

Commercial Contracts and The Most Heavily Litigated Provisions



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Agenda – Heavily Litigated Provisions

Covered in our Materials:

- Best Efforts, Commercial Efforts, Alternatives
- Most Favored Nation (MFN) Clauses
- Average Sales Price, Earn-Outs, and Accounting Disconnects
- Termination Provisions
- License Grants
- Confidentiality and Non-Disclosure (NDA) Obligations
- Exclusivity, Sole, and Like Rights
- Using Letter of Intent (LOI), MOUs, Agreements to Agree (ATAs)
- Limitation of Liability (LOL)

Honorable Mention:

- Minimum Commitment or Take-or-Pay Obligations
- Force Majeure and Frustration Clauses
- Quality, Warranty, Recall, Epidemic Failures, Failure Analysis, Etc.
- Dispute Resolution, Arbitration, Mediation



Best Efforts, Commercially Reasonable Efforts

Things to Consider

- “Best efforts” creates higher obligations than “reasonable efforts” terms
- “Best efforts” often means “leaving no stone unturned” or “doing all you can do get the job done”
- While a company is often not held to drive itself into bankruptcy for “best efforts,” the needs/harm to the other party is given greater consideration
- Looking to the industry, some may argue ALL things usually, routinely, or reasonably done must be done to satisfy “best efforts,” this is a high bar
- On average, litigated cases show the “best” standard is not met more than it is met
- A court or arbiter can imply a standard of effort when it is not expressly in the contract, so disclaiming any kind of “standard of effort” may be wise for high stakes performance/risks in a contract.



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3

Example Clause 1

Company A shall use best efforts to deliver fully tested and functioning product to Company B.

Example Clause 2

Company A shall:

- (a) Wafer probe all wafers received from the Fab as set forth in Exhibit A and mark any dies that are open, shorted, or non-functioning in any manner;
- (b) Final test the die as set forth in Exhibit B to at least 99% test coverage and completion for all circuitry contained on each die;
- (c) Burn-in test each die for the first 3 months of production as set forth in Exhibit C for a minimum of 70 hours and report yield losses to Company B weekly
- (d) Conduct system level test as set forth in Exhibit D with the peripherals and operating system versions set forth in Section 8.

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3

Most Favored Nation (MFN) Clauses

Things to Consider

- Should you consider volume differences between customers?
- How different must the Product X be in terms of features, performance, function to be considered “equivalent”?
- Do you consider non-monetary consideration or secondary deal factors that may govern price (e.g., the rights granted, equity, or liability assumed)?
- Does the pricing correct for rebates, volume discounts, warranty replacement, demo units, bundling, etc?
- Do you consider tariffs, taxes, and the like?
- What about geographic/market differences and global variance in trends that effect price?
- How do you address internal transfers, internal sales, or use inside the “selling” company?
- What about timing and time duration of sale?
- How do you get access to info and transparency?



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4

Example Clause 1

If during the term of this contract Company A sells or processes Product X of similar quality to the Product X sold hereunder at a price, inclusive of all rebates, discounts or free goods, lower than that provided under this contract, taking into account the Product X Reservation Fee in determining comparable pricing, then Company A will notify counterparty of such price and adjust the price set forth in Section 8 to meet such lower price, also taking into account the Reservation Fee set forth in Section 8(a) above, subject to the following exceptions: (A) Company A’s sales to its Affiliates for their own use; (B) Company A’s sales for delivery outside of the NAFTA Region; (C) Company A’s sales to industries different than counterparty’s; and (D) [Company A’s] sales to co-producers.

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4

Most Favored Nation (MFN) Clauses (*continued*)

Things to Consider

- Do you consider volume differences between customers?
- How different must the Product X be in terms of features, performance, function to be considered “equivalent”?
- Do you consider non-monetary consideration or secondary deal factors that may govern price (e.g., the rights granted, equity, or liability assumed)?
- Does the pricing correct for rebates, volume discounts, warranty replacement, demo units, bundling, etc?
- Do you consider tariffs, taxes, and the like?
- What about geographic/market differences and trends that effect price?
- How do you address internal transfers, internal sales, or use inside the “selling” company?
- What about timing and time duration of sale?
- Access to information and transparency?



5

Example Clause 2

If Company B sells Product Y of a similar quality to Product Y sold hereunder, in quantities substantially the same as those deliverable under this Contract for a similar period of time, for shipment to the United States, Canada or Mexico to a domestic manufacturer which is not a Company B Affiliate, at a price lower than that provided under this Contract after taking into consideration the Equity Contribution set forth in Section 6 below, Company B shall sell the same volume to counterparty at the same price as part of the volume set forth in Section 3(a), above.



5

Earn Out Clauses; Average Sales Price (ASP)

Things to Consider

- What accounting rules apply to financial calculations?
- Do you consider non-monetary items?
- How do you parse out price when the component-in-interest is bundled or a small piece of a system-level sale?
- Does the pricing consider third party losses/payments, rebates, warranty replacement, free demo units, recalls, etc?
- What is a “sale” and at what time does it occur?
- What is the process and time period for aggregating payment and reporting?
- What audit rights do you need to ensure compliance, and what is the expense and hassle of these terms?
- What are the ramifications for not properly paying fees that are due on time or to proper amounts?



6

Example Clause 1

“Earnout Accounting Principles” means GAAP applied on a basis consistent with the preparation of the Company A’s audited financial statements for the fiscal year ending in 2022; provided, however, that in the event a question arises with respect to the proper application of GAAP to any accounting entry for which Company A had not pre-Closing adopted accounting principles under GAAP as reflected in the Company’s audited financial statements for the fiscal year ended in 2022, Parent in consultation with its outside public accounting firm and the Company A CEO will determine the proper accounting principles under GAAP that will apply with respect to such accounting entry.

Example Clause 2

Company B shall pay a royalty to Company A of 15% of the average sales price of each unit sold.



6

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