

## Outside Counsel

## Expert Analysis

# Reconsidering the Recital Of Consideration

By  
**Kenneth A.  
Adams**



In the United States, a standard feature of business contracts is a recital of consideration placed immediately before the body of the contract. Here's an example:

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:

In general, drafters shouldn't use this kind of recital of consideration or any other—they're unnecessary. This article explains why.

Let's start by considering the ostensible function of recitals of consideration.

The phrase 'in consideration of' can be used as a way to express, from the perspective of one side to a transaction, the exchange taking place. (The phrase 'as consideration' can serve this function too.) Here's an example:

In consideration of \$1,000, Able hereby sells the Equipment to Baker.

Such a recital of consideration might seek to express what the parties have actually bargained for. If instead what is being offered wasn't bargained for as part of an exchange, it's a pretense. In that case, the recital is said to provide for "nominal" consideration, usually a small amount of money.<sup>1</sup> And if the parties never intended for the amount stated—whether bargained for or not—to be paid, that too involves pretense, and the recital is said to provide for "sham" consideration.<sup>2</sup>

### Backstop Recitals

That's the taxonomy of consideration you find in case law and commentary, but it's not complete. It doesn't explain the kind of recital of consideration routinely placed just before the body of the contract, like the one at the beginning of this article.

Such recitals of consideration don't specify consideration but merely assert that it exists. In contracts in which such recitals occur, an exchange constituting the actual consideration is usually specified explicitly elsewhere in the contract, albeit without labeling it as consideration.

The only possible function of such recitals of consideration would be to establish that the contract is supported by consideration even if the contract

otherwise doesn't attempt to state consideration or states something that isn't valid consideration. That's why this article calls them "backstop" recitals of consideration. (A backstop is a person or thing placed at the rear of or behind something as a barrier, support, or reinforcement.) Like nominal and sham consideration, backstop recitals of consideration are a form of pretense.

In recent years, some courts have indicated that a backstop recital of consideration is sufficient to support a contract.

But in this author's experience, practitioners and clients pay no attention to backstop recitals of consideration. They're simply a standard feature of copy-and-paste drafting and as such are blithely recycled.

### Pretense Consideration

Nevertheless, could a backstop recital of consideration alone be enough to establish that a contract is supported by consideration? According to commentary, the answer is no: Because both nominal and sham consideration are a pretense, they don't generally constitute consideration,<sup>3</sup> and by extension that applies to backstop consideration too. (Option contracts and guarantees are discussed below.) Instead, courts generally give a recital of consideration some weight but permit contrary evidence to be introduced.<sup>4</sup> That makes sense—if a backstop recital of consideration were all that it takes to establish consideration, that would nullify the requirement of consideration.<sup>5</sup> Every contract would include a backstop recital of consideration and we could all forget about the requirement of consideration.

But in recent years, some courts have indicated that a backstop recital of consideration is sufficient to support a contract. For example, in *Network Pro-*

*tection Sciences v. Fortinet*,<sup>6</sup> the U.S. District Court for the Northern District of California, applying Texas law, held that a recital stating that the patents at issue were assigned "[f]or good and valuable consideration, the receipt of which is hereby acknowledged," was "conclusive" on the issue of consideration.

And in *Urban Sites of Chicago v. Crown Castle USA*,<sup>7</sup> the Appellate Court of Illinois pointed to a backstop recital of consideration in stating, in dictum, that "the evidence contained in the record establishes that there was adequate consideration as a matter of law."

One could argue that based on such cases, it would be prudent always to include a backstop recital of consideration in a contract, in case a dispute comes before a court that is misinformed regarding the law of consideration or is willing to rely on pretense consideration to achieve a given outcome. But that's too speculative a prospect to justify cluttering every contract with a backstop recital of consideration.

### Rebuttable Presumption

There's case law to the effect that a recital of consideration establishes a rebuttable presumption that consideration exists.<sup>8</sup> That has led one commentator to recommend including a backstop recital of consideration in contracts governed by the law of a state that recognizes the rebuttable presumption.<sup>9</sup>

But that accomplishes little. For one thing, in the case of sham consideration or a backstop recital of consideration, rebutting that presumption would simply require showing lack of any payment or other exchange that could constitute consideration. Moreover, the rebuttable presumption doesn't make sense when applied to backstop recitals of consideration: They state no specific consideration, so anyone looking to rebut the presumption would have nothing specific to rebut.

More fundamentally, if you're invoking the rebuttable presumption, you're already in a fight. A characteristic of the approach underlying traditional contract drafting—what this author calls "passive drafting"—is a focus on prevailing in disputes. It makes more sense to engage in "active drafting," with the aim of avoiding disputes by stating clearly what the deal is.<sup>10</sup> Those who draft or review contracts (as opposed to those who litigate contract disputes) have available simple and effective alternatives to invoking in a dispute a recital of consideration that's a pretense—whether it's nominal or sham consideration or a backstop recital of consideration.

KENNETH A. ADAMS is author of *A Manual of Style for Contract Drafting* (3d ed. 2013) and president of Adams Contracts Consulting.

## Structuring Consideration

First, state any actual consideration clearly. (But don't state it as a recital of consideration; see "Eliminating Other References," below.)

Second, if a transaction actually lacks consideration, fix that. For example, if a party to an existing contract wants the other party to agree to a disadvantageous change in the terms, that change might be enforceable only if the party agreeing to the change has received consideration for doing so. If that consideration is lacking, then arrange for appropriate consideration and state it clearly in the contract.

Third, the performing party could waive consideration and acknowledge that the other party will be relying on that waiver. Most U.S. courts would probably view reliance as an independent basis for enforcing a promise, so reliance might make a promise enforceable even in the absence of consideration.<sup>11</sup>

And fourth, you can take advantage of formalities offered by law as a way to establish consideration, although they're annoyingly legalistic. If the governing law requires no consideration for contracts under seal, you could make the contract one under seal.<sup>12</sup> And under the Uniform Written Obligations Act, enacted only in Pennsylvania, a written release or promise will not be unenforceable for lack of consideration if the signer states that it intends to be legally bound—a statement that otherwise serves no purpose in a contract.<sup>13</sup>

Eliminating any function for pretense consideration would allow you to eliminate recitals of consideration. As regards backstop recitals of consideration, you could drop from them any mention of consideration and all associated clutter, notably 'good and valuable'<sup>14</sup> and 'receipt and sufficiency.'<sup>15</sup> Dispense with any remaining archaisms and you're left with a simple lead-in to the body of the contract: "The parties therefore agree as follows" (if the contract contains recitals) or "The parties agree as follows" (if there are no recitals).

## Option Contracts

But option contracts and guarantees must be considered separately.

Section 87(1) of the Restatement (Second) of Contracts suggests that in option contracts, a recital of nominal consideration supports a promise. Under the Restatement's approach, it would be irrelevant whether the nominal consideration is in fact paid.<sup>16</sup>

Some courts have endorsed the Restatement's approach—for one, the Supreme Court of Texas.<sup>17</sup> So one might conclude that although in most contexts nominal or sham consideration or a backstop recital of consideration wouldn't establish consideration where none exists, it would be prudent to retain such recitals in option contracts.

But the Restatement's approach remains the minority position.<sup>18</sup> In jurisdictions that haven't adopted the Restatement's approach, the prudent thing to do would be to set a plausible option price, recite it in the contract, and make sure it's paid.

You might want to do that even in jurisdictions that have adopted the Restatement's approach. It would allow you to avoid relying on something that doesn't make sense—a sham endorsed by law.<sup>19</sup>

If you wish to rely on the Restatement's approach, consider using nominal consideration instead of a backstop recital of consideration—even if a court might otherwise be inclined to accept pretense consideration, it's not clear how courts would react to backstop recitals of consideration. The case law on option contracts mostly involves a recital of a con-

sideration for a stated amount of money, and the illustrations in the Restatement involve purported consideration in the form of stated amounts of money.

Thankfully, you can safely dispense with consideration for option contracts governed by the law of a state that has by statute specified that option contracts don't need to be supported by consideration. New York is one such state.<sup>20</sup> And section 2-205 of the Uniform Commercial Code says that a firm offer to buy or sell goods is not revocable for lack of consideration.

## Guarantees

As regards what constitutes consideration, guarantees are analogous to option contracts.

If Able guarantees Baker's debt to Charlie at the same time as Baker incurs that debt, Charlie's willingness to lend money to Baker is valid consideration for Able's promise to pay Baker's debt. Generally that's not the case if Able guarantees Baker's debt after Baker incurs it.<sup>21</sup>

But section 88 of the Restatement (Second) of

---

Section 87(1) of the Restatement (Second) of Contracts suggests that in option contracts, a recital of nominal consideration supports a promise. Under the Restatement's approach, it would be irrelevant whether the nominal consideration is in fact paid.

Contracts and section 9 of the Restatement (Third) of Suretyship suggest that for purposes of guarantees, a false recital of consideration would support a promise. The case law endorsing that approach is negligible, so it would be rash to assume that a court would endorse it for purposes of a given contract. Able must have some reason for guaranteeing Baker's existing debt. Because that reason constitutes Able's consideration, Charlie the creditor would be better protected by having that reason stated in Able's guarantee instead of relying on pretense consideration.

## Eliminating Other References

As noted above, the phrases 'in consideration of' and 'as consideration' can be used to express part of the actual exchange taking place in a transaction, as contrasted with use of either phrase in stating pretense consideration.

But those phrases can fail to make it clear what is happening. Consider again the example offered above: In consideration of \$10,000, Able hereby sells the Equipment to Baker.

In this example, is the \$10,000 being paid at signing? In that case, it would be clearer to say the following:

Able hereby purchases the Equipment from Baker for \$10,000, which Baker acknowledges having received from Able concurrently with the parties' signing this agreement.

Or is the \$10,000 being paid later? In that case, it would be better to express payment by Able as an obligation:

Able hereby purchases the Equipment from Baker for \$10,000, which Able shall pay Baker no later than 30 days after the date of this agreement.

So in addition to dispensing with backstop recitals of consideration (along with nominal and sham consideration), you should be able to dispense entirely

with the word 'consideration' to express any part of a bargained-for exchange. You should have no qualms about that—referring to consideration as such has no bearing on whether a given transaction is supported by consideration.<sup>22</sup>

1. See 2-5 ARTHUR LINTON CORBIN, CORBIN ON CONTRACTS §5.17 (Joseph M. Perillo ed., 2015) [hereinafter CORBIN ON CONTRACTS].

2. See id.

3. See id.

4. See 3 RICHARD A. LORD, WILLISTON ON CONTRACTS §7:23 (4th ed. 2015) [hereinafter WILLISTON ON CONTRACTS]; 17A AM. JUR. 2d Contracts §111.

5. See WILLISTON ON CONTRACTS, supra note 4, §7:23 ("It would destroy the requirement of consideration to hold that an admission of consideration in an unsealed writing prevented the promisor from showing that no consideration existed.")

6. No. C 12-01106 WHA, 2013 WL 4479336, at \*6 (N.D. Cal. Aug. 20, 2013).

7. 2012 IL App (1st) 111880, ¶39, 979 N.E.2d 480, 493.

8. See 3 WILLISTON ON CONTRACTS, supra note 4, §7:22.

9. See TINA L. STARK, DRAFTING CONTRACTS: HOW AND WHY LAWYERS DO WHAT THEY DO 86 (2d ed. 2014).

10. See Kenneth A. Adams, "Eliminating the Phrase 'Represents' and 'Warrants' from Contracts," 16 Tenn. J. Bus. L. 203, 227-28 (2015) (comparing passive drafting and active drafting).

11. See 3 WILLISTON ON CONTRACTS, supra note 4, §7:2.

12. See KENNETH A. ADAMS, A MANUAL OF STYLE FOR CONTRACT DRAFTING ¶5.41 (3d ed. 2013).

13. See id. ¶2.156.

14. See Kenneth A. Adams, "Good and Valuable Consideration," Adams on Contract Drafting (Nov. 16, 2015), <http://www.adamsdrafting.com/good-and-valuable-consideration/>.

15. See 1-3 JOHN EDWARD MURRAY, JR., MURRAY ON CONTRACTS §60[A] (5th ed. 2011) ("Sufficiency," however, is often used as a redundant qualification of the existence of consideration. Yet, consideration either exists or it does not exist, i.e., one cannot find 'insufficient' consideration and still have 'some' consideration.")

16. See id. §62[B][4] (stating that under the Restatement's position, "it is irrelevant whether the recited amount has or has not been paid since the payment of a nominal sum is not the inducement for the promise").

17. 1464-Eight v. Joppich, 154 S.W.3d 101, 110 (Tex. 2004).

18. See id. at 110; MURRAY, supra note 15, §62[B][4] (quoting Joppich).

19. See 2-5 CORBIN ON CONTRACTS, supra note 1, §5.17 (describing fictional recitals of a purported consideration as "charades" that "should not be a part of a mature legal system").

20. N.Y. GEN. OBLIG. LAW §5-1109 (McKinney 2015).

21. See MURRAY, supra note 15, §62[B][2].

22. See 17A AM. JUR. 2d Contracts §110 ("Consideration for a contract need not be recited or expressed in the writing, since, if not expressed, consideration may be implied by or inferred from the terms and obvious import of the contract, or it may be proven by parol evidence.")