



**DEAL
STRUCK**

THE WORLD'S BEST
DRAFTING TIPS

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Contents

About Ross Guberman	3
About Gary Karl	5
INTRODUCTION	10
THE BIG PICTURE	13
The Heart of the Deal	14
The Core Four	15
THE HEART OF THE AGREEMENT	16
Shall We? Affirmative and Negative Obligations	17
Will Power: When "Will" Will Do Just Fine	19
Within My Rights: May I?	20
Escape Hatches and Bated Breath: Conditions	21
THE STATE OF THE WORLD	24
"I Solemnly Swear": Representations and Warranties	25
Spill the Beans: Exceptions to Representations and Warranties	28
Risky Schemes: Mitigating Against Misrepresentations	30

CLEAN-UP	31
Who Cares? Materiality, Material Adverse Change, Material Adverse Effect	32
What Did You Know and When Did You Know It? Knowledge Qualifications	34
Fix-It Man: Remedies for Misrepresentations, Breaches, and Failures to Perform	36
No Harm, No Foul? Types of Remedies	38
Not My Problem: Indemnification	39
DRAFTING TIPS AND TRAPS	41
Try as I Might: Efforts and Endeavors Clauses	42
Pick Your Poison: And, Or, And /Or	44
On Second Thought: Provisos and Exceptions	45
Once Upon a Time: When?	47
Fear of Math: How Much?	48
Pointing Fingers: Cross-Referencing	49
FRONT AND BACK	50
Navel Gazing: Recitals	51
"I Declare": Defining Terms	52
Who Goes There? Naming Names	54
Have We Met? Where to Put Definitions	55
BOILERPLATE PROVISIONS	56
Assignment and Delegation	57
Successors and Assigns	58
Governing Law / Choice of Law	59
Waiver of Jury Trial	60

Escape Hatches and Bated Breath: Conditions

Catchy titles track key business challenges

Conditions reflect what must, or must not, happen before a party is obligated to perform some or all of its obligations under a contract. A condition might be an action that a party is obligated to take, a state of facts that must exist, or an event that's outside a party's control.

Take, for example, a contract for the purchase and sale of a home. The contract typically lists some routine conditions: the buyer need not pay the purchase price unless the seller executes and delivers an acceptable deed; the seller, for its part, need not transfer title unless the buyer pays the purchase price. The conditions thus outline what will happen at the closing.

Conversational tone and inviting formatting

But the buyer's obligation to close might also be subject to another obligation on the seller's part (such as to repair or replace a broken door), to facts that must exist (clear title, for example), or to an event that must occur (say, the lenders must give the buyer a mortgage, or the closing must occur on or before a "drop-dead date").

If any of these conditions isn't met, then the buyer need not complete the purchase. And the buyer suddenly gains some new options:

Waive the condition and close the deal anyway;

Wait to see if the condition can be satisfied later;

Transform the condition to closing into a post-closing covenant to be performed by the seller;

Renegotiate the deal on presumably more favorable terms.

Practical context for drafting choices

Conditions can thus create an “out” or an “escape hatch” from obligations that a party would otherwise have to perform.

Because a condition is an all-or-nothing proposition—for example, failure of a closing condition can torpedo the deal—courts are reluctant to find that a contract term is a condition. Instead, courts prefer to construe a supposed condition as an obligation and then remedy the breach by awarding damages rather than terminating the contract altogether.

Follow these steps if you want to draft a condition:

● When you express conditions, be as specific as possible about what must happen.

● Use **subject to, unless, on the condition that, if, or only if** to distinguish conditions from obligations.

■ Avoid **shall** for conditions.

Clear examples
both good and bad

■ Avoid using **provided that** or other provisos to express conditions.

Example: The Seller shall deliver the goods to the Buyer only if the Buyer has paid the purchase price.

A novel green-yellow-red color scheme

Example: The Seller's obligation to close is conditioned on Buyer's obtaining a novel green-yellow-red color scheme for the purchase price."

Use **subject to, unless, on the condition that, if, or only if** to distinguish conditions from obligations.

- *In the event* and *in the event that* are wordy but not incorrect.
- *In the event of* is appropriate before a noun, as in “In the event of default.”

Avoid *shall* for conditions. Reserve *shall* for covenants (what the party has a duty to do). (See *Shall We?*) In fact, using *shall* to express a condition might suggest an obligation.

- CONDITION OR OBLIGATION?: Jones *shall* submit any dispute notice within 30 days after receipt of the working-capital calculation, or he shall be deemed to have accepted the calculation.
- CONDITION: *Unless* Jones submits a dispute notice within 30 days after the date Smith delivers the working-capital calculation, Jones will be deemed to have accepted the calculation.

Avoid using *provided that* or other provisos to express conditions, because provisos can be read to suggest an obligation instead. (See *On Second Thought*.)

- CLEAR: Jones may submit a dispute notice only within 30 days after receipt of the working-capital calculation, after which date

● Consider whether any party is subject to special requirements before it is eligible to perform its obligations under the contract.

Substantive advice that goes beyond language

● For individuals, draft reps that attest to their legal capacity.

- Can make and perform the contract without conflicting with any of the following:

Its governing documents,

Its other existing contracts,

Applicable law, and

Applicable judgments and orders

- Has duly executed and delivered a contract that is enforceable against that entity.

Is any party subject to special requirements before it is eligible to perform its obligations under the contract? Consider such requirements as these:

- Financial condition /creditworthiness
- Regulatory status, especially for regulated industries requiring licenses like the following:

Insurance

Banking

Financial advisory and management

Health care

Telecommunications

Public utilities

The professions (law, medicine, accounting, engineering, architecture)

- Any other regulatory status essential to the transaction:

Accredited investor status under securities laws

Prohibited transaction status under ERISA

Are any of the parties individuals? If so, draft reps clarifying that the party has the legal capacity to enter into the agreement and to consummate the transaction either as an individual or as an agent.

No Harm, No Foul?

Types of Remedies

Below are some of the most common contractual remedies:³

REMEDY	PURPOSE	WHEN APPROPRIATE	WHEN NOT
<i>Termination</i>	Relieves the parties of their obligations for continued performance	When the parties have not yet substantially performed	Once substantial performance of obligations has been rendered
<i>Acceleration</i>	Allows the lender to demand that the borrower repay the entire balance	Debt financings	Any transaction other than a debt financing
<i>Indemnification</i>	Requires the breaching party to pay costs, damages, and losses that the other party incurred because of the misrepresentation or breach (often subject to caps)	Almost always, but particularly in private acquisitions	By convention, in public company mergers
<i>Liquidated damages</i>	Requires the payment of a specified amount upon the occurrence of events such as these: <ul style="list-style-type: none"> • <i>Severance payment under an employment contract made to an employee terminated without cause</i> • <i>Increase in borrower's interest rates if its credit rating is downgraded</i> • <i>Pre-payment penalties and other make-whole provisions in a loan agreement</i> 	When actual damages would be difficult to compute, so liquidated damages would be a good-faith proxy	Whenever actual damages would be reasonably easy to compute

Tables condense what other books discuss for 50 pages

Key cases cited for reference

³ Many contracts also provide for injunctive relief or specific performance. Some courts will enforce these provisions, particularly, but not exclusively, in real estate transactions. See, e.g., *In re IBP, Inc. Shareholders Litig.*, 789 A.2d 14 (Del. Ch. 2001). But because injunctive relief and specific performance are equitable remedies, these provisions do not necessarily bind the court. Be sure to research the law of the jurisdiction governing the agreement.

Mandatory Arbitration Clause

Issues to consider addressing:

- What disputes are subject to arbitration?
- Is the award subject to judicial review, or is it a binding decision subject only to judicial enforcement?
- Which arbitral association will be used?
- Who pays for the arbitration? Both parties, or just the prevailing party?
- What law governs?
- How will the panel be composed and selected?
- Where will the arbitration take place?
- In international arbitrations, in what language will the arbitration be conducted?
- Will discovery be limited? (This issue is especially important in the US, which allows for exceptionally broad discovery, including e-discovery, in commercial litigation.)
- Does the award/decision/judgment need to be “reasoned”—that is, supported with a written explanation?

▲ Consider addressing these often-overlooked issues related to **arbitration**.

Checklists help even the most seasoned drafters

Authoritative models

● Consider these model arbitration clauses from the ICC and the AAA.

Arbitral associations provide sample mandatory-arbitration provisions that track the case law of the jurisdiction.

EXAMPLE FROM THE INTERNATIONAL CHAMBER OF COMMERCE:

“All disputes arising out of or in connection with the present contract shall be finally settled under the Rules of Arbitration

▲ Be sure to research important distinctions in your jurisdiction. US and UK courts often interpret arbitration clauses differently, for example.

of the International Chamber of Commerce by one or more arbitrators appointed in accordance with the said Rules.”

EXAMPLE FROM THE AMERICAN ARBITRATION ASSOCIATION: “Any controversy or claim arising out of or relating to this contract, or the breach thereof, shall be settled by arbitration administered by the American Arbitration Association under its Commercial Arbitration Rules, and judgment on the award rendered by the arbitrator(s) may be entered in any court having jurisdiction thereof.”

As for what disputes are subject to arbitration, be sure to research important distinctions in your jurisdiction between “arising out of,” “related to,” “related in any way to,” “in connection with,” “under,” “in respect of” (UK), and “with regards to” (UK) the agreement.

In the United States, for example, the broadest scope is through a “broad-form clause”: “all disputes arising out of, connected with, or relating in any way to this Agreement.”

UK courts make fine distinctions as well, holding, for example, that “in respect of” is far broader than “in connection with.”

Key jurisdictional
differences highlighted

Index

A

AAA model mandatory-arbitration provision 68
acceleration of payments as remedy 38
according to 71, 72
acronyms 54
although vs. while 47
amendments only in writing 63
and 44
and/or 44
anti-assignment 57
anti-delegation 57
arising out of 68
assignment and delegation 57
assignments
 definition of 57
assure 70
attorneys' fees 70
attorneys' fees as indemnity 39

B

because vs. since 47
best efforts (best endeavors) 42, 43
between [the parties] vs. among [the parties] 70
breach (failure to perform)
 remedies for 15, 36, 38, 39

broad-form mandatory-arbitration clause 68
by and [between or among] 70
by (for time) 47

C

cannot 18
choice of law 40, 59
 and conflict-of-law principles 59
 and exclusive-remedy provision 40
concurrently 47
conditions 15, 21, 22, 23, 37
 consequences of unsatisfied 21, 22, 37
 enforceability of 23
 vs. provisos 45
conflict-of-law principles
 excluding from choice-of-law provisions 59
consequences
 drafting 37
 of conditions 21
 of future events and circumstances 19
contract automation 80
could result in 33
counterparts 65
cross-referencing 49

D

damages
 and indemnity 39
 for misrepresentation 30
liquidated 38

days' notice 70

default 30
remedies for 30

defining terms
choosing 54
embedding terms within 52
nested definitions 52
placement of 53, 55

delegation
definition of 57

disclaimer of recourse 40

disclaimer of reliance 40

disclosure schedules 28

drafting process 14, 74, 76

duties
common law 23

E

earlier of vs. earliest of 70

efforts (endeavors) clauses
drafting 42
leading cases on 42

ensure 70

entire-agreement clause 40, 64
and waiver of extra-contractual remedies 40

exception schedules 28

exceptions to representations 28
responding to 29

except that 45

exclusive-remedy provisions 40, 59, 64

extra-contractual remedies 40, 59, 64

F

force majeure 37
remedies for 37

formatting 84

formulas 48
vs. words 48

forthwith 47

from ... through (for time) 47

from ... to (for time) 47

G

Golden Rule of Drafting 17, 19

governing law 59

greater of vs. greatest of 70

H

hereby 40
and indemnity 40

hereinafter 52, 82

hereunder 49

I

ICC model mandatory-arbitration provision 67, 68

if and only if 22, 82
if vs. in the event [that] 22
if vs. to the extent [that] 23

immediately 47

in accordance with 71, 72



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