



# Basic Concepts in Drafting Contracts

**December 10, 2014**


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presented by

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to

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## *Basic Concepts in Drafting Contracts*

### Summary of Presentation: What this Presentation Covers

- Preliminary Matters

- Legal Drafting vs. Conversation/Prose Writing
- The Importance of Language
- Preferences in Contract Drafting
- Practical Considerations

- The Framework of a Contract

- Preamble
- Recitals
- \*\* Body
- Signature Pages

- Definitions
- Language of Performance
- Obligations
- Discretionary Language
- Language of Declaration
- Language of Policy

- Legal Archaisms

## *Basic Concepts in Drafting Contracts*

### Summary of Presentation: What this Presentation does *NOT* Cover

- The law\*
- The structure of any agreement in particular (e.g., asset purchase agreements, stockholders' agreements, license agreements, etc.) – rather, it deals with *how* to express concepts in contracts generally
- The drafting process (e.g., integration of comments from multiple sources)
- Certain advanced/specifically nuanced drafting concepts.
- Using drafting skills in connection with negotiations (e.g., “negotiating through the document,” how to use vagueness and ambiguity to your advantage)

\* To the extent that this presentation is required to cover the law in order for attorneys to obtain CLE credit, this presentation is deemed to cover the law.



*Basic Concepts in Drafting Contracts*

Preliminary Matters

- Legal Drafting vs. Conversation/Prose Writing
- The Importance of Language
- Preferences in Contract Drafting
- Practical Considerations

## *Basic Concepts in Drafting Contracts*

Preliminary Matters > [Legal Drafting vs. Conversation/Prose Writing](#)

### Forget common sense

Example: If my wife wants me to take out the garbage each week, “Vincent, you’re responsible for taking out the garbage” should do the trick. You get the idea – I take out the garbage each week, it gets picked up, I bring the garbage cans back in and I do it all over again in advance of the next scheduled pick-up.

## *Basic Concepts in Drafting Contracts*

Preliminary Matters > [Legal Drafting vs. Conversation/Prose Writing](#)

*Vincent, you're responsible for taking out the garbage.*

*But as an attorney, if I wanted to poke holes in the deal, I could ask:*

- What day and time during the week do I take out the garbage?
- Can I take out the garbage only once, or is this an ongoing obligation?
- Can I let the garbage pile up for a year and then take it out?
- Do I need to take out all of the garbage in the house, or just some of it?
- Does the garbage need to be bagged? Can I just throw a half-eaten chicken wing on the front porch?
- Can I sub-contract my garbage-taking-out responsibilities to my daughter?
- ...and what exactly constitutes “garbage” anyway?

## *Basic Concepts in Drafting Contracts*

Preliminary Matters > [Legal Drafting vs. Conversation/Prose Writing](#)

*Vincent, you're responsible for taking out the garbage.*

*Written in lawyer speak...*

“No later than 6 a.m. New York time each Monday and Thursday (and no earlier than 7 p.m. each Sunday and Wednesday, respectively), Vincent shall: (i) place all Garbage on the interior of the house on the premises (the “House”) in trash bags (any such trash bag into which Garbage has been placed, a “Trash Bag”); (ii) seal and place each Trash Bag in one of the garbage cans located on the exterior of the House (any such garbage can into which a Trash Bag has been placed, a “Garbage Can”); and (iii) thereafter place each Garbage Can no more than one inch south of the curb of the sidewalk relating to the premises and between one and seven feet west of the driveway on the premises. Vincent shall place all Garbage Cans on the east side of the House (and adjacent thereto) as of 6 a.m. New York time each Tuesday and Friday. Vincent’s obligations under this paragraph are personal in nature and, as such, are not delegable in whole or in part. “Garbage” means rubbish, as determined by Christine in her sole discretion.”



## *Basic Concepts in Drafting Contracts*

Preliminary Matters > [Legal Drafting vs. Conversation/Prose Writing](#)

- The point is, forget “you-get-the-idea” drafting. Forget “contract-as-a-mere-guidebook” drafting. If you want to make a contract tight and less subject to uncertainty and multiple interpretations, ask the questions and plug the holes. Otherwise:
  - The law will plug the holes for you\*
  - Your adversary will plug the holes for you
  - It will be unclear what rule will apply, or whether different rules apply in different contexts

\* e.g., “public policy” and “fairness” doctrines.

## *Basic Concepts in Drafting Contracts*

Preliminary Matters > [The Importance of Language](#)

# *Quality contract drafting saves \$\$\$*

- Court opinions on contract language disputes are the tip of the iceberg (e.g., arbitration, re-negotiation, submission to contract terms that have been drafted unfavorably)
- Cost savings in addressing problems up front
- Systematic approach to expressing concepts in a contract leads to: (1) meeting of the minds, (2) uncovering hidden ambiguities and topics not addressed, and (3) better understanding of the contract after it is entered into



## *Basic Concepts in Drafting Contracts*

Preliminary Matters > [Preferences in Contract Drafting](#)

Some general preferences in contract drafting are listed below. Note that an “improvement” in one characteristic might result in a “decline” in other characteristics.

- \* **Unambiguous** is better than **Ambiguous**
- **Concision** is better than **Redundancy**
- **Shorter** is better than **Longer**
- **Predictability** is better than **Uncertainty**
- **Plain English** is better than **Jargon**
- **Precision** might or might not be better than **Vagueness**
- **Consistency** is better than **Inconsistency**
- **Straightforward** is better than **Confusing**

## *Basic Concepts in Drafting Contracts*

### Preliminary Matters > [Practical Considerations](#)

- Law as a backdrop/basis for provisions
- Reliance on forms (a blessing and a curse)
- Know your audience
  - For this presentation, we will assume that sophisticated business people and attorneys are your audience
- Detail vs. Generality (Will too much of good thing spoil the deal?)
- Holding the pen vs. reacting
- Integrating comments
- \* Universal drafting “rules” vs. good practice vs. your own style
- For more junior attorneys, start developing good drafting habits now so you can easily implement them going forward
  - Quickly draft a tight agreement when you’re holding the pen
  - Spot and exploit drafting weaknesses in opposing counsel’s draft

## *Basic Concepts in Drafting Contracts*

Preliminary Matters > [Practical Considerations](#)

### Useful Resources for Learning/Improving Drafting Skills

- *A Manual of Style for Contract Drafting (Third Edition)*, Kenneth A. Adams (2013)
- *The Structure of M&A Contracts*, Kenneth A. Adams (2011)
- *Garner on Language and Writing*, Bryan A. Garner (2009) – more generalized concepts (including writing skills for litigators)
- *Negotiating and Drafting Contract Boilerplate*, Tina L. Stark (Ed.) (2003) – For the intersection between law and contract language
- *Typography for Lawyers*, Matthew Butterick (2010) – This what happens when a font designer becomes an attorney. Great book on formatting legal documents – and more than just fonts!
- Annotated forms
- Successive “redlines” of a document
- Board resolutions
- Due diligence materials
- Experience

## *Basic Concepts in Drafting Contracts*

### The Framework of a Contract

- Preamble
- Recitals
- Body
  - Definitions
  - Language of Performance
  - Obligations
  - Discretionary Language
  - Language of Declaration
    - ✓ Representations and Warranties
    - ✓ Acknowledgements
  - Language of Policy
- Signature Pages

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > [Preamble](#)

### Example:

This ASSET PURCHASE AGREEMENT (this “Agreement”), dated as of December 10, 2014, is made between Big Bad Corporation, a Delaware corporation (the “Buyer”), and Little Guy, LLC, a New York limited liability company (the “Seller” and, collectively with the Buyer, the “Parties”).

- Type of agreement
- Date of agreement
- Parties to agreement (including jurisdiction of organization and entity type)
- Save descriptive relationships between the parties for the recitals or the body of the contract (e.g., the representations)

## *Basic Concepts in Drafting Contracts*

### The Framework of a Contract > [Recitals](#)

- Describe background; give the reader context
- Set up defined terms

#### Example:

A. The Seller is engaged as a going concern in the business of designing, manufacturing, marketing, distributing, and selling paper clips (such business, the “Business”);

- Can serve as evidence of intent and help to resolve ambiguity (but there’s not going to be any ambiguity in contracts that you draft, right?)



## *Basic Concepts in Drafting Contracts*

### The Framework of a Contract > [Recitals](#)

- Do not put operative provisions (e.g., language of performance, representations, or obligations) in recitals
  - ☺ A. The Parties desire to amend the Loan Agreement in order to, among other things, extend the maturity date of the Loan to December 31, 2015.
  - ☹ A. The Parties are hereby amending the Loan Agreement to extend the maturity date of the Loan to December 31, 2015.
  - ☹ A. The Parties shall take such actions as are necessary to implement the terms of this Agreement.

## *Basic Concepts in Drafting Contracts*

### The Framework of a Contract > [Recitals](#)

- Immediately after the recitals, there is typically a lead-in stating that the parties are agreeing to what follows.
  - ☹ NOW, THEREFORE, in consideration of the premises and the respective covenants, representations, warranties and undertakings of the parties hereinafter set forth, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto hereby agree as follows:
  - ☺ The Parties hereby agree as follows:

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > [Body](#)

- Definitions
- Language of Performance
- Obligations
- Discretionary Language
- Language of Declaration
  - Representations and Warranties
  - Acknowledgements
- Language of Policy



*Basic Concepts in Drafting Contracts*

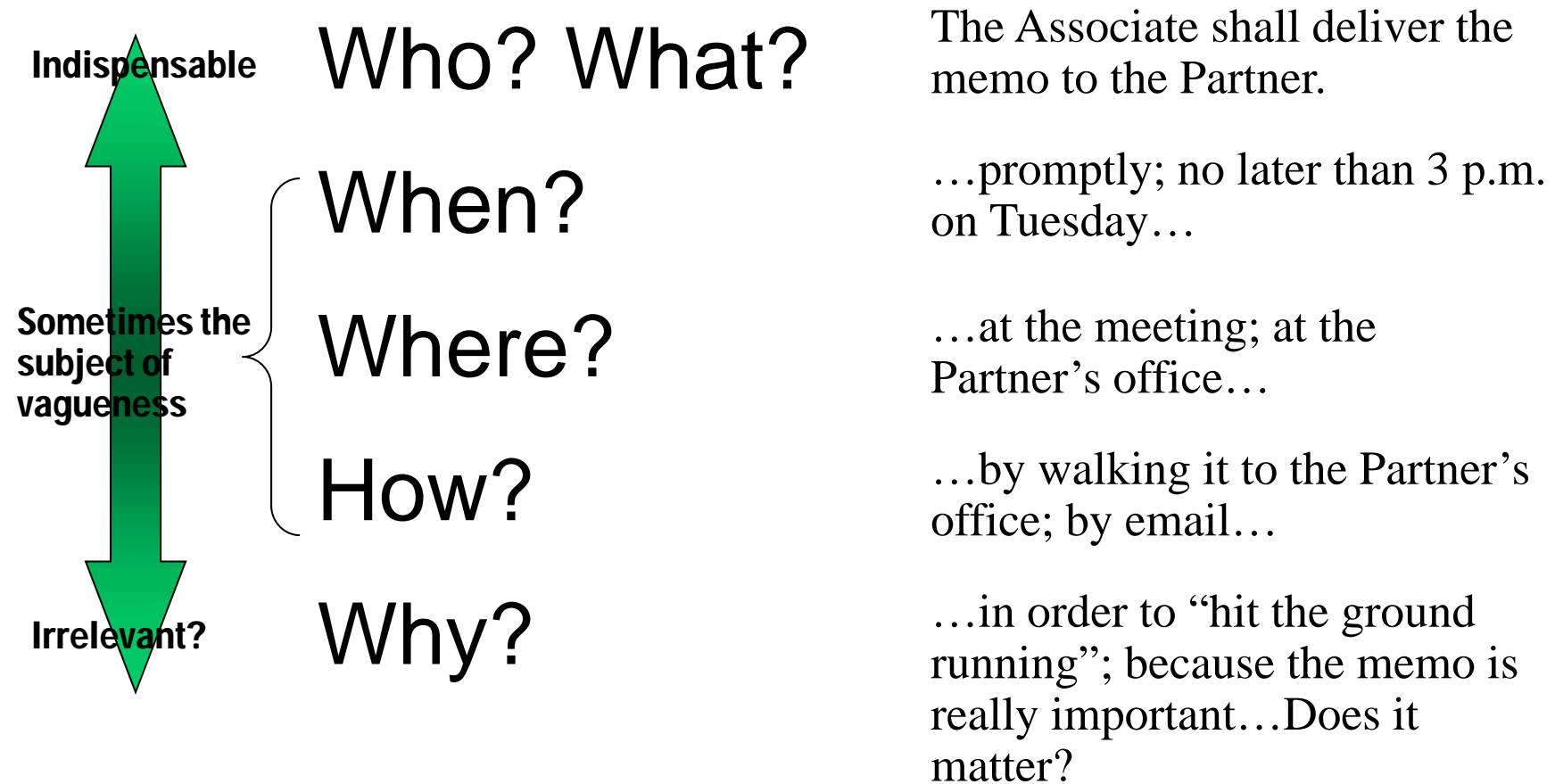
The Framework of a Contract > Body > [An Initial Thought](#)

## An Initial Thought:

*The Who? What? When? Where?  
How? Why? Hierarchy*

## Basic Concepts in Drafting Contracts

The Framework of a Contract > Body > [An Initial Thought](#)





*Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Definitions](#)

# Definitions

## Lots of power in defined terms!

1. A. The Seller is engaged as a going concern in the business of designing, manufacturing, marketing, distributing, and selling paper clips (such business, the “Business”).
- 2(a). The Company shall not sell or distribute (each of the foregoing, a “Transfer”) the Shares.
- 2(b). The Company shall not sell, **assign, pledge, encumber, hypothecate, distribute (as a dividend or otherwise), transfer, or otherwise dispose of** (each of the foregoing, a “Transfer”) the Shares.
3. “Attorney” means an attorney, a legal assistant, a chef, or any individual residing in the state of New York.

## “Stacking” defined terms

This STOCKHOLDERS’ AGREEMENT (this “Agreement”) is made as of December 10, 2014, between Example & Co., Inc., an Idaho corporation (the “Company”), those holders of the Company’s Series A Preferred Stock listed in Exhibit A (the “Series A Holders”), those holders of the Company’s Series B Preferred Stock listed in Exhibit B (the “Series B Holders” **and, collectively with the Series A Holders, the “Preferred Stockholders”**), and those holders of the Company’s common stock that are listed in Exhibit C (the “Common Stockholders” **and, collectively with the Preferred Stockholders and those persons that become a party to this Agreement in accordance with the terms of this Agreement, the “Holders”**; the Holders and the Company, collectively, the “Parties”).





## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Definitions](#)

### Defining “on site” vs. Defining in a “Definitions” Provision

#### **Defining “On site”**

“Transfer” has the meaning set forth in Section 2.3.

...

Section 2.3. The Company shall not sell, assign, pledge, encumber, hypothecate, distribute (as a dividend or otherwise), transfer, or otherwise dispose of (each of the foregoing, a “Transfer”) the Shares.

#### **Definitions Provision**

“Transfer” means, with respect to a given asset, any sale, assignment, pledge, encumbrance, hypothecation, distribution (as a dividend or otherwise), transfer, or other disposition of such asset. When used as a verb, “Transfer” has a correlative meaning.

...

Section 2.3. The Company shall not Transfer the Shares.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Definitions](#)

If defining a term “on site,” make sure it is clear which text a definition relates to

- ☹ Section 1.1. Johnny shall sell apples to Eve in accordance with Section 1.2 and shall sell oranges to Adam in accordance with Section 1.3 (any such sale, a “Required Sale”).
  - There’s ambiguity as to whether a Required Sale includes sales to Adam only, or includes sales to Eve and sales to Adam.
- ☺ Section 1.1. Johnny shall sell apples to Eve in accordance with Section 1.2 and shall sell oranges to Adam in accordance with Section 1.3 (any such sale to Eve or Adam, as the case might be, a “Required Sale”).

**OR**

- ☺ Section 1.1. Johnny shall sell apples to Eve in accordance with Section 1.2 and shall sell oranges to Adam in accordance with Section 1.3. “Required Sale” means any sale described in this Section 1.1.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Definitions](#)

### *It's ok to.....*

- ...use the lowercase term as part of a definition
  - “Transfer” means any **transfer**, sale, pledge, hypothecation, encumbrance, or other disposition.
  - “Permitted Automobile” means any **automobile** that is permitted on the Long Island Expressway, including, without limitation, my old 1983 Pontiac Firebird.
- ...use other defined terms within a definition
  - “Law” means any constitution, law, statute, treaty, rule, directive, requirement, regulation, **Order**, or any rules or regulations of any self-regulatory organization.
  - “Order” means any order, writ, judgment, **injunction**, decree, determination, or award, in each case that is issued by a **Governmental Entity**.
  - “Governmental Entity” means any court, **administrative agency**, commission, or other governmental authority or instrumentality, domestic or **foreign**, federal, state, or local.

A “Law” therefore includes, e.g., any **injunction** issued by a **foreign administrative agency**.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Definitions](#)

*...but do not...*

- ...embed obligations within a definition
  - ☹ “Net Earnings Statement” means a statement of the Company’s net earnings during the Post-Closing Period in the form attached as Exhibit A, **which the Company shall provide to the Seller no later than 30 days after the last day of the Post-Closing Period.**

*BETTER TO BREAK IT UP AS FOLLOWS:*

- ☺ “Net Earnings Statement” means a statement of the Company’s net earnings during the Post-Closing Period in the form attached as Exhibit A.

...

Section 2.4. No later than 30 days after the last day of the Post-Closing Period, the Company shall provide the Net Earnings Statement to the Seller.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Definitions](#)

*...and do not...*

- ...simply use “includes”

☹ “Permitted Automobile” includes, without limitation, my old 1983 Pontiac Firebird.

- ...use more than one term for the same definition

☹ Verbiage Co., a Delaware corporation (“Verbiage” or the “Company”), is a subsidiary of the Parent.

- ...use “shall” to define a term

☹ “Securities Act” shall mean the Securities Act of 1933, as amended.



*Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Language of Performance](#)

# Language of Performance

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Language of Performance](#)

- Deals with actions being taken by the parties **by virtue of** entering into a contract
- Think: “hereby”
- Use the active voice, not the passive voice
  - ☹ The License is **hereby granted** to the Licensee by the Licensor.
  - ☺ The Licensor **hereby grants** the License to the Licensee.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Language of Performance](#)

### Some examples

#### *Language of Performance*

- The Licensor **hereby grants** to the Licensee a non-exclusive worldwide license to use the Product.
- The Buyer **hereby assumes** the Assumed Liabilities.

#### *Obligations*

- The Licensor **shall grant** to the Licensee a non-exclusive worldwide license to use the Product.
- The Buyer **shall assume** the Assumed Liabilities.



*Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Obligations](#)

# Obligations

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Obligations](#)

### Affirmative Obligations

- What a party **has to do** pursuant to a contract
- Think: “shall”

### Negative Obligations (Prohibitions)

- What a party **is prohibited from doing** pursuant to a contract
- Think: “shall not”

## *Basic Concepts in Drafting Contracts*

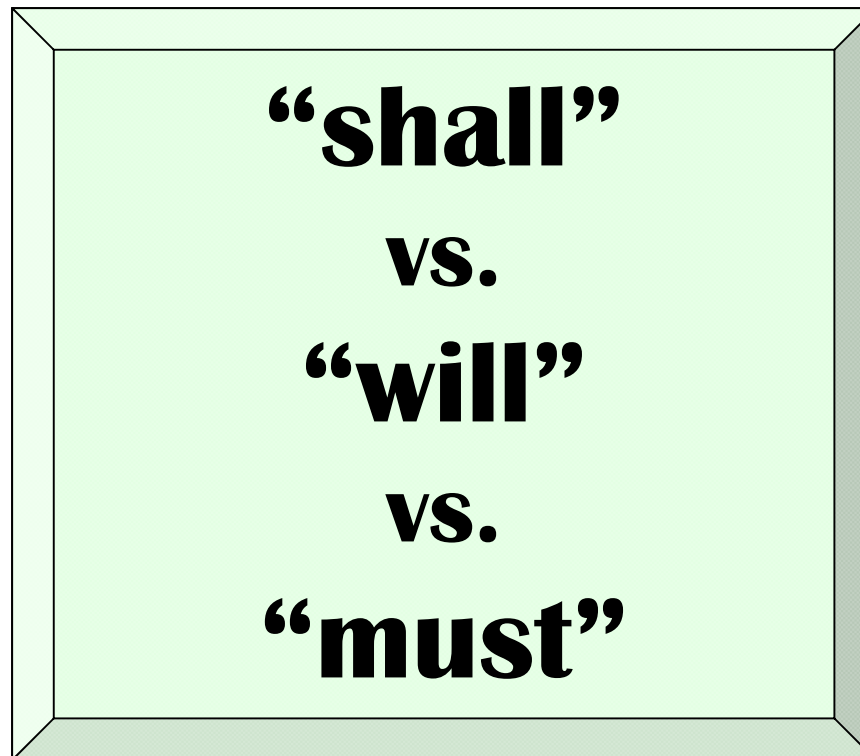
The Framework of a Contract > Body > [Obligations](#)

### Examples:

- The Purchaser **shall pay** the Purchase Price to the Seller at the Closing.
- Each of Moses and his constituents **shall not** covet his respective neighbor's wife.
- The Presenter **shall not** use any fancy visual effects when transitioning between slides.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligations > “shall” vs. “will” vs. “must”



## Basic Concepts in Drafting Contracts

The Framework of a Contract > Body > Obligations > “shall” vs. “will” vs. “must”

✦ **“Shall” → “hereby has/have a duty to”**

*The Purchaser shall wire the Purchase Price to the Seller.*

=

*The Purchaser hereby has a duty to wire the Purchase Price to the Seller.*

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligations > [“shall” vs. “will” vs. “must”](#)



**Do NOT use “shall” unless  
you want to create an  
obligation.\***

\* Avoid the temptation of using “shall” as a proxy for “...and I really mean it!”

- ☹ This Agreement shall constitute the entire agreement of the Parties with respect to the subject matter hereof.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligations > “shall” vs. “will” vs. “must”

- “Will” is sometimes used to create an obligation.
  - ☺ The Purchaser **will** wire the Purchase Price to the Seller.
- But “will” can also convey futurity, whereas “shall” (in ordinary parlance) is an awkward choice (unless you’re King Arthur).
  - ☺ Davey hereby bets Lou that the Mets **will** win the World Series this year.
  - ☹ Davey hereby bets Lou that the Mets **shall [i.e., hereby have a duty to]** win the World Series this year.

*In fact, Davey just lost the bet!*

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligations > [“shall” vs. “will” vs. “must”](#)

- “Must” means “is/are required to.” This could arguably be used as an alternative to “shall” to impose an obligation.
  - ☹ The Purchaser **must** wire the Purchase Price to the Seller.
- But “must” really asserts that a duty merely exists, not that it derives from the provision in which it is used.
  - ☺ If companies **must [are required to]** pay an excise tax on the Product of 20% or less pursuant to applicable law, then Newcomer Co. **shall [hereby has a duty to]** sell the Product.
  - ☹ If companies **shall [hereby have a duty to]** pay an excise tax on the Product of 20% or less pursuant to applicable law, then Newcomer Co. **shall [hereby has a duty to]** sell the Product.



## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligations > “shall” vs. “will” vs. “must”

- Note that “must” works in instances in which “shall” does not, e.g., in expressing conditions.
  - ☺ In order for Lindsay to drive the car home from the pub, she **must** first convince her mom to give her the keys.
  - ☹ In order for Lindsay to drive the car home from the pub, she **shall** first convince her mom to give her the keys.
    - ❖ You should not draft the sentence this way since Lindsay is not **obligated** to convince her mom to give her the keys, and there should not be a cause of action against Lindsay if she failed to convince her mom to give her the keys. (In fact, it could very well be the other way around if she succeeded in convincing her mom....)

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligation and Prohibitions > “shall” vs. “will” vs. “must”

### **Use:**

- “shall” to convey an obligation
- “will” to convey futurity
- “must” to convey a condition to be satisfied or to point to an obligation that exists but that derives from another provision

### **Do not use:**

- “is obligated to”
- “agrees to”
- “covenants and agrees to”
- “shall be obligated to”
- “undertakes to”



*Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligations > [Active Voice vs. Passive Voice](#)

Active Voice  
vs.  
Passive Voice

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligations > [Active Voice vs. Passive Voice](#)

General rule: Use the active voice rather than the passive voice when imposing an obligation.\*

- Makes clear which party is the actor
- More concise than the passive voice
- Easier to read/More natural than the passive voice
- In the context of an obligation, consistent with substituting “hereby has/have the duty to” for “shall”

\* There are certain instances in which it makes sense to use the passive voice (e.g., those in which the identity of the actor does not matter).

## *Basic Concepts in Drafting Contracts*

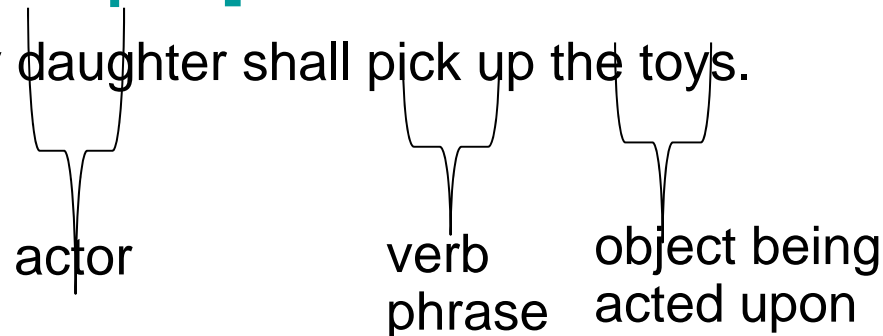
The Framework of a Contract > Body > Obligations > [Active Voice vs. Passive Voice](#)

**Active Voice: The actor is the sentence's subject.**

General format (for an obligation) =

**[actor] + shall/shall not + [verb (or verb phrase)] + [object being acted upon]**

Example: My daughter shall pick up the toys.



## Basic Concepts in Drafting Contracts

The Framework of a Contract > Body > Obligations > [Active Voice vs. Passive Voice](#)

**Passive Voice (with identified passive agent): The subject of the sentence is not the actor.**

General format (for an obligation) =

**[subject being acted upon] + shall/shall not + [verb (or verb phrase)] + by + [passive agent]**

Example: The toys shall be picked up by my daughter.

subject being acted upon      verb phrase      passive agent

- Does not fit the “hereby has/have a duty to” rule
- Less concise and more awkward than active voice

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligations > [Active Voice vs. Passive Voice](#)

**Truncated Passive Voice (no identified passive agent): The actor is not identified.**

General format (for an obligation) =

**[subject being acted upon] + shall/shall not + [verb (or verb phrase)] + ~~by + [passive agent]~~**

Example: The toys shall be picked up.

subject being  
acted upon

verb  
phrase

## Basic Concepts in Drafting Contracts

The Framework of a Contract > Body > Obligations > [Active Voice vs. Passive Voice](#)

### Truncated Passive Voice (no identified passive agent)


Example: The toys shall be picked up.

subject being acted upon

verb phrase

Who is obligated to pick up the toys?

- My daughter, Julia?
- My son, Matthew?
- ☹ Answer: Mommy and Daddy.



*Hey! Was the passive agent intentionally omitted?*



## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligations > [Third Parties](#)

\*\* You can't impose obligations upon persons that are not party to the contract.

☹ Upon final resolution of all Disputed Items, **the Accountants shall issue** a report showing a calculation of the Final Net Working Capital. **The Accountants shall make** their determination of the Disputed Items within 60 days after having been selected.

- ❖ What if the Accountants don't issue a report showing a calculation of the Final Net Working Capital?
- ❖ What if the Accountants don't make their determination within 60 days?

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligations > [Third Parties](#)

\*\* You can't impose obligations upon persons that are not party to the contract.

- ☺ Upon final resolution of all Disputed Items, **the Accountants must issue** a report showing a calculation of the Final Net Working Capital. **The Accountants must make** their determination of the Disputed Items within 60 days after having been selected.
- ☺ Upon final resolution of all Disputed Items, **the Parties shall cause the Accountants to issue** a report showing a calculation of the Final Net Working Capital. **The Parties shall cause the Accountants to make** their determination of the Disputed Items within 60 days after having been selected.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Obligations > [Third Parties](#)

\*\* You can't impose obligations upon persons that are not party to the contract.

- ☺ If the Parties are unable to resolve any disagreement as to one or more Disputed Items within 30 days after the Receiving Party's receipt of a Protest Notice, then the Parties **shall promptly engage** Big Accountant Co. (the "Accountants") by signing an engagement letter with the Accountants pursuant to which, among other things, the Accountants **agree to comply with** procedures set forth in this Section 2.4(b)(iii)....The Parties **shall use their respective reasonable best efforts to cause** the Accountants to reach a final determination with respect to all Disputed Items (such determination, a "Final Determination") and to provide to the Parties, no later than the 60th day after the Accountants have been engaged pursuant to this Section 2.4(b)(iii), a report with respect to the NWC Statement (the "Final Determination Report") that includes a calculation of the Net Working Capital.



*Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Discretionary Language](#)

# Discretionary Language

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Discretionary Language](#)

- Deals with what a party is permitted to do
- Think: “is/are permitted to”
- Discretionary language is really an exception to prohibitions:
  - in a contract (i.e., an exception to “shall not”)
  - that are default rules (e.g., Section 18-702(b) of the Delaware Limited Liability Company Act provides that, unless otherwise provided in a limited liability company agreement, a member of a limited liability company ceases to have the power to exercise any rights or powers of a member upon the assignment of all of the member’s limited liability company interest)

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Discretionary Language > [“is/are permitted to” vs. “might possibly”](#)

- “May” can convey what a party ***is entitled/permitted to do***, or it can convey what a party ***might possibility do*** (particularly when used with respect to a third party).
- Example: “may” = “is permitted to”
  - ☹ The Seller shall not encumber the Shares; except that the Seller **may pledge** the Shares to the Bank in connection with a loan provided by the Bank to the Seller.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Discretionary Language > “is/are permitted to” vs. “might possibly”

### **Some background on “may”**

- Example: “may” = “might possibly”
  - ☹ The Seller shall deliver in a timely manner all Products that are required to be delivered pursuant to all purchase orders that Key Customers **may submit** during the Pre-Closing Period.
    - ❖ There is ambiguity here: is the provision referring to (1) all the Purchase Orders that Key Customers “might possibly submit” or (2) only those Purchase Orders that Key Customers “are permitted to submit”?
  - ☺ If a Key Customer delivers a purchase order to the Seller during the Pre-Closing Period, then the Seller shall deliver in a timely manner all Products that are required to be delivered pursuant to such purchase order.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Discretionary Language > [“Naked” Discretion](#)

- Use discretionary language to create an exception to a prohibition in a contract.
  - ☺ At the Closing, the Buyer shall convey the Assets to the Seller. During the period (such period, the “Post-Closing Period”) beginning on the Closing Date and ending on the date that is 10 days after the Closing Date, the Buyer **shall not sell** the Assets to any Competing Enterprise; except that, **during the Post-Closing Period**, the Buyer **is permitted to sell** the Assets to any Key Vendor that is a Competing Enterprise.
- In this example, it is clear that “is permitted to sell” is being used as the exception to the prohibition “shall not sell.”



## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Discretionary Language > [“Naked” Discretion](#)

- Generally, do not use discretionary language if the permitted action is not otherwise prohibited.
  - ⊖ At the Closing, the Buyer shall convey the Assets to the Seller. During the period (such period, the “Post-Closing Period”) beginning on the Closing Date and ending on the date that is 10 days after the Closing Date, the Buyer **shall not sell** the Assets to any Competing Enterprise. **After the expiration of the Post-Closing Period**, the Buyer **is permitted to sell** the Assets to any Key Vendor that is a Competing Enterprise.
- “is permitted to sell” does not add anything here: there is nothing otherwise prohibiting the Buyer from using the Assets after the Post-Closing Period.
- In fact, including the superfluous language might create an unwanted implication: the Buyer is permitted to sell the Assets after the Post-Closing Period, *but only* to Key Vendors that are Competing Enterprises.

*Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Language of Declaration](#)

# Language of Declaration

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Language of Declaration](#)

- Assertions of fact memorialized in a contract
- Two types:
  - Representations and Warranties
  - Acknowledgments

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Language of Declaration > [Representations and Warranties](#)

- Statements made by a party of what was, is, or will be true to induce someone to enter into a contract
- Need not be within the control or knowledge of the party making the representation or warranty
  - Within control/knowledge: Al represents and warrants to George that all of the papers he has written through the date hereof concerning global warming attribute the primary causes of global warming to humans.
  - Not within control/knowledge: Al represents and warrants to George that at least 51% of all reports written through the date hereof by reputable scientists concerning global warming attribute the primary causes of global warming to humans.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Language of Declaration > [Representations and Warranties](#)

Example: Matt represents to Julia as follows:...

- ☺ During December 2013, Matt did not make fun of Julia. (*Past circumstance or event; within the representing party's control/knowledge*)
- ☺ During December 2013, Caroline did not make fun of Julia. (*Past circumstance or event; not within the representing party's control/knowledge*)

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Language of Declaration > [Representations and Warranties](#)

Example: Julia represents to Matt as follows:...

- ☺ Julia is a member of the Justice League. (*Present circumstance or event; within the representing party's control/knowledge*)
  
- ☺ Schedule A contains a complete and accurate list of all people in Caroline's class. (*Present circumstance or event; not within the representing party's control/knowledge*)

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Language of Declaration > [Representations and Warranties](#)

Example: Caroline represents to Daddy as follows:...

☹ Caroline will not whine at the dinner table. (*Future circumstance or event; within the representing party's control/knowledge*)

➤ This is probably better phrased as an obligation, as follows:

☺ Caroline **shall not** whine at the dinner table.

## Basic Concepts in Drafting Contracts

The Framework of a Contract > Body > Language of Declaration > [Representations and Warranties](#)

Example: Caroline represents to Mommy as follows:...

- ☺ None of Caroline's friends will whine at the dinner table. (*Future circumstance or event; not within the representing party's control/knowledge*)
  - We could phrase this as **an obligation**, as follows:
    - ☺ Caroline **shall encourage** each of her friends to not whine at the dinner table.
  - Phrasing this as a representation, however, ensures (at least to a certain degree) that Caroline is "on the hook" if any of her friends whine at the dinner table, whether or not she encouraged them to do so.
    - ☹ Each of Caroline's friends **shall not whine** at the dinner table.



## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Language of Declaration > [Acknowledgments](#)

- A statement in a contract that a party accepts as true
- Why?
  - Aligns intentions
  - Serves as an estoppel
  - Stronger than recitals

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Language of Declaration > [Acknowledgments](#)

### Examples:

- The Shareholder acknowledges that the Shares have not been registered under the Securities Act.
- The Consultant acknowledges that he has reviewed a copy of the Company Policies as in effect on the Effective Date.
- The Employee acknowledges that she has had an adequate opportunity to consult with her own counsel in connection with this Agreement.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Language of Declaration > [Acknowledgments](#)

### Do not...

- ...use acknowledgments to introduce other categories of language.
  - ☹ The Purchaser acknowledges that it shall pay the Closing Costs at the Closing.
- ...use “unconditionally” or “expressly” (or other adverbs) before “acknowledge”
  - ☹ Luke Skywalker begrudgingly acknowledges that the Dark Side of the Force has a certain appeal.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > Language of Declaration > [Acknowledgments](#)

### Do not...

- ...use “acknowledges and agrees”
  - ☹ The Consultant acknowledges and agrees that he has reviewed a copy of, and shall comply with, the Company Policies as in effect on the Effective Date.
  - ☺ The Consultant acknowledges that he has reviewed a copy of the Company Policies as in effect on the Effective Date. The Consultant shall comply with the Company Policies.



*Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Language of Policy](#)

# Language of Policy

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Language of Policy](#)

### Two basic types:

- Language that states rules governing an event or circumstance
- Language addressing the scope, meaning, or duration of a contract or provision

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Language of Policy](#)

Language that states rules governing an event or circumstance

- Any purported transfer in contravention of Section 2.1 will be void.
- The Post-Closing Statement will be deemed final upon the Accountant's delivery of the Final Report.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Language of Policy](#)

Language addressing the scope, meaning, or duration of a contract or provision

- This Agreement terminates on December 31, 2014.
- This Agreement constitutes the agreement of the Parties with respect to the subject matter hereof.
- If any provision of this Agreement is determined by a court of competent jurisdiction to be unenforceable by reason of excessive scope as to geographical, temporal, or functional coverage, then such provision will be deemed to extend only to the maximum geographic, temporal, and functional scope as to which it is permitted to be enforceable.



## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Language of Policy](#)

### Verb Tenses: Present vs. Future

- Use present tense for policies that apply on the effectiveness of the contract
  - ☺ This Agreement **constitutes** the entire agreement of the Parties with respect to the subject matter hereof.
  - ☹ This Agreement **shall constitute** the entire agreement of the Parties with respect to the subject matter hereof.

## Verb Tenses: Present vs. Future

- Use “will” for policies relating to future events that might or might not take place
  - ☺ If the Prevailing Interest Rate drops below the Adjusted Rate, then this Agreement **will terminate**.
  - ☺ If the Prevailing Interest Rate drops below the Adjusted Rate, then this Agreement **will *thereby* terminate**.
  - ☺ If the Prevailing Interest Rate drops below the Adjusted Rate, then this Agreement **will terminate *by virtue thereof***.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > Body > [Recap](#)

- Definitions
- Language of Performance
- Obligations
- Discretionary Language
- Language of Declaration
  - Representations and Warranties
  - Acknowledgements
- Language of Policy

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > [Signature Pages](#)

Entities can sign on behalf of limited liability companies and partnerships – you need to “reach an authorized human.”

Each Party is signing this Agreement as of the Effective Date.

**BASIC STRUCTURE, INC.**

By: \_\_\_\_\_  
Name: Adam Smith  
Title: President

**ULTIMATE SUB, LLC**

By: PASS-THROUGH, LP,  
its Managing Member

By: USELESS INTERMEDIATE SUB, LLC,  
its General Partner

By: ULTIMATE PARENT, INC.,  
its Managing Member

By: \_\_\_\_\_  
Name: Dr. Complicated  
Title: Chief Difficulty Officer

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > [Signature Pages](#)

### Drafting tips for the lead-in on the signature page

- ☹ Each of the Parties has executed this Agreement as of the \_\_\_\_ day of December, 2014.
- ☹ Each of the Parties has executed this Agreement as of December \_\_\_\_, 2014.
- ☹ Each of the Parties has executed this Agreement as of \_\_\_\_\_, 2014.
- ☺ Each Party is signing this Agreement as of the Effective Date.
- ☺ Each Party has executed **and delivered** this Agreement as of the Effective Date.

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > [Signature Pages](#)

### Practical Tips

- On the page prior to the sig page:
  - Use “[Signature page follows]” rather than “[THE REMAINDER OF THIS PAGE INTENTIONALLY HAS BEEN LEFT BLANK]”
  - Insert a “Section Break” prior to the sig page, not a “Page Break”
- Get rid of headers and footers on the sig page
  - Exception: You might want to specifically label the footer of the sig page to denote the counterpart being signed (e.g., “*Signature Page to Assignment Agreement (Foreign Seller to Domestic Purchaser)*”)

## *Basic Concepts in Drafting Contracts*

The Framework of a Contract > [Signature Pages](#)

### Practical Tips

- Make sure that you and your adversarial counterpart are “on the same page” – Think ahead!
  - Same exact counterparts
  - Number of executed originals per document (be mindful of documents that are negotiable instruments....)
- Make sure that you and your client are “on the same page” – Think ahead!
  - Number of executed originals per document (be mindful of documents that are negotiable instruments....)
  - \*\* Executive availability

*Basic Concepts in Drafting Contracts*

Legal Archaisms

*Ready thy quill and powdered wig! It's time for...*





## *Basic Concepts in Drafting Contracts*

### Legal Archaisms

#### **“that” vs. “which” (vs. “, which”)**

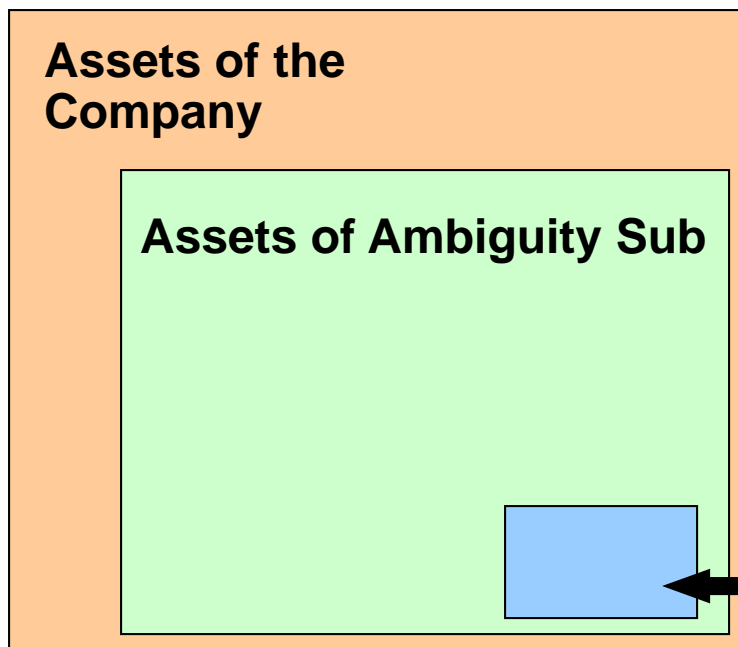
- **“that”** – Think: restrictive; limiting
  - I’ll give you all the books in my library **that** I have read.
    - ❖ i.e., I’m not going to give you all of the books in my library – just those that I have read.
- **“, which”** – Think: descriptive
  - I’ll give you all the books in my library, **which** I have read.
    - ❖ i.e., I have read all of the books in my library and I will give them to you.
- **“which”** [no preceding comma] – Think: Can I replace with “that”?
  - I’ll give you all the books in my library **which** I have read.
    - ❖ It’s unclear whether you get all the books in my library or only those that I have read.

## Basic Concepts in Drafting Contracts

### Legal Archaisms

#### “that” vs. “which” (vs. “, which”)

- ☠ “Purchased Assets” means all of the assets owned by the Company and its Subsidiaries, other than those assets owned by Ambiguity Sub **which** are not material to the Company’s operations.



- If “which” is interpreted to mean “that”, then only the blue (small) rectangle gets carved out
- But if “which” is interpreted to mean “, which”, then the green (medium) rectangle gets carved out

Immaterial Assets of Ambiguity Sub

## *Basic Concepts in Drafting Contracts*

### Legal Archaisms

- ☹ WHEREAS,
- ☹ NOW, THEREFORE,
- ☹ IN WITNESS WHEREOF,
- ☹ Do hereby/does hereby
- ☹ Undertakes to –

- just use “shall”

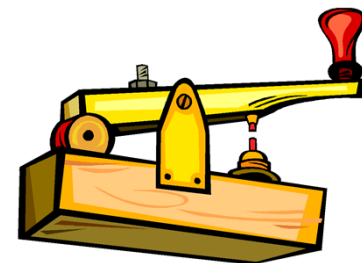


Lancelot does hereby conveyeth his undying love for Guenevere and henceforth shall stave off with sword all others who attempteth to bring her harm.

## *Basic Concepts in Drafting Contracts*

### Legal Archaisms

All notices, consents, approvals, reports, designations, requests, waivers, elections, and other communications (collectively, “Notices”) authorized or required to be given pursuant to this Agreement shall be given in writing and either personally delivered to the Partner to whom it is given or delivered by an established delivery service by which receipts are given or mailed by registered or certified mail, postage prepaid, or sent by **telex, electronic telecopier or telegram**, addressed to the Partner at his or its address listed beneath such Partner’s respective signature hereto.



## *Basic Concepts in Drafting Contracts*

### Legal Archaisms

☹️ WITNESSETH:

☹️ W I T N E S S E T H:

☺️ W I T N E S S E T H:

## *Basic Concepts in Drafting Contracts*

### Summary

- Language matters.
- The law matters, too. But that's a story for another day...
- Understand the concept, then put it in words – this is often easier said than done!
- Separate out the function of each provision or clause (e.g., language of performance, language of obligation, language of declaration, etc.).
- Taking time to develop good drafting habits now will make you a much more effective drafter when time is of the essence.
- Read what you draft to see if it makes sense. If not, fix the problem/cure the ambiguity.

*Basic Concepts in Drafting Contracts*

The End > [This is the end of the presentation. Any questions? Please feel free to ask me now, as I'm packing up, or via email or a phone call.](#)

# Questions?



**Vincent R. Martorana** is Counsel in the Corporate & Securities Group with Reed Smith's New York office. His practice includes the representation of clients in domestic and cross-border mergers, stock and asset acquisitions and divestitures, joint ventures, strategic alliances, licensing arrangements, corporate restructurings, private equity investments, and securities offerings. He also regularly provides advice on corporate governance and state laws governing business entities (including Delaware and New York corporate, partnership, and limited liability company law). Vincent has represented a wide range of clients—from start-up and early-stage companies to well-established enterprises—in various industries, including technology, healthcare, pharmaceutical products, and consumer products.

Vincent has extensive experience providing advice on contract drafting, analysis, and interpretation relating to disputes, settlements, and negotiated transactions. He has presented his continuing legal education contract-drafting courses for in-house legal departments and at various other venues, including Practising Law Institute, Strafford Webinars, The Business Development Academy, the National Academy of Continuing Legal Education, the American Bar Association, the New York State Bar Association, the New York City Bar Association, the New York County Lawyers Association, the Brooklyn Bar Association, the Suffolk County Bar Association, and the Westchester County Bar Association.

He is also the author of *Drafting Points* ([www.draftingpoints.com](http://www.draftingpoints.com)), a blog that is dedicated to contract-drafting issues, and is the author of the Reed Smith white paper, *A Guide to Contract Interpretation* (July 2014).

Vincent received a J.D. from the University of Chicago Law School and a B.S. in Economics (with concentrations in Finance and Operations & Information Management), *magna cum laude*, from the Wharton School at the University of Pennsylvania.




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*Fin!*