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## PRINCIPALS OF CONTRACT DRAFTING

When an ordinary man wants to give an orange to another, he would merely say, " I give you this orange." But when a lawyer does it, he says it this way :

"Know all men by these presents that I hereby give, grant, bargain, sell, release, convey, transfer, and quitclaim all my right, title, interest, benefit, and use whatever in, of, and concerning this chattel, otherwise known as an orange, or citrus orantium, together with all the appurtenances thereto of skin, pulp, pip, rind, seeds, and juice, to have and to hold the said orange together with its skin, pulp, pip, rind, seeds, and juice for his own use and benefit, to himself and his heirs in fee simple forever, free from all items, encumbrances, easements, limitations, restraints, or conditions whatsoever, any and all prior deeds, transfers or other documents whatsoever, now or anywhere made to the contrary notwithstanding, with full power to bite, cut, suck, or otherwise eat the said orange or to give away the same, with or without its skin, pulp, pip, rind, seeds, or juice."

Robert H. Mundheim, general counsel of the U.S. Treasury Department, in a memo to senior Treasury officials.

Though the above have been said in good humour but the fact is that the law of contract is most complex because it lays down the legal rules relating to promises - their formation, their performance and their enforceability. It is intended to ensure that what a man has been led to expect shall come to pass ; that what has been promised to him shall be performed.

The law of Contract is applicable not only to the

business community but also to others. Everyone enters into number of contracts everyday in his life without realising about it. When he gives his car to a mechanic for repair he enters into a contract of bailment, when he buys a packet of cigrette, he is making a contract of the sale of goods or if he goes to see a movie in the cinema hall, he is making another contract. Hence contract law furnishes a basis for the other branches of Mercantile laws. That is why the law of contract precedes the study of all other sub-divisions of Mercantile Law. Most of the law of contract is based on judicial precedent.

The broad basis of contract law is that it shall not lay down absolute rights and liabilities of the contracting parties instead it lays down only the essential of a valid contract in the absence of anything contrary agreed to by the parties. Secondly expectations created by promises of the parties shall be fulfilled and their non-fulfilment shall give rise to the legal consequences. A simple definition of a contract could be an agreement enforceable by law. Thus a contract should have an agreement and a Legal obligation.

2. Agreement - When one party makes a proposal or offer to the other party and that other party signifies his assent or acceptance an agreement comes into existence. In short, an agreement is the sum total of "offer" and "Acceptance."

It, therefore, follows that there should be atleast two persons to make an agreement as no one can enter into agreement with himself. Secondly both the parties must agree about the subject matter of the agreement in the same sense and at the same time i.e. ad-idem.

3. Legal Obligation :- As pointed out above an agreement

to become a contract must give rise to legal obligation i.e. duty enforceable by law. Thus an agreement is wider term than a contract. All contracts are agreements but all agreements are not contracts. For example agreements of moral, religious or social nature e.g. promise to lunch together, to take a walk together are not intended to be enforceable by law. Hence in all business agreements the presumption is usually that the parties intend to create legal relations. Therefore, there are certain essential elements of a valid contract which are understood world over. These could be briefly :-

1. Offer and Acceptance - As has been mentioned above, there must be a 'lawful offer' and a 'lawful acceptance' of the offer. The lawful adjective means that the offer and acceptance must satisfy the related contract Act.

2. Intention to create Legal Relations - The agreement should be attended by legal consequences and obligations.

3. Lawful Consideration - There must be present a consideration which is the price paid by one party for the promise of the other. It could be an act of doing something or forbearance of not doing something or a promise, relating to past, present or future. A consideration is lawful unless it is forbidden by law, is fraudulent or involves or implies injury to the person or property, is immoral or is opposed to public policy. Subject to certain exceptions, gratuitous promises are not enforceable at law.

4. Capacity of the Parties :- The parties to the agreement must be competent to contract. They should be of the age of majority and of sound mind and must not be disqualified from contracting by any law to which they are subject like lunacy, idiocy, drunkenness etc.

5. Free Consent : - It means that the parties must have agreed upon the same thing in the same sense. Consent should not have been obtained by coercion, undue influence, fraud, mis-representation or mistake. A contract entered into under mutual mistake is void.

6. Lawful Object : - The object should not be fraudulent, illegal, immoral, opposed to public policy or must not imply injury to the person or property. Such agreements are void.

7. Writing and Registration : - It could be oral or in writing but in many cases it is mandatory that the contract must be in writing and registered. For example an agreement to pay time-barred debt or to make a gift, arbitration agreement, sale of immovable property etc. require normally a written agreement.

8. Certainty : - The terms of agreement must not be vague or uncertain and must be capable of being explained the meaning of the agreement.

9. Possibility of performance : - An agreement to do an act impossible in itself is void because both physically and legally it is not possible to perform it.

10. Not expressly declared void : - The example of such agreements could be to put restraint on marriage or trade or an agreement by way of wages etc.

## Kinds of Contract

From the point of view of enforceability a contract may be valid, voidable, void, unenforceable or illegal.

From the point of view of mode of creation a contract may be express, implied or constructive.

From the point of view of the extent of execution a contract may be executed or executory.

Now to negotiate, enter and draft an agreement which satisfies the various requirements as briefly mentioned above, it is essential to prepare oneself with certain preliminary information. It is necessary to identify the requirements based on the nature, place and objective of the agreement. It is unlikely that all the following requirements are to be fulfilled for all the agreements. Since, no two agreements would be identical in absence of identical contracting parties yet they can serve as the guidelines. This purpose can also not be served by a model agreement as each negotiation is different and depends upon tact, skill, knowledge and urgency of each of the parties to the agreement. A few tips could be :

1. Ascertain the names, description and address of the parties to the instrument.
2. Read the introductory note, or, if time permits, the literature on the subject of the instrument. Note down the most important requirements of the law which must be fulfilled to draft a complete instrument on the subject.
3. Obtain particulars about all necessary matters which are required to form part of the instrument.
4. Peruse the forms which are allied to the subject in the precedents provided in this book.
5. Enquire whether the clauses in the instrument should be comprehensive or brief. In all events be precise.
6. Note down with precision any particular directions or stipulations which are to be kept in view and incorporated in the instrument.
7. Technical words should be freely used after ascertaining

their meaning and import.

8. Facts should be stated in chronological order wherever necessary.

9. A rough sketch in logical order must always be drawn up and revised.

10. Each clause which relates to a contractual obligation must not be contrary to law. Each clause relating to conveyance must conform to the law relating to transfer of property. Each restriction or reservation on the enjoyment of property imposed on the transferee or reserved for the transfer must not be prohibited by law.

11. As the whole object of the drafting of an instrument is to express the intention of the parties in the language used in the instrument such language should not be ambiguous or susceptible of more than one meaning.

12. There should not be a repetition of covenants of the operative words in the instrument.

13. Great care should be taken in drafting deeds of transfers that the title of the transferor has been fully investigated by reference to original deeds or orders where possible. Nothing should be assumed and search in the Registration Department about prior dealings with the property agreed to be transferred should invariably be insisted upon. A prudent transferee should not ignore inspection of the registers in Registration Department.

14. If the transaction is incorporated in more than one deed drawn up simultaneously, care should be taken that the same phraseology is used in all of them.

15. Schedules may usefully be annexed to deeds where the properties deal with in the deed are numerous or their description

must necessarily be elaborate.

16. As income-tax law is inter-connected with various writings and deeds therefore, it will be worth its while to consult thembefore drafting deeds.

A contract has to be correct and fair and never set a target that can not be achieved. Please ask the question would I sign the contract if I were in my partner's position? The contract is a homogeneous entity and not simply a loose collection of clauses. They must be inter-related and consistent with each other. The main purpose of the contract is the realisation of the project which it must serve hence study the subject intensely. It must mirror a process of successful implimentation with the sequence of events and their precondition.

In a contract the rules of the parties are continuously reversed. For example once it is the transferor who is obliged to do something and in subsequent clause he may demand fulfilment of an obligation. Hence it may release the first party from the consequences foreseen in the contract for his delay or defective supplies. Therefore minimum requirements and conditions should be clarified and possible limits beyond which his counterpart cannot go.

The strategy and tactics of negotiations when drafting should be carefully developed and play the game what could go wrong. He should consider what happens if the market changes, what happens if a competitor also jumps in the fray and patent is declared invalid, a newer technology is offered by another source, a new licensee is introduced in the common market, if someone were to infringe our

licence rights and how he can get out of the agreement. These are a few questions which he must ask himself and develop the draft to take care of these situations.

It is always a teamwork but drafting should be a one man job. He must however be assisted by technical, financial and administrative team.

Since no two contracts are same because a concluded contract is only the end result of the compromises made. Similarly a model contract can work as a check list for what is to be left out and structure of the agreement. The drafting is a time consuming job but it is always a paying proposition saving money by preventing problems and damages.

It is also necessary to decide who should draft. That initiative should be taken because even if the other party makes many changes their will be some favourable points which will stick. It is thus always better to prepare ones own draft for negotiation. All competent people who have a responsibility in the project and whose knowledge and work is necessary for its success should be associated at one stage or the other. These people can submit the draft relating to their field of work. It is said that most legal man write what they believe is important for us and not what really is important to us. Hence who should draft the contract whether a legal, technical or commercial person is important one.

The type of contract should be studied carefully. An American type contract expresses intention in "whereas clauses" but the Anglo-Saxon one start with "Now therefore". The clarity of terms and notions is a must and do not take anything for granted. For example capacity must be defined

in quantity, time and period for each product. Tons in metric, short or long tons, Days in working days, Calender days or one ,two or three shifts of 6,8 or 10 hours. In France sometimes one year means thirteen months because August is taken as a non-working month. Same is with Acres and gallons which has different sizes in different countries.

The language of contract should be as far as possible the language understood by both the parties. Otherwise it could be the language used during the negotiation. A check list of problems to be addressed in the contract and the other of chapters or sections with main clauses be prepared. It is advised that for this purpose a uniform decimal system with sub-decimals must be devised. The language used should not be too technical and should be as simple as possible used in day todays life. The words are very important— synonym should be avoided. Definitions must be clear, exact, unambiguous, concise and yet explicit.

Ambiguity and vagueness must be avoided at all cost. Words like 15 March to 15 June whether they are inclusive and indivisible should be used with caution. The adjective used to define a particular word should have only one meaning. It must be ascertained that the level of precision attained is sufficient reasonably to serve the business needs of the parties in so far as these can be foreseen.

The actual drafting should be undertaken only after having clarified all preliminary facts and features and discussed them both with the transferor and the team members. Thereafter if details of the technology, the economic aims and purposes of the project and the contract are clear, the process of implementation thought over and its sequence put

on paper, the structure of contract and its language selected, only then should the drafter start the work of actually drafting.

First of all chose the law governing the contract. It could be law of licensee's country, licensor's country or of a third country. Both parties should be aware about concept of law, what one is obliged to do, what are laws of sale of goods, bailment, warranties, guarantees, rights of purchaser, damages, suits of recovery, penalties if any, limitations of time and restrictions etc.

Secondly to obtain the exact names and addresses of both the parties and spell them exactly. After this formulate the aims and purpose of the contract. Why the project is needed and what the contract is expected to achieve. The next question would be the subject of the contract. It could be a license on the patent, know how, trade mark, model, software, transfer of technology, supply of equipment or possible services. Their content and limitations should be worded. The warranty against legal defects and the problem of infringement should be dealt with. Technical clauses dealing with basic engineering, documentation and training, performance guarantees should follow in that order.

Here for performance guarantee, how the tests should be performed, all conditions for tests, how the results should be registered, evaluated and calculated and what the consequences of such results should be very clearly and precisely spelt out. Since this may have serious financial implications this clause be most balanced and fair to both the parties. Impossible should not be tried to be achieved.

This could be followed by clauses on equipment supplies mentioning specifications, delivery times, packaging, markings

transportation, delays, erection, commissioning, quality control etc. The programme for indigenisation should also be covered in as much detail as possible.

In the same way financial conditions like prices, conditions of payments, documents for payments, financial securities and insurances could be spelt out. The escalation clauses, fluctuation in currency limits if any in such situation, how it should be paid, local cost payment to foreign experts are necessary ingredients of this clause.

Normally this clause is followed by the termination clause and rights surviving the term and arbitration clauses for settling the disputes. The normal conditions of termination are when licensor does not transfer or supply technology at all or only after long delay losing the expected gains of the project, failure to supply equipment, providing unsuitable unintended technology, refusal to transfer improvements, failure to pay licence fee and submit prescribed reports and allow to check, false report of audit, voilation of secrecy obligation and breach of any other contractual obligation of material nature.

The cooperation of the parties after the expiry of the contract could follow the above clause. This would cover exchange of development results, consultations, joint research and development, rights and obligations originating from such cooperation, their terms and expenses involved.

This is to be followed by the clause on arbitration in case of dispute. There can be various models, single, bipartite and tripartite. The last named has been mostly preferred with representative of each party and in case of difference in opinion could be referred to a neutral mutualy agreed to Umpire arbitrator. It could also be Court of Justice of defendent's country, Courts

of arbitration or International Chamber of Commerce, Paris. However, language of the proceedings, applicability of law and sharing of expenses must find place in this clause itself to avoid any dispute later.

This clause would be followed by Force majuere which is a standard clause world over and is best to be adopted as such.

All other conditions to befollowed by the 'coming into existence" clause would conclude a reasonable draft agreement. One could append a glossary of definitions and various appendix referred to in the body of the draft.

After the draft is prepared it must be checked and revised by all concerned together and separately. It is good to know their reaction and suitable modification should be carried out otherwise it must be clarified to the person. Normally it is a joint agreement within the party first and then the bilateral. After internal revision the draft could be sent to lawyer to ascertain any legal infirmity. When he has also seen it, it is now ready to be handed over to the other party for negotiation.

Since the draft has been prepared in full knowledge of his offer it may be reasonably hoped that he will not reject it totally. But there may be certain differences of opinion which may require to be negotiated for which an advance tactics may be worked out because there may not be many surprises.

Practical Tips for a Technology Transfer Agreement

Though the guiding factors for a valid contract have been described above yet this being a typical contract and could be a detailed subject of discussion it would be useful to give a few hints as a ground rule to be kept in view at the time of

negotiating a technology transfer agreement.

This may be required for

(i) Filling a technological gap in the industrial sector

(ii) The indegenous technology is closely held

(iii) Updating the existing technology

(iv) Linking with the substantial exports.

It may involve either payment or royalty or lumpsum payment. Therefore, prescribe the limit of royalty period and the percentage. The reasonable period could be 5 to 8 years and quantum could be upto 5% or 7.5% in exceptional cases. Royalty with lumpsum could be upto 8% over a period of not exceeding 10 years maximum.

Further following concessions may also be attempted.

(1) Foreign equity investment should be as far as possible in cash without linking to imports of machinery, equipment or payment of know-how, trade marks, brand names etc.

(2) The licensee should be free to sublicense the technical know-how/product design/engineering design to another domestic party on mutually agreed terms

(3) The royalty should be calculated on ex-factory sale price minus the imported components and bought out parts and is linked with the unit and volume of production.

(4) There should be no payment of a minimum guaranteed royalty.

(5) There should be no binding with regard to capital goods, raw-material, procurement and freedom for import from any source be available.

(6) There should be no restriction for export of products except to the countries where another sub-licensee exists or which is a traditional market of the licensor.

(7) Use of foreign brand name for domestic market be avoided.

(8) The licensee should have a right to produce the item

even after the expiry of the collaboration without any additional payment.

(9) Duration of the agreements should be fixed.

(10) The licensee should develop and set up their own design and research facility during the period of agreement.

(11) Deputation of foreign experts, terms, numbers, remuneration period may be provided for.

(12) The provision for payment of interest on delayed payment be avoided.

(13) The royalty amount should cover, the compensation for use of patent rights in the licensee's country.

(14) Any consultancy should be arranged from licensee's country but if it is unavoidable that they should be made the prime consultant.

(15) The agreement should be subject to licensee's laws as the project will be executed in his country.

(16) If there are any buy-back arrangements they should be properly guaranteed by the licensor.

The list can go on. The above is only an illustrative list and not the exhaustive one. One could bring in many more suggestions depending upon the nature of the transactions.

Conclusion -

Since joint venture is a marriage between the two parties hence it depends upon mutual goodwill, truthful long-term cooperation, tomeet each others obligation. Since the contract is the first step it requires to be balanced, readable, easily understood, clear in its content and precise, without any alternative interpretation as far as possible. These are only a few ideas not the model and one should develop his own ideas and language based on exhaustive discussion and understanding.

Remember always that that contract is best which is not consulted after it has been written.