

Drafting anew day

Who needs that ‘recital of consideration’?

By **Kenneth A. Adams**

It's hardly a shocking notion that any given contract could contain one or more provisions that reflect an inaccurate or outdated view of contract law. What's more noteworthy is the fact one such provision — the traditional recital of consideration — appears in most corporate agreements.

In this article, I explain why that traditional recital of consideration fails to serve its intended purpose and why omitting it could only improve a contract.

The ostensible function of a recital of consideration is to render enforceable a contract that would otherwise be held unenforceable due to lack of consideration. In corporate agreements, the recital of consideration is placed in the “lead-in,” which comes at the end of the recitals and serves to introduce the body of the contract.

A recital of consideration can be specific as to consideration — for instance, by stating that the consideration for Doe's promise is Acme's having paid Doe a given amount — but most often it is entirely vague. A representative, if relatively full-blown, example of a lead-in containing a recital of consideration is as follows: *NOW, THEREFORE, in consideration of the premises and the mutual covenants set forth herein and for other good and valuable consideration, the receipt and sufficiency of which*

are hereby acknowledged, the parties hereto covenant and agree as follows.

Recitals of consideration raise a number of issues of legal usage. For example, *NOW, THEREFORE* is archaic, while *in consideration of the premises* is simply an obscure way of saying “therefore” and is superfluous given the preceding “therefore.” And references to the value or sufficiency of consideration are outdated: With the rise of the “bargain test of consideration” reflected in the *Restatement (Second) of Contracts*, the focus of judges has shifted from the substance of the exchange to the bargaining process. Of greater interest, however, is whether traditional recitals of consideration in fact serve any purpose, or rather enough of a purpose to justify their presence.

For a traditional recital of consideration to fully serve its ostensible function, any inquiry as to whether a contract is supported by consideration would begin and end with the recital of consideration. In this respect, however, the utility of recitals of consideration is very circumscribed. For one thing, a recital cannot transform into valid consideration something that cannot be consideration.

If in a contract Acme makes an unenforceable promise to pay a consultant, Roe, a cash bonus for past services, that promise is not rendered enforceable by having Acme recite that the payment is “in consideration for past services.” (Since this is not the place for an overview of the relevant case law, I point you to E. Allan

Farnsworth, *Farnsworth on Contracts* 150 (2d. ed. 1998).) It follows that using instead the vague language of a traditional recital of consideration would be equally ineffective.

Similarly, a false recital of consideration cannot create consideration where there was none. If, in the contract between Acme and Roe, Acme recites falsely that the payment to Roe was in consideration of future services and Acme subsequently refuses to pay the bonus, Acme should prevail in any action brought by Roe if it succeeds in proving that the recital was false. (Again, see *Farnsworth*.) The outcome would be the same if the contract contained a traditional recital of consideration. Allowing a false recital — whether specific or vague — to trump a lack of consideration would effectively do away with the requirement of consideration.

Although these principles together indicate that recitals of consideration cannot remedy a lack of consideration, there is authority for the proposition that for purposes of option contracts and guaranties, a false recital of consideration will support a promise. (An option contract is a contract representing an irrevocable offer.)

Section 87 of the *Restatement (Second) of Contracts* provides that an option contract that is lacking in consideration is enforceable if it is in writing, is signed by the offeror, and “recites a purported consideration for the making of the offer.” In Section 88, the *Restatement* provides the same with respect to guaranties, and this is mir-

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rered by Section 9(b)(2) of the *Restatement (Third) of Suretyship*, which provides that no showing of real consideration is necessary if the writing evidencing a guaranty recites that consideration exists, whether or not that recitation is truthful.

You could conclude from this that while in most contexts a traditional recital of consideration would not be effective to create consideration where none exists, it nevertheless would be prudent to retain it so that it could be relied on in those contexts where a false recital of consideration would support a promise.

There are three problems with this reasoning. The first is that the approach of the *Restatements* not only elevates form over substance, but also would have the law recognize a sham. In his book *The Law of Suretyship and Guaranty*, Peter Alces says, in defense of Section 9(b)(2) of the *Restatement (Third) of Suretyship*, that “this rule makes a good deal of commercial sense,” as “the fact that a consideration, albeit nominal, is recited is enough to confirm that the parties came to terms on, or at least raised, the consideration issue.”

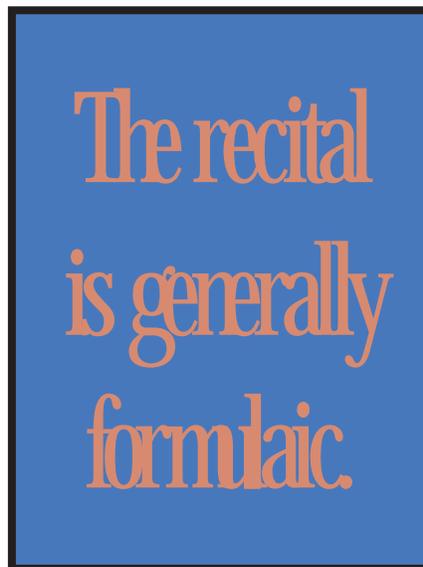
In my experience, however, corporate agreements are drafted and negotiated without the clients or their lawyers devoting a second's thought to the recital of consideration, which is generally formulaic.

Of more practical significance is the second problem, which is that the case law does not uniformly reflect the *Restatements'* approach. In the context of options, some courts have found a false recital to be legally effective, but others have held the opposite. And in the context of guaranties, the reporter's notes to Section 88 of the *Restatement (Second) of Contracts* cite only one decision of uncertain significance.

The third problem is that even if you assume the case law demonstrates unequivocally that there are contexts where a false recital of consideration would be effective to remedy a lack of consideration, by statute certain contracts no longer need to be supported by consideration. Under Section 2-205

of the Uniform Commercial Code, signed firm offers by merchants are enforceable without consideration. In addition, Section 5 of the New York General Obligations Law provides that an option contract does not need to be supported by consideration.

And under the Uniform Written Obligations Act, enacted only in Pennsylvania, any written release or promise will not be unenforceable for lack of consideration if the signer states that it intends to be legally bound; such statements are sometimes tacked on to the lead-in or concluding clause of a contract, but they are outside the scope of the recital of consideration as traditionally conceived. (Note that



unless it were validated by statute, as in Pennsylvania, I would not include in a contract a statement that the parties intend to be legally bound, as it is not a condition to the enforceability of a contract that the parties have, or explicitly express, an intent to be legally bound.)

So the traditional recital of consideration will in most contracts be ineffective to remedy a lack of consideration, while in the case of options contracts and guaranties, a recital of consideration either cannot be counted on to do so or would be unnecessary because the requirement for consideration has been dispensed with by statute.

That does not mean, however, that

recitals have no bearing on consideration: Since recitals can shed light on the parties' intent, courts give some weight to recitals of consideration when determining whether a promise is supported by consideration, but permit contrary evidence to be introduced.

But that does not constitute an argument for retaining the traditional recital of consideration. Given that the parties to a contract, and their lawyers, invariably give no thought to the traditional recital of consideration, a court should disregard it when determining whether a promise was supported by consideration.

Instead of relying on a traditional recital of consideration, you can craft recitals so as to ensure that they contain much more meaningful information pertaining to consideration. Recitals can serve a number of functions, one of which is to state briefly and in broad terms what the parties wish to accomplish by entering into the contract.

If Acme Financing were lending money to Widgetco on the strength of a guaranty from Doe, I would state in the recitals of the guaranty that it is a condition to Acme's lending the money that Doe provide Acme with the guaranty. I would also explain that Doe, as the principal shareholder of Widgetco, has an interest in Acme's providing financing to Widgetco.

In most contexts, providing this sort of information would simply help orient the reader, but on rare occasions when it is not otherwise readily apparent, it could help establish that the contract is supported by consideration. Instead of being shoehorned into the lead-in, this sort of information is best placed in the preceding recitals. Strictly speaking, recitals containing such information could be termed “recitals of consideration,” but they bear no resemblance to the traditional recital of consideration.

While there is value to knowing that an informative set of recitals could help a court to find consideration supporting a promise, in the vast majority of transactions the existence of consideration would be evident from the

rights and obligations of the parties; only in exceptional circumstances would a court be forced to look to the recitals.

In some of those cases, there may in fact be a lack of consideration, such as when a landowner grants to a potential purchaser, without receiving any payment in return, an option to purchase the property. (A lack of consideration would of course be irrelevant in a state that has enacted a statute eliminating the requirement of consideration for option contracts.) In such circumstances, reverting to a traditional recital of consideration in the hopes of satisfying any court called on to find consideration would, given the limited and mixed case law, seem reckless. If possible, you should instead remedy the lack of consideration, for instance by having the holder of an option pay a fee for it.

Assuming that a given set of recitals also contains, to the extent necessary, meaningful background information

relating to consideration, retaining the traditional recital of consideration would, in a substantive sense, be not so much pernicious as pointless. That does not mean, however, that nothing is lost by retaining it. For one thing, as long as the traditional recital of consideration continues to be widely used, corporate lawyers will continue to be under the misapprehension that it is effective to remedy a lack of consideration.

In addition, the impenetrable legalese of the traditional recital of consideration causes readers — whether lawyers, business people or judges — to needlessly stub their toes on the threshold of the body of the contract. It can also suggest to the discerning reader that the drafter is in thrall to the voodoo trappings of legal practice.

Stripping from the lead-in the traditional recital of consideration makes the lead-in much more readable. Once you eliminate the remaining archaisms

and redundancies, you are left with my preferred form of lead-in: *The parties therefore agree as follows.*

If you remain unconvinced that the drawbacks of the traditional recital of consideration merit changing an ingrained habit, consider that good drafting, like any form of writing, requires of the drafter myriad decisions on points of usage; opting for one inferior usage might not cause a problem, but if you take enough wrong turns it will quickly take a toll on the readability, efficiency and even enforceability of your drafting. The traditional recital of consideration is such an obvious candidate for the scrap heap that if you insist on retaining it, it is highly likely that other archaisms, inefficiencies and redundancies lurk in your drafting.

Of course, leaving the traditional recital of consideration out of a contract will occasionally cause other lawyers to suggest that you should restore it. Such are the perils of progress. **blt**