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PREFACE

Whenever a businessman signs a commercial contract, he does so with the prospect of doing business. To him a good contract will lead to high profits; a poor contract will lead to the opposite, perhaps even a loss.

This little booklet is not a guide to profitable contracts.

In this booklet a contract will be considered good if it provides you with a clear and concise understanding of your rights and duties. Such a contract will allow you to concentrate on your business rather than on cunning and shifty interpretations.

This booklet will focus on some simple instruments to be considered in connection with contract drafting with a view to minimising the occurrence of misinterpretations.

As long as both parties agree on a mutual understanding, actions before the courts are seldom necessary. The risk to which you expose yourself by leaving the interpretation to the court is excellently described by the judge himself in The High Court of Justice, Queen's Bench Division, in case 1996 G 227, 6th March 1996: "... with the best will in the world, even the most experienced Counsel cannot always forecast the likely outcome of ... proceedings before a Judge in Chambers."

We hope that you will find your future contract drafting to be an intellectual challenge.

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OBJECTIVE AND STRATEGY

The fundamental rule behind the negotiation of any commercial contract is to work out your objective. Make it clear to yourself what you want to achieve as a party to the contract.

Since commercial contracts frequently contain several elements, it is essential for a potential contractor to evaluate in his own mind which points are vital and which points are negotiable.

One mistake frequently made is for one party to leave vital requirements unclear, either as a result of incompetence, or as a result of a desire not to flag to the other party just how vital these requirements are. Many contracting parties simply hope that it will be all right on the night and do not insist on an unequivocal wording.

Make all clauses subject to close scrutiny while making your own personal analysis. Decide for yourself if and to what extent you are really prepared to accept the consequences.

The negotiation of commercial contracts is in itself a matter of buying and selling, and of course you are willing to accept certain commercial risks; - if not, you would not be a businessman. However, if you know which elements of the contract you consider to be of cardinal importance to you and your company, you should emphasise this from the very beginning of the negotiation in order to give your business partner a clear picture. This will spare you future problems and you will avoid remarks such as *"Why didn't you say so in the first place?"*

Key Notes:

- Announce to your counterpart all elements of the contract which you consider to be of cardinal importance.
- Consider the foreseeable consequences.
- Trade off advantages and disadvantages.

YOU ARE LAYING DOWN THE RULES

When drafting a commercial contract the rules governing the relationship between you and your counterpart will be your own responsibility.

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While laying down the rules you should not be superficial. Consider the making of the rules an intellectual challenge.

The contract is the set of rules that stipulates the rights and obligations of both parties. If and when the parties are in doubt as to the interpretation of the contract, the question will be left with the courts to solve. The courts constitute an independent body in society and provide rulings on the interpretation of the law.

The courts will consider a number of elements before reaching a judgement, but above all, the contract itself will be of importance. Consequently, the parties to a contract should never rely on implicit understandings, no matter how clear and obvious they may seem to the parties.

Implicit understandings are not always obvious to judges of the courts. What seems natural to the parties at the time of signing the contract may not be so obvious later on.

Key Notes:

- When in doubt, include rather than exclude.
- Make sure that an outsider, even a stiff-legged old judge, will have a full understanding of the contract just by reading it.

ALL CONTRACTS COME TO AN END

One day all contracts come to an end. It may appear to be an unsophisticated statement, but often businessmen seem to forget that even contracts pertaining to continuing relationships will inevitably come to an end.

Although commercial contracts contain several elements concerning rights and obligations, the contract itself is rarely used as a tool for solving problems arising from day-to-day business. Generally, parties to a contract solve their day-to-day problems without consulting the contract.

The document is left in the drawer, either until the contract is breached or until it is terminated.

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You have no way of knowing if the other party to the contract is likely to be in breach sometime in the future, nor when or how. But it is essential to realise that eventually the contract will expire for whatever reason. Therefore, you should always be thinking in terms of "when" and not "if" with regard to the expiry and the consequences thereof. Some day, The Time Will Come. And when that happens, it will be too late to regret any superficiality which might have been displayed when the contract was signed.

The advice is that you should insist on having included in the contract the terms setting up the conditions when the contract expires. Preferably, in order to avoid being caught by surprise, you should know the rules of the game from day one.

Key Notes:

- Do not get caught by surprise; always remember that some day every contract comes to an end.
- Clear and concise regulation of rights and obligations when the contract is terminated may save you from being the party to a costly law suit.

THE "NACHFRIST" NOTICE

Most common law lawyers are unfamiliar with this term. The Nachfrist Model is rooted in German, Austrian and Swiss Law. These regimes influenced the UN Vienna Convention 1980 on Contracts for International Sales of Goods (CISG), Art. 47, under which a party may fix an additional period of time of reasonable length for the performance by the other party of his obligations when this other party is in breach.

In general, the parties to a commercial contract have no intention of deliberately seeking disputes and court litigation. In particular this is true at the time of signing.

One method which might be employed with a view to reducing the number of commercial disputes is the so-called "Nachfrist " model. Where applied, this model imposes upon each party to the contract the obligation of giving notice in cases where the other party is in breach provided, however, that such breach is remediable.

To give an idea you should take a look at this example:

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This contract may be terminated by either party immediately upon written notice

(i) if the other party should become insolvent or start negotiations with its creditors or a petition in bankruptcy should be filed by or against it or it makes an assignment for the benefit of its creditors;

or

(ii) if the other party should fail to fulfil any of its obligations under this contract and *if such failure is not remedied within thirty (30) days from the date of receipt of a request for such remedial action from the first party.*

As one can see, the draftsman made a distinction between breach of contract that cannot be remedied (i) and breach that might be repairable (ii).

Key Note:

- Most businessmen prefer to do business by doing business rather than by litigation. A "Nachfrist" clause could be the means by which to avoid legal action.

FOREIGNERS HAVE DIFFERENT HABITS & LIVE IN FOREIGN JURISDICTIONS

Foreigners are strangers and they may appear also to be strange. Foreigners live in another culture; they have different habits; they may also have different business practices and often also expectations that vary from your own.

To make a successful commercial contract between enterprises in two different countries both parties are required to pay attention to the particular needs and expectations of the other party. This is not only a question of appreciating the other party and his peculiarities. It is just as much a question of providing information, on your own part, to the other party in order to make him understand your expectations, even if they might seem evident to you.

By the way ! Who is your business partner ? You got his business-card, but is he representing a limited liability company? Is he working on his own as an independent businessman? Is he and his company a fake? Believe it or not, in legal practise it is not uncommon – at a later stage - to realize that this so-called “company” never existed. Always ask for documentation. If you think it is impolite to question the honesty of your future business-partner, blame it on your accountant who need official proof of the VAT number.

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Key Notes:

- Get to know your business partner, and make sure that he gets to know you (and your peculiarities).
- Ask yourself: Why does he want to do business with me?
- Tell him why you want to do business with him.
- Write it all down in the contract.
- Check the legal identity of your foreign partner.

CONSIDERATION

As a party to a commercial contract you will be likely to concentrate on the strengthening of your rights against the other party and at the same time imposing a maximum of obligations on the said party. Forget it; even if you are the stronger party, which “allows” you to dictate the commercial conditions.

By exaggerating your own strong contractual position when drafting and signing the contract, you are running a potential risk that the courts will refute the contract partly or in full.

In “one-sided” contracts the so-called waiver-clause is often found. You should not rely completely upon the validity of such clauses; especially if and when the day-to-day business practise proves to be exercised completely differently from the procedures prescribed for in the contract.

If and when you are a stronger party, you should consider why the other party still wants to do business with you. Certainly you will have an idea of this. These reasons should be part of the contract in order to explain - also to the judge - why both parties accepted the contract and especially what opportunities it contained for the other party.

Key Note:

- A commercial contract always describes an exchange of rights and duties. Make sure that the descriptions in the contract are balanced in the sense that obligations imposed on one party match the consideration.

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LONG TERM OR SHORT TERM ?

The criteria for success are never exactly the same for both parties, but if you are aiming at a long term relationship it is imperative that the criteria for commercial success are the same as far as possible for both parties.

You yourself want to enter into the contract with a business perspective for your own selfish reasons! – but - so do your counterpart! If you want to benefit from the relationship over a long period of time make sure there is something in it for the other party as well. If the benefits are limited, it will be the beginning towards the end from the very start of the relationship.

Key Note:

- If you want to have a long-term relationship, make sure that also your counterpart is happy.

LAW AND FORUM

A commercial contract will never be complete in the sense that it will provide the answers to all possible matters. Some times disputes arise irrespective of how careful the agreement was drafted.

The law on the formation of contracts varies from county to country.

The construction and interpretation of the contract will be affected by the governing law.

The internationally accepted rules are the following: A contract shall be governed by the law chosen by the parties. To the extent that the law applicable to the contract has not been chosen, the contract shall be governed by the laws of the country with which it is most closely connected.

Please remember that in some jurisdictions some provisions of national law are mandatory or considered "ordre public". In such cases the parties cannot derogate from the law.

And which court has jurisdiction? As a main rule the parties to a commercial contract may agree that a specified court shall have exclusive jurisdiction.

If the contract is silent with regard to the forum, then: Persons shall be sued in the courts of the state in which they are domiciled or alternatively (within the EU) in matters relating to a commercial contract, a

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person may also be sued in courts having jurisdiction at the place of performance of the obligation in question.

Arbitration is an alternative to ordinary court proceedings but often more expensive, and there is no option for appeal. On the other hand, arbitration is less time consuming; there is no publicity; and above all, arbitral awards are enforceable in most jurisdictions.

Key Notes:

- Try to avoid unpleasant surprises; check up on the relevant legislation.
- Wherever possible, include a clause stating which system of law is to apply to the contract and where any litigation should take place.
- Consider arbitration as an alternative to national courts.
- If a contract may have to be enforced in a particular country, it is wise to have the contract checked by a lawyer from that country.

THE PREAMBLE

The preamble forms the introduction to the contract giving some basic information on the parties, their intentions and their capabilities of entering into the cooperation set out in the contract.

Normally, in conventional clauses, you are not able to include the information required for a third person to understand fully the background of the contract.

The preamble consists of factual information that is more or less evident to the parties. The importance hereof should, however, not be underestimated. What may seem evident to you may not be quite as evident to others.

When in doubt as to the true understanding of the nature of the cooperation you will often end up with the contract itself as the only important document. This document should provide evidence as to the purpose of the cooperation. You should make sure that also an independent third person will be able to catch the true meaning by merely reading the contract. That third person might be a judge on some future occasion. And if the background is clear to everyone who happens to be holding the document before him, disputes may be avoided altogether.

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Key Notes:

- The preamble gives evidence as to how the parties see the scenario for the cooperation.
- The preamble is a useful key to understanding the contract.
- It should be noted that in some countries, notably common law countries, a preamble may well be held of no contractual effect.

"DON'T YOU TRUST ME?"

You have heard it before! You have taken the liberty of questioning one of the delicate clauses of the contract; a clause which you fear might unreasonably be turned against you at some future occasion. And you are met with the following: *"It's just a standard form from our legal department accepted by all others; we have no intention of dragging you to court. We are here to do business, not to discuss trivial elements; don't you trust our company?"* - And now it is up to you. How do you react?

The answer of course is: "Yes", you do place trust in the other party, and Yes again, you also want to do business. But the orally exchange of words during the negotiation does not form part of the contract. Furthermore, at some future time, it might very well be up to somebody else to interpret the contract. And this somebody was not present at the conversation.

Let the answer be: *"Yes, I trust you because I know you, but I don't know your successor, so how could I trust him"*. And then add to the contract what was orally said.

If you fail to succeed during the negotiations you have two options: You can either drop the contract, or accept it as it is. In the latter case you know what you are doing; it is a poor contract, but you value the business opportunities highly. You are making a commercial decision.

Key Notes:

- The exchange of words during the negotiation is not part of the contract.
- An oral contract ain't worth the paper it is written on.
- Every important provision should be clearly written into the contract. If the other party is not prepared to do this, you are certainly right not to trust him.



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