

TIPS FOR DRAFTING A COMMERCIAL AGREEMENT (AND WHEN TO USE A LAWYER)

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If you work for a manufacturer or retailer and are involved in handling negotiations with a supplier or customer, it is likely that sooner or later you will have to take responsibility for drafting a contract to memorialize the deal. Here are some tips for how to approach that process and on whether (and when) to involve an attorney.

Outline the Deal

Begin by preparing a list of the most important substantive provisions that need to be in the contract. Start with listing the most important things you want from the deal, i.e. the fundamentals of what you have bargained for. This might include key dates by which things must be done, quantities that need to be delivered, important pricing issues, and pre-conditions that need to be met for the deal to go through. It is important to do this task first so that you have firmly in mind all of the important provisions that you want to see in the contract. Next, revise the list to include everything the other side wanted and that you agreed to. One of the advantages of being in control of the drafting process is that you can frame the agreement and are best positioned to have the terms read the way you want. Following these steps is the best way to use your role as drafter to your best advantage.

Use Clear, Ordinary Words, not Legal Jargon

You are now ready to begin the drafting process. By all means, use a “model” contract from another deal to assist you, but make sure you don’t follow it slavishly. Many of the provisions in another contract may be completely irrelevant to the contract you are drafting. If you do use a “model” make sure it was prepared or reviewed by an experienced contract attorney. Don’t try to use legal-sounding terms for the sake of it. A good contract should be written using clear, ordinary words.

Parties and Definitions

Begin by reciting the parties to the agreement and the date of execution. This should go in the first paragraph. When you describe the other party to the deal, make sure this is the entity you want to be bound by the agreement. If it’s a subsidiary, for example, make sure it has assets and can be held to performance of the obligation. Find out now. Make sure the signature lines that will appear at the end of the agreement match the parties you have described here at the beginning. After this description of the parties, you should leave a space for a definitions section where important terms will be defined (this will be filled in later).

The Substance of the Deal

Next comes the substance (or subject matter) of the transaction. You should be careful to address each of the following issues, where applicable:

- 1) Accurately describe what is being sold (this may be either simple or complicated, depending on the nature of the item. For example, if the contract is for goods that are to be manufactured, the contract would at least include product specifications and perhaps even a description of required testing procedures or protocol);
- 2) Describe the price and how and when it is to be paid;
- 3) Describe the delivery date and the required method of delivery;
- 4) If the agreement contemplates an ongoing relationship between the parties, you should include a provision describing the expected term of the agreement and whether it will renew automatically or on some other basis.

Here, a simple, but often overlooked rule needs to be emphasized – leave nothing out. Article 2 of the Uniform Commercial Code requires that a quantity of goods be described in writing. If it is not, the contract may fail for lack of certainty. And (at least in most states) the Statute of Frauds declares void any agreement that cannot be performed within one year unless it is in writing. The lesson from this is clear – do not rely on unwritten promises: when a deal goes bad, a handshake is as good as the paper it was written on.

Protective Provisions

Next, you should include a series of terms that protect you in case the other side does not meet its obligations, and one that limits the damages against you if you are unable to meet yours. You may need legal advice to know which clauses to include and you should always have them reviewed by counsel before the agreement is signed. How and when to seek legal advice is discussed below. These provisions should include:

- 1) Appropriate representations and warranties. What is ‘appropriate’ will depend on the nature of the contract. Likewise, disclaimers of warranties and the impact of any statute of limitations on different types of warranties must be considered. On these important subjects you need expert legal advice;
- 2) Provisions for indemnification and insurance. Both are important – make sure the seller provides you with a certificate of insurance covering your company and insist on seeing the policy to ensure there is no deductible;
- 3) Where appropriate, consider using liquidated-damages and cancellation clauses. The Massachusetts Supreme Judicial Court has recently affirmed its approval of the practice of including a liquidated-damages provision, so long as the figure is not disproportionate to anticipated damages. If the contract is a requirements contract (typically executed in the form of

or in conjunction with a purchase order) a buyer should make sure there is a cancellation clause which limits the seller to recovery of specified costs on product actually ordered;

4) A termination clause. If the agreement is for a defined term, consider the need for a termination provision describing the circumstances in which either party can terminate the agreement before its natural end date.

Add Definitions of Ambiguous or Complex Terms

Read over the contract and decide whether any of the terms are unclear or ambiguous. If they are, add a definition of all such terms near the beginning of the contract. Technical terms and terms of art are prime candidates for inclusion in the definition section.

Make Sure the Agreement is to be Signed by an Authorized Person

Add a signature line for the individuals who are to sign the contract and make sure that those persons are authorized to sign on behalf of their companies.

Obtaining Legal Advice.

Other than for the most basic contracts, you should attempt to have every contract reviewed by a lawyer experienced in the drafting and interpretation of different types of contracts. Bear in mind that it is always better to incur the small expense of having the contract reviewed by an attorney before it is signed than to suffer the damage to your business that can be caused by a costly drafting mistake or by ending up in a lawsuit because the agreement was flawed.

When should this be done? If a deal is complex, you should try to consult with an attorney at the start. It's often important to be aware of unusual legal issues that may apply to the subject matter – and impact what you would agree to –before negotiations even begin. Contracts affecting employment, for example, nearly always need expert legal advice from the start. Usually, however, it is sufficient –and much less costly – to present a draft agreement to counsel for his review before sending it in on to the other side. If the above steps have been followed, the legal review process can itself take place more efficiently than if the attorney is asked to draft the agreement from scratch.

Finally, make sure that after the contract is signed, it is appropriately filed in a designated location where all the company's agreements are maintained and can be subjected to a regular review process.

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