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Drafting Agreements With a Litigator's Eye: a Practical Guide

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VIEWING commercial contracts from a litigator's perspective may minimize recurring litigation issues that commonly arise in corporate agreements and increase the likelihood of a better outcome should litigation happen. Some of the root causes of litigation involving contracts are: (a) ambiguity; (b) the inclusion of provisions that appear unfair or inequitable; (c) the failure to take into account the larger implications of an agreement; (d) the failure to recognize that judges, juries and arbitrators will not always enforce a provision as written even though it is clear and finds support in the law; and (e) the use of forms from previous transactions.

Consider the following drafting strategies that may help avoid the foregoing problems.

Overall Approach

The Importance of Clarity. In the drafting of any agreement, it is critical to include clearly expressed contractual obligations. Clarity provides increased certainty to the parties, minimizes the risk of litigation, and ultimately minimizes the duration and complexity of litigation. However, clarity is more than an absence of ambiguity. An agreement should contain all definitions, terms and provisions necessary for a stranger to the agreement to understand exactly what the parties have agreed to. Therefore, when counsel draft corporate documents it is important to write for the trier of fact. You undoubtedly know the exact details of the parties' negotiation and terms, but in the event of any dispute only the actual document will be considered.

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Clarity does not require the inclusion of unnecessary detail. For example, if the agreement requires the parties to address an issue at a future date, the CEO or CFO should not be identified (by name or title). Indeed, the mention of the name of any personnel should be avoided if possible. Such persons will be the first to have their depositions noticed in litigation.

Although finalizing a deal is often dependent on "finessing" language, such provisions should nevertheless be as clear as possible. Terms such as "good faith," "reasonable," "best efforts," "materially" and "related" are particularly problematic and should be avoided. They increase the likelihood of litigation and virtually assure the presence of issues of fact that preclude entry of summary judgment.

In summary, clarity is best achieved in plain English than with florid prolixity.

Fairness. Occasionally agreements include provisions that appear unfair to an impartial observer. Such provisions, even though legal, should be avoided because as a practical matter, courts and arbitrators will often find a way either not to enforce or to mitigate the effects of a provision they deem to be unfair. For example, requiring an employee located in New York to consent to jurisdiction in California in the event of a dispute, while legal, may not always be enforced. The provision appears to be unfair and cause significant hardship to the employee.

The Larger Implications. In the representation of large, diverse companies, it is important to recognize that agreements entered into by one division of the company may have unintended consequences on a different division of the same company. The drafter must consider potential conflicts between entities with respect to the agreement, whether the entity that was not a party to the agreement can or will in fact deliver what is expected of it in the agreement and whether another entity should also be a party to the agreement. Moreover, contract counterparties will not recognize that a company is comprised of separate business units. If one business unit makes a representation, it will for all practical purposes bind the company as a whole.

Will This Provision Accomplish What I Want? When an agreement contains a clear provision that the opposing party has indisputably breached, courts may nevertheless refuse to enforce the contractual provisions as written, if the provision is overly harsh. For example, corporations often put venue provisions in employment agreements. If an employee is located outside of the venue chosen, courts may not enforce the provision, since it would cause hardship to the employee. Even if the agreement has been drafted perfectly, there are some provisions that, while enforceable, are unlikely to afford complete relief in practice.

Careful Use of Precedents

Form precedents and "boilerplates," while helpful, must be used carefully. Some of the more important common provisions routinely included in corporate agreements that can impact a litigation are as follows.

Choice of Law. Choice of law provisions can be useful in providing certainty. They are generally enforced by courts and arbitrators, as long as the selection of the law is rationally related to the transaction. A choice of law provision can have crucial implications. For example, choice of

California law would be unwise for an employer in an employment agreement that contains non-competition provisions, since such provisions are difficult, at best, to enforce in California.

Integration and “No Representation” Clauses. Most courts will enforce properly worded integration clauses and prohibit the introduction of parol evidence to vary or alter the terms of the writing. This may not be true for arbitrators. The most frequently litigated exceptions to this rule occur when the agreement is ambiguous or when a party alleges that it was fraudulently induced to enter into the agreement.

It is also advisable to insert a “No Representation” clause making clear that neither party relied on any representations outside of the agreement. This clause will typically preclude a dissatisfied party from arguing that he was fraudulently induced into entering into the written agreement. It is important to use an integration clause only after you have confirmed that all relevant terms from previous agreements are included in the current agreement. In addition, any side agreements should be incorporated by reference into the agreement that contains the integration clause.

Choice of Dispute Resolution

Arbitration. While current conventional wisdom favors arbitration as a cheap and quick alternative, arbitration is no panacea. Judges are willing to grant dispositive motions, but arbitrators almost never grant these types of motions. Arbitrators emphasize achieving an equitable result rather than the result that would be required by the strict application of the law. Discovery is limited in arbitration. There is also no meaningful appeal from an arbitrator’s decision.

Historically it has been thought (and many still maintain today) that arbitration is less expensive and faster than litigation. This may hold true for short, simple cases. For cases of greater complexity, however, arbitration can be as expensive as traditional litigation and more time-consuming. Arbitration clauses permit the parties to fashion many aspects of the arbitration process including the number of arbitrators, the requisite background and experience of the arbitrator(s), and discovery methods, and more substantive provisions such as no recovery of interest or punitive damages and whether attorney’s fees are recoverable.

Mediation. Mediation is generally nonbinding. It serves the useful purpose of focusing the parties on the issues in dispute and on reaching a resolution of those issues. It is also helpful to get a third party’s view on the strengths and weaknesses of the case. However, inserting a provision requiring mediation before proceeding with litigation is rarely a good idea. Mediation can be expensive, especially when using a private dispute resolution organization. However, some



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courts will offer mediation services free of charge or even require it.

Mediators view success as the consummation of a settlement—any settlement. As a result, mediation may favor the more intransigent party, since the mediator will not achieve a settlement if the more recalcitrant party is not pacified.

State or Federal Court. The court system remains an effective forum for dispute resolution. The rules of the courts are clear and well developed, full discovery is permitted, application of the law is the norm, busy judges want to dispose of meritless cases, and adverse rulings may be appealed.

Large corporations are often concerned about litigating in courts because juries are unpredictable and sometimes tend to view the corporation as the proverbial “deep pocket.” One way of addressing that concern is to waive the right to a jury trial. Most jurisdictions will enforce a clear and unambiguous jury trial waiver provision; however, it is important to check the law in the particular jurisdiction. In federal court, the validity of a jury trial waiver is determined by federal law.

Overall, non-jury trials are faster than jury trials and less expensive, and substantially reduce the likelihood of runaway damage awards.

Consent to Personal Jurisdiction and Venue. Parties to a contract may agree in advance to submit themselves and/or the controversy to the jurisdiction of a given court. The parties cannot consent to confer subject matter jurisdiction on a federal court—the court either does or does not have subject matter jurisdiction based on diversity of citizenship or federal question.

There are two general types of venue or forum selection provisions. A mandatory forum selection clause grants exclusive jurisdiction to a selected forum; a permissive forum selection clause only reflects the parties’ consent to resolve disputes in a certain forum, but does not require that disputes be resolved in that forum.

The rules in federal and state court can be somewhat different depending on the jurisdiction where the litigation is pending. For example, New York state courts will enforce a forum selection clause that reasonably conveys the parties’ intention to select an exclusive forum. In contrast, many federal courts require that the contract contain “exclusion language” that makes clear that the forum selected is mandatory rather

than permissive. There are no magic words, but specific language of exclusion must be used. If a forum selection clause is permissive, it is still subject to challenge on forum non conveniens, venue and transfer grounds.

Liquidated Damages

By agreeing to a liquidated damages provision, parties agree to forgo their actual damages in favor of a fixed approximation ex ante of those damages. These provisions are generally enforceable if the damages are difficult to calculate and the approximation is reasonable. The provision will not be enforced if it is viewed as a penalty to the breaching party.

It is important to consider that a liquidated damages provision may simplify the litigation process, as the amount of damages may no longer be an issue, which may obviate the need for expert testimony.

Attorney’s Fees Provisions

Courts usually enforce unambiguous contractual provisions that provide for the recovery of reasonable attorney’s fees. It is important to use the phrase “attorneys’ fees” explicitly (as opposed to simply “costs” or “fees”).

Conclusion

In sum, in the drafting of agreements, it is important to remember to: (1) have clarity; (2) provide fairness; (3) recognize and account for larger implications; (4) accomplish goals of the written provisions; and (5) use precedents carefully.

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