KEY CLAUSES

Mastering Your Contract Roadmap

Drafting a contract need not be haphazard or frantic. Rather the process can flow logically and predictably, using the following roadmap.

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Law Insider

Table of Contents

1 Frame the Contract Clearly

Lawyers are often asked to write contracts with minimal detail or direction at the outset. This forces them to figure it out as they go. This is not the best way to effectively represent a client.

It's always best to begin with a non-binding term sheet, memorandum of understanding, or letter of intent that (i) summarizes the key deal points; (ii) lays out deadlines and responsibilities; and (iii) frames what the parties have agreed to in principle.

Much of the drafting stage can be accomplished efficiently by first constructing a sturdy framework for the contract before penning specific clauses.

Ground rules for thoughtful drafting should always include:

- **Clarity –**
  Write the contract in a simple, clear, and declarative style that a layperson can understand (or in a way that a smart lawyer can explain in everyday terms). Adopt the active voice; avoid the passive voice.
- **Complexity –**
  Adopt a level of complexity suitable for the transaction at hand. For example, a cooperation agreement for a local non-profit client will not require the same level of complexity as a multi-party loan agreement.
- **Client –**
  Pay careful attention to whom your client is and how best to angle the contract to protect your client's best interests. For instance, a commercial lease agreement will look considerably different when it is drafted on behalf of the lessor as opposed to the lessee.
- **Disputes –**
  Keep an eye out for potential conflicts and anticipate how disputes may arise. Plan for dispute resolution ranging from friendly negotiation to binding arbitration.

(Continue)

1 Frame the Contract Clearly (Continued)

- **State and federal jurisdiction –** Understand how state and federal law will influence the contract. While many contracts are adaptable regardless of jurisdiction, state law or relevant federal law will always come into play. For example, a community property state may require spousal consent for certain types of contracts.

A written memorialization between the parties prior to drafting a formal contract should do the following: (i) outline the material terms and conditions between the parties with respect to the proposed transaction; (ii) acknowledge that amendments or refinements to the parties' initial understanding will likely occur as a result of ongoing discussions and the due diligence process; and (iii) contain language indicating that the term sheet, memorandum of understanding, or letter of intent is non-binding until definitive transaction documents between the parties are executed and delivered.

2 Adapt a Back Story

A thoughtfully considered contract will provide the back story of how the parties came together in the first place, usually through a succinct, clear, and logical recital of the facts on the first page of the contract.

Contract recitals precede the main text of a contract and are referred to as the "whereas" clauses. Contract recitals introduce the reader to the purpose of the contract, the parties involved, and the reason they are entering the agreement. Contract recitals should also refer to any pre-existing or contemporaneous agreements between the parties that will impact the contract at hand.

While the business principles may understand the back story, the drafting lawyer often may not. Constructing the contract recitals is critical for helping the drafting lawyer understand what they will need to craft a solid contract. The contract recitals set the table for the issues that the drafting lawyer must consider in creating the finished product.

Contract recitals should not include specific rights or obligations; they are in place simply to explain the back story of the contractual relationship. And while there is no prescribed format for drafting the contract recitals, they will contain a concise statement of the facts describing the principal circumstances and details relevant to the establishment of the contract. Statements of intent and references to related or ancillary agreements are always helpful.

Finally, the drafting lawyer should remember that the contract recitals will help future readers understand what preceded the current agreement between the contracting parties, especially if the contract does become a matter of dispute.

3 Build the Legal Puzzle Piece by Piece

Drafting a contract is analogous to building a puzzle; all the pieces must fit together just so and in a logical sequence. The principal contract provisions include:

- **Required contractual parties –**
  While the parties to a contract may often be self-evident, many situations include multiple parties at the table with varying degrees of relationship. This is true particularly in complex financial and business transactions.

- **Defined terms, deadlines, and closing responsibilities –**
  Even routine contracts involve a litany of legal terms. Complex contracts may often include multiple pages or special exhibits dedicated to defining these terms. Deadlines and actions and responsibilities prior to closing are common in transactional contracts involving multiple parties. Synthesizing various contract pieces falls to the drafting lawyer.

- **Representations and warranties –**
  Representations and warranties in a contract provide (i) representations (facts) that are relied on as being true on the date the representation is made and (ii) warranties (security or protections) should the statements of fact prove to be inaccurate or untrue at any time during the transactional relationship. More often than not, representations and warranties are employed interchangeably and provided by the principal parties to the contract. Representations and warranties are used in nearly all transactional contracts but most especially in business combination, joint venture, consulting, employment, and financing contracts. For example, in a loan agreement, the borrower will provide representations and warranties designed to entice the lender to issue a loan. In an acquisition or merger agreement, the acquiring company will certainly want the target company to agree to a number of representations and warranties in order to close the transaction, focusing on corporate authority, legal compliance, financial statements, taxes, litigation, capitalization, and other issues.

3 Build the Legal Puzzle Piece by Piece (Continued)

- **Governing law and dispute resolution –** The governing law and dispute resolution provisions of the contract will detail how a contract breach or default is meant to be handled. This includes who will be responsible for attorneys' fees and whether arbitration or litigation will be considered, as well as other issues. A distinction should be drawn between the governing law clause and the dispute resolution clause. While the former deals with the substantive law governing the contract, the latter establishes the forum for adjudicating contractual disputes.

- **Term and termination –** The term of the contract should be specified, including renewal opportunities and party actions that may result in premature termination of the contract. If the contract concerns ongoing services, a provision should always be included to allow for reasonable prior notice to terminate the contract without cause. More on this below.

- **Standard provisions –** Most contracts include certain standard provisions addressing confidentiality, severability, amendments, successors and assigns, force majeure, notices, and other issues. Even such routine matters need to be spelled out clearly to complete the contract. The standard (boilerplate) provisions will often be grouped together at the end of the contract under the heading of "General" or "Miscellaneous."

4 Parting is Such Sweet Sorrow

The termination clause (i) is a written provision in the contract that defines the circumstances under which the contract will end and (ii) should be included in just about every type of contract.

- **Fulfillment –**
  The contract runs its natural course and terminates according to its stated terms and conditions.

- **Mutual agreement –**
  The parties reach an understanding and agree to nullify the contract and the respective duties defined by the contract.

- **Impossibility of performance –**
  Because of unforeseeable or uncontrollable circumstances, it becomes impossible or impracticable for the parties to perform their respective obligations. In other words, force majeure rears its ugly head and provides an out for all concerned parties. This option has become increasingly common during the era of COVID-19.

- **Mistake, fraud, or misrepresentation –**
  The contract fails to include all necessary information or misrepresents certain circumstances that are important to the completion of the contract—an obvious failure by the drafting lawyer.

- **Breach of contract –**
  If one of the contracting parties does not perform its duties, this constitutes a breach. As a result, the non-breaching party is entitled to recover its losses and terminate the contract.

5 Remember Your Audience

While the goal of drafting a solid contract is to avoid ending up in court, it is always best to draft a contract with the expectation that it will end up being litigated.

Draft as a lawyer, but remember that your ultimate audience (the client) will probably not be other lawyers. Language should be clear and understandable. Avoid ambiguity, and write in a way that a layperson could read and understand the contract. Once a party or term is defined, use the term consistently throughout the contract.

6 Use Exhibits, Schedules, and Addenda Judiciously

Exhibits, schedules, and addenda are frequently attached to contracts; and they are usually established prior to executing the agreement.

Exhibits, schedules, and addenda all differ in purpose and should be specifically referenced in the body of the principal contract.

- **Exhibits –**
  An exhibit is an additional document attached to the end of a contract that becomes an integral part of the transaction. An exhibit will frequently include documents both ancillary and inter-related to the principal contract. Examples might be additional agreements presented alongside a preferred stock offering or a promissory note integral to a loan transaction. Exhibits are used to expand upon information in the contract, such as when a real-estate legal description is needed to specify which property is the subject of the contract.

- **Schedules –**
  A schedule is also attached to the end of a contract. However, unlike exhibits, schedules consist of information essential to the terms of the contract. Schedules frequently include technical information that is best read in a list or tabular format. In a merger or acquisition contract, the seller's representations and warranties will frequently reference specific information attached in a cross-referenced schedule. Since schedules include information essential to the contract, the contract should state that all schedules are incorporated into the contract.

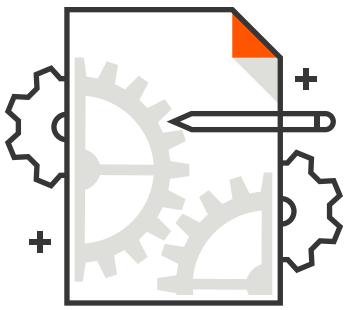
- **Addenda –**
  Also attached to the end of a contract, an addendum expands upon the contract's terms. The form of the addendum is agreed upon when a contract is executed. An addendum might change a pre-printed form contract in which the parties have agreed to something that differs from the standard form. An addendum is commonly used in a residential real-estate purchase contract to add contingencies, deadlines, or other requirements. Another common use of addenda is in cases where the parties have a master agreement, governing their business arrangement, but they expect to include specific purchases under the master contract.

← Back to Table of Contents

7 Develop and Leverage Reliable Resources

Good lawyers develop form libraries over the course of their careers, which are invaluable in drafting a variety of contracts.

Cultivating a deep reservoir of model contracts with key provisions helps in building well-constructed contracts. Fortunately, there are now online resources to identify a model contract or exceptionally well-drafted clause or definition. LawInsider.com is one of the best English-language resources to locate reputable, publicly available model contracts, clauses, and definitions.



8 Manage Client Expectations

One of the surest ways to manage client expectations is to spend time with your client to explain what the contract is meant to accomplish and what the contract is not meant to accomplish.

For example, several years ago while working with a successful entrepreneur to draft a family constitution, I learned that the client expected that the family constitution would shield family-held shares in the private business in case a family member got divorced. I explained to my client that this would require a prenuptial or antenuptial agreement.

Other ways to manage a client's expectations and improve the process of concluding a successful contract include:

- **Asking questions –**
  Pose questions that not only deal with the pertinent information of the contract, but also consider your client's thought on the potential transaction at hand.

- **Revisiting client goals –**
  As the drafting and transaction process rolls along, a best practice is to regularly revisit your client's goals. Client goals and expectations can change over time, which may lead to frequent reassessments of contract objectives.

- **Polishing and redrafting –**
  Contract drafters are writers and require time to assess and reassess; remember, however, that great is frequently the enemy of good.

- **Engaging clients –**
  Of course, one of the initial and most important ways to manage client expectations is to establish the lawyer's relationship with the client in a comprehensive engagement letter, setting out the terms of the engagement including budget, scope, deliverables, and timeline. If you don't clarify and document expectations at the outset, your client will likely have different and often grander expectations than you about what you're going to do for them. Establishing the scope of your engagement also helps you focus on what really matters: delivering value to the client.

Conclusion

I recall the late-November day during my first semester in law school when our contracts professor unexpectedly announced that the next class session would be devoted to a lecture on black letter law. The professor apparently could tell that months of approaching contract theory through the Socratic method was beginning to wear thin. After a steady diet of reading cases and trying to assemble in my mind what this offer, acceptance, consideration business was all about, I was thrilled to hear that we were actually going to be taught something practical. It's not hard to keep a weary, first-year law student happy. And evidently, the students in the other contracts section felt the same; the next contracts class was standing room only. Every first-year law student attended.

While we did not learn about how to draft a contract during Black Letter Day, we did learn that the law of contracts does follow a reasonably predictable pattern. Learning the actual nuts and bolts of drafting contracts did not come during law school; that skill was acquired through grinding years of law-firm boot camp.

In the end, the drafting lawyer serves as a precision engineer on behalf of his or her clients, guarding against imprecise thinking and inarticulate writing that all too often lead to disputes and complications. Mastering the roadmap to drafting contracts provides the lawyer a valuable tool to better serve their clients.

ABOUT

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