THE COHEN LAW GROUP
A Professional Corporation

MARK COHEN

JEFFREY D. COHEN, J.D., LL.M., C.P.A.
THE COHEN LAW FIRM, P.C.
Of Counsel

TEN THINGS TO CONSIDER BEFORE SIGNING A CONTRACT

A contract governs the rights and duties of the parties to it. A contract may be oral, but lawyers prefer written contracts to help make certain that the parties agree on the terms of the contract. This article summarizes ten critical things you should consider before signing any contract.

1. Determine the Parties to the Contract

There are two parties to most contracts, often a buyer and a seller. Make sure the contract accurately identifies the parties. A common error is to use the name of a person representing an entity rather than the name of the entity. For instance, if your business is a corporation and is entering into a contract to purchase equipment, make sure the contract identifies the corporation as the purchaser, not you personally. If you sign a contract in your individual capacity, rather than as the representative of the entity, you will be personally "on the hook" and you have lost the limited liability that was likely one of your reasons for forming the entity in the first place. Never blur the distinction between you and the entity you own or represent.

2. Make Sure the Contract Clearly States the Rights and Duties of the Parties

This is the heart of any contract. The contract should specify what each party will do and when they will do it. Many contracts require one party to provide goods or services in return for payment from the other party. A good contract clearly states what goods or services will be provided and when and how the other party will make payment. For instance, if your business contracts with a website design company to build a website, make sure the contract specifies all the features that the website will contain. In many construction contracts, the parties will actually attach or incorporate the specifications and architect's drawings so they become part of the contract. Ambiguity invites disputes. Make sure the contract clearly defines all relevant terms, leaving no room for misunderstanding. An experienced contract attorney can help you identify and clarify ambiguous terms.

3. Determine What Remedies the Contract Contains for Breach of the Contract

People and businesses generally enter into a contract holding a good faith belief

that the other party will uphold its end of the bargain, but sometimes this does not happen. The contract should specify what remedies will be available to the damaged party if the other party breaches the contract. Generally, if one party breaches the contract, the other party is entitled to seek damages and/or a court order directing the other party to perform (specific performance). In some instances, the parties contemplating entering in a contract know that damages may be difficult to determine; in such cases, they sometimes include a "liquidated damages" clause -- a clause that specifies in advance the amount of money damages one party will be entitled to if the other party breaches the contract.

4. Specify How Disputes Will Be Resolved

Disputes may be resolved by mediation, arbitration, or litigation.

Mediation is a non-binding process where the parties try to resolve their dispute with a mediator's help. Typically, each party pays 1/2 of the mediator's fees, so specify that the mediation will last no more than a specified number of hours.

Arbitration is a binding process where the parties tell their stories and the arbitrator makes a ruling. Arbitration can sometimes facilitate a quick decision, but the right to engage in discovery is limited and you may not be able to issue subpoenas or take depositions like you would be able to do if the dispute was being resolved in court. Arbitration often favors "the big guy" over "the little guy" because it limits the ability of "the little guy" to obtain documents he needs from "the big guy" to prove his case, and the up-front costs of arbitration are often greater than those involved in filing suit.

Litigation is just a fancy word for a lawsuit. If a contract anticipates that disputes will be resolved in court, the contract should specify which court will resolve any disputes. To avoid being dragged into court in another state or in a county that is far away, the contract should specify that the exclusive venue for any litigation will be in the county and state in which you reside or where your business has its headquarters.

5. Consider Attorney's Fees and Costs

In Colorado the general rule is the each party to a lawsuit pays its own attorney's fees and costs; however the parties to a contract can alter this rule by agreement. Frequently the parties include a clause that provides that in any litigation the losing party shall pay the prevailing party's attorney's fees and costs.

6. Include a Merger / Integration Clause

The purpose of a contract is to make sure there are no misunderstandings, but what happens when one party claims the other made oral promises not included in the contract. The Parol Evidence Rule prevents a party from contradicting the contract by

use of evidence outside the contract, but the rule only applies if the contract is intended to be the final agreement of the parties, so a contract should contain a clause such as:

> THIS AGREEMENT and any addendums that are signed by an authorized officer or director of the parties, correctly sets forth the final and entire Agreement between the parties. The parties intend this Agreement to be a complete and exclusive statement of their agreement. No Agreement or understandings shall be binding on either of the parties hereto unless specifically set forth in this Agreement, and all prior communications are merged into this Agreement. No modifications of this Agreement shall be binding unless they are in writing and signed by the parties.

7. Make Sure the Contract Cannot Be Assigned Without Your Written Permission

People and businesses enter into contracts with other people and businesses because they trust the other party and believe the other party is able to do the job. But if that other party attempts to assign its rights under the contract to a third party, you may find yourself doing business with an entity you are not familiar with. For this reason, a contract should specify that neither party can assign the contract without the written consent of the other party.

8. Consider Consequential Damages

A party who has been the victim of a breach of contract has the right to seek damages from the breaching party. For instance, one party may seek to make the breaching party pay the costs incurred to repair or complete the work the breaching party was supposed to perform. However, the law also recognizes something called consequential damages, which includes damages such as lost profits. A contract may specify that neither party may seek consequential damages from the other party. Such clauses are common in documents prepared by architects or contractors, for example. Such clauses greatly limit the exposure of the architect or contractor, but may not be in the best interest of the other party.

9. Address When and How the Contract Will Terminate

A good contract should make clear when the contract will terminate. The parties may want the contract to remain in effect until terminated by one party. Or they may want it to terminate on a specific date or upon completion of a specified task or the happening of a certain event. Does the contract allow the parties to terminate the contract at any time, or does it require that the terminating party notify the other party in advance of its decision to terminate the contract? Sometimes a contract will specify that either party can terminate the contract without cause on thirty days written notice to the other party, but that either party can terminate the contract for cause immediately.

These are issues to consider when drafting termination language to be included in a contract.

10. Have an Attorney Review the Contract

An ounce of prevention is worth a pound of cure. We are amazed at the number of clients – even very large businesses – that enter into significant transactions without having a lawyer review the contract. Recently, we represented an organization that entered into a contract for the construction of a 5,000 square foot facility, but the parties were so anxious to complete the project that they did not bother to negotiate a written contract. Predictably, disputes arose after construction began and both parties ended up paying legal fees that were far in excess of what they would have paid to have lawyers draft and review a written contract.

Years ago there was a TV commercial for an automotive repair service that featured a mechanic saying, "You can pay me now or pay me later." His point was that it is cheaper to pay for preventative maintenance than to pay for expensive repairs that would not have been needed if the preventative maintenance had been done in the first place. It is the same in legal profession.