranty
- Rep – allocates risk by establishing a standard of liability – the statement of fact
- Party making reps should make minimum reps
- Receiving party should make reps broad and unqualified
- Knowledge qualifiers and materiality qualifiers

Past, Present & Future

- Organization and Good Standing - Do not use currently or presently in reps
- Statements about future are opinions or speculation – or covenants
- Drafting in active voice – exception
- Warranty may be in the future e.g. apple

Risk Allocation

- Providing only a warranty and not representation
- Software contracts have only warranties and no representations

Conditions

- Use “Must” and “If Then”
- ”Must Be” + have + have been
- Consequences of the condition is not satisfied or waived

Closing Related Provisions

- Closing Date Provision
  - When and where the closing is to take place.
- Closing Deliveries Provision
  - Each party covenants how it will deliver its performance at closing.

Declarations

- Statement of fact or policy that the parties will govern their actions during the agreement.
- Neither party has stated the fact to induce the other party to act.
- A party cannot sue on a declaration to obtain damages.
- No rights or remedies.

Remedies

- Termination – of contract, or covenants?
- Acceleration
- Indemnity – caps, buckets, cut-off and termination
- Liquidated Damages
- Material Breach – CISG?
- Hair Trigger Remedial Provisions – expiry of time before right to remedy is triggered

Discretion

- Unfettered? Or Reasonable?
- "Sole Discretion"
- Use "may"

Termination v. Endgame

- Specific Survival of Contract Provisions
- Dispute Resolution
- Notice of Termination and Termination Notice – do they terminate the agreement?
- Termination Event Notice – Notice of Intent to Terminate – Notice of Intent to Exercise Remedies
- Effective only on receipt and sent by national courier or registered post or by hand

Neutral Terminations

- Without fault of either party – 30 days?
- Neutral – without surviving common law remedies
- Termination by Written Agreement?
- Termination, except for cause?

Friendly Termination

- Expiry of the Term
- Parties return to status quo – return of IP
- Loose ends – final payment, expenses
- Exit Strategies – IPO, Take-over, Buy-outs

Un-Friendly Termination

- Default and Cross - Default
- *"What if"* exercises
- The "Mechanics" of the parties
- Notice of Termination

Cure Periods

- Insurance and Credit Agreements
- Cure periods without notice?
- Default should have occurred and be continuing

No Termination

- Contractual Solutions instead of Termination
- Mitigation and cure by the non-defaulting party
- Liquidated Damages
- Indemnity – exclusive or cumulative
- Set-off

Injunctive Relief

- Can parties influence Court decisions on injunctive relief?
- Specific Performance of Celebrity Contracts

Dispute Resolution

- Adjudicate, Arbitrate or Mediate – when not to provide for arbitration!
- People, Place, Procedure, Time, Law
- Governing law, forum selection and service of process (Notice)
- Exclusive Jurisdiction Clauses
- Waiver of objections
- Cost and expenses

THANK YOU