

# LawWorks – IHPBD

## Contracts 101

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# Contract formation

## WHAT IS A CONTRACT?

- A contract is a legally enforceable agreement which gives rise to rights and duties among those who agree to its terms
- Key elements of a contract: offer, acceptance, consideration (not required for a deed), intention to create legal relations, certainty of terms

## HOW CAN A CONTRACT BE FORMED?

- Orally, by means of the spoken word
- Partly orally and partly in writing
- May be implied from the conduct of the parties
- Via email, or by clicking a button on a website (provided the key elements are present)

## PRACTICE POINTS

- An enforceable contract can be created more easily than you might think
- Take care not to bind yourself inadvertently to a contract (for example, by outward actions)
- Avoid making an enforceable contract accidentally and prematurely before all of the terms have been agreed
- If an offer attempts to incorporate terms and conditions into the contract by reference, it is important to locate and read these
- Check whether there is any applicable contracting policy before agreeing/executing a contract covering e.g. required consents

# Pre-contract documents

LETTER OF INTENT (LOI), MEMORANDA OF UNDERSTANDING (MOU), HEADS OF TERMS (HOT)

- Frequently used when negotiating commercial transactions
- Records an outline of the terms that the two parties have agreed in principle and a framework for future negotiations

## PRACTICE POINTS

- Mark all pre-contract correspondence and documents with “subject to contract” to avoid inadvertently creating a binding contract
- Consider if any elements of any pre-contract documents (e.g. confidentiality or exclusivity provisions in a HoT) should be binding. If so: (i) ensure the relevant parts that should be binding are expressed to be binding, (ii) ensure it is explicit in the document that all other elements of the pre-contract document are not binding; and (iii) the binding elements of the document should be treated and reviewed like any contract
- Ensure the commercial terms in any pre-contract documents are accurate before drafting the full form agreement
- Set out the entire understanding of the parties in a single document with appropriate "entire agreement" and other “boilerplate” clauses
- Check all terms in pre-contract documents are included in the full form contract
- If required, incorporate any other documents by reference, or as schedules / appendices

# Deed vs simple agreement

## WHAT IS A DEED AND WHY USE ONE?

- Deeds (unlike simple agreements) are binding where there is no consideration from a contracting party, i.e. where there is a one-sided agreement benefitting only one of the parties
- Certain contractual arrangements must take the form of a deed by law (e.g. power of attorney, transfer of land)

## HOW TO TELL THE DIFFERENCE BETWEEN A DEED AND A SIMPLE AGREEMENT?

- The document will state that it is a deed, normally either on the title page, the top of the document or on the signature page
- The signing requirements for a deed are more onerous than for a simple agreement. Individual signatures will need to be witnessed and often two signatures will be required for each entity (in the case of a UK entity)

**IN WITNESS** of which this Deed has been executed and delivered as a deed by the Parties and takes effect on the date written at the beginning hereof.

**EXECUTED** and **DELIVERED** as a **DEED** by  
**[PARTY]**  
acting by a duly authorised signatory: \_\_\_\_\_  
in the presence of:  
Signature of witness: \_\_\_\_\_  
Witness name: \_\_\_\_\_  
Address of witness: \_\_\_\_\_

**EXECUTED** and **DELIVERED** as a **DEED** by  
**[PARTY]**

Acting by \_\_\_\_\_      Acting by \_\_\_\_\_  
Name: \_\_\_\_\_      Name: \_\_\_\_\_  
Title: \_\_\_\_\_      Title: \_\_\_\_\_

# Before you start!

## KEY POINTS TO CHECK AT THE START OF THE CONTRACTING PROCESS:

- *Who will be signing?*
  - Make sure you know who is ultimately going to sign the contract (internally and externally)
- *Do the signatories have authority?*
  - Check any applicable contracting policy
- *Do the signatories know they will have to sign?*
  - Make sure the signatories know about the contract in advance and proposed timeline for execution so there are no signing hold-ups
- *Are the commercial terms correct?*
  - Make sure that the commercial terms reflect what has been agreed between the parties
- *Subject to contract?*
  - Ensure the correspondence and documents are marked with “subject to contract” to avoid inadvertently creating a binding contract (as per previous slide)
- *Is the document a Deed?*
  - Additional formalities will apply

# Parties

## PARTIES CLAUSE

- Full names and addresses of the parties to the contract should be inserted
- For companies, charities, limited partnerships and limited liability partnerships, the registered office and registration number should be provided
- These details can be found by checking:
  - the Companies House register (<https://find-and-update.company-information.service.gov.uk/>) or
  - for Charities only, the Charity Commission register (<https://register-of-charities.charitycommission.gov.uk/charity-search>)
- When reviewing this clause make sure that the parties are clearly identified and check if they are who you expect to enter into the contract. Parties must have capacity to enter into contracts. If it is unclear whether a counterparty has capacity, ask them to provide evidence.
- Check whether the parties to the contract are defined and the appropriate term is used consistently throughout

# Recitals / background / interpretation

## RECITALS / BACKGROUND

- Statements of fact before operative clauses which set out the background to the contract, e.g. the reasons for the contract
- This is not essential and is not included in every contract, but usually feature in longer contracts to provide a brief explanation
- Can be a useful way to record, for persons referring to a contract in the future who may not have been involved with the contract's creation and evolution over time, the background to that contract and why, when and how it has been amended over time

## INTERPRETATION OR PRECEDENCE CLAUSES:

- *What/Why?*
  - A series of legal principles which apply to interpret a contract and resolve internal inconsistencies
- *Where found?*
  - Usually at the start, after the definitions
- *Importance?*
  - Singular/plural; masculine/feminine, headings, references to clauses



# Definitions

## WHAT/WHY?

- Defined terms in a legal contract which mitigate the chance of misunderstanding
- Clear and unambiguous terms
- Avoids repetition each time the term is used throughout the contract

## WHERE FOUND?

- A separate section/clause either at the start (after the Parties and Preamble) or end of the contract

## IMPORTANCE?

- Crucial to check any defined terms are consistently used
- Beware changes made to the body of the agreement but not the definitions
- If changes made to definitions, check that those changes make sense whenever the definition is used in the body of the agreement
- Take note of any general interpretative rules that apply to the contract and consider the potential impact of those rules when reviewing provisions in the contract, such as rules that:
  - the word 'including' always means 'including, but not limited to'; and
  - the word 'person' means any individual and/or any type of company, partnership or other legal entity or governmental body of any kind.

# Substantive provisions

## WHO IS TO DO WHAT?

- Clearly describe the obligations of each party under the contract

## WHERE IS IT TO BE DONE?

- Depending on the nature of the services/goods, consider if necessary to be stated

## HOW IS IT TO BE DONE?

- Consider if performing party's detailed steps required versus simple end result obligation. Consider requirements for service levels, ongoing relationship etc.

## WHEN IS IT TO BE DONE?

- Are specific dates required? Time of the essence. Best vs reasonable endeavours

## WHAT IF?

- Whilst not always necessary (since failure to fulfil a contractual obligation may simply constitute a breach of contract giving rise to a potential legal claim against the party in breach), consider if it may be appropriate to stipulate explicitly in the contract the consequences of a party failing to fulfil an obligation (e.g. early termination of the contract in its entirety, delay/termination of one or more specific obligations of the 'innocent' party under the contract, application of default interest on a payment obligation, ability for the 'innocent' party under the contract to procure that a third party fulfil the obligation and pass on the cost to the party in breach etc.)

# Income contracts vs expenditure contracts

INCOME CONTRACT: Documents the receipt of funds by a party

EXPENDITURE CONTRACT: Documents the expenditure of funds by a party

PRACTICAL TIPS FOR REVIEW:

- *Payment obligations*
  - Amount, currency and method of payment (e.g. bank transfer, letter of credit)
  - Whether or not prices include VAT (20%) or other taxes (VAT will be treated as included in the price unless the contract provides otherwise)
  - Frequency of multiple payments, longstop for final payment
  - Name of bank and account details, with an ability to change these details on notice
  - Timing of payment.
- *What happens if the payer does not pay?*
  - Grace period to rectify non-payment
  - Default interest (if so, check the rate and whether this increases over time)
  - Notification requirements under the contract in the event of failure to pay / breach of contract
  - Retention of title clause – allows the seller/provider to retain title of goods until they are paid and the contractual terms met
  - Goods and services the income/expenditure relates to are correctly described

# Warranties and representations

## WHAT IS A WARRANTY?

- Contractual statements in the form of an assurance or promise given at a specific point in time
- Breach of a warranty may give rise to a claim for damages for breach of contract (but cannot give rise to a right to terminate the contract) – damages are subject to the common law rule on remoteness
- Damages will seek to put the aggrieved party in the position it would have been if the contract had not been breached, subject to the duty on the claimant to mitigate their loss
- Examples include: title, authority, capacity, validity, quality of goods/services
- If a party is providing any warranties, check these are appropriate and are factually correct before agreeing to them, and consider adding timing, materiality and/or knowledge qualifiers to limit the scope of the warranty

## WARRANTY OR REPRESENTATION?

- A representation is a statement made by one party to the contract which may have induced the other party to enter into the contract
- Representations can be written in to the contract
- Breach of a representation may give rise to a claim for misrepresentation, with remedies including rescission (setting the contract aside) or tort damages (with no remoteness limit)
- For this reason it is generally better only to give warranties and not representations

# Indemnities and guarantees

## WHAT IS AN INDEMNITY?

- A promise to reimburse the indemnified party in respect of a particular type of liability (should it arise) – sometimes also referred to as “holding harmless”
- Shifts the risk of a particular event or matter occurring to the indemnifying party
- Allows the indemnified party to recover on a pound-for-pound basis, without being required to mitigate its loss
- The language used in indemnities will usually be very wide and typically include interest and costs
- Easier to enforce at law merely by establishing loss and causation (e.g. avoiding common law rules of remoteness of damage)
- Check the cap on the indemnity (1) is appropriate and (2) falls within any financial cap applicable to the indemnifying party.

## INDEMNITY OR GUARANTEE?

- A guarantee is a promise to ensure that a third party fulfils an obligation (or a promise to fulfil such obligation if the third party fails to do so)
- A guarantee requires an existing / underlying primary obligation between two parties, which the guarantor supports as a secondary obligation, whereas an indemnity is a primary obligation
- Check carefully before agreeing that a party will guarantee any third party obligations as that party could end up liable for the payment / indemnity obligations of the third party (which may not be capped)

# Limitations of liability

- Certain contracts attempt to limit liability for breach of obligations
- This could be a complete exclusion of liability for some clauses, or a cap on liability up to a particular sum (and may include a time limit after which a party may cease to have any liability for breach of all or certain obligations)
- Liability cannot be limited for:
  - fraud (dishonesty) by a contracting party
  - injury or death caused by a lack of reasonable care
  - supplying goods without the right to do so
- A clause cannot exclude a party's liability for breach of all of its duties under the contract and it cannot leave a party without any meaningful remedy for breach
- How to approach an exclusion or limitation clause:
  - Identify the risks for both parties and consider whether there are other ways to minimise them
  - Consider what insurance is available – risks which are not insured should be limited
  - Decide which liabilities should be excluded, capped or accepted
  - Reciprocity of exclusions; watch out for one-sided liability exclusions
- Force majeure: acts of God, strikes, epidemic, pandemic, war, fire, riot, sabotage or terrorism...

# Termination

## *When does the contract terminate?*

- Is it clear?
- Is there a fixed term or an 'expiry date'?

## *Early termination provisions*

- How much notice is required for either party to terminate early?
- Is a written notice required? Where should it be sent to?

## *Why terminate early?*

- E.g. breach of contract by the other party, you no longer need the goods or services, the other party is insolvent
- Can either party terminate for any / no reason (fault vs non-fault-based termination)?

## *Effect of termination*

- Both parties are normally released from further performance of their main contractual duties (e.g. to deliver goods and to pay for them), however the accrued rights under the contract survive (e.g. unpaid financial obligations)
- Future obligations (e.g. payment obligations) and rights should fall away
- Be aware in general of any rights or obligations expressed as continuing post-termination (either for a finite period or indefinitely)

# Confidentiality

## CONFIDENTIALITY PROVISIONS

- *When to include?*
  - If the transaction involves disclosing confidential information
  - If confidentiality provisions are included, ensure there is an ability for your organisation to disclose confidential information (i) to its affiliates, trustees, employees and professional advisors and (ii) if required by applicable law, regulation or court order
- *Consider omitting?*
  - If the transaction will not involve sharing confidential information or there is already an existing duty of confidentiality giving adequate protection (such as a separate NDA)
  - If confidentiality obligations are omitted on the basis of an existing duty of confidentiality under an NDA, ensure the application of the NDA is preserved under the “entire agreement” boilerplate clause in the contract

## ADDITIONAL POINTS TO NOTE

- Confidentiality clause can: improve disclosing party’s rights; clarify intentions and set an end date (if no separate NDA)
- Can improve a party’s rights but does not cure the problem of enforcement
- No confidentiality provision does not equal no protection
- Some disclosures cannot legally be restricted



# Boilerplate clauses

## WHAT IS A BOILERPLATE CLAUSE?

- Regulates the operation of the contract: its duration, interpretation, transferability and enforceability

## COMMON EXAMPLES OF BOILERPLATE CLAUSES

- Commencement: Agrees when performance will start, if it is not obvious
- Counterparts: Confirms the validity of counterparts or duplicates of the contract
- Force majeure: Agrees a way to deal with non-performance due to events beyond a party's control
- Assignment and subcontracting: Controls who performs the contract and who can receive benefits under the contract
- Entire agreement: Contract constitutes the entire agreement between the parties and supersedes any prior agreements, negotiations or discussions
- Notices: Address for each party to receive notices relating to the contract and provisions for sending valid notices, including service of process in a potential litigation scenario
- Third party rights: Can limit non-parties' rights to enforce contract terms
- Variation/Amendment: Agrees a procedure for a valid variation/amendment of the contract

# Boilerplate clauses (continued)

## COMMON EXAMPLES OF BOILERPLATE CLAUSES

- Further assurance: May help to deal with accidental omissions in the contract
- Severance: Agrees the contract will survive deletion of an unenforceable provision
- Survival: Confirms that specified clauses remain effective after contract expiry or termination (e.g. confidentiality clauses)
- Governing law: In practice, suppliers almost always stipulate the law of their own country of establishment as the governing law – consider whether this is acceptable
- Jurisdiction: Agrees where proceedings can be brought (exclusive v non-exclusive). In practice, suppliers almost always stipulate the courts of their own country of establishment as having exclusive jurisdiction. Consider if the following are acceptable (if they apply): (i) the courts of a jurisdiction other than England and Wales is stipulated; (ii) a contract provides for non-exclusive jurisdiction such that one party to the contract has the right to bring claims against the other party in the courts of jurisdictions other than England and Wales; or (iii) an alternative method of dispute resolution is included in the contract (e.g. mediation and/or arbitration) which provides for that alternative method of dispute resolution to be conducted in a jurisdiction other than England and Wales.

Always read the boilerplate provisions – these impact on the whole contract and can make all the difference in the event a dispute were to arise!

# Execution

## AUTHORITY

- Have the relevant persons approved the contract, in line with any applicable contracting policy?
- Does everyone signing the contract have the authority to do so?

## IS THE CONTRACT READY TO SIGN?

- Are all details agreed and all schedules attached?
- Carry out a final check of any placeholders, square brackets, bullet points etc. that need populating

## ELECTRONIC EXECUTION

- Simple contracts can be signed electronically in the UK (including by DocuSign)

## AND FINALLY...

- Remember to date the contract only once you have all signatures and not before
- If the signatures need to be provided before the contract is ready to date, explicitly state when providing these (e.g. on email) that they are being provided in escrow, subject to confirmation of release in due course. This is a way to provide signed documents to the other contracting party/ies without being bound by those documents at the time of provision
- Make sure all parties receive a copy of the final signed and dated agreement
- Save the final signed document internally for future reference

Any questions?