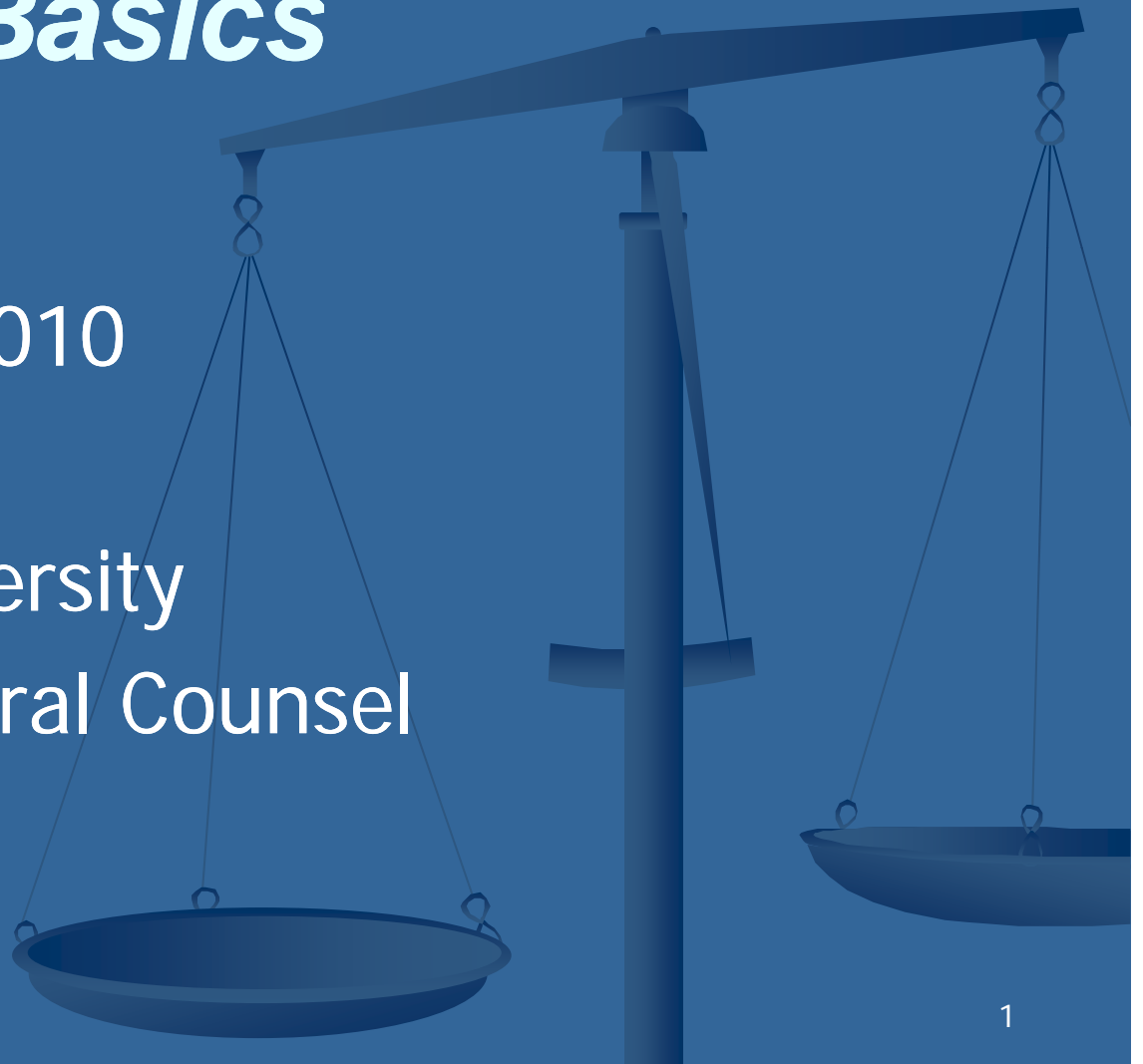


# *Legal Updates: Contract Basics*

April 23, 2010

Lehigh University  
Office of the General Counsel



# Part I: The Basics

- Definitions
- Why We Enter Contracts
- Sources of Contract Law & Types of Contracts
- Elements of a Contract
- Contract Clauses To Incl. & “Boilerplate” Provisions
- Challenges, Problems & Pitfalls
- Remedies for Breach of Contract



# Contract:

“[a]n agreement between two or more persons which creates an obligation to do or not do a particular thing... A legal relationship consisting of the rights and promises constituting an agreement between the parties that gives each a legal duty to the other and also the right to seek a remedy for the breach of those duties.”

*[Black's Law Dictionary, 6<sup>th</sup> ed.]*

In other words ...

A contract is a legally  
enforceable promise



# Why does Lehigh enter into Contracts?

There are almost as many reasons as there are departments and functions at Lehigh...

- Pursuit of our missions (education and research)
- Buy or sell goods
- Buy or sell services
- Employment of faculty, staff, teaching assistants, etc.
- Relationships with our students

# What are the Sources of Contract Law ?

- *Common law* : judge-made law, as distinguished from laws passed by legislature
- *Uniform Commercial Code (UCC)* : model code on commercial transactions adopted by all states (except Louisiana)

# Contract law asks and answers the following questions:

1. Have the parties acted in such a way as to create legally recognizable expectations in one another;
2. If so, how should we characterize and understand those expectations;
3. Was the understanding of the parties faithfully carried out; and
4. If not, what if anything should the law do about it?

[Excerpt from "Concepts and Case Analysis in the Law of Contracts", 2Ed., Marvin A. Chirelstein, 1990]

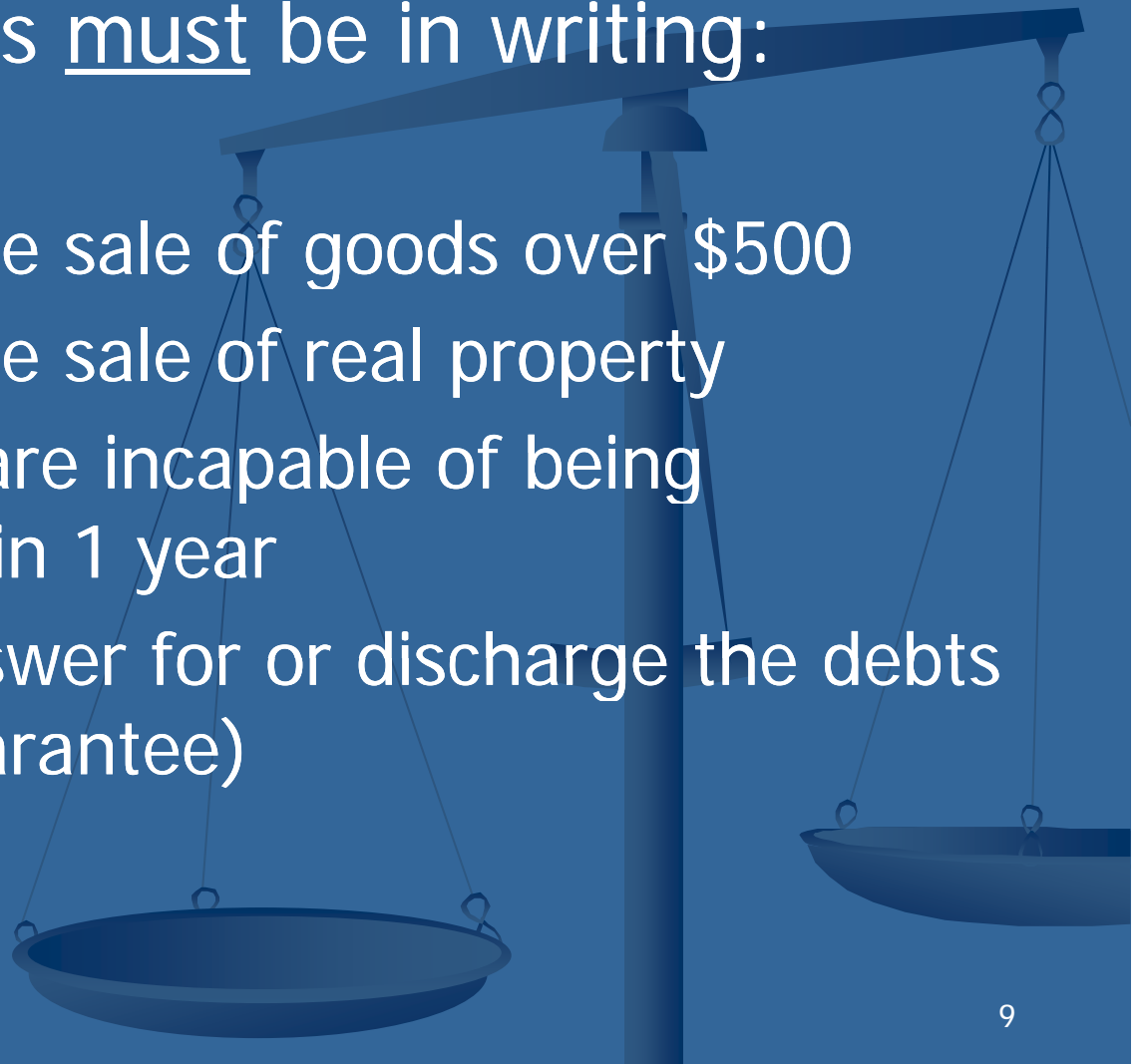
What form must a contract  
take to be a legally  
enforceable?





# A Contract Can Be Written or Oral

- Certain contracts must be in writing:
  - Contracts for the sale of goods over \$500
  - Contracts for the sale of real property
  - Contracts that are incapable of being performed within 1 year
  - Promises to answer for or discharge the debts of another (Guarantee)



# Written and Oral Contract Terms



- Sometimes a contract may be in writing, but if a dispute occurs, an issue will be whether oral terms have modified written terms
  - This is why we have “merger” clauses in contracts, such as:

*“ This Agreement sets forth the entire understanding and agreement between the parties and supersedes all proposals or communications, oral or written, between the parties relating to the subject matter of the Agreement.”*

# Written and Oral Contract Terms (cont.)

- *Parol Evidence Rule* - when a “final” agreement between parties has been reduced to writing, evidence of any earlier oral or written expressions is not admissible to vary the terms of the writing...
  - UNLESS...one party can prove a material ambiguity or omission exists in the written terms ...THEN oral testimony about contract terms is considered

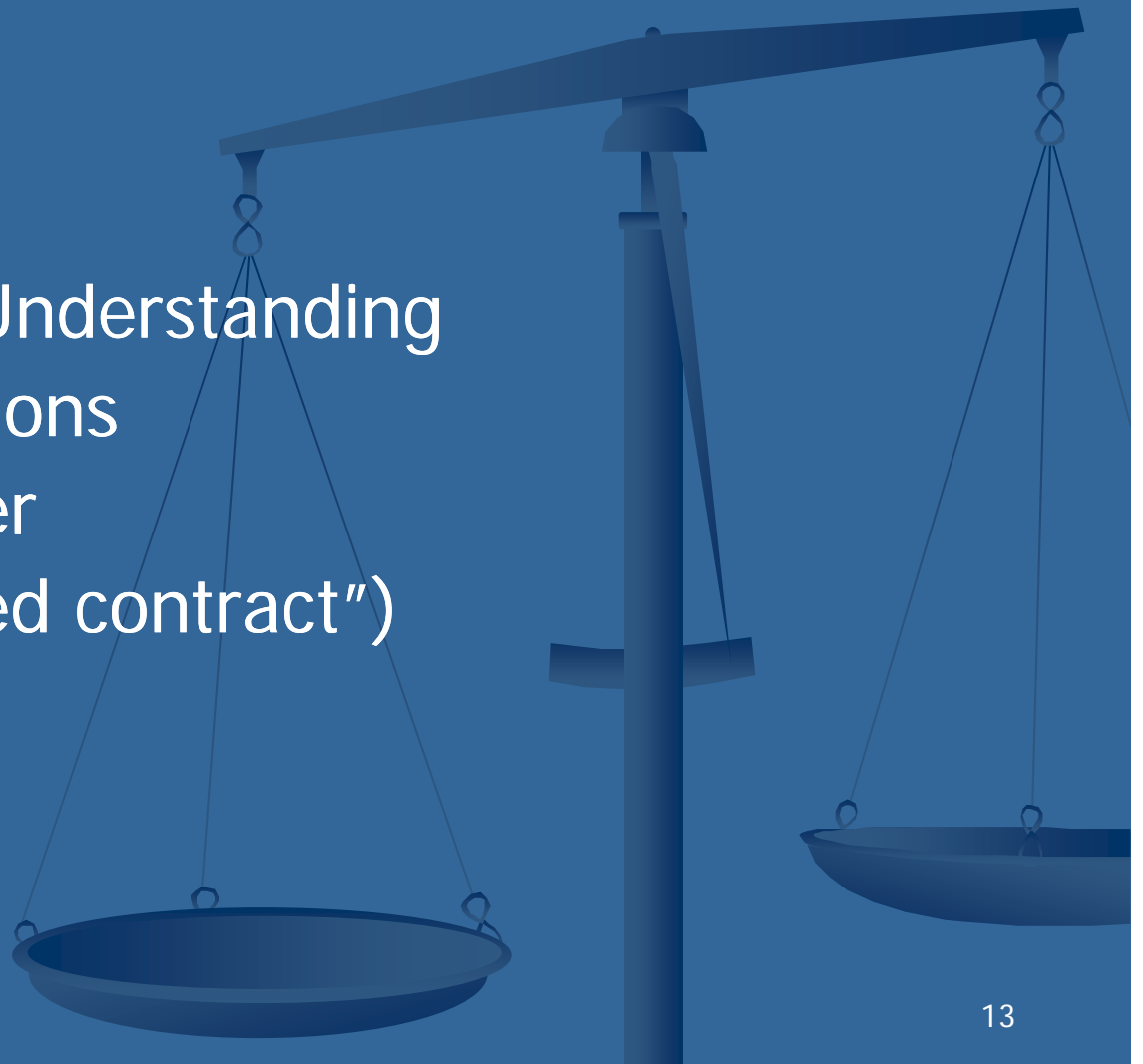
# Written and Oral Contract Terms (cont.)

Evidence questions become crucial if there is a contract dispute

A contract is only as good as what you can later prove to be the terms of the contract

# Contracts can have many names...

- Contract
- Agreement
- Purchase Order
- Memorandum of Understanding
- Terms and Conditions
- Appointment Letter
- Handbook (“implied contract”)
- License
- Ticket



# Or no name at all...

- a letter...
- a telephone call...
- an e-mail...
- even ... words on a napkin



# What are the Elements of a Contract?

- Offer
- Acceptance
- Consideration
- Mutuality



# Offer:

- A proposal to do a thing or pay an amount, usually accompanied by an expected acceptance, counter-offer, return promise or act
- The offeror is the “master of his offer”.



# Acceptance:

- Compliance by the offeree with terms and conditions of an offer
- A manifestation of assent to terms of offer in a manner invited or required by the offer
- The offer and acceptance must match ("mutuality" ...more on this soon...)

# Acceptance:

Does not necessarily occur only by signature of a contract

Acceptance can occur by:

- Action
  - using goods
  - opening the package (software)
  - entering an establishment or participating in an activity
- Inaction –not returning goods

# Acceptance:

Sometimes acceptance does not appear  
"voluntary," but it is still sufficient

Contracts of Adhesion:

- "Take it or leave it" terms
- Not bargained for

# Consideration:

- Something of legal value; anything that induces you to give up something
- May be something other than money (i.e., a promise to do something; a promise to refrain from doing something)

# Consideration:

What is the "value" of a contract?



# Consideration:

The value of a contract:

It's not only what the University receives or pays, but also:

- What the University agrees NOT to do :
  - confidentiality clauses
  - non-compete clauses
- What risks and liabilities the University is exposed to

# Mutuality:

- A “meeting of the minds” with respect to material contract terms
  - A signature is deemed to be sufficient to evidence this requirement
  - Therefore, it is crucial that you read carefully and understand all of the terms of a contract before you sign it

# Additional Contract Elements:

- Both parties must be legally competent
  - Over 18 and mentally capable of understanding the agreement
  - Authority to negotiate for and bind the University





# Information that you should include in University contracts ...

- Clear and specific statements of the University's requirements and expectations
  - Type of performance expected
  - Quality, including inspection before acceptance
  - Timing of performance
  - Warranties or guarantees, if applicable

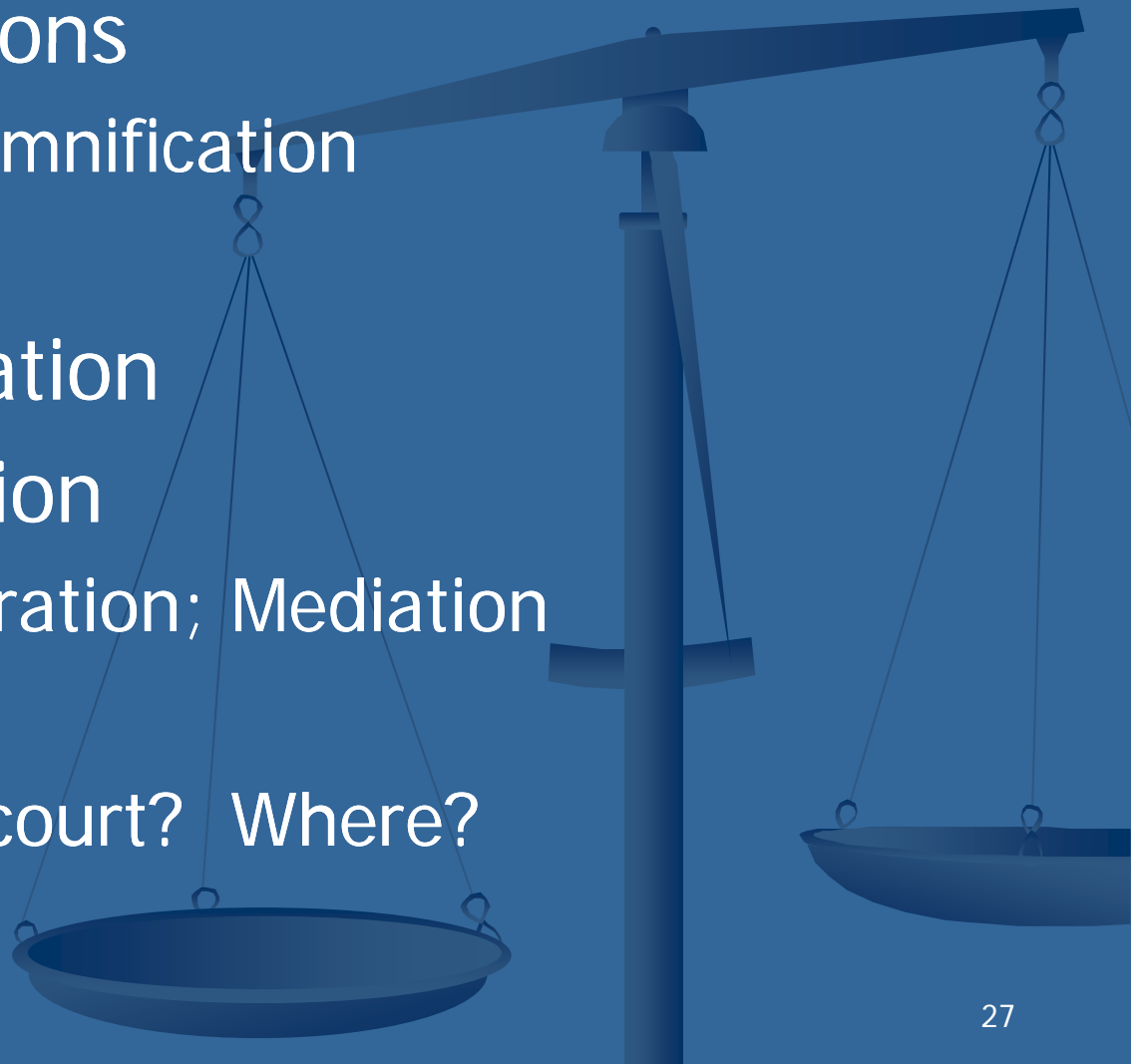
# Contract Clauses to Include (cont.)



- Clear statements that specify all terms, documents, attachments, proposals, etc. that are included in the contract
  - (Answer the question: What is our agreement?)
- Provisions that protect the University's interests, assets, and information (i.e., confidentiality; tax exempt status; publicity/endorsement prohibitions)

# Contract Clauses to Include (cont.)

- Liability Protections
  - Defense & Indemnification
  - Insurance
- Term & Termination
- Dispute Resolution
  - Litigation; Arbitration; Mediation
  - Governing Law
  - Forum – What court? Where?



# Indemnification

- To restore the victim of a loss, in whole or in part, by payment, repair or replacement. To make good; compensate. [Black's Law Dictionary, 6<sup>th</sup> Ed.]
- Theory: tool to allocate risks between contracting parties based upon economic considerations and without regard to either party's relative degree of fault

# Why Insurance?

## ■ Financial Assurance

- Ensure the other party can honor its promise to indemnify Lehigh
- Ensure the other party has the financial ability to pay Lehigh for damages regardless of a contract or an enforceable indemnity provision

# Types of Insurance

- Commercial General Liability (CGL): bodily injury; personal injury; property damage; contractual liability; products and completed operations; independent contractors
- Automobile Liability Insurance
- Workers' Compensation
- Umbrella Liability Insurance
- Professional Liability

# “Additional Insured” Status

- Provides University with insurance protection under the other party’s insurance policies
- Allows Lehigh to present a claim directly to the other party’s insurer
- Protects Lehigh from adverse loss experience
- May cover defense and damages if indemnity doesn’t apply or is ruled invalid

# Term

- Contract term, including renewals, should not exceed five years without the express approval of the General Counsel's Office
- Automatic renewals are not favored; better for parties to agree in writing to any renewal terms



# Termination



- *For cause (breach)*: gives aggrieved party the right to terminate because other party did something “wrong”
  - Party in breach often given the opportunity to “cure” the breach
- *For convenience*: contract can be cancelled because we want to do so

# Dispute Resolution



- *Negotiation*: between 2 parties with no guidance by 3<sup>rd</sup> party
- *Mediation*: between 2 parties but with independent 3<sup>rd</sup> party whose job is to try to bring parties to agreement
- *Arbitration*: private, non-govt. "litigation", binding or non-binding. Arbitrator(s) may apply specific body of law or special rules of an industry/profession
- *Litigation*: the parties go to court for resolution; public, government-run process

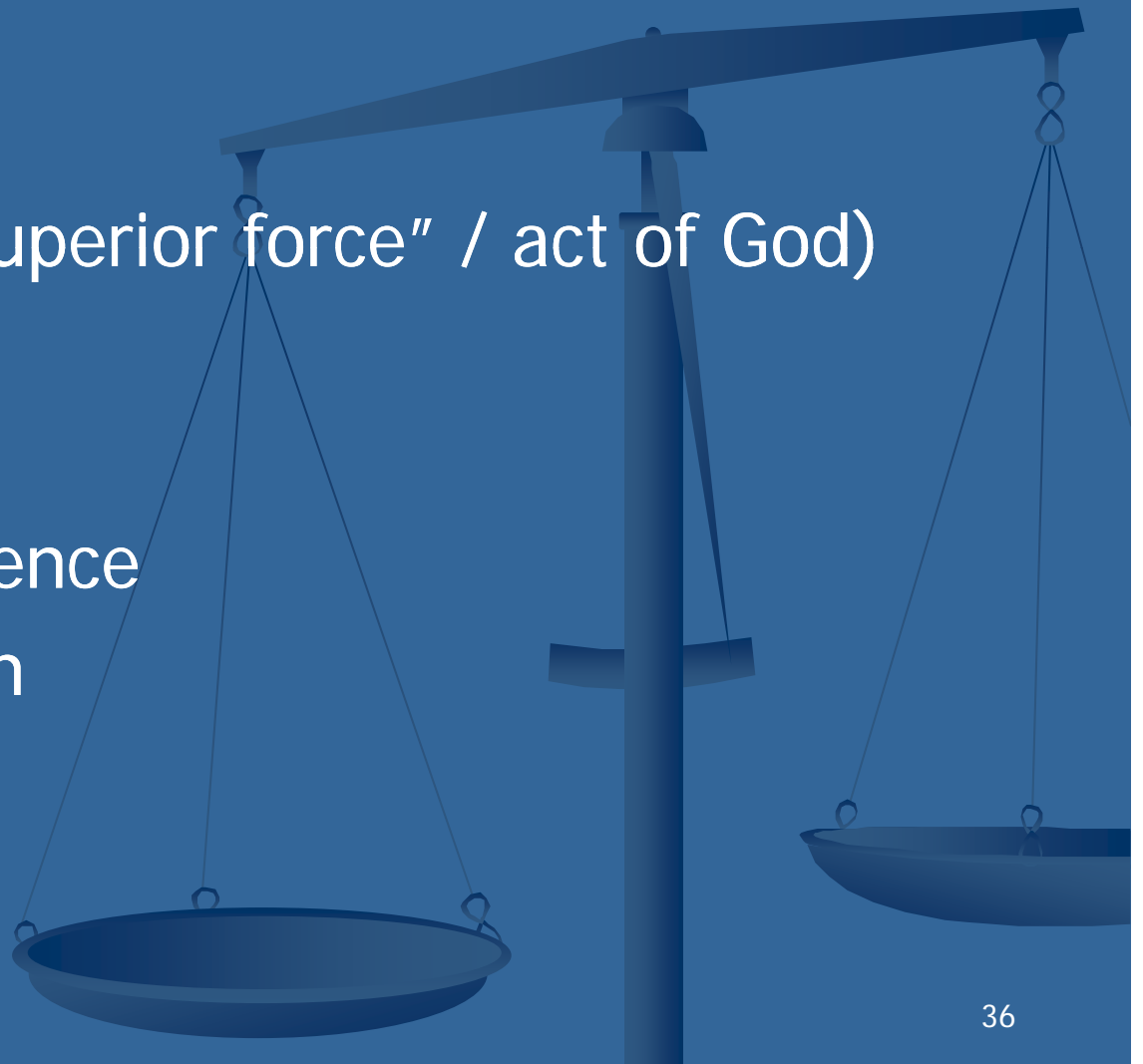
# Governing Law & Forum

- The “home court” advantage
- Pennsylvania: the law we know & practice
- Less expensive to litigate
- Judges/juries more favorable to us



# “Boilerplate” Provisions

- Assignment
- Merger Clause
- Force Majeure (“superior force” / act of God)
- No Waiver
- Severability
- Time is of the Essence
- Non-Discrimination



# Challenges, Problems & Pitfalls



# Potential Contract Pitfalls

- Not reading and understanding the contract (i.e., assuming it's all "legalese")
- Not negotiating and documenting the contract's terms as needed to reflect Lehigh's requirements
- Not being specific enough; using overly broad and vague language
- Starting work/services before the contract is signed = acceptance of terms.

# Potential Contract Pitfalls



- Disclaimers or limitations on the other party's performance; disclaimers of warranties, etc.
- Any clause permitting the other party to change contract terms without the permission of the University in writing
- Failure to specify all terms, documents, etc. that are included in the contract or failure to show acceptance (i.e., signing or initialing changes)

# Potential Contract Pitfalls (cont.)

- Reference to terms, documents or websites that the University has not been provided
- Failure of the parties to initial all changes, whether hand-written, erased by white-out or added on a separate piece of paper
- Indemnification, Liability Releases, Limits on Other Party's Liability



# Potential Contract Pitfalls (cont.)

## ■ Termination of Contract

- Excessive opportunity for the other party to cure its breaches of the contract
- Excessive or unreasonable penalties imposed on the University for terminating the contract

- Dispute Resolution in distant locations (other party's home city and state) and under laws of a distant state (other party's home state)

Is it necessary to read and negotiate “boilerplate” or “legalese”?

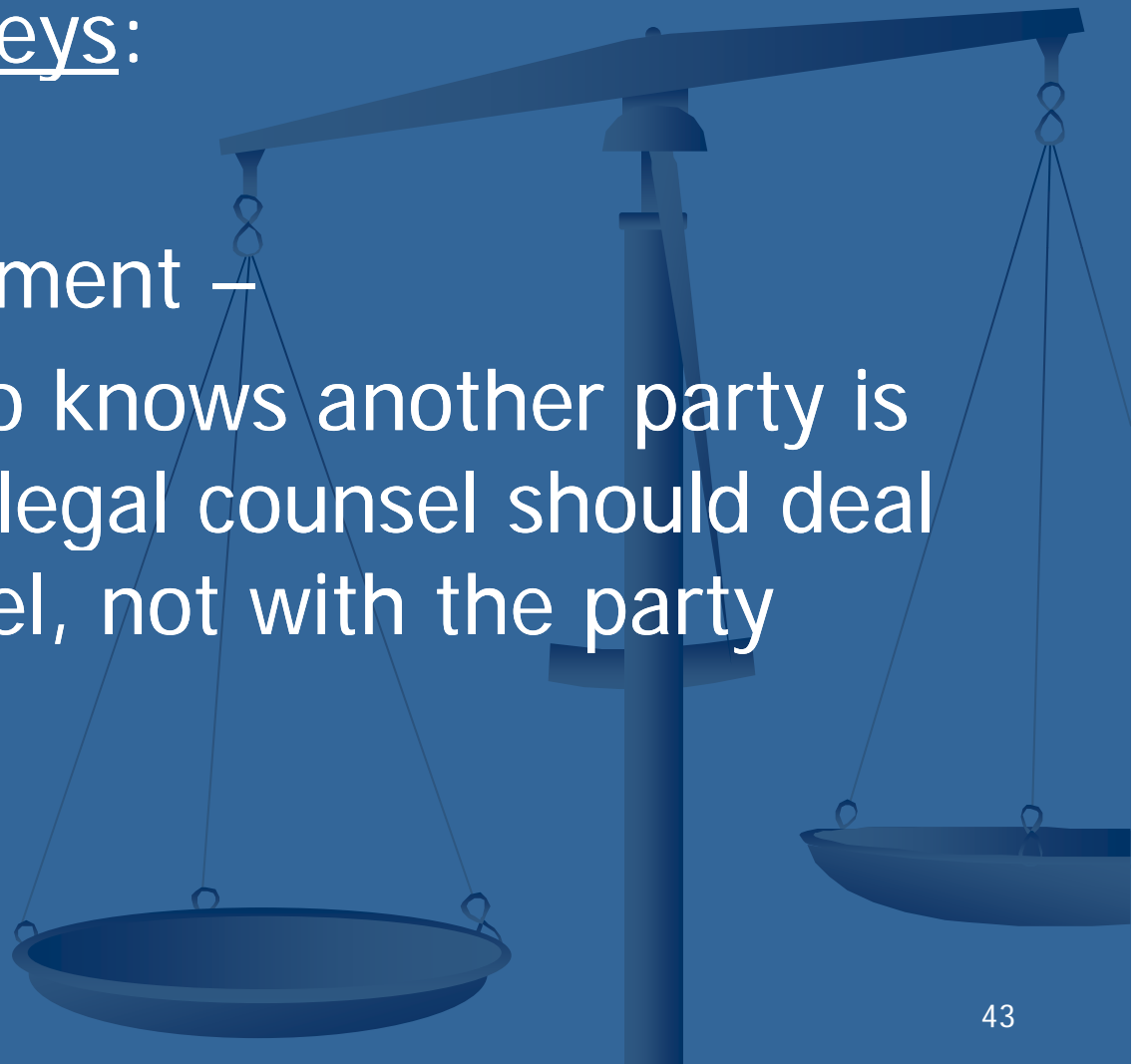
...the 70-page Confidentiality Agreement that was all “just boilerplate”...

# Potential Contract Pitfalls (cont.)

## The role of attorneys:

An ethical requirement –

An attorney who knows another party is represented by legal counsel should deal with that counsel, not with the party directly.



# Potential Contract Pitfalls (cont.)

- Is a promise to make a gift (a pledge) a contract?
  - No consideration, so not a binding contract unless...
    - reasonable reliance by intended recipient and to its detriment
    - (e.g., starting construction on a building, inducing other donors to give)

# Potential Contract Pitfalls (cont.)

“Always look a gift horse in the mouth ...”

- The “free” Velcro wall that cost \$750,000 ...
- Underground gas tanks and drycleaners

What if a contract is  
breached?



# Remedies for Breach of a Contract



- Money Damages:
  - Examples: compensatory; punitive; nominal; consequential or liquidated damages
- Specific Performance (for unique property):
  - Money damages aren't adequate to give the plaintiff the "benefit of the bargain"
  - So, the defaulting party is required to perform its obligations under the contract

# Things to Remember...

- Use University form contracts (including Purchase Orders), whenever possible
- Beware of pressure tactics
- Be as specific as possible
- Always read and understand all terms and provisions of contract before signing



# Who May Sign A Contract?

- Only those individuals who have been expressly delegated signature authority by the Board or senior administration
  - Unauthorized individuals who sign contracts on behalf of the University expose themselves to possible personal liability
  - Contract may be void or unenforceable if not signed by someone with authority

What is the difference between  
“attest” and “witness”?



# Battle of the Forms



- Modern business transactions are often conducted primarily through forms

*Example:* Lehigh decides to buy a computer

- Purchasing sends a purchase order to the vendor containing standard terms and conditions that are favorable to Lehigh
- After receiving the order, vendor sends a written acceptance or confirmation of the order on its form which contains the basic contract terms and a series of pre-printed terms that are favorable to the vendor

# This is where the Battle Begins...

- If there is a contract dispute, which form will prevail?
  - Common law: the acceptance must mirror the precise terms of the offer and any variance from that constitutes a rejection of the offer or a counteroffer
  - UCC: says that, on premise that both parties recognize a contract despite their clashing forms, a contract is formed, unless the vendor specifically states that there shall be no contract unless his set of terms is accepted by the original offeror

## ...continues

- **If:** the offeree's (vendor) response contains terms *additional* to those contained in Lehigh's original offer (purchase order)
- **Then:** a contract exists consisting of the terms on which the offer and acceptance agree
  - The additional terms are merely a proposal for additions to the contract

## ...and ends

- **If:** the offeree's response contains terms which are *inconsistent* with the original offer
- **Then:** the court looks at the parties' conduct to determine whether they acted as though a contract was formed
  - If so, the conflicting terms cancel each other out and necessary terms are provided by the UCC or custom.

# A note about the “plain language” movement in contracts ...

In the event a Claim is made upon the 2<sup>nd</sup> Party, the 2<sup>nd</sup> Party shall promptly give notice of such Claim to the 1<sup>st</sup> Party, and shall promptly deliver to such 1<sup>st</sup> Party all information and written material available to the 2<sup>nd</sup> Party relating to such Claim. If such Claim is first made upon the 1<sup>st</sup> Party, the 1<sup>st</sup> Party shall promptly give notice of such Claim to the 2<sup>nd</sup> Party. The 2<sup>nd</sup> Party will, if notified of the 1<sup>st</sup> Party's election to do so within fifteen (15) days of the date of notice of a Claim, permit the 1<sup>st</sup> Party to defend in the name of the 2<sup>nd</sup> Party and Claim in any appropriate administrative or judicial proceedings and take whatever actions may be reasonably requested of the 2<sup>nd</sup> Party to permit the 1<sup>st</sup> Party to make such defense and obtain an adjudication of such Claim on the merits, including the signing of pleadings and other documents, if necessary; provided that the 1<sup>st</sup> Party shall defend the Claim with counsel reasonably satisfactory to the 2<sup>nd</sup> Party and provide the 2<sup>nd</sup> Party with evidence reasonably satisfactory to the 2<sup>nd</sup> Party that the 1<sup>st</sup> Party can satisfy the Claim if it is upheld. In addition to the liability for the ultimate settlement or judgment, if any, arising out of such Claim under this Agreement, the 1<sup>st</sup> Party shall be solely responsible for all the expenses incurred in connection with such defense or proceedings, regardless of their outcome. However, the 1<sup>st</sup> Party shall not be responsible for any expenses, including attorneys fees and costs, incurred by the 2<sup>nd</sup> Party to monitor the defense of the Claim by the 1<sup>st</sup> Party.

# Contract Review & Approval Web Page

- *Creators:* Offices of Purchasing, Research & Sponsored Programs & General Counsel
- *Purpose:* Streamline the contract review and approval process for faculty and staff
- *Process:* Answer a few contract-related questions, upload your contract and click submit



# Part II: Research Contracts

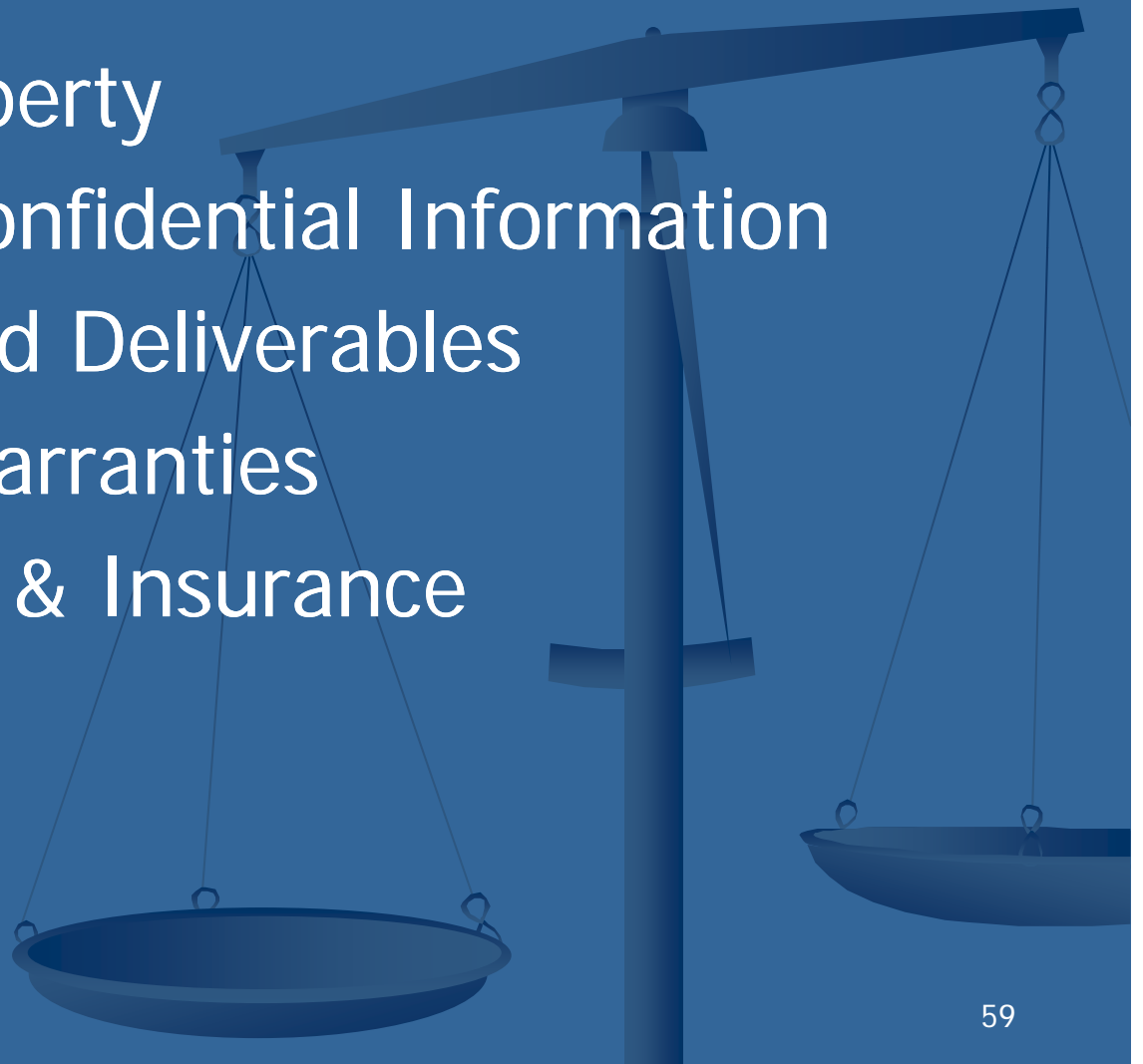
- Sponsored Research
    - Government funded
    - Corporate sponsored
  - Research & Testing
  - Consulting & Services
  - Use of University Equipment
  - License Agreements
  - Liaison Membership Agreements
- 

# The Parties: Important Distinctions

Universities	For-Profit Corps.	Government
Non-profit : Revenues to mission	For-profit : Revenues to private s/hs	The Public
Tax-exempt : Public benefit	Taxed : Private benefit	Taxing authority enforcing distinction between 2 others
Mission of general knowledge generation	Lines of business to produce profit	Public benefit via taxing, spending, regulation, etc.
Creation / dissemination of knowledge for public benefit	Creation / control of knowledge for competitive advantage	Creation / dissemination of knowledge for public benefit

# Frequently Negotiated Provisions in Research Agreements

- Intellectual Property
- Publication & Confidential Information
- Performance and Deliverables
- Disclaimer of Warranties
- Indemnification & Insurance



# *Intellectual Property (IP) & Federal Law*

If IP results from federally funded research:

- Bayh-Dole Act applies

If IP results from use of University's resources  
(equipment, space, expendables, University-paid time  
or employment, etc.)

- IRS tax exempt entity rules & regulations apply\*

(\*apply regardless of whether other resources  
[federal, corporate, etc.] were also used)

# *Federal Regulation of Tech. Transfer: Bayh-Dole Act (1980)*

Allows universities (as federal research grantees) to own IP resulting from federally funded research (if not elected, federal agency takes title)

Requires utilization of IP for public benefit

Requires / favors certain elements in licensing of IP:

- preference for license to small businesses
- mfg. of products in U.S. if products sold in U.S.

Federal Govt. retains “march-in” rights to take back IP ownership if university grantee does not comply with Act

# *Intellectual Property Rights & Tax Exempt Status*

As nonprofit, tax-exempt org., University must own IP  
resulting from use of its resources

AND ... cannot transfer assets, profits, resources, etc...

to private parties to engage in profit-making  
activities for commercial gain

unless... Univ. receives some legal consideration  
(fair market value) in return for the transfer

Not receiving fair market value

= private inurement / private gain

= tax + penalties on recipient + university

## *More Federal Tax Law as Background : The Research vs. Testing Distinction*

Research = Incident to tax-exempt educational missions;  
acquisition of knowledge / experience by faculty + students  
= NOT taxable

Testing = Incident to commercial enterprise; sampling or certifying to a  
known standard; routine, not novel  
= TAXABLE

- Must be reported to University Controller's Office  
as unrelated business taxable income (UBTI)

Important elements of tax exempt research:

- Results freely publishable
- Results available for public benefit (licensed w/  
requirement of due diligence to commercialize, not shelve IP)

# More Tax Law : Use of Univ. Resources for Private Gain

University resources (equipment, space, faculty / staff / student time or effort) are tax exempt resources

- Should be used for University's tax exempt missions
- Use for private gain must be **limited**, **charged** at **market rates**, and **reported** as unrelated business activity
- If requested to be used for private gain (by external party or University faculty / staff / student):
  - Follow all University policies, R & P, Policy on Use of Major Research Instrumentation, etc.
  - Obtain guidance from General Counsel's & Controller's Offices on legal compliance
  - Federal excise taxes & penalties can be imposed on individuals and managers
- Also... note 5% limitation on commercial use of tax exempt bond financed facilities



# Publication Rights



- Another means to satisfy in part the requirements of tax-exempt status
- University missions: creation and dissemination of knowledge
- The challenge: for-profit corporations seek to keep information secret for competitive advantage

# Confidentiality

- Requires one or both parties to keep the other's proprietary information confidential for a defined period of time (typically 5 years, although we prefer 2 years or less)
- The challenge: Universities do not meet commercial standards of confidentiality

# Confidentiality Exclusions

- Typical exclusions exempt information which:
  - Is already in public domain;
  - Becomes publicly known through no fault of receiving party;
  - Receiving party acquires from 3<sup>rd</sup> party on non-confidential basis;
  - Is independently developed by anyone at receiving party who hasn't seen the info; or
  - Is required to be disclosed by law or court order

# Confidentiality Clause Pitfalls

- If dispute, clause often used as basis for breach of contract lawsuit because:
  - Easy to claim breach by unauthorized disclosure
  - Difficult to defend (prove no disclosure)
  - Definition of confidential information often open-ended as to form (written, tangible or oral), subject matter and/or time
  - Alleged damages due to disclosure are often very significant (\$\$)

# Performance & Deliverables

- University conducts research; does not guarantee results or solutions
- Reasonable efforts vs. best efforts
- Ownership of deliverables impacts IP rights and publication rights

# Disclaimer of Warranties & Limitation of Liability

- Entire provision must be “clear and conspicuous” (ALL CAPS)
- Theory:
  - Primary mission of education and research, so institutional decision not to assume risk
  - Unlike for-profit companies, we do not meet commercial standards of quality control

# Indemnification & Insurance in Research Agreements

- Need to be certain that University is not liable for a Sponsor's use of research results
- University does not purchase:
  - Products liability insurance
  - IP / non-infringement insurance

# QUESTIONS?

