CONTRACT LAW AND THE OIL & GAS ATTORNEY

presented to students in the

Spring 1989
Energy Development: Private Lands Course
University of Tulsa College of Law

18 March 1989
Tulsa, Oklahoma

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B. Oklahoma Statutory Contract Law - "General" Contract Law

1. Much of the basic contract law governing agreements in Oklahoma has a statutory base.

2. The contract law of most states is a product of the "common law." The common law of contract consists of the reported judicial decisions addressing contract principles in the context of a specific dispute.

   a. Typically these decisions are not arranged into any sort of formal code - although they could be if the legislature so desired.

   b. The committees and reporters of the American Law Institute have examined all cases on contract law and attempted to extract from them basic principles of contract law in the form of a "Restatement" of the law of contracts.

      (1) The Restatement (First) of Contracts was published in 1932.

(2) The Restatement (Second) of Contracts was published in 1981.

(3) Although nothing contained in the Restatements is binding upon the courts, it is highly persuasive authority and an excellent research tool.

c. Much of Oklahoma's contract law is "common law" either because the statute does not address the matter or the cases interpret the scope, meaning, and application of the statute.

3. Oklahoma's statutory contract law is patterned after portions of the "Field Code."

a. David Dudley Field, in the nineteenth century, prepared a civil code which many states adopted. For example, California, Georgia, Montana, North Dakota, South Dakota, and Idaho adopted parts of the Field Code.

b. The presence of such statutes requires that they be consulted first when addressing a contract issue. See Sunco Mfg. Co. v. Hargrove, 581 P.2d 925, 928 (Okla. App. 1978) ("The basis of our contract law is statutory although it follows the contours of the common law and evolves like the common law through judicial construction.")

4. Oklahoma statutory definition of a contract and the basic requirements for an enforceable agreement:

a. Okla. Stat. tit. 15, § 1 (1981) defines a "contract" as: "[A]n agreement to do or not to do a certain thing."

b. Okla. Stat. tit. 15, § 2 (1981) lists the requirements for an enforceable contract:

"It is essential to the existence of a contract that there should be:

1. Parties capable of contracting.

2. Their consent.

3. A lawful object; and,

4. Sufficient cause or consideration."

c. See, for example, Smalley v. Bond, 92 Okla. 178, 218 P. 513 (1923), where the court states:

> "To constitute a valid and enforceable contract there should be, first, parties capable of contracting; second, their consent; third, a lawful object; fourth, sufficient cause or consideration, and the consent of parties must be mutual, and consent is not mutual unless the parties agree on the same thing at the same time."

C. Oklahoma Statutory Contract Law - Article 2 of the Uniform Commercial Code ("UCC")

1. Article 2 of the UCC is a special body of contract law which governs certain types of commercial transactions: the sale of "goods."

2. Recognizing that transactions in goods are national in scope, the UCC is an attempt to adopt uniform state law to govern these transactions.

3. Article 2 modifies many of the traditional contract principles.

   a. Generally, under Article 2 many agreements will be enforceable which would be unenforceable under non-UCC law.

   b. Article 2 provides the contracting parties with many unique remedies for a party's nonperformance.

4. Okla. Stat. tit. 12A, § 2-204 (1981) demonstrates the UCC's greater tolerance for creating enforceable agreements:

> "(1) A contract for sale of goods may be made in any manner sufficient to show agreement, including conduct by both parties which recognizes the existence of such a contract.
>
> (2) An agreement sufficient to constitute a contract for sale may be found even though the moment of its making is undetermined.
>
> (3) Even though one or more terms are left open a contract for sale does not fail for indefiniteness if the parties have intended to make a contract and there is a reasonably certain basis for giving an appropriate remedy."

D. Application of Article 2 to Oil and Gas Contracts

1. Definition of "Goods." Okla. Stat. tit. 12A, § 2-105 (1) defines "goods" to mean: "[A]ll things . . . which are movable at the time of identification to the contract for sale . . . ."

   a. This simple definition also demonstrates the interrelationship of the UCC provisions and the need to define a number of terms to decipher its meaning.

   b. For example, what is a "contract," a "contract for sale," or a "sale?" What is "identification?"

   c. § 2-106 (1) defines a "contract" or "agreement" to mean "those relating to the present or future sale of goods. 'Contract for sale' includes both a present sale of goods and a contract to sell goods at a future time."

   d. § 2-106 (1) also provides: "A 'sale' consists in the passing of title from the seller to the buyer for a price . . . ."

   e. To decipher the definition we also need to know what are "future goods." Looking at the index of definitions in § 2-103 we are sent to § 2-105. § 2-105(2) informs us that:

      "Goods must be both existing and identified before any interest in them can pass. Goods which are not both existing and identified are 'future' goods. A purported present sale of future goods or of any interest therein operates as a contract to sell."

   f. What does "identification" mean? § 2-103 (2) tells us to look at § 2-501. § 2-501 states:

      "[I]dentification can be made at any time and in any manner explicitly agreed to by the parties. In the absence of explicit agreement identification occurs

      (a) When the contract is made if it is for the sale of goods already existing and identified;

      (b) if the contract is for the sale of future goods . . . , when goods are

shipped, marked or otherwise designated by the seller as goods to which the contract refers . . . ."

g. The importance of identification is noted in § 2-401 which provides, in part:

"Insofar as situations are not covered by the other provisions of this Article and matters concerning title become material the following rules apply:

(1) Title to goods cannot pass under a contract for sale prior to their identification to the contract (Section 2-501), and unless otherwise explicitly agreed the buyer acquires by their identification a special property as limited by this Act."

See Kinetics Tech. Intern. Corp. v. Fourth Nat. Bank, 705 F.2d 396, 401 (10th Cir. Okla. 1983) (dispute over title to specially manufactured "furnace economizers" that were seized by bank when the bank's debtor, the seller/manufacturer, became insolvent; court holds title to the incomplete goods passed to buyer because they had become identified to the purchase contract and a sale was completed when the first progress payment was made under the purchase contract).

h. Note that § 2-501 and § 2-401 contain another common characteristic: the parties can "explicitly agree" when an event will occur and then provides for the event if the parties fail to address the matter.

DRAFTING NOTE: Whenever a statute provides a standard, such as "explicitly agree," special care must be taken to ensure your selected language meets the standard.

E. Common Oil and Gas Transactions as a "Sale of Goods"

1. As noted in the previous section, "goods" means all things . . . which are movable at the time of identification to the contract for sale . . . ." Okla. Stat. tit. 12A, § 2-105(1) (1981).

2. To determine whether an oil and gas transaction is a sale of goods, and governed by the contract law of UCC Article 2, § 2-107 must be consulted.

§ 2-107 provides:

"(1) A contract for the sale of minerals or the like, including oil and gas . . . is a contract for the sale of goods within this article if they are to be severed by the seller, but until severance, a purported present sale thereof which is not effective as a transfer of an interest in land is effective only as a contract to sell."

The Oklahoma Code Comment to § 2-107 states:

"(1) [M]inerals . . . are treated as realty, unless they are to be severed by the seller. Until severed, however, the agreement is effective only as a contract to sell, and not as a present transfer of property . . . ."

3. EXAMPLE: The typical gas sales agreement is a sale of "goods" governed by Article 2 of the UCC. The gas is "severed by the seller" (the producer) and delivered at a designated point to the purchaser. Although the gas contract may purport to cover all gas produced from specified wells or leases, the usual form of agreement is merely a contract to sell gas when it is actually severed from the ground by production.

   a. For example, in Manchester Pipeline Corp. v. Peoples Natural Gas, 862 F.2d 1439, 1444-45 (10th Cir. Okla. 1988), the court applies Article 2 of the Uniform Commercial Code to determine whether Manchester had entered into a gas sales contract whereby Peoples agreed to take or pay for gas. The court notes:

   "[S]ince the alleged contract related to the sale of natural gas reserves to be severed from the earth by the seller, Oklahoma's codification of the Uniform Commercial Code applies."

   See also Sunflower Elec. Co-op v. Tomlinson Oil Co., 7 Kan.App.2d 131, 638 P.2d 963, 969 (1981) (UCC applies to gas contract which included a dedication of reserves from specified acreage).

   b. In Golsen v. ONG Western, Inc., 756 P.2d 1209, 1220 (Okla. 1988), Justice Kauger, in a concurring opinion, observes: "A contract for delivery of natural gas is recognized as

a sale of goods under the UCC."

c. Contrast a sale of natural gas with a sale of an oil and gas lease. In Casper v. Neubert, 489 F.2d 543 (10th Cir. Okla. 1973), the court, holding that a sale of oil and gas leases is not a sale of "goods," states:

"[S]ince the buyer-lessee has the right to sever, the seller's remedies of the [Uniform] Commercial Code are denied to vendors of oil and gas leases and the Code points to real property law for such protection."

4. Using the code terminology, the gas contract is a "contract for the sale of future goods." The goods (gas) become identified to the contract when they are produced and metered in accordance with the contract.

a. Note that a processing agreement, to the extent there is no sale of the gas or liquids, is a service agreement governed by general contract law instead of the UCC.

b. A sale of oil and gas leases, or similar rights to the oil and gas while in the ground, is not governed by the UCC.

c. A transportation agreement is a service agreement and not governed by the UCC.

d. How will a processing agreement be treated which provides for the processing of gas in return for a share of the liquids? Is it a sale of goods - the liquids? Or is it merely a service agreement where a share of the liquids are being used to pay for the service? Or, is the processor merely using the service as the consideration to purchase liquids?

This type of issue is usually resolved by determining whether the contract is primarily for services or for the sale of goods. See E. Farnsworth, Contracts § 1.10, 33, n.15 (1981).

5. A sale of crude oil, to be severed by the seller, is also governed by Article 2 of the Uniform Commercial Code. Amoco Pipeline Co. v. Admiral Crude Oil Corp., 490 F.2d 114, 116 (10th Cir. N.M. 1974).

F. Classification Of The Transaction

1. Must determine whether the transaction is covered by the UCC to ascertain what law applies to the transaction. If the transaction is a sale of goods, the UCC Article 2 provisions will govern to the extent the issue is addressed by the Code.

2. If the contract concerns a sale of goods, and a provision of Article 2 addresses the issue, you cannot rely upon the statutory or common law applied to non-goods contracts.

   For Example: In Bradford v. Plains Cotton Cooperative Ass'n, 539 F.2d 1249, 1253 (10th Cir. Okla. 1976), the court finds the trial judge erroneously relied upon Oklahoma statutes regulating non-sales transactions to resolve a dispute concerning a contract for the sale of cotton.

3. However, § 1-103 of the UCC provides:

   "Unless displaced by the particular provisions of this Act, the principles of law and equity, including the law of merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions."

   a. In Bradford v. Plains Cotton Cooperative Ass'n the court notes that for a sale of goods the general statutory provisions concerning mutual assent have been replaced by the UCC provisions.

   b. However, many basic contract doctrines are not addressed by the UCC. For Example: The law of third party beneficiary, detrimental reliance, and determining who has the authority to enter into a contract.

G. Oklahoma Statutory Contract Law - Special Rules Governing Certain Types of Agreements

1. In addition to general principles which govern a contractual relationship (UCC if sale of goods; Field Code and common law if not a sale of goods), you must determine whether there are any statutes designed to regulate a certain type of agreement.

a. For example, there may be special statutes that apply when the agreement contains a particular clause - such as an arbitration clause, or an indemnity clause.

b. The statutes may go even further and dictate many of the terms concerning a contract on a particular subject matter - such as insurance.

2. A statute may affect the rights of the contracting parties unless they expressly agree otherwise. For example, consider the Oklahoma Surface Damages Act, Okla. Stat. tit. 52, §§ 318.2 through 318.9 (1981 & Supp. 1988).

H. Conflict Of Laws - Choice Of Law

1. To properly address a contract law problem, you must first determine which jurisdiction's law will be applied to the dispute. Depending upon the nature of the contract, we may be required to apply federal law, state law, Indian law, or the law of a foreign nation.

2. The logical sequence of analysis requires resolution of this issue before considering whether the transaction is governed by the UCC or general contract law.

3. For Example: Assume the Montana Supreme Court has held that a gas processing agreement, where the processor receives a percentage of the liquids as a processing fee, is a service contract governed by general contract law. Assume the Texas Supreme Court has held that such a processing agreement is governed by UCC Article 2. You are negotiating a gas processing agreement in your Houston, Texas office concerning processing of gas to be produced from your wells in the Cedar Creek Anticline in Montana.

You have an opportunity to choose the law most favorable to your position, as well as avoiding a possible battle later on concerning which state's law should apply.

4. Oklahoma's General Contract Choice of Law Rules:

a. Okla. Stat. tit. 15, § 162 (1981) provides:

"A contract is to be interpreted according to the law and usage of the place

where it is to be performed, or, if it does not indicate a place of performance, according to the law and usage of the place where it is made."

b. If the contract does not indicate the "place where it is to be performed" then the court will apply the law of the state where the contract was created.

For Example: In Rhody v. State Farm Mut. Ins. Co., 771 F.2d 1416 (10th Cir. Okla. 1985), the litigation concerned the interpretaion of an insurance policy issued in Texas. The automobile accident giving rise to the claim against the policy occurred in Oklahoma. If Oklahoma law applied, the uninsured motorist coverage would be $30,000 ($10,000 x three insured vehicles); under Texas law, the coverage would be limited to $10,000. In holding that Texas law applied the court states:

"We believe the language of Okla. Stat. tit. 15, § 162 (1971), compels a reading which restricts application of the law of the place of performance of a contract to cases in which the place of performance is indicated in the contract. Appellants' insurance policy does not indicate a place of performance within the meaning of that statute . . . . The policy was issued to appellants in Texas by State Farm's agent in that state. Thus, the laws of the state of Texas, which do not provide for stacking of uninsured motorist coverage, apply to determine State Farm's liability to appellants." Rhody, 771 F.2d at 1420 (emphasis by the court).

c. The place where the contract is "made" is the place where the offer is accepted and the contract comes into existence. Le Flore County Gas and Electric Co. v. Sickmann, 348 P.2d 312, 314-15 (Okla. 1959). If the contract is valid where made, it will be valid everywhere - assuming it will not violate the public policy of the enforcing state.

d. See generally Hamilton v. Telex Corp., 576 P.2d 767, 768 (Okla. 1978) (court notes "the general rule of law is that the law where the

contract is made or entered into governs with respect to its nature, validity, and interpretation."). Court fails to cite Okla. Stat. tit. 15, § 162, but the context of the case indicates the contract was not only "made" but was also "performed" in Oklahoma and the court suggests the contract "provided that Oklahoma law would apply . . . ."

e. The parties can expressly provide in their contract that a certain state's law will apply to the transaction.

(1) This can be done indirectly by indicating the "place of performance" of the contract. Legg v. Midland Savings & Loan Co., 55 Okla. 137, 154 P. 682 (1916) (contract made in Oklahoma, to be performed in Colorado, governed by Colorado law - one qualification to this rule: cannot violate the public policy of the enforcing state).

(2) It can be done directly by stating, in the contract, what state's law will apply. Midland Savings & Loan Co. v. Henderson, 47 Okla. 693, 150 P. 868 (1915) ("The parties having in good faith contracted that the law of Colorado should control, and there being no statute in force in the Indian Territory, forbidding nonresident building and loan companies from transacting business and making loans of the character under review [at a usurious rate under Oklahoma law], the parties must be held to a performance of their respective undertakings."

5. An important exception to being able to designate what state's law will govern your contract: Matters relating to interests and encumbrances on land will usually be governed by the law of the state where the land is located. See, e.g., Webster Drilling Co. v. Walker, 286 F.2d 114, 117 (10th Cir. Okla. 1961).

6. The UCC Choice of Law Rules:

a. Okla. Stat. tit. 12A, § 1-105 (Supp. 1988) provides, in part:

"(1) Except as provided hereafter in

this section [§ (2)], when a transaction bears a reasonable relation to this state and also to another state or nation, the parties may agree that the law of either this state or of such other state or nation shall govern their rights and duties. Failing such agreement, this act applies to transactions bearing an appropriate relation to this state."

b. The UCC "reasonable relation/appropriate relation" conflicts test will apply when the transaction concerns a sale of goods or is otherwise subject to the terms of the UCC.

c. For Example: In Collins Radio Co. of Dallas v. Bell, 623 P.2d 1039 (Okla.App. 1980) (mandate recalled 1981) the court held that a sale of a radio transmitter was a "sale of goods" so the choice of law provisions of the UCC (§ 1-105) would apply instead of Okla. Stat. tit. 15, § 162.

d. The Oklahoma Code Comment indicates:

"The provision providing that this act applies to transactions bearing an 'appropriate relation' to this state is new, and probably changes the law in Oklahoma. The conflicts of law rules heretofore most frequently applied in commercial transactions in Oklahoma may be summarized as follows: All matters bearing upon the execution, interpretation and validity of a contract were determined by the law of the state in which the contract was made. [citations omitted]; but questions of performance were governed by the place of performance, and the remedy was governed by the place where suit was brought."

e. The UCC provision permits the parties to expressly designate the state's law that will apply to their transaction. All that is necessary it that the transaction bear some "reasonable relation" to the state's law that is selected.

(1) § (2) of § 1-105 lists other UCC choice of law provisions which cannot be changed by the parties - such as the law that will apply in determining perfection of a security interest under

Article 9 of the UCC.

(2) UCC Comment 1 indicates:

"Ordinarily the law chosen must be that of a jurisdiction where a significant enough portion of the making or performance of the contract is to occur or occurs."

f. If the parties fail to designate a state's law, the Oklahoma UCC applies to transactions bearing an "appropriate relation" to Oklahoma. UCC Comment 2 states:

"Of course the Act applies to any transaction which takes place in its entirety in a state which has enacted the Act."

g. In Collins Radio Co of Dallas v. Bell, 623 P.2d 1039 (Okla.App. 1980) (mandate recalled 1981), the court applies the "appropriate relation" language to a dispute over whether Texas or Oklahoma law should be applied to interpret the contract. Each state was found to have an "appropriate relation" to the transaction so the court proceeds to determine which of the two states has the "most significant relationship" to the contract. Employing the rules of the Restatement (Second) of Conflict of Laws, the court evaluates the following factors:

(1) The place of contracting;

(2) The place of negotiation;

(3) The place of performance;

(4) The location of the subject matter of the contract; and

(5) The domicile, residence, nationality, place of incorporation and place of business of the parties.

Collins Radio, 623 P.2d at 1047. Restatement (Second) of Conlict of Laws § 188(2), 575 (1971). However, in a sale of goods one of the most significant contacts, under § 191 of the Restatement, is the place of delivery - unless another state has a more significant relationship.

h. Applying the Restatement analysis, the court in Collins Radio notes:

(1) The contract specified that the place of delivery of the radio transmitter would be "the place and location of Collins' factory from which Collins elects to make shipment." Collins Radio, 623 P.2d at 1047.

(2) In this case, delivery was made at Collins' factory in Dallas, Texas. Texas was also the place where the contract was "made."

(3) However, the court holds Oklahoma has more significant contacts with the transaction because the contract was negotiated and performed in Oklahoma, the subject matter of the contract - the transmitter, was located in Oklahoma, and the dispute concerned warranties which were orally made in Oklahoma. The contract also contemplated a continuing relationship between the parties - as opposed to a one-time sale at a fortuitous location. Collins Radio, 623 P.2d at 1048.

(4) Since the court finds that Oklahoma law applies, the plaintiff cannot seek treble damages under the Texas Deceptive Trade Practices and Consumer Protection Act. Collins Radio, 623 P.2d at 1048.

II. CONTRACT FORMATION - REQUIREMENTS FOR AN ENFORCEABLE AGREEMENT

A. Mutual Assent - The Parties Must "Agree"

1. Have the parties expressed an intent to be presently bound to an agreement?

2. To have an enforceable agreement the parties must agree on something. This agreement is referred to as "mutual assent."

a. The presence of mutual assent is typically determined by examining the objective (outward) manifestations of each party.

b. To evaluate whether mutual assent is present, the analytical process of offer and

acceptance is employed. If there has been an "offer," followed by an "acceptance," there is mutual assent.

3. The Offer - Would a reasonable person conclude, from your actions, that you presently desire to enter into an agreement? If so, an "offer" has been made that creates a "power of acceptance" in the person to whom the offer is directed.

4. The Acceptance - Would a reasonable person, in the position of the party who made the offer, conclude, from your actions, that you have accepted the offer? If so, an enforceable agreement is formed - assuming the other requirements for a contract are satisfied.

5. Since the outward (objective) actions of each party govern whether an offer has been made, or accepted, an enforceable agreement may be created even though a party may not actually intend to make an offer, or exercise a power of acceptance. Their subjective intention is generally irrelevant.

6. The Oklahoma statutes employ different terminology regarding offer and acceptance.

   a. Mutual Assent or "Consent." Okla. Stat. tit. 15, § 66 (1981) provides:

      "Consent is not mutual unless the parties all agree upon the same thing in the same sense. But in certain cases, defined by the article on interpretation, they are to be deemed so to agree without regard to the fact."

   b. The Offer or "Proposal." Okla. Stat. tit. 15, § 67 (1981):

      "Consent can be communicated with effect, only by some act or omission of the party contracting, by which he intends to communicate it, or which necessarily tends to such communication."

   c. Acceptance. Okla. Stat. tit. 15, § 69 (1981):

      "Consent is deemed to be fully communicated between the parties as soon as the party accepting a proposal has put his

acceptance in the course of transmission to the proposer . . . ."

B. The Basic Goal

1. During the pre-contract phase, the major goal is be to control all outward manifestations so that a clear signal is sent to the other party regarding your intentions.

2. Ideally, you should be able to examine a transaction at any stage and clearly identify if you have made or accepted any offers or are merely engaged in preliminary negotiations.

3. The major obstacle to obtaining our goal is the informal process by which a contract can be created. As noted by the court in Fry v. Foster, 65 P. 1224 (1937): "An agreement which constitutes a contract may come into existence by means of informal communications between the parties."

   a. Usually these "informal communications" are made by the non-laywers of an organization.

   b. The UCC has made the process even more informal - increasing the instances in which a contract can be formed. See, e.g., Apex Oil Co. v. Vanguard Oil & Service Co. Inc., 760 F.2d 417 (2d Cir. N.Y. 1985) (million dollar fuel oil sale created by telephone call and subsequent confirmation by telex).

   c. In keeping with the objective theory of contracts, a party's conduct may result in a contract. As the court notes in Queen Anne Candy Co. v. Eagle, 88 P.2d 630, 632 (Okla. 1939):

      "'In determining the question of the existence of a contract, the court will consider the acts, conduct, and statements of the parties as a whole . . . ."

   d. In Bradford v. Plains Cotton Cooperative Ass'n, 539 F.2d 1249, 1253 (10th Cir. Okla. 1976) the court notes: "The Code [Article 2 of the UCC] rejects the subjective test of intent to contract and replaces it with mutuality of assent as manifested by the conduct of the parties."

C. Analysis of the Offer

1. Restatement (Second) of Contracts, § 24 (1981) provides:

"An offer is the manifestation of willingness to enter into a bargain, so made as to justify another person in understanding that his assent to that bargain is invited and will conclude it."

The Restatement defines the term "bargain" to mean "an agreement to exchange promises or to exchange a promise for a performance or to exchange performances." Restatement (Second) of Contracts § 3.

2. If you don't intend to make an offer, but rather are merely probing the contours of a possible deal with the other person, you are involved in "preliminary negotiations." The Restatement (Second) of Contracts § 26 provides:

"A manifestation of willingness to enter into a bargain is not an offer if the person to whom it is addressed knows or has reason to know that the person making it does not intend to conclude a bargain until he has made a further manifestation of assent."

a. If you do not intend to make at offer, you should ensure that all correspondence and contact with the other party is such that they "know" or have "reason to know" that you do not intend to currently create a contract.

b. Language and labels are not necessarily determinative.

c. If you don't intend to presently make an offer, in your correspondence consider using language similar to the following:

"These are only my preliminary thoughts on the matter; this letter is not intended to create any sort of present offer to contract."

3. A common technique to try and control the contract formation process is to solicit an offer from the other party and then control the process by which you accept the offer. One way to do this is with a "management approval" or "home office approval" clause.

a. For Example: In Truscon Steel Co. v. Cooke, 98 F.2d 905 (10th Cir. Okla. 1938), Truscon had submitted a bid to Cooke in which Truscon proposed to provide steel to Cooke. The bid contained the following statement:

"Prompt acceptance of this quotation by you and the written approval of our Home Office shall constitute a binding contract."

Cooke promptly "accepted" the quotation - however, a contract was not formed. Instead, Cooke had made an offer to Truscon.

b. Note that there is a danger for Truscon as well as Cooke in this situation - Cooke can change his mind anytime prior to Truscon's acceptance by the written approval of its' home office.

4. In some situations, you may need to engage in formal written negotiations prior to making an offer. Usually a document titled "Letter of Intent" is used for this purpose.

a. The letter of intent is typically used to work out the details of a proposal before either party agrees to be bound.

b. The letter may also be necessary to get third parties to take preliminary action necessary to the consumation of a contract. For example, a letter of intent may be used to prompt a bank to consider whether it will finance a particular transaction being negotiated.

c. The letter of intent should clearly indicate that the parties are not bound by the terms of the letter. Typically this is expressed by requiring some subsequent act to indicate assent - such as a "formal written agreement" signed by all parties.

5. It is common to encounter language which says that the agreement of the parties is "subject to a formal written agreement" or "our attorney preparing the necessary papers." The problem is determining whether the parties:

a. Intend to be presently bound, but with the obligation to state their agreement in some

formal manner; or

b. Intend that no binding agreement will arise unless and until the required agreement is prepared and signed by the parties.

6. The Restatement (Second) of Contracts § 27 provides:

"Manifestations of assent that are in themselves sufficient to conclude a contract will not be prevented from so operating by the fact that the parties also manifest an intention to prepare and adopt a written memorial thereof; but the circumstances may show that the agreements are preliminary negotiations."

a. The parties may have come to agreement on many facets of a deal - either by oral agreement or an exchange of correspondence or letters of intent. Often the deal breaks down before the final documents are signed. The party feeling they had negotated a good deal may assert one or more contracts arose through such oral and written communications - and that a final written agreement was merely one of the covenants of the deal as opposed to a condition to the formation of a contract.

b. To avoid this situation, the negotiating parties should expressly agree that they intend to be bound only upon the execution of a formal written agreement by the parties.

7. In Pierce Petroleum Corporation v. Hales, 294 P. 160 (Okla. 1930), an agent for Pierce Petroleum entered into an oral agreement to purchase oil from Hales for a specified amount and duration. However, the formal written contract had not been signed by the president of Pierce Petroleum. Pierce Petroleum's president never signed the written contract and asserts Hales "offer" was never accepted.

a. The court notes the general rules, stating:

"'Where parties to an agreement make its reduction to writing and signing a condition precedent to its completion, it will not be a contract until this is done, and this is true although all the terms of the contract have been agreed upon. But where parties have

assented to all the terms of the contract, and they are fully understood in the same way by each of them, the mere reference in conjunction therewith of a future contract in writing will not negative the existence of a present contract.'"

b. The court finds, in this case, a contract came into existence when the oral agreement was made and the writing was not a condition to the formation of a contract.

c. NOTE - since the contract had a duration in excess of one year there was a statute of frauds problem. However, the writing requirement was satisfied by a letter from (and signed by) the company's purchasing agent to the company's president describing the terms of the oral deal he made with Hale.

8. Revocation of an Offer

a. Suppose an offer has been made, the other party (the offeree) has not accepted, and you would like to change your mind and extinguish the power of acceptance you have created in the offeree.

b. Okla. Stat. tit. 15, § 73 (1981) provides:

"A proposal is revoked:

1. By the communication of notice of revocation by the proposer to the other party, before his acceptance has been communicated to the former.

2. By the lapse of the time prescribed in such proposal for its acceptance, or if no time is so prescribed the lapse of a reasonable time without communication of the acceptance.

3. By the failure of the acceptor to fulfill a condition precedent to acceptance; or,

4. By the death or insanity of the proposer."

c. The Restatement (Second) of Contracts § 36 generally follows the Oklahoma statutory provisions:

"(1) An offeree's power of acceptance may be terminated by

(a) rejection or counter-offer by the offeree, or

(b) lapse of time, or

(c) revocation by the offeror, or

(d) death or insanity of the offeror or offeree.

(2) In addition, an offeree's power of acceptance is terminated by the non-occurrence of any condition of acceptance under the terms of the offer."

NOTE: The effect of the death or insanity of the offeree is not addressed by the Oklahoma statute.

9. Rejection occurs when the offeree manifests an intent not to accept the offer to the offeror.

   a. Restatement (Second) of Contracts § 38 provides:

   "(1) An offeree's power of acceptance is terminated by his rejection of the offer, unless the offeror has manifested a contrary intention.

   (2) A manifestation of intention not to accept an offer is a rejection unless the offeree manifests an intention to take it under further advisement."

   b. The most common form of a rejection is the counter-offer.

10. If the reply purports to be an acceptance, but conditions acceptance upon terms differing from the offer, the power of acceptance terminates.

   a. The counter-offer operates as a rejection of the original offer. Note, however, the original offeree's purported acceptance may create a power of acceptance in the original offeror with regard to the counter-proposal.

   b. Okla. Stat. tit. 15, § 71 (1981) provides:

"An acceptance must be absolute and unqualified . . . . A qualified acceptance is a new proposal."

c. If the offeree wants to continue negotiations, while keeping the existing offer alive, they may respond stating: "I am still considering your offer. However, if you would be interested in accepting $1.55/MCF we could conclude a deal right now."

11. If the offer states a specific time in which to accept the offer, it will terminate once the specified time has lapsed. If no time is specified, the offer will terminate after a reasonable time has passed.

a. § 41(2) of the Restatement (Second) of Contracts states:

"(2) What is a reasonable time is a question of fact, depending on all the circumstances existing when the offer and attempted acceptance are made."

b. Comment b. to § 41 indicates some of the circumstances which can influence what is a reasonable time:

"[T]he nature of the proposed contract, the purposes of the parties, the course of dealing between them, and any relevant usages of trade. In general, the question is what time would be thought satisfactory to the offeror by a reasonable man in the position of the offeree . . . ."

12. In any event, the offeror controls the terms of the offer and can create whatever conditions deemed appropriate to maintain control over the mutual assent process.

a. For example, the offeror may specify a particular mode of acceptance, such as personal notification to the offeror. The offer can make acceptance effective only upon actual receipt of a written notice of acceptance.

b. Okla. Stat. tit. 15, § 68 (1981) provides:

"If a proposal prescribes any conditions

concerning communication of its acceptance, the proposer is not bound unless they are conformed to; but in other cases any reasonable and usual mode may be adopted."

D. Analysis Of The Acceptance

1. Restatement (Second) of Contracts § 50 provides:

"(1) Acceptance of an offer is a manifestation of assent to the terms thereof made by the offeree in a manner invited or required by the offer.

(2) Acceptance by performance requires that at least part of what the offer requests be performed or tendered and includes acceptance by a performance which operates as a return promise.

(3) Acceptance by a promise requires that the offeree complete every act essential to the making of the promise."

2. Okla. Stat. tit. 15, § 67 (1981) provides:

"Consent can be communicated with effect, only by some act or omission of the party contracting, by which he intends to communicate it, or which necessarily tends to such communication."

3. Okla. Stat. tit. 15, § 68 (1981) provides:

"If a proposal prescribes any conditions concerning the communication of its acceptance, the proposer is not bound unless they are conformed to; but in other cases any reasonable and usual mode may be adopted."

4. Okla. Stat. tit. 15, § 71 (1981) provides:

"An acceptance must be absolute and unqualified, or must include in itself an acceptance of that character, which the proposer can separate from the rest, and which will include the person accepting. A qualified acceptance is a new proposal."

5. By statute in Oklahoma, acceptance is deemed to be "communicated to the proposer" "as soon as the party accepting a proposal has put his acceptance in the course of transmission to the proposer . . . " Okla. Stat. tit. 15, § 69 (1981).

Therefore, if a reply by mail is an authorized

means of accepting an offer, the acceptance becomes effective upon properly depositing the acceptance in the mail.

6. The requirement that the acceptance conform exactly to the terms of the offer is known as the "mirror image rule."

7. If the object of the transaction is a sale of goods, Okla. Stat. tit. 12A, § 2-207 (1981), alters the mirror image rule by providing:

"(1) A definite and seasonable expression of acceptance . . . operates as an acceptance even though it states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms.

(2) The additional terms are to be construed as proposals for addition to the contract. Between merchants such terms become part of the contract unless:

(a) the offer expressly limits acceptance to the terms of the offer;

(b) they materially alter it; or

(c) notification of objection to them has already been given or is given within a reasonable time after notice of them is received.

(3) Conduct of both parties which recognizes the existence of a contract is sufficient to establish a contract for sale although the writings of the parties do not otherwise establish a contract. In such case the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of this act.

a. § 2-207 was designed to combat the "battle of the forms" where buyers and sellers send their form documents back and forth without ever reading them until a dispute arises.

b. The goal of § 2-207 is to provide fair contract terms when the parties act as though they have a contract but their writings do not agree.

E. Formalities

1. Although a contract can be created through the very informal process of offer and acceptance, the law may impose certain formalities in order to successfully enforce your contract.

2. The most common formality is that certain contracts, falling within the "statute of frauds," be in writing.

3. Okla. Stat. tit. 15, § 136 (1981) provides:

> "The following contracts are invalid, unless the same, or some note or memorandum thereof, be in writing and subscribed by the party to be charged, or by his agent:
>
> 1. An agreement that, by its terms, is not to be performed within a year from the making thereof.
>
> 2. A special promise to answer for the debt, default or miscarriage of another, except in the cases provided for in the article on guaranty.
>
> 3. An agreement made upon consideration of marriage, other than a mutual promise to marry.
>
> 4. Repealed.
>
> 5. An agreement for the leasing for a longer period than one (1) year, or for the sale of real property, or of an interest therein; and such agreement, if made by an agent of the party sought to be charged, is invalid, unless the authority of the agent be in writing, subscribed by the party sought to be charged."

4. If the transaction is a sale of goods, the UCC statute of frauds applies. Okla. Stat. tit. 12A, § 2-201 (1981) provides, in part:

> "(1) Except as otherwise provided in this section a contract for the sale of goods for the price of Five Hundred Dollars ($500.00) or more is not enforceable by way of action or defense unless there is some writing sufficient to indicate that a contract for sale has been made between the parties and signed by the party against whom enforcement is sought or by his authorized agent or broker. A writing is not insufficient because it omits or incorrectly states a term agreed upon

but the contract is not enforceable under this paragraph beyond the quantity of goods shown in such writing.

(2) Between merchants if within a reasonable time a writing in confirmation of the contract and sufficient against the sender is received and the party receiving it has reason to know its contents, it satisfies the requirements of subsection (1) against such party unless written notice of objection to its contents is given within ten (10) days after it is received."

F. Detrimental Reliance

1. In certain situations, although you do not have all the formal requisites for an enforceable agreement, equitable considerations will protect you from loss. See generally Frey and Long, "Detrimental Reliance On A Promise (Promissory Estoppel) In Oklahoma," 52 Okla. B. J. 409 (1981).

2. The Restatement (Second) of Contracts § 90 provides, in part:

"(1) A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise. The remedy granted for breach may be limited as justice requires."

III. CONTRACT FORMATION EXERCISE

Assume The Following Facts:

Acme Oil Company discovered and developed the Manchester Field in Grant County, Oklahoma. In 1983, Acme had completed four wells in the field and began contacting natural gas purchasers to discuss a possible sale.

In November 1983 Acme began negotiations with Oklahoma Pipeline Company ("OPC") concerning a gas purchase agreement. Acme and OPC representatives met on numerous occasions. OPC provided Acme with sample gas purchase contracts for Acme's review.

In April 1984, Acme's gas sales representative [Mary] met with OPC's gas purchase representative [Tom]. Sometimes Tom would tell prospective gas sellers that

any offer he made was subject to OPC management approval. Tom's superiors knew about Tom's negotiations with Mary. Tom's superiors will testify that Tom had no actual authority to execute documents on behalf of OPC. Mary will testify that Tom told her he had authority to negotiate contracts - but he didn't imply that he had authority to sign contracts.

On May 14, 1984 Tom sent Mary a letter "offering" to purchase natural gas from the Manchester Field at $2.65 per MMBtu for 20 years.

The parties continued to negotiate during the following months. On three occasions, Tom sent Mary a single copy of a sample gas purchase contract. Each of these were stamped "DRAFT" in red ink.

On September 12, 1984 Tom sent Mary three copies of a document titled "Gas Purchase Contract" covering Acme's wells in the Manchester Field. This was not marked as a draft. The documents provided for a 10 year term and contained detailed price and take-or-pay provisions. These copies were forwarded with a letter from Tom stating:

> Enclosed for your review and approval, please find three copies of our Gas Purchase Contract covering acreage referenced above.
>
> If you find this Contract acceptable, please fully execute all three copies, (including notary pages) and return to this office. Following OPC's execution, one completed Contract will be forwarded to you.

The presidnet of OPC will testify that it would not be normal OPC procedure to send out a contract for a gas producer to sign unless OPC management found the terms of the contract acceptable.

On September 18, 1984 the vice president of Acme executed the contracts and returned them to Tom.

OPC never executed the contracts and denies that they have any sort of agreement with Acme. OPC's president will testify that it decided not to enter into the contract because it had lost one of its largest industrial customers and the gas market was becoming soft.

Acme sues OPC seeking $1,450,000 in damages arising from OPC's refusal to honor the gas purchase agreement.

IS THERE A CONTRACT?

WHAT STATE'S LAW SHOULD BE APPLIED TO EVALUATE THIS DISPUTE?

ASSUMING OKLAHOMA LAW WILL APPLY, WHAT CONTRACT LAW SHOULD BE APPLIED TO EVALUATE THIS DISPUTE?

WHAT ARGUMENTS WOULD YOU MAKE ON BEHALF OF OPC THAT A CONTRACT WAS NEVER CREATED?

WHAT ARGUMENTS WOULD YOU MAKE ON BEHALF OF ACME?

IF YOU FIND THAT A CONTRACT WAS NEVER CREATED, WILL ACME STILL BE ENTITLED TO SOME SORT OF RELIEF?

HOW COULD OPC HAVE AVOIDED THIS DISPUTE?

See Manchester Pipeline Corp. v. Peoples Natural Gas, 862 F.2d 1439 (10th Cir. Okla. 1988) (court holds Acme and OPC had a contract; Acme recovered $1,450,000 in damages for OPC's breach).

How can we determine the authority of Tom? See Section IV. below.

IV. CAPACITY TO CONTRACT

A. Legal Capacity

1. As noted in Section I, to have an enforceable agreement the parties to the agreement must have the legal "capacity" to contract. In Oklahoma you must have "parties capable of contracting." Okla. Stat. tit. 15, § 2 (1981).

2. Although the Restatement and the Oklahoma statutes focus on capacity problems with minors and the mentally ill, most issues encountered in the business world concern whether the individual we are negotiating with has the power to make and accept offers to contract.

3. If the person is contracting in their individual capacity, then we only need to concern ourselves with whether they are a minor or mentally ill. See Okla. Stat. tit. 15, § 11 and § 12 (1981).

   a. In Oklahoma a minor is a person under 18 years of age. Okla. Stat. tit. 15, § 13 (1981).

b. The statutes provide certain exceptions to the incapacity of minors and the mentally ill. Generally, their contracts are only voidable at their election.

c. As with any other situation, you always need to ensure that the party you are dealing with (whether as an individual or as an agent or employee) has the authority to contract with regard to the subject matter of the contract.

4. In most situations the person you are contracting with is acting in some sort of representative capacity - such as an employee of a corporation, partnership, joint venture, a trustee, administrator or executor of an estate, federal, state, or local government representative, an "attorney in fact" operating under a power of attorney, or perhaps an operator of a well.

a. In these situations you need to ascertain whether they can properly act on behalf of the entity or person they purport to represent.

b. We also need to define the scope of their authority.

B. Transactions With Agents: The Corporate Example

1. All the business of a corporation is transacted by its agents. The key is to ensure the agent you are dealing with has the authority to bind the corporation to the agreement.

2. Autority to bind the corporation can come from one of three general sources:

a. Express Authority. The corporation expressly confers authority on a corporate officer or a designated person to take certain action. Express authority may arise from statute, the certificate of incorporation, the corporate bylaws, a resolution of the board of directors, or other written authority.

b. Implied or Incidental Authority. This would include all authority that may be necessary, usual, and proper to exercise the agent's express authority. Implied authority may also arise from a course of conduct whereby the corporation permits its agent to act in a certain manner.

c. Apparent Authority - Estoppel. As stated in 18B AmJur2d § 1526 (1985):

"[W]hen, in the usual course of the business of a corporation, an officer or other agent is held out by the corporation or has been permitted to act for it or manage its affairs in such a way as to justify third persons who deal with him in inferring or assuming that he is doing an act or making a contract within the scope of his authority, the corporation is bound thereby, even though such officer or agent has not the actual authority from the corporation to do such an act of make such a contract."

"Stating the rule in terms of estoppel, a corporation that, by its voluntary act, places an officer or agent in such a position or situation that persons of ordinary prudence, conversant with business usages and the nature of the particular business, are justified in assuming that he has authority to perform the act in question and deal with him upon that assumption, is estopped as against such persons from denying the officer's or agent's authority."

3. The first place to look for "authority" to act is in the Oklahoma General Corporation Act, Okla. Stat. tit. 18, §§ 1001 - 1155 (Supp. 1988).

4. Okla. Stat. tit. 18, § 1006 (Supp. 1988) provides:

"B. . . . the certificate of incorporation may also contain any or all of the following matters:

1. Any provision for the management of the business and for the conduct of the affairs of the corporation, and any provision creating, defining, limiting and regulating the powers of the corporation, the directors, and the shareholders, or any class of the shareholders . . . .

C. It shall not be necessary to set forth in the certificate of incorporation any of the powers conferred on corporations by the provisions of the Oklahoma General Corporation Act."

a. The General Corporation Act makes the certificate of incorporation the paramount document governing the management of the

corporation.

b. Usually, however, the details of corporate management will be specified in the bylaws.

5. Okla. Stat. tit. 18, § 1013 (Supp. 1988) provides:

"B. The bylaws may contain any provision, not inconsistent with law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its shareholders, directors, officers or employees."

a. For Example: In East Cent. Okl. Elect. Coop., Inc. v. Oklahoma G. & E. Co., 505 P.2d 1423 (Okla. 1973), the court notes that the bylaws of the Electric Cooperative provided:

"'[T]he Board of Trustees may authorize any officer or officers, agent or agents, to enter into any contract or execute and deliver any instrument in the name and on behalf of the Cooperative, and such authority may be general or confined to specific instances.'"

b. Usually the bylaw provision would be followed up by specific documents specifying what the officers and agents can do. Typically this will be through a resolution, specific statement in the bylaws, a power of attorney, or other oral or written communication.

6. Okla. Stat. tit. 18, § 1016 (Supp. 1988) provides:

"Every corporation . . . shall have power to:
. . . . 13. Make contracts . . . ."

7. Okla. Stat. tit. 18, § 1015 (Supp. 1988) provides:

"In addition to the powers enumerated in . . . [§ 1016] of this act, every corporation, its officers, directors and shareholders shall possess and may exercise all the powers and privileges granted by the provisions of the Oklahoma General Corporation Act or by any other law or by its certificate of incorporation, together with any powers incidental thereto, so far as such powers and privileges are necessary or convenient to the conduct, promotion or attainment of the business or purposes set forth in its certificate of incorporation."

8. Okla. Stat. tit. 18, § 1027 (Supp. 1988) delegates all corporate authority to the board of directors. § 1027 A. provides:

"The business and affairs of every corporation organized in accordance with the . . . Act shall be managed by or under the direction of a board of directors, except as may be otherwise provided for in the . . . Act or in its certificate of incorporation."

9. Okla. Stat. tit. 18, § 1028 (Supp. 1988) suggests the proper way to confer authority on an officer is through the bylaws or by a resolution of the board of directors which is "not inconsistent" with the bylaws.

10. Special statutes may address particular types of transaction.

    a. For Example: Any instrument "affecting real estate or authorizing the execution of any deed, mortgage or other instrument relating thereto" must follow the rules stated in Okla. Stat. tit. 16, §§ 91-95 (1981 and Supp. 1988).

    b. § 92 provides that any instrument affecting real estate that is executed and acknowledged in accordance with §§ 93-95 "shall be valid and binding upon the grantor, notwithstanding any omission or irregularilty in the proceedings of such corporation or any of its officers or members, and without reference to any provision in its constitution [certificate of incorporation] or bylaws."

    c. § 93 requires that the name of the corporation be "subscribed" to the document by an "attorney in fact or by the president or any vice-president of such corporation . . . ."

    d. § 94 requires that when the document is being signed by the president or vice-president, it must be "attested" by the "Secretary, assistant secretary or clerk of such corporation, with the corporate seal attached."

    e. § 95 requires that the signature of the officer or attorney in fact be "acknowledged" and provides a suggested acknowledgment form.

V. CORPORATE CAPACITY TO CONTRACT EXERCISE

Assume The Following Facts:

United States Carpet Mills, Inc. (Carpet Mills) wants to build a new plant on land near Bristow, Oklahoma. Carpet Mills negotiated with Oklahoma Gas & Electric Company (OGE) and East Central Oklahoma Electric Cooperative, Inc. (East Central) regarding electrical service.

The assistant manager (Mary) for East Central had been given general authority by its board of trustees [directors] to enter into new commercial electrical service contracts. Prior to August 1, 1969 the board and the general manager of East Central expressly authorized Mary to negotiate an electrical service agreement with Carpet Mills.

On August 1, 1969 Mary called the president of Carpet Mills to make an offer regarding electrical service. The president of Carpet Mills accepted Mary's offer.

On August 7, 1969 a written contract concerning the electrical service was signed by the president of Carpet Mills and the president and assistant manager of East Central.

On August 11, 1969 the Board of Trustees for East Central ratified the contract.

On August 4, 1969 the land on which the Carpet Mills plant was being built was annexed by the City of Bristow.

OGE seeks an injunction to prohibit East Central from providing electrical service to Carpet Mills because OGE has an exclusive franchise to serve all customers within the city limits of Bristow. However, if Carpet Mills and East Central had a service contract in place before the plant became part of the city [August 4, 1969], then OGE's exclusive franchise will not apply.

IS THERE A CONTRACT?

WHEN WAS IT FORMED?

ASSUMING OKLAHOMA LAW WILL APPLY, WHAT CONTRACT LAW SHOULD BE APPLIED TO EVALUATE THIS DISPUTE? DOES IT MATTER WHETHER THE CODE APPLIES IN RESOLVING THIS CAPACITY DISPUTE?

HOW COULD EAST CENTRAL HAVE AVOIDED THIS DISPUTE?

See East Cent. Okl. Elec. Coop., Inc. v. Oklahoma G. & E. Co., 505 P.2d 1324 (Okla. 1973) (the assistant manager had authority to enter into the oral contract so the East Central contract was in existence prior to the annexation).

A. General Observations By The Court In East Central Regarding Capacity To Contract

1. "A corporation is an artificial person, which of necessity must act by and through its agents."

2. "Unless he [the assistant manager] is expressly restricted to the performance of certain specified acts, he may do anything which naturally and ordinarily has to be done to carry our the paramount purpose of the corporation."

3. "Except where it is required by statute or by the articles of incorporation or by-laws of the corporation that the authority of an officer or agent must be conferred in a particular manner, authority to make a particular contract need not necessarily be expressed, but may be inferred from the facts and circumstances of the particular case, as from a course of conduct or dealing by the corporation with its officers and agents."

4. "[A] corporation acting within the scope of its legitimate purpose may make, and be bound by its parol contracts to the same extent as an individual."

B. Observations By The Court Regarding Formation Of The Contract

1. "The fact that the parties may have contemplated the subsequent formal execution of the contract does not necessarily imply that they have not already bound themselves to a definite and enforceable contract the terms of which could only be altered by mutual assent."

2. "Ordinarily nothing after acceptance is required to make a contract effective. The act of acceptance closes the contract. No formalities are required. It is sufficient if in the course of the transaction the party to be charged in some writing signed by him or his duly authorized agent recognized or ratifies an agreement sufficiently explicit in terms . . . ."

VI. INTRODUCTION TO LEGAL DRAFTING

A. Demystifying Legal Writing

1. For centuries clients have been subjected to the mystical writings of their attorneys. Contracts, deeds, pleadings, wills, statutes, regulations, and any other "legal" document bore the mark of the lawyer's craft.

2. However, during the past two decades the "craft" has been exposed as an inherent weakness in legal writing - and legal thought.

   a. The ultimate test of your work is often litigation. Usually this means, regardless of the outcome, you failed your drafting task.

   b. However, drafting by the attorney can only be as durable as the foresight of the attorney and their client. Many times a defective drafting process eliminates or reduces the opportunity for exercising foresight.

3. The reformist movement in legal writing has a single basic goal: To communicate - using clear, concise, and plain English in a workable format.

4. Pursuit of communication as a goal has a number of ancillary benefits.

   a. It elevates communication above form and tradition.

   b. It forces attorneys to evaluate problems more carefully to decide what language is required to address the situation.

   c. It requires a reevaluation of the tautology of the law to define what it means and then evaluate if it is necessary.

   d. It provides the client with a more active and meaningful role in the drafting process.

   e. It permits the client to assume greater responsiblity for the finished product since they should understand what is being said in the document.

   f. It forces a more demanding review of the drafting task which should result in better

analysis of the task and a better product.

g. All of this should result in reduced litigation and increased client satisfaction.

5. My approach to demystifying the drafting process:

a. First, we identify the problem by evaluating common examples of traditional legal writing. (The Problem)

b. Second, we address language problems identified in the first step. This will provide us with the basic building blocks for expressing ourselves in the remaining steps of the process. (Language)

c. Third, we define the basic legal requirements for forming the relationship the document will create. (Validation)

d. Fourth, we design the structure of the document. (Design)

e. Fifth, we evaluate, with our client, what the document should address and how it will be used. (Content Planning)

f. Sixth, we write, striving to express the relationship in clear, concise, and plain English. (Draft)

g. Seventh, we evaluate the document, with our client, to identify problems and rewrite. (Edit)

B. A Critical Analysis of Legal Writing (The Problem)

1. A major contributor to poor legal writing is the drafter's failure to adequately think about the writing portion of their drafting task.

a. This lack of thought is often promoted by the use of forms to <u>begin</u> a drafting task. Often the drafting process is associated with the selection of the proper form.

b. Nothing is wrong with using forms - where they come from, and how you use them, determine whether the form will aid or sabotage your drafting.

(1) Too often the form is used to initiate

the drafting process - and in effect becomes the drafting process. Not surprisingly, the finished product often looks very similar to the selected form.

(2) Too often the contents of the form are not understood. Why did the person who prepared the form use a clause, sentence, phrase, or word? Until these questions are answered, the form cannot be properly evaluated.

(3) Forms should be used at the end of the drafting process - once you fully understand the legal and factual requirements of the transaction and have selected your language to express the transaction.

(4) You will be able to compile and use your forms as you address each problem. The significant difference, with your own form, is you should have thought through each of its terms (at least once) and know their effect.

2. The most common problem with legal writing is the use of meaningless language which clogs the document with unnecessary words.

   a. Basic goal - omit all unnecessary words, phrases, sentences, and sections.

   b. Stray language obstructs understanding of the working language and creates an opportunity for ambiguity. With ambiguity comes the minefield of judicial interpretation and construction.

3. The common law baggage:

   a. England had several legal languages during its history. This resulted in using words from each of several languages in legal documents. For example, documents may contain strings of words which have a Celtic, Latin, Anglo-Saxon, and French origin.

   b. The tendency in America has been to adopt the English practice of using a string of similar words to express a single concept.

   c. Thomas Jefferson observed that American

lawyers drafting statutes followed the old English style of "making every other word a 'said' or 'aforesaid,' and saying everything over two or three times, so that nobody but we of the craft can untwist the diction and find out what it means . . . ."

d. For example:

(1) "If lessee fails to pay delay rental when due, this lease shall be totally null and void and of no further force and effect whatsoever."

(2) Consider this alternative:

"If lessee fails to pay delay rental when due the lease terminates."

4. For an example of how entrenched the old English style has become in America consider the Texas statutory deed form found at Tex. Property Code Ann. § 5.022 (Vernon 1984):

§ 5.022. Form

(a) The following form or a form that is the same in substance conveys a fee simple estate in real property with a covenant of general warranty:

"The State of Texas,

"County of _____

"Know all men by these presents, That I, _____, of the _____ (give name of city, town, or county), in the state aforesaid, for and in consideration of _____ dollars, to me in hand paid by _____, have granted, sold, and conveyed, and by these presents do grant, sell, and convey unto the said _____, of the _____ (give name of city, town, or county), in the state of _____, all that certain _____ (describe the premises). To have and to hold the above described premises, together with all and singular the rights and appurtenances thereto in any wise belonging, unto the said _____, his heirs or assigns forever. And I do hereby bind myself, my heirs, executors, and administrators to warrant and forever defend all and singular the said premises unto the said _____, his heirs, and assigns, against every person whomsoever, lawfully claiming or to claim the same, or any part thereof.

"Witness my hand, this _____ day of _____, A.D. 19__.

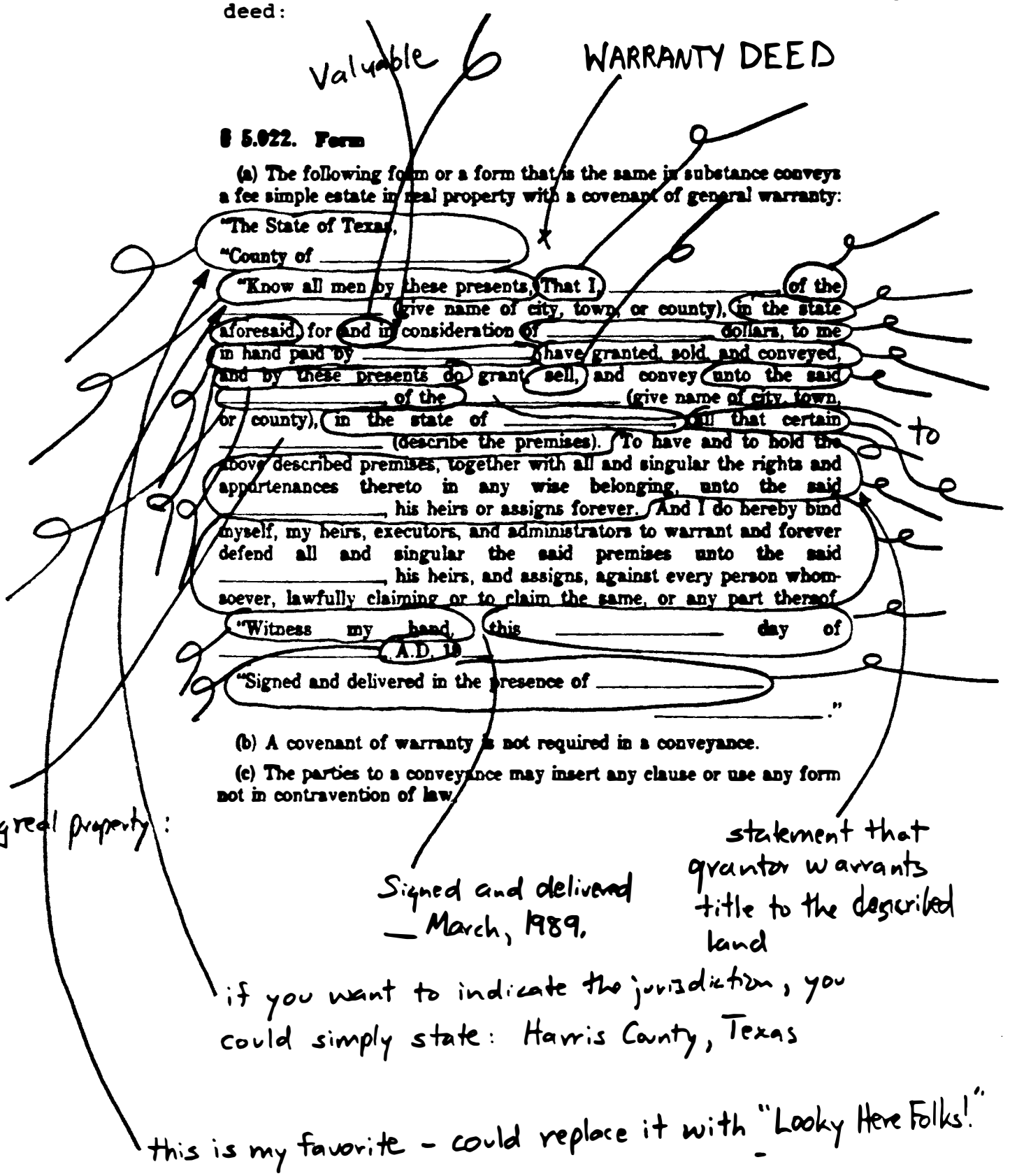
"Signed and delivered in the presence of _____

_____."

(b) A covenant of warranty is not required in a conveyance.

(c) The parties to a conveyance may insert any clause or use any form not in contravention of law.

5. Consider this edited form of the Texas statutory deed:



Valuable

WARRANTY DEED

§ 5.022. Form

(a) The following form or a form that is the same in substance conveys a fee simple estate in real property with a covenant of general warranty:

"The State of Texas,

"County of _____

"Know all men by these presents, That I, _____, of the _____ (give name of city, town, or county), in the state aforesaid, for and in consideration of _____ dollars, to me in hand paid by _____, have granted, sold, and conveyed, and by these presents do grant, sell, and convey unto the said _____, of the _____ (give name of city, town, or county), in the state of _____, all that certain _____ (describe the premises). To have and to hold the above described premises, together with all and singular the rights and appurtenances thereto in any wise belonging, unto the said _____, his heirs or assigns forever. And I do hereby bind myself, my heirs, executors, and administrators to warrant and forever defend all and singular the said premises unto the said _____, his heirs, and assigns, against every person whomsoever, lawfully claiming or to claim the same, or any part thereof.

"Witness my hand, this _____ day of _____, A.D. 19__.

"Signed and delivered in the presence of _____

_____."

(b) A covenant of warranty is not required in a conveyance.

(c) The parties to a conveyance may insert any clause or use any form not in contravention of law.

to

the following real property:

Signed and delivered _ March, 1989.

statement that grantor warrants title to the described land

if you want to indicate the jurisdiction, you could simply state: Harris County, Texas

this is my favorite - could replace it with "Looky Here Folks!"

6. The statutory deed form in Oklahoma is also a remnant of the old English drafting style. Okla. Stat. tit. 16, § 40 (1981) provides:

"A warranty deed to real estate may be substantially in the following form, to wit:

Know all men by these Presents:

That_____ part___ of the first part, in consideration of the sum of_____ dollars, in hand paid, the receipt of which is hereby acknowledged, do hereby grant, bargain, sell and convey unto_____ the following described real property and premises, situate in_____ County, State of Oklahoma, to wit:_____ together with all the improvements thereon and the appurtenances thereunto belonging, and warrant the title to the same.

To have and to hold said described premises unto the said part_____ of the second part, heirs and assigns forever, free, clear and discharged of and from all former grants, charges, taxes, judgments, mortgages and other liens and encumbrances of whatsoever nature;

Signed and delivered this_____ day of_____ 191___.

_____"

7. Contrast the Oklahoma and Texas approach with the modernized Kansas approach of Kan. Stat. Ann. § 58-2203 (1983):

"Any conveyance of lands, worded in substance as follows: A.B. conveys and warrants to C.D. (here describe the premises), for the sum of (here insert the consideration), the said conveyance being dated, duly signed and acknowledged by the grantor . . . ."

The statute then continues, indicating the effect of the "conveys and warrants" language:

it "shall be deemed and held a conveyance in fee simple to the grantee, his or her heirs and assigns, with covenants from the grantor, for himself or herself and his or her heirs and personal representatives, that the grantor is

lawfully seized of the premises, has good right to convey the same and guarantees the quiet possession thereof, that the same are free from all encumbrances, and the grantor will warrant and defend the same against all lawful claims."

C. Rebuilding The Legal Document (Language)

1. Looking at poorly-drafted documents and asking a few questions will help you to develop an eye for needless words.

   a. Question 1 - Why is this word, phrase, sentence, paragraph, or section here? Does it serve any real purpose?

   b. Question 2 - What does it mean?

   c. Question 3 - What will happen to the agreement if I take it out?

   d. Question 4 - Will it improve the agreement to leave it in?

2. Determine whether your sentences have too many "glue" words in proportion to the "working" words.

   a. Working words - words that carry the meaning of the sentence.

   b. Glue words - words that hold the working words together.

   c. For Example, the working words in the following sentence have been underlined:

      The word "GAS" as used herein is hereby declared to include all gaseous substances including oil well gas (casinghead gas) purchased and/or processed hereunder.

   d. Saying the same thing with less "glue" we might write:

      The word "GAS" includes all gaseous substances including oil well gas (casinghead gas).

3. Avoid compound phrases when a single word will suffice.

   a. "in the event that" - "if"

   b. "in order to" - "to"

   c. "prior to" - "before"

   d. "subsequent to" - "after"

4. Avoid unnecessary phrases such as "the fact that," "because of the fact that," "despite the fact that," "the question as to whether or not."

5. See two excellent books on this subject (each can be read in less than two hours):

   Richard Wydick, Plain English for Lawyers (2d ed. Carolina Academic Press 1985).

   William Strunk, Jr. and E.B. White, The Elements of Style (3d ed. MacMillan 1979).

D. The Document's Legal Requirements (Validation)

1. You have just finished talking with your client. They want you to draft a contract authorizing the client to locate a compressor on land located in Michigan.

   a. First, you consider the requirements for creation of a contract.

   b. Certain issues may require special attention. For example, you discover that the entity owning the land is not Acme Oil Company, but rather the Bear Creek 1988-1 Limited Partnership for which Acme is one of the general partners. You have a capacity issue that will need to be researched to ensure you are contracting with the appropriate parties and can request the proper information to confirm their authority.

   c. If your client wants to record the contract, to give constructive notice of your contract rights, you will need to determine what is required to record a contract in Michigan.

      For example, you may need to have the document acknowledged, witnessed, or comply with other formalities before it can be recorded.

      You may be able to record a memorandum of your contract and achieve the same constructive notice goal without disclosing the precise terms of the contract.

      Consider the Michigan example which has many statutory requirements before a document can be recorded - Mich. Comp. Laws Ann. §§ 565.201 and 565.201a (West 1988):

565.201. Requirements for recording with register of deeds

Sec. 1. No instrument by which the title to real estate or any interest therein is conveyed, assigned, encumbered or otherwise disposed of, executed after the effective date of this act shall be received for record by the register of deeds of any county of the state unless the same complies with each of the following requirements:

(a) The name of each person who executed such instrument shall be legibly printed, typewritten or stamped upon such instrument immediately beneath the signature of such person and the address of each such person shall be printed, typewritten or stamped upon the face of the instrument;

(b) No discrepancy shall exist between the name of such person as it appears either in the body of such instrument, the acknowledgment or jurat, as printed, typewritten or stamped upon such instrument by the signature, or in the signature of such persons;

(c) The name of each witness to such instrument shall be legibly printed, typewritten or stamped upon such instrument immediately beneath the signature of such witness;

(d) The name of any notary public whose signature appears upon such instrument shall be legibly printed, typewritten or stamped upon such instrument immediately beneath the signature of such notary public;

(e) Wherever in this act it is required that the name of a person shall be "printed, typewritten or stamped upon such instrument immediately beneath the signature" of such person, it is the intent of the legislature to require that such signature be written upon such instrument directly preceding such name so "printed, typewritten or stamped". Such signature shall not, however, be superimposed upon such name so as to render either illegible. Such instrument shall, however, be entitled to be received for record if such name and signature are in the discretion of the register of deeds so placed upon such instrument as to render the connection between the 2 apparent. Any instrument received and recorded by a register of deeds shall be conclusively presumed to comply with the requirements of this act. The requirements contained in this act shall be cumulative to the requirements imposed by any other act relating to the recording of instruments;

(f) The address of each of the grantees in each deed of conveyance or assignment of real estate, including the street number address if located within territory where such street number addresses are in common use, or, if not, the post office address shall be legibly printed, typewritten, or stamped in such instrument;

(g) Instruments shall not be typewritten or printed in type smaller than 8 point size, and the size of any sheet in any such instrument shall not exceed 8½ by 14 inches, and shall be legible and on paper of not less than 13 (17×22—500) pound weight. Nothing in this subdivision shall affect instruments executed outside the state or the filing or recording of plats or other instruments, the size of which are regulated by law.

565.201a. Recording requirements; scrivener's name and address on recorded instruments

Sec. 1a. Each instrument described in section 1 [1] executed after January 1, 1964 shall contain the name of the person who drafted the instrument and the business address of such person.

2. The validation process begins by defining the task - draft a contract, deed, division order, indemnity provision, pleading, etc.

3. Next you define the basic legal requirements for creating a valid document. At this stage we really aren't concerned with the specific content of the document - instead we want to define the general content requirements. For example, what is required for an effective conveyance of rights in an oil and gas lease?

4. You may have to refer to some general references to learn about the document you are about to draft.

5. After you have a general understanding of the document, research the applicable statutes that govern the document. May need to follow this with an examination of regulations.

6. Consider any relevant case law addressing the topic.

E. The Structure Of The Document (Design)

1. Consider structural requirements dictated by the validation process. For example, if you want to disclaim a warranty in a sale of goods, you will have to use special language and ensure that your limitation is "conspicuous." Okla. Stat. tit. 12A, § 2-316 (1981). This may dictate placement and type size.

2. Begin drafting by selecting a descriptive title for the document:

   OXY/ACME COTTONWOOD FIELD FARMOUT AGREEMENT

3. Identify the parties to the agreement and establish a short-form reference:

   OXY NGL INC. ("OXY") and ACME OIL COMPANY ("Acme") agree as follows:

   a. Select a form of reference that will not require returning to the first page to see who is "party of the first part" and "party of the second part."

   b. I prefer to avoid even "buyer" and "seller." However, the nature of the contract may dictate that you use an indefinite reference

for at least one of the parties - but try to make it a distinctive reference.

4. Attempt to have all blanks that need to be completed, such as the date, signatures, etc. located in one location so you can tell at a glance whether all the blanks have been completed.

   Avoid including multiple date blanks.

5. Recitals are often unnecessary. However, in some cases they may be helpful to set the stage for the agreement; such as reference to a dispute which leads up to the settlement agreement.

   a. Traditional Approach: Begin each statement with a "Whereas . . . "

   b. I would designate a paragraph as "Background:" followed by the numbered recitals.

6. Don't confuse recitals with representations.

7. Contracts often include a definition section. I prefer to define each word when it is first used and then provide an index of terms that refers to the place in the agreement where the term is defined.

   a. Once you define a term, you may want to use distinctive type whenever it is used in the contract.

   b. Once you define a term use it consistently throughout the agreement.

8. Break up the operative language for your reader in logical divisions. Use section designations, avoid long paragraphs, and avoid unnecessarily long sentences.

9. Signature lines - place them where all the other blanks are located.

10. Economize your drafting whenever possible. For example:

    An Oklahoma statute authorizes the following acknowledgment form for a corporate conveyance:

"State of Oklahoma,)
) ss.
_____ County.)

Before me, a_____ in and for said county and state, on this_____ day of 19___, personally appeared_____, to me known to be the identical person who subscribed the name of the maker thereof to the foregoing instrument as its (attorney-in-fact, president, vice-president, or mayor, as the case may be) and acknowledged to me that he executed the same as his free and voluntary act and deed, and as the free and voluntary act and deed of such corporation, for the uses and purposes therein set forth."

Okla. Stat. tit. 16, § 95 (1981).

A different Oklahoma statute authorizes the following form of certificate of acknowledgment:

"State of_____
County of_____

This instrument was acknowledged before me on (date) by (name(s) of person(s)) as (type of authority, e.g., officer, trustee, etc.) of (name of party on behalf of whom instrument was executed).

_____
(Signature of notarial officer)

(Seal, if any)

_____
Title (and Rank)
(My commission expires:_____)

Okla. Stat. tit. 49, § 119 (Supp. 1988)

F. The Document's Factual Requirements (Content Planning)

1. After identifying general requirements, we must address the specific facts of the transaction to determine what will be included and how we must draft to validate special requirements of the transaction.

2. For Example: Suppose you are entering into a gas

purchase agreement and the gas purchaser is obligated to lay gathering lines to the wells. The producer wants to ensure that the lines are promptly layed so production sales can commence.

a. The contract provides: "Gas purchaser will begin construction of the line so that sales can commence on or before March 14, 1989."

b. If the gas purchaser fails to meet the March 14, 1989 date is it a material breach of the contract permitting the producer to cancel the contract? This will depend upon whether time is considered an important element of the contract.

c. The Oklahoma statutes regarding contract interpretation indicate the producer's attorney has a drafting task they must address. Okla. Stat. tit. 15, § 173 (1981) provides:

"Time is never considered as of the essence of a contract, unless by its terms expressly so provided."

3. The attorney must be attuned to identify all possible issues that may require special drafting attention.

4. As with any contract, the attorney will engage in the "what if" game with their client to try and identify contingencies that need to be addressed in the contract. For example, what does the client want to do if on March 14, 1989 the gas purchaser has not completed the line? We may want to provide for some stated remedy - such as daily liquidated damages.

5. As the factual requirements are identified, you should begin to arrange them into logical groupings. These will become the sections and subsections of your contract.

G. State The Agreement In Clear, Concise, And Plain English (Draft)

1. Now you are ready to take your design, add the language necessary to validate the agreement, and then write the specific content of the agreement.

2. After you have completed a draft of your agreement, you may want to refer to other

agreements (forms) to check and see whether you have omitted something that needs to be in the document.

H. Rewrite, Evaluate, Obtain Client Input (Edit)

1. Your client will often be the best source of information regarding what needs to go into the agreement and how it needs to be organized for their administration.

2. Ensure your client <u>understands</u> each term in the document and appreciates why they have been included - or why certain provisions have been excluded. If your client doesn't fully understand the document, you've got problems. They must understand the contract; particularly if they will be administering it terms.

3. Rewrite until you and your client are satisfied. Send it to the other party (who hopefully has been involved in at least the initial phases of defining the contours of the deal). If the other party has problems understanding provisions, redraft them until you are satisfied everyone knows what is intended and how the contract will operate.

4. During this stage you may identify additional issues that need to go through the validation/design/content planning process.

VII. CONTRACT ADMINISTRATION

A. The Contract Is A "Living" Instrument

1. Carefully negotiated and drafted rights and obligations in the contract can be lost through poor administration.

NOTE: This is something attorneys, particularly tax attorneys, should consider when drafting agreements or requiring relations to be structured in a particular way.

a. Can the proposed agreement be efficiently administered once it takes effect?

b. Does your client have the capacity to function under the contract?

2. Read the contract periodically and audit its

operation.

For Example: May need to request a deliverability test to determine the "average daily quantity" of gas used to calculate take-or-pay obligations.

3. Diligently pursue any failure to adhere to the express terms of the contract to avoid later claims of "waiver" and "estoppel."

Determine what your course of action can (and should) be for any deviation from contract terms. Notify the other party how you plan to treat present, and future, deviations.

4. Each contract, even with the same party, has a separate existence.

CAUTION! Avoid settling disputes under one contract through nonperformance of other contracts. For Example: Gas Purchaser (GP) buys gas from X under three different contracts. GP believes X has tampered with the meters to wells under contract #1, resulting in an overpayment to X. GP withholds payment for gas under contracts #1, 2, and 3 until the overpayment is recovered. GP has breached contracts #2 and 3 unless they specifically authorize GP to withhold payment under these circumstances.

B. Obtain Legal Advice Whenever There Are Performance Problems

1. If you have a potential breach of contract (whether you are the breaching party or the other party commits the breach), obtain legal assistance.

2. If you are the breaching party, there may be ways to cure the default, minimize damages, and maintain the contract in effect.

3.. If you believe the other party has breached the agreement, proceed with caution. A wrong move, a moment of overreaction, or a poorly phrased declaration, could make you the breaching party.

VIII. DIVISION AND TRANSFER ORDERS

A. The Division Order

1. Defined: A contract between the owner of

COMMON OIL AND GAS DEVELOPMENT SEQUENCE

Parties	Contract	Parties
1. Mineral Owner (Lessor)	**Oil & Gas Lease**	Developer (Lessee)
2. Lessee	**Investment Agreement**	Investors
3. Lessee	**Lease Purchase and Sale Agreements**	Other Developers
4. Lessee	**Assignments**	Investors & Developers
5. Lessee	**Exploration Agreements**	Other Developers
6. Lessee	**Farmout Agreements**	Other Lessees
7. Lessee	**Operating Agreement**	All Working Interest Owners
8. Mineral Owner Working Interest Owners Non-Working Interest Owners	**Pooling Agreement**	All Interest Owners
9. Operator	**Drilling Contract**	Drilling Company
10. Operator	**Well Service Contracts**	Service Companies
11. Mineral Owner Working Interest Owners Non-Working Interest Owners	**Oil Division Order**	Oil Purchaser
12. Mineral Owner Non-Working Interest Owners	**Gas Division Order**	Working Interest Owner
13. Working Interest Owner	**Gas Division Order**	Gas Purchaser
14. Working Interest Owner	**Gas Processing Agreement**	Gas Processor
15. Working Interest Owner	**Gas Sales Agreement (End User)**	End User
16. Working Interest Owner	**Transportation Agreements**	Pipelines
17. Working Interest Owner	**Marketing Agreements**	Gas Marketer/Broker
18. Working Interest Owner	**Gas Sales Agreement (Pipeline)**	Pipeline