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Boilerplate Blunders: 12 Mistakes to Avoid When Drafting Commercial Contracts

Commercial and Contracts


CONTRACT

CHEAT SHEET

- ***Boilerplate.*** Boilerplate provisions can have a meaningful impact on the enforceability of commercial contracts, determining whether your clients will receive their wanted benefits.
- ***Create your own.*** Take inventory of what the company contract needs are and develop a set of boilerplates that can easily replace sections or be added in a contract.
- ***Check.*** Create boilerplate checklists that can be used to mark up provisions during a time crunch.
- ***Back-up plan.*** If you are unable to make edits or wholesale changes of certain provisions, impress upon your clients the significance of conceding on these points.

Other than unannounced on-site regulatory visits, there are very few things that can derail an otherwise good day more than a material ambiguity or inconsistency in a commercial contract coming to light as a result of a contractual dispute. Sales, supply, and license agreements memorialize a company's most vital nonemployee relationships. A dispute with a counterparty about the meaning or implications of a key provision can result in wasted resources (time and money) and jeopardize the stability of critical business relationships that have been years in the making. Accordingly, it is

important for counsel and business partners to avoid costly drafting errors (or omissions) in material commercial contracts.

In the increasingly complex and fast-paced nature of business, general counsel and external counsel both suffer at the hands of the same nemesis — time. There is never enough of it. Technology allows lawyers to work more efficiently; however, client demands have outpaced the time savings leaving little time or attention for attorneys to devote to important matters while putting out fires on more pressing matters. Attention to “standard” boilerplate provisions are among the first casualties when counsel are under the gun. Boilerplate provisions are often relegated to the “miscellaneous” section at the very end of contracts with little fanfare, despite the surprisingly significant impact that these provisions can have on the respective rights of the parties and the logistics of enforcing those rights. The traps for the unwary are many; however, the following 12 tips can significantly decrease the risk associated with drafting boilerplate provisions in commercial contracts. In all cases, it is important to take inventory of what the company’s needs are and then develop a set of boilerplate provisions that will be easily accessible for counsel to add to, or replace, in a contract with little notice.

1. Incorporation by reference

Many agreements incorporate other terms and conditions by reference. Sometimes these terms and conditions are attached as an exhibit or appendix, but you may also see terms and conditions applicable to one party that may only be available online or separately documented within vendor guidelines. It is important both to read and understand the substance of these provisions and also have a clear understanding in the contract as to which provisions prevail to the extent that there are conflicts or inconsistencies among the documents.

Tips

- Completely understand incorporated terms and conditions or exclude such terms.
- Include provisions that clarify the “base” contract prevails (to the extent that there are conflicts).

2. Expenses

Business partners are often frustrated and surprised to learn that the general rule in the United States is that attorneys’ expenses incurred to enforce a contract are not recoverable, in the absence of statutory relief or an express clause to share or shift responsibility for such expenses. If it is important to business team members to shift this burden, then indemnity or prevailing party provisions should be included. If a prevailing party provision is included, then “prevailing party” must be clearly defined. For example, should the burden be split between the parties based on culpability, or is a favorable disposition on a majority of claims sufficient to shift the entire burden for fees to the loser? Does the disposition need to be final and non-appealable? Do the expenses need to be “reasonable”? Should the loser pay for torts (e.g., fraud) in addition to contractual claims? Note that in some states, such as Florida, Texas, and California, attorneys’ fees provisions are required to be interpreted as reciprocal by statute (Fla. Stat. Ann. §57.105; Tex. Rev. Civ. Stat., Art. 38.001; Cal. Civ. Code §1717) but only as to contractual claims.

Tips

- Include loser pays/prevailing party indemnity provisions in contracts where business partners

require such protection.
- Clearly define what it means to prevail and when right to reimbursement is vested.
- Understand local laws that may require reciprocity.

3. Notices

It is important to identify how, when, where, to whom, and what type of communication must be delivered in the manner described. Often the effective date of notice determines when a breach has occurred, the time period that one party has to cure a breach, and the consequence of a breach (e.g., termination rights, interest, or liquidated damages). Ambiguity or logistical constraints within these sections may delay or frustrate the intention of the parties. For example, if email is a permissible means of providing notice, what happens if email is diverted by a spam filter? Should notice of certain significant events require more formal notice? What happens if the designated contact person ceases to be employed by the receiving company? If one party fails to provide notice of a change of address, should there be a consequence to such party? Should there by different delivery methods for non-US parties? Many agreements permit service of process to be delivered in the means described in the notices section. If notice delivery methods will also apply for service of process, then it is even more important that such methods mechanically work.

Tips

- Include multiple means of delivering notice (e.g., national courier and email with confirmation of receipt).
- Consider including multiple recipients of notices to increase likelihood of receipt.
- Consider limiting proper notice to personal delivery or national courier service if service of process may be made by the method indicated in the notices provisions of the contract.

4. Interpretation

Often, agreements may include language that informs how the contract is to be construed. As is the case with all boilerplate, if a provision introduces ambiguity to the agreement, then the language should be excluded. For example, a contract may say that all references to other contracts or statutes are deemed to be such contracts or statutes as modified from time to time. This may be appropriate in some instances but depending upon how and when such other contracts can be modified, such modifications may materially amend the terms of the primary contract in unknown or unknowable ways. If the agreement is being translated into multiple languages, which version governs in the event of a translating inconsistency? Clarifying the intention of the parties in this situation is important.

Tips

- Avoid general interpretation principles that add ambiguity.
- If contracts are translated and presented side-by-side versions in two languages, then include a clause that specifies which version prevails if there are translation-related inconsistencies between the versions.

5. Entire agreement (merger clause)

A well-crafted merger clause should clearly affirm that the contract supersedes all memoranda of

understanding, term sheets, and letters of intent, as well as any prior oral discussions and emails. However, if the parties have other agreements that could reasonably be construed to relate to the same subject matter and are not intended to be superseded, then the other related agreements (e.g., guarantees, collateral documents, side letter, confidentiality agreement, etc.) should be expressly noted as exceptions to the merger clause.

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Tips

- Include merger clause with specific exceptions for other existing and related agreements.

6. Anti-assignment

Generally, contract rights are freely assignable (although certain jurisdictions vary from that rule and certain contracts are not freely assignable, e.g., personal service contracts and exclusive IP licenses). It is therefore prudent to include anti-assignment clauses in most commercial contracts to avoid the risk of being subject to a contract with an undesirable counterparty. For particularly sensitive contracts, counsel may need to consider additional protections to avoid circumvention of the intent of anti-assignment provisions. For example, prohibited assignments may be crafted to include assignments by operation of law, merger, consolidation, or changes of control. Counsel should also consider including provisions that any purported assignment in violation of agreement is null and void to ensure that damages are not the only remedy for breach of anti-assignment provision. Depending upon business needs, certain exceptions to the anti-assignment clause may be necessary, for example, assignment to affiliates.

Tips

- Include an anti-assignment clause with consent required for assignments by operation of law.
- Include language that states assignments without consent are null and void.

7. Third-party beneficiaries

Generally, unless a contract provides otherwise, a third party, despite not having originally been an active party to the contract, may have a right to enforce the contract if they are an intended beneficiary who relies on or assents to the relationship between the original parties to the contract. It is important to remove or tailor such clauses to avoid confusion when an agreement expressly contemplates benefits to third parties, such as indemnity provisions that include shareholders, officers, directors, etc. It is also important to remember that state law may override contractual provisions to the contrary. California has at least one case in which employees that were not party to an agreement were permitted to enforce certain post-closing benefits, despite an express no third-party beneficiary clause.

Tips

- Avoid contradiction of clauses that specify that there are no third-party beneficiaries when the

agreement specifically identifies rights running to third parties, such as officers and directors.
- Understand that local laws may override the express provisions of the agreement.

8. Amendment, modification, or waiver

Purchase orders, emails, and oral communications often deviate from the express terms of master agreements and may create “battle of forms” concerns, parole evidence issues, questions about the course of dealing between the parties, and implied waivers. It is important to require certain formality and specificity (e.g., manually signed written amendments and signature of the person granting the waiver), to avoid inadvertent amendments or waivers. With multiparty agreements, the agreement should specifically address whether all parties need to execute amendments or waivers, or if some subset of parties can authorize such modifications.

Tips

- Include provisions requiring that all amendments and waivers be in writing.
- Specifically identify which parties must authorize specific amendments or waivers of multiparty contracts.

9. Governing law

Governing law provisions are very important but rarely deliberated at length during the preparation and negotiation of contracts. The differences in law among jurisdictions globally are substantial and no 50 US state survey or G7 country survey could ever adequately cover the multitude of statutory differences. Also, case law in many jurisdictions have rendered governing law provisions moot, particularly when a reasonable nexus to the state or other jurisdiction has not been chosen. Many states have enabling statutes that specify criteria for what constitutes sufficient legal nexus for a particular contract to be governed by that state’s laws. Unless there is a strong advantage to utilizing the governing law of a particular jurisdiction (e.g., New York’s long history and legal precedent in the banking and finance industry), the first choice jurisdiction is often the jurisdiction of formation or the headquarters of the company. The company’s formation and/or registration to do business is likely to satisfy the nexus requirement of most states and the company should hopefully be more familiar with the rules of the road in its home venue. However, governing law may be a negotiated item just like any other term of an agreement, and if the company does not have leverage to push for its preference, then it may have to compromise. Some states have requirements as to the actual text of a governing law clause. For example, Texas requires that a governing law clause be in all caps, bold face, or otherwise conspicuous text. It is also important to include language that states that the choice of law principles from the state are excepted from application of the local law, as this would have the effect of providing a court with the discretion to apply a different jurisdiction’s law.

Tips

- Understand which countries or states have laws that are most favorable and push for the use of such governing law.
- When in doubt, try to push for the jurisdiction of formation or the headquarters of the company to be governing law.
- Use all caps and/or bold face for governing law provisions.
- Include language that makes choice of law principles an exception from the chosen governing law.

- Understand that local laws may override the express provisions of the agreement.

10. Submission to jurisdiction

Similar to governing law provisions, selecting the venue for disputes is also important and may be affected by case law on the appropriateness of the personal and subject matter jurisdiction of the mutually agreed upon court. The expense of litigating a dispute in a distant jurisdiction can increase costs and inconvenience and may mean less familiarity with the court system. It is important that the consent to jurisdiction provision match the governing law provision when possible to avoid court in a jurisdiction that does not give effect to enabling statute provision from the selected jurisdiction. Parties should include language that explicitly waives forum non conveniens and other potential defenses or objections to the selected jurisdiction. It is also recommended that language is included that permits service of process in the manner described in the notices section, especially when a counterparty is based outside of the jurisdiction. Certain courts may have specific prerequisites, such as dollar amount prerequisites or, for US federal courts, either diversity or subject matter jurisdiction that override the express terms of the agreement. Finally, if exclusive jurisdiction is intended, the contract should expressly so state, with the understanding that courts may not ultimately enforce such exclusive jurisdiction consent.

Tips

- When possible, push for an exclusive forum that is convenient for the company.
- Include explicit waivers of challenges to the selected forum.
- Include language allowing service of process in the manner described for notices.
- Understand that local laws may override the express provisions of the agreement.

11. Waiver of jury trial

Waiver of jury trials is particularly important for agreements dealing with complicated subjects or contracts where juries may be more likely to sympathize with one party or another, irrespective of whether the contract is clear on particular terms. As is the case with many boilerplate provisions, it is important to understand whether jury trial waivers are effective in the jurisdiction whose laws govern (or whose laws may apply because of a public policy exception). In many jurisdictions, there is a presumption against waiving the right to a jury trial. In all jurisdictions, the waiver must be knowing, intentional, and voluntary. In a few jurisdictions, such as Georgia, waivers of jury trials are not permitted at all.

Tips

- Include explicit waiver of jury trials for complex contracts.
- Understand that local laws may override the express provisions of the agreement.

12. Arbitration

Arbitration of disputes can dramatically expedite and decrease the costs of dispute resolution. It is important that arbitration clauses are crystal clear on the specifics of the arbitration — who, what, where, how, and when. The agreement should clearly specify how many arbitrators there will be and how the arbitrators will be selected. In most cases, it is simplest to have one arbitrator selected by a reputable arbitration organization, such as the American Arbitration Association (AAA). The contract

should specify what procedures govern arbitration proceedings. Again, AAA procedures may be a natural choice. Most importantly, the arbitration clause must state that the arbitration will be binding on the parties. The contract should identify the location of the proceedings and how the process will be initiated. Finally, the contract should state how the expenses of the arbitration will be allocated between the parties.

Tips

- Include details on the specifics of the arbitration and the procedures to be applied.
- State that the arbitration is binding.
- Describe how arbitration expenses will be paid.

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Conclusion

Boilerplate provisions can have a meaningful impact on the enforceability of commercial contracts and determine whether or not your clients reap the benefits that they have so valiantly negotiated for. As the expert, take inventory of what the company's needs are for contracts in various aspects of the company's business and then develop a set of boilerplate for the various applications that will be easily accessible to add to, or replace, in a contract with little notice. It is also a good idea to develop boilerplate checklists that paralegals can use (with attorney supervision) to mark up provisions when one is under a time crunch. When circumstances dictate that you are unable to make edits or wholesale changes of certain provisions, make sure that your clients understand the importance of conceding on these points.

ACC EXTRAS ON… Commercial contracts

ACC Docket

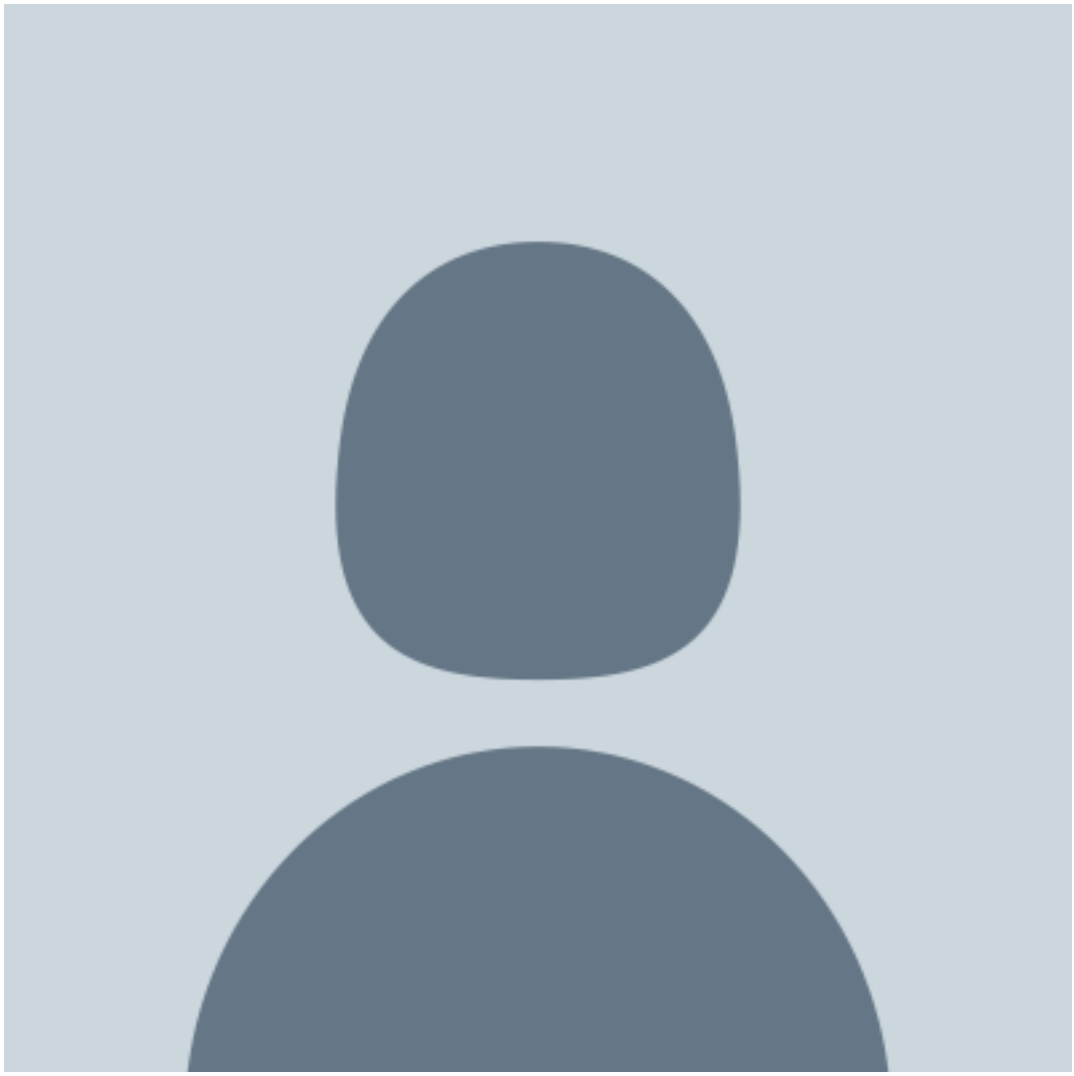
Contracts Unleashed (June 2019).

Deploying Robust Default Rules: International Commercial Contracts Under UNIDROIT (March 2019).

Are You Quantifying Your Risks in Contracts? (Oct. 2018).

Traps, Pitfalls, and "Gotcha" Moments to Avoid with Business Contracts (Oct. 2017).

Richelle E. Burr



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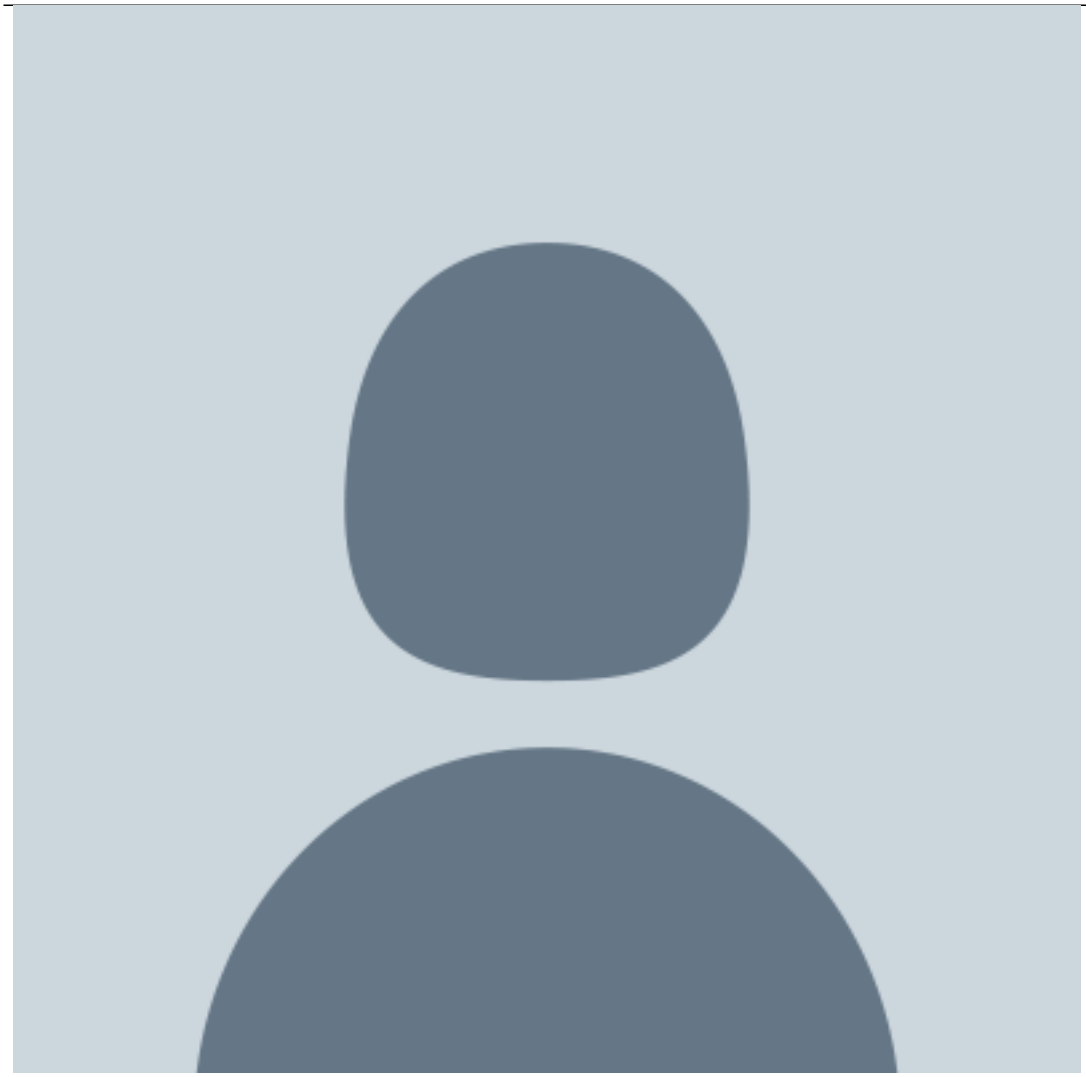

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