Keeping your Contract out of the Courtroom: Contractual Rules for Drafting Partnership and Operating Agreements, including a Helpful Checklist.

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I. Introduction

You know what I love about contract drafting? You have the chance to create a private body of law between the contracting parties. You get to build and define their legal relationship with your own two hands and sharp legal mind. As a transactional lawyer, that process can be very rewarding. It is incredibly challenging, but the feeling of closing on a major merger and acquisition deal or finalizing the corporate documents of an up-and-coming business is no less exciting than completing that big jury trial.

However, what is a rewarding and challenging task as a lawyer is also a tremendous responsibility. How do I adequately capture in words what my client is seeking out of this deal? How do I ensure that my client receives the benefits it is hoping to receive? How do I protect my client from a potentially bad business partner? How do I ensure that all necessary issues are covered? How do I draft a contract, a body of law, that will be read and interpreted by everyone in the exact same way? These are only a few of the questions that transactional attorneys must answer when they are embarking on a new drafting project.

Like all good legal work, transactional drafting carries both rewards and great responsibility. This paper is intended to help the transactional lawyer identify and address drafting issues in all agreements including partnership and operating agreements.

Under the Texas Business Organizations Code, partnership and company agreements are powerful contractual tools for establishing the relationship among the partners or members and their organizations. Because partnership and company agreements serve such an important role in establishing these relationships, errors in the drafting of those agreements can create profound problems in the relationship of the partners or members. This paper addresses techniques and rules to assist with drafting partnership and operating agreements in order to avoid those problems and potential litigation.

Before jumping into the handy checklist, it is important to keep in mind the overarching goals of a transactional lawyer. First, you want to negotiate a good deal for your client. Second, you want to memorialize that deal so precisely and unambiguously that you discourage potential litigation. All of the points we have listed below seek to further these two goals.

II. Rules for Drafting, Reviewing, and Interpreting Agreements

A. Basic Information. Effective drafting requires a clear understanding of the subject matter of the agreement, the parties, and other subject matter or objectives of the agreement.

1. *Subject Matter of the Agreement and the Representation*. It is important that an attorney drafting or reviewing an agreement have a clear understanding of the transactions to be governed by the agreement.

a. Know your client's business. Often, this will require you to learn more about your client's business. For example, your client manufactures food products and runs a large manufacturing plant. Your client wants to enter into a manufacturing agreement with a new customer and has asked you to draft or review the agreement. You know very little about manufacturing food products. It is incumbent upon you to learn everything you can about your client's business. Whether you are drafting the manufacturing agreement or reviewing a draft from another attorney, you need to understand the actions that each party must take to make the relationship successful. In any contracting situation, it is helpful to picture the parties performing from start to finish. Determine the actions each party must take, when those actions must be taken, how the actions will be taken, where the actions will be taken, and who will take each action. In order to do this effectively, you must understand the nature of your client's business. Educate yourself and ask questions.

2. *Your Client*. Know – and make sure your client and the other parties understand – who you are representing in the transaction and who you are not. The answer to this question will drive important questions such as considerations of privilege (a rule of evidence) and confidentiality (a rule of professional responsibility), the professional liability and standards with respect to the services performed, and the ever popular who is responsible for paying you.

3. *Your Role in the Transaction*. Are you preparing, amending, or reviewing documents? If amending or reviewing documents, do you have the most current version? Are you rendering an opinion? If so: What is the question? Who are you rendering the opinion to? Why do they want to know (what is the function of the opinion)? As a transactional attorney, you will be called upon to draft agreements but also to advise, negotiate, and educate. However, remember and understand the difference between legal decisions and business or policy decisions. You help with legal decisions, not business or policy decisions (unless specifically asked to do so by your client).

4. *The Parties*. Make sure that the parties to the contract are the parties necessary for the transaction. Make sure you have the parties who can do the deal.

5. *The Deal*. Know what your client and the other parties want to achieve – understand the deal. Find out what communications have occurred with the other party about the proposed deal. Know your client's purpose and any concerns they have about the deal. Again, educate yourself on the nature of the business involved.

B. Drafting or Revising the Agreement Each of the following items should be considered in drafting an agreement from scratch, reviewing an existing agreement for a party to the agreement, and in amending an existing agreement.

1. *Organization*. Make a list of topics to be covered in the contract. This includes topics the parties want to cover, but also legal issues you have identified.

2. *Forms*. Use forms, do not rely on forms, transcend forms. Control of the form is power. Forms and other contract examples can be incredibly helpful but remember that each transaction is unique. Use of a form contract still requires consideration of each provision to ensure that it meets the needs of your particular transaction. If a form or other contract example includes a provision you don't understand or a provision that you are unsure applies in your specific transaction, then consider whether it needs to be included. Research the language and ask other attorneys if they are familiar with the provision and its purpose. Think critically about whether it should be included in your agreement. Don't assume that a provision should be included in your agreement because the provision was included in the form contract you are using. You must make an independent determination about the language's utility and purpose for your specific transaction.

3. *Particularized Agreements*. Generally particularized contracts (partnership agreements, land contracts, etc.) should conform to traditional form.[1] Among the issues that may be involved are the level of dignity and formalities required such as notarization and acknowledgement of the document.

4. *Issues*. Address every issue neither more nor less than once. In many respects inconsistent resolutions of the same issue can be more expensive to the parties than not addressing at all. Remember, when drafting or reviewing an agreement, it is helpful to imagine the parties performing under the agreement from start to finish. You want to identify and address each step of that process. But, address each issue or step in the process only once. Multiple references to a single issue can lead to ambiguity.

5. *Terminology*. To the extent possible use terms that have clear meanings and, if in doubt define them in the agreement. Be careful of using terms that have meanings in particular businesses if you don't understand them and don't be afraid to ask the client to explain the term. Define terms for economy, but make sure you need the definition.

6. *Consequences*. For every promise there should be a consequence for failure to perform. In any agreement you can have general defaults, specific defaults, or a mix of both. General defaults are default procedures that apply to all obligations.

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[1] See, e.g. Adams, A Manual of Style for Contract Drafting, ABA 2004.

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