

Considerations for Drafting Legal Agreements

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At the signing of the Declaration of Independence, Benjamin Franklin was thought to have said: “We must all hang together, or assuredly we shall hang separately.” While most documents attorneys draft do not have the significance of the Declaration of Independence, many attorneys draft, prepare and negotiate legal documents their clients consider essential.

The preparation and creation of legal documents can be an integral part of an attorney's daily activities. Civil litigators routinely draft complaints, pleadings, interrogatories, briefs and motions. Attorneys specializing in trusts and estates draft wills, trust agreements and succession plans. Transactional attorneys draft agreements on all topics involving all subject matters, including employment agreements, purchase agreements, leases, license agreements, shareholder agreements and other organizational documents. Lender's counsel draft loan agreements, security agreements, promissory notes, and numerous other agreements relating to a loan transaction.

Regardless of your area of specialization, in all likelihood, you will be charged with the task of drafting a legal document. With this in mind, this article is a guide for attorneys when drafting any legal document. Since both authors practice primarily transactional law, the article will focus on considerations that should be explored by a transactional attorney.

Background

The ultimate goal of an agreement is to enter into a clear, concise and unambiguous arrangement acceptable to all parties. An executed agreement, once signed, is usually put in a drawer and forgotten about until there is a question regarding a particular aspect of the relationship or, worse, a dispute. Therefore, it is vital that the agreement accurately reflect each party's understanding of the relationship.

It is also imperative that the agreement be drafted in a manner easily understood by third parties having no involve-

ment in, or understanding of, the relationship beyond what is written on the paper. When questions or disputes arise, the businesspeople familiar with the issues may not be those involved with the drafting, negotiating and execution of the underlying agreement, which often occurred months or years before.

Often, the attorneys who are asked by their clients to interpret the agreement and answer questions are not the same attorneys involved in initially drafting the agreement. Should litigation arise, the attorneys charged with litigating the dispute probably had no input in the initial drafting or subsequent interpretation. Consequently, it is essential that whoever reviews the agreement, whenever the situation arises, and whatever the question, can clearly understand it on its face.

The first step in preparing an agreement is to draft an outline setting forth the general topics that must be included within the document. An outline not only assists in organizing the drafter's thoughts, but also will ultimately result in a more concise agreement that flows smoothly.

Consulting a similar agreement drafted previously may be helpful. The use of forms can be an invaluable tool because they save time, and as a result money, since there is no need to begin from scratch. But any reliance on forms should be considered carefully.

An attorney must not force the transaction into an existing form. A form agreement must be viewed as a resource or starting point, to be revised carefully and appropriately to address the transaction and issues at hand. That said, many inexperienced attorneys rely too heavily on a form and are afraid to depart from its language. Remember, the form being relied

upon was used for a specific transaction, most likely with a different set of facts, and possibly prepared by a less experienced attorney.

Drafting

Again, every agreement is unique to the facts of the subject transaction. Yet, the general structure of most agreements is similar. They begin with identifying the parties and the general subject matter, then proceed to the transaction's particular issues, and end with miscellaneous provisions. As an example, consider a general employment agreement to illustrate the various parts.

Opening Paragraph

All agreements should begin by identifying the parties.

THIS EMPLOYMENT AGREEMENT,
dated as of the __ day of ____, 200__
by and between _____
(the "Employer") and _____
(the "Employee").

This is a typical header of an employment agreement, which identifies it as an employment agreement, notes the date upon which it was executed, and identifies all applicable parties. Careful consideration should be given to the applicable parties. Within the global economic structure in which companies operate, it is not unusual for an entity to have numerous subsidiaries and affiliates, both domestic and foreign.

In an employment agreement, it must be clear exactly who the "employer" is, so it is not misstating the employer as an affiliate or a subsidiary of the intended entity. This consideration applies to all transactions. For instance, in the event an entity is selling its business, the correct entity must be identified as the seller.

Recitals or Whereas Provisions

The next provision in an employ-

ment agreement, and most others, is the recitals, sometimes known as the "Whereas" provisions. Whereas provisions are not legally required, but are a useful tool. They provide a basic overview of the content of the agreement. The goal is to set forth, in simple terms, the basic purpose of the agreement, some background information to set the stage, and the nature of the transaction. This gives the reader a basic understanding of the transaction in order to draft the more detailed provisions that follow.

WHEREAS, the Employer is engaged in the business of _____; and
WHEREAS, the Employee has experience as a _____; and
WHEREAS, the Employer desires to employ the Employee and the Employee desires to be employed by the Employer on the terms and conditions hereinafter set forth.

These provisions are not usually part of the legally binding provisions of the agreement (unless incorporated by reference into the body of the agreement). The drafter should attempt to only summarize the overall relationship, rather than include specific deal points. Whereas provisions are only intended to set the stage. The details of the transaction will be set forth in the body of the agreement.

Duties and Obligations

Typically, the first substantive provision in an agreement is the respective duties and obligations of the parties. In an employment agreement, duties and obligations may consist of the following:

Duties: The Employee shall devote his or her full professional time, and attention, and energy as reasonably necessary for him or her to perform all duties assigned or delegated to him or her by the Board of Directors of the

Employer.

The Employee shall devote such time as may be reasonably necessary to cooperate with the efforts of the Board of Directors in the management and governance of the Employer's business. Such duties shall be delegated to the Employee by the Board of Directors from time to time.

The Employee shall have and fulfill the duties assigned to him or her from time to time by the Employer. The Employee shall devote his or her full time and attention to the business of the Employer and shall to the utmost of his or her abilities work for the profit and benefit of the Employer. The Employee shall not, without the express prior written consent of the Employer, render services or otherwise be employed by any person, corporation, partnership, firm or entity other than the Employer. The Employee will not do anything to compete with the Employer's present or contemplated business, nor will he or she plan or organize any competitive business activity. The Employee will not enter into any agreement which conflicts with his or her duties or obligations to the Employer.

Without limiting the generality of the foregoing, the Employee shall have the following specific obligations and _____ duties:
_____.

This is alternate generic language relating to the duties and obligations of an employee in an employment agreement. Whether an employment relationship, a sale of a business, or other transaction, the duties and obligations of each party must be specifically stated.

In an employment relationship, they address specific job functions, time commitment, and location of services, among other things. For a sale of a business, these obligations usually consist of the seller agreeing to sell its business, or a portion of it (perhaps consisting of

specific assets, goodwill, employees and other intangible items), and the buyer agreeing to certain post-closing responsibilities, such as assisting with the collection of the seller's open accounts receivable, among other things. In the case of a lease or license of an item, such as an office, software or other equipment, the lessor agrees to lease the identified items to the lessee, and the lessee agrees to certain use restrictions and obligations. In any event, the agreement should state exactly what is required of each party.

When each party's responsibilities are not clear, a dispute is more likely to arise. The drafter may attempt to prevent this by being overly specific when identifying the responsibilities. Sometimes, certain responsibilities are not known at the time of the drafting, and very broad language is inserted. This can lead to disputes, since one party may believe the other is not honoring the intent of the agreement.

Other times, the agreement calls for specific responsibilities to be determined later. In this case, the subsequent determination must be memorialized in writing. The initial agreement should identify what happens if the parties are unable to agree at that later time.

Financial Considerations

Although it is not unusual for a party to agree to provide goods or services in exchange for another party's goods or services, in most cases one party is providing goods or services in exchange for a payment. For example, in the employment context:

Compensation. For all services rendered under this Employment Agreement, the Employer shall pay the Employee a base salary of equal to \$_____ per annum which shall be paid in installments in accordance with the Employer's payroll practices, subject to applicable withholdings.

In an employment relationship, this provision is clear. It specifies how much the employee is to receive and when it is to be received. Since it is relatively simple, including only a flat salary, in reality there is little ambiguity, resulting in less chance of a conflict.

The same principle applies in the sale of a business or the license or lease of an asset. It is not unusual for a transaction, such as in the case of a sale of a business, to include not only fixed cash payments, but also earn-out payments or other payments tied to the achievement of financial thresholds or a formula. In this situation, it is essential the formula be clearly stated, including who initially proposes the earn-out or other formulaic amount; whether there is a review opportunity and, if so, the terms; and should a dispute arise, whether an accountant or other third party would be the final arbiter. Providing examples is highly recommended, so a complicated formula can be more easily understood.

Termination

Most relationships must eventually come to an end. In the employment realm, certain obvious termination events exist, such as death. There are many other events that could trigger a termination (and all such events may not be applicable in all relationships).

Consider the following:

Termination. This Employment Agreement shall terminate and the Employee shall cease to be an employee of the Employer and all of the rights of the Employee hereunder shall terminate and the obligations of the Employer to make payments hereunder shall immediately cease upon the occurrence of any of the following events:

- (i) By the mutual agreement of the Employee and the Employer.
- (ii) By the death of the Employee.
- (iii) By the Employer or the Employ-

ee on the disability of the Employee as determined by the Employer in accordance with the Employer's policies thereon.

(iv) By the Employee or the Employer on at least _____ () days advance written notice to the other party.

(v) By the Employer, immediately, on the occurrence of "Cause", the existence of which shall be determined in the sole discretion of the Employer which shall include, but not be limited to any of the following:

(A) the Employee's recurring absence, other than for illness or disability; or

(B) the Employee's failure to abide by the terms of this Employment Agreement, after notice and a ten (10) day opportunity to cure to the satisfaction of the Employer; or

(C) the loss of the Employee's license to [insert any required licenses]; or

(D) fraud, theft, dishonesty, embezzlement, misappropriation, or similar actions by the Employee; or

(E) the committing of any act or failure to act where there is a duty to act by the Employee, where such act or omission constitutes an indictable criminal offense; or

(F) the Employee's intoxication while on duty; or

(G) the Employee's illegal use or possession of drugs or intoxicants; or

(H) any other conduct of the Employee which the Employer deems detrimental to its practice or which constitutes cause for termination in the Employer's reasonable discretion, it being impossible to specifically enumerate all events, conduct, and occurrences which would be injurious to the Employer and which would constitute cause.

In essence, these provisions state that the relationship is terminable upon death, disability, without cause upon

appropriate notice, and for cause immediately. A lease and a joint venture relationship also can be terminable. Any type of agreement should clearly enumerate each party's termination rights, if any.

Representations and Warranties

Representations and warranties are the formal description of certain facts or circumstances. Technically, representations are statements of past or existing facts. Warranties are promises existing facts are or will continue to be accurate. For the most part, these terms are used interchangeably.

Representations and warranties are a formal way for one party to learn about the other party before or while entering into an agreement. They are also used in addition to, or in lieu of, other due diligence activities. Further, they provide a basis for a party to seek redress against another party in the event one has breached a representation or warranty (or a representation or warranty is inaccurate).

Due diligence is conducted within an agreement, through the representations and warranties, and outside of the agreement, through the review of a party's documentation and business, as well as by a physical inspection or asking questions. Representations and warranties written in the framework of a definitive agreement may provide an aggrieved party with an easier path to obtaining relief from a breach, as compared to a situation where no written representations and warranties have been given.

Some customary representations in an employment relationship include:

The Employee hereby makes the following representations and warranties to the Employer:

(a) The Employee is under no obligation, restriction or limitation, contractual or otherwise, to any other

individual or entity that would prohibit or impede the Employee from undertaking and performing the duties, responsibilities and obligations under this Employment Agreement, and the Employee is free to enter into and perform the terms and provisions hereof.

(b) The Employee is under no physical or mental disability that would hinder, with or without reasonable accommodations, the Employee's ability to carry out the duties, responsibilities or obligations to be rendered by the Employee under this Agreement.

(c) The Employee is duly licensed as a _____ without restriction or limitation in the State of _____.

In an acquisition of a business or asset, or the lease or license of an asset, as with most other relationships, representations and warranties are appropriate, although they differ from situation to situation. Each party must ask itself what basic assumptions it is making about the other party and the transaction, and whether it is appropriate to seek a representation or warranty from the other party.

Miscellaneous Language

In almost all agreements, the final set of provisions is typically called miscellaneous or boilerplate language. *Black's Law Dictionary* defines boilerplate language as language "used to describe standard language in a legal document which is identical in instruments of a like nature." Many attorneys make a practice of viewing it as standard language, and fail to give boilerplate language the attention it deserves, and in some cases, any attention at all.

Governing Law and Venue. This Agreement shall be governed by and construed in accordance with the domestic laws of the State of New Jersey without giving effect to any choice or

conflict of law provision or rule (whether of the State of New Jersey or any other jurisdiction) that would cause the application of the laws of any jurisdiction other than the State of New Jersey. Each of the parties submits to the jurisdiction of any state or federal court sitting in the State of New Jersey in any action or proceeding arising out of or relating to this Agreement and agrees that all claims in respect of the action or proceeding may be heard and determined in any such court. Each party also agrees not to bring any action or proceeding arising out of or relating to this Agreement in any other court. Each of the parties waives any defense of inconvenient forum to the maintenance of any action or proceeding so brought and waives any bond, surety, or other security that might be required of any other party with respect thereto.

Entire Agreement and Integration. This Agreement contains the entire understanding of the parties hereto. This Agreement supersedes all other prior and contemporaneous agreements and statements on the subject matter contained herein.

Construction. This Agreement shall be construed as a whole, according to its fair meaning, and not in favor of or against any party. The headings of the paragraphs hereof are inserted for convenience only, and do not constitute part of and shall not be used to interpret this Agreement.

Attorneys' Fees. The Employee shall promptly pay (or reimburse, as the Employer may elect) all costs and expenses, including, without limitation, attorneys' fees and court costs and expenses, which the Employer may incur in connection with the enforcement of this Agreement.

Severability. If any term, provision, covenant or condition of this Agreement, or the application thereof to any person, place or circumstance,

shall be held to be invalid, unenforceable or void, the remainder of this Agreement and such term, provision, covenant or condition as applied to other persons, places and circumstances shall remain in full force and effect.

Nonwaiver. The failure of either party, whether purposeful or otherwise, to exercise in any instance any right, power or privilege under this Agreement or under law shall not constitute a waiver of any other right, power or privilege, nor of the same right, power or privilege in any other instance.

Notices. Any notice, request, consent or approval required or permitted to be given under this Agreement or pursuant to law shall be sufficient if it is in writing, and if and when it is hand delivered or sent by regular mail, with postage prepaid, to the Employee's residence (as noted in the Employer's records), or to the Employer's principal office, as the case may be.

At first blush, this seems innocuous. Yet, many issues can arise if not adequately considered.

In the case of modifications to the agreement, where there are multiple parties to an agreement, a modification requiring the agreement of all parties essentially gives any one party a veto right, even if it is not affected by the proposed amendment.

Erroneously providing jurisdiction in a venue where a party has no ties can result in administrative headaches. For instance, a party's attorney may not be licensed in the applicable jurisdiction, requiring them to seek new counsel.

Overlooking or failing to consider appropriate governing laws, can result in a court reviewing a contract, or a provision of the contract, with disfavor, or with an unintended consequence. For example, many jurisdictions are reluctant to enforce a restrictive covenant

upon an employee, and if a party designates this jurisdiction's law as governing, they may have a problem enforcing a restrictive covenant that may be essential to a transaction.

The inclusion of an entire agreement or integration provision, stating the agreement supersedes all other and prior agreements, also may have an unintended consequence. Often, parties have entered into and/or exchanged documentation prior to the execution of the definitive agreement, such as a confidentiality agreement, a statement of work, and the like, which they intend to survive and incorporate into the relationship. However, the integration provision may bar such an incorporation.

Many attorneys merely cut and paste the boilerplate language from a prior agreement, but appropriate time and thought should be spent on the boilerplate language provisions.

Other Considerations

The use of defined terms in an agreement helps avoid needless repetition, and allows more clarity when reviewing an agreement. Ordinary words, used in the agreement in their normal context, need not be defined.

It is beneficial to define terms and phrases that are used uniquely in an agreement. That said, defining a term or phrase that is only used once or relatively infrequently is probably unnecessary. If possible, define the term or phrase by a related commonly used word or phrase. Defining otherwise will only confuse the reader.

Definitions should be written with initial capitalization and placed within the framework of the agreement in a location easily found by the reader. Often, definitions appear in the opening or closing section to an agreement or in an appendix to an agreement. It is not unusual to have all defined terms in one location. For those terms not defined in this location, identify the

cross reference to the applicable section where it is defined. In essence, the goal is to allow the reader to quickly and easily identify a defined term.

Likewise, headings and cross references are useful tools. Legal conclusions should not be interpreted from the heading, but headings should be used to help the reader quickly locate an applicable provision. Without the headings, a simple answer may require a review of the entire document. Cross references allow a reader to easily access the applicable defining provision.

Finally, most attorneys have been involved in late-night and last-minute negotiations, when all parties want to execute an agreement immediately, as soon as some last-minute changes have been made. All attorneys must keep in mind that these last-minute changes are just as significant as the remainder of the document, and should be carefully reviewed in the context of the agreement.

If drafted inaccurately, or if a last-minute change has an unintended impact on another provision in the agreement or on an aspect of the transaction, it will not matter months or years from execution that all parties requested the revisions be made in haste so the agreement could be executed. Do not rush the final last-minute issues.

Conclusion

The goal of every scrivener should be to create a clear, unambiguous and concise agreement that reflects the understanding of the parties. Take your time, be careful and thoughtful, and the result will be a clearly defined, binding contract. ☺

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