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Efforts Clauses - Drafter Beware

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Efforts clauses

Efforts clauses are common in commercial agreements, including those involving real estate. Where one or both parties cannot guarantee a particular outcome, efforts clauses attempt to qualify obligations. Typically, efforts clauses require a party to expend some level of effort to achieve a desired result. For example: "The Tenant shall use [best], [reasonable], [commercially reasonable] efforts to obtain permits and approvals for the proposed use." But how much effort is a party required to expend in achieving a result? Is there a difference between "best efforts," "reasonable efforts," "commercially reasonable efforts"? Do courts see a difference or rank these terms in some sort of hierarchy? Are there ways to draft an efforts clause that can keep a litigator from later coming out of the mists to shoot the wounded?

The three most common efforts clause standards are "best efforts," "reasonable efforts," and "commercially reasonable efforts." Many transactional attorneys see and believe these terms are distinct and are ordered in a clear hierarchy: best efforts being the most demanding, reasonable efforts as somewhat lesser, and commercially reasonable as the least demanding.

However, the UCC and case law do not necessarily or clearly support this view or a hierarchy among the terms. The UCC, for example, uses various formulations interchangeably. UCC Section 2-306(2) and its related Comment 5 use "best efforts" interchangeably with "good faith and reasonable diligence." Case law is also far from univocal in its interpretations of and holdings about efforts clauses.

Courts and uncertainty

In interpreting efforts clauses, a court often will first look to see if the chosen term is defined in the contract or agreement where it is found. If it is defined, and the definition itself is clear, the court will apply the definition. In fact, some courts will only enforce an efforts clause where the underlying agreement includes objective guidelines or criteria against which a party's efforts can be measured. See, e.g., *DaimlerChrysler Motor Co. LLCZ v. Manuel*, 362 S.W. 3d 160 (Tex.App. 2012) and *Kevin M. Ehringer Enter. v. McData Serv*. 646 F.3d 321, 326 (5th Cir. 2011). This is not the rule in other jurisdictions, and parties often do not define in their contracts what is meant by "best", "reasonable" or "commercially reasonable efforts." This means in the event of a dispute, the parties will leave it to the court to do the defining—determining not only whether an effort has been made, but what level of effort was required. Courts have wide latitude in determining these matters. A court's interpretation will often turn on situation-specific circumstances, factors, and jurisdiction-specific legal principles. Accordingly, it is important to understand the principles courts in the relevant jurisdiction have applied, although even within a given jurisdiction the rules may not be entirely clear.

For example, New York courts have held that "best efforts" and "reasonable efforts" are interchangeable. However, New York courts also have held that there is a hierarchy, with "best efforts" being a more onerous standard than "reasonable efforts." This divergence led Judge Friendly to remark that New York law on the matter was "far from clear." See, *Bloor v. Falstaff Brewing Corp*., 601 F.2d 609 (2nd Cir. 1979). And while Judge Friendly made his observation many years ago, numerous commentators have noted that the lack of clarity remains.

Other jurisdictions have added their own twists. Delaware courts, for example, have held that "commercially reasonable efforts" or "best efforts" obligate parties to cooperate in challenging circumstances. See, e.g., *Williams Companies, Inc. v. Energy Transfer Equity L.P*., 159 A. 3d 264 (Del. 2017) and *Akron, Inc., v. Fresenius Kabi AG*, 2018 WL 4719347 (Del. Ch. Oct 1, 2018), aff'd. 198 A.3d 724 (Del. 2018).

Massachusetts courts view efforts clauses flexibly with an eye towards "acting in good faith," and "reasonably." For example, Massachusetts courts have held that "[b]est efforts" do not require "unreasonable, unwarranted or impractical efforts and expenditures of time and money out of all proportion to economic reality," and did not entail a duty "to make an investment that would be significantly different in kind from that contemplated by the agreement, involving additional outlay or alteration of the business risks." *Macksey v. Egan*, 36 Mass.App.Ct. 463, 471-472 (1994).

In most jurisdictions, unless the document defines the efforts term or clause, in determining whether an efforts clause is satisfied a court will apply rules of interpretation, which can include a consideration of the relevant facts and circumstances. In fact, most courts agree that to determine whether a party has satisfied an efforts clause, no matter the formulation, the court must conduct a fact-intensive analysis. This can implicate unique and arcane industry practices and standards, the specific facts of the case, and the parties' business relationship.

Reducing uncertainty

Given the divergence of the case law around the country on these issues, there are good reasons to proceed with caution when it comes to employing efforts clauses in agreements. Here are some things contract drafters can do that may help to reduce uncertainty.

1. **If possible, avoid efforts clauses.** Make the desired result an express obligation.
2. **If unavoidable, define the words.** Give the court a standard. Try to eliminate judicial subjectivity. For example, if the effort could involve additional costs, set a not-to- exceed amount. If an attempt to obtain permits is involved, define whether appealing a denial or defending a permit obtained is part of the best, reasonable, or commercially reasonable effort. Define efforts that are not required, e.g., in no event shall the party who is required to use efforts be required to do [fill in the blank].
3. **Use objective criteria.** If a party needs to take action, state not only the action, but a date by which an action needs to be given or taken and the manner in which it should proceed.

Final thoughts

While there is much uncertainty around efforts clauses, especially when subject to judicial review, a few conclusions can be drawn:

- Unless specifically agreed, no efforts clause requires a party to do everything possible to achieve a desired result;
- Depending on the jurisdiction, "best" and "reasonable" or "even commercially reasonable" may mean the same or nearly the same—or they may not; so better to try to define the effort more specifically and not rely on the shorthand;
- If the desired result is important, and the counterparty is unwilling to commit to an absolute obligation, consider objective details and definitions to take the interpretation out of a court's hands and, hopefully, eliminate a litigator's playground.