Incorporating a Litigator's View in Transactional Matters Avoids Later Problems

by Robert M. Travisano

Asset sales and other corporate transactions can benefit from the involvement of a litigator. While deal counsel typically is focused on closing the transaction itself, a litigator can lend perspective to what may arise down the road if, for whatever reason, the parties fail to live up to their obligations under the agreement. In addressing that exigency in the context of cross-state transactions, it is important to obtain a litigator's input on the handful of contractual provisions that ultimately could affect the outcome of a dispute over the terms of the transaction. Such provisions typically include choice of law, forum selection and dispute resolution clauses. Following is a non-exhaustive discussion of some common issues related to these three types of clauses.

Choice of Law Clauses

The application of one state's law versus that of another can be critical to the outcome of a legal dispute. It may affect a litigant's very ability to maintain a legal action (in the case of statutes of limitation or repose), overall liability (application of charitable immunity or comparative fault laws) or even the amount and types of damages a plaintiff may be able to recover. Rather than blindly casting a client's lot to some court's potentially amorphous interest analysis relative to which law applies, including a choice of law clause in the transaction agreement should alleviate a large part of the mystery.

It is important to note at the outset that a federal court exercising its diversity jurisdiction will utilize the choice of law rules of the state in which the action is pending.[1] The practical impact of this rule is that the law of the selected state memorialized in the agreement will not automatically apply from the matter's inception in federal court. Rather, the forum state's law will govern with respect to which law applies in the first instance and throughout the litigation with respect to procedural issues.

For the most part, New Jersey law regarding the enforcement of choice of law clauses is well settled. Where parties to a contract have agreed to be governed by the laws of a particular state, New Jersey courts ordinarily will give effect to the parties' choice of law, unless it violates public policy.[2] This bright line rule, of course, is not without exception. Notwithstanding the fact that the parties may have memorialized in an agreement their choice of governing law, New Jersey law nonetheless will apply where: 1) the chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties' choice; or 2) application of the designated state's law would be contrary to a fundamental policy of a state that has a materially greater interest than the chosen state with respect to a particular issue and that would otherwise be the state whose law would be applied had the parties not chosen the governing law.[3]

A substantial relationship exists where one of the parties is headquartered within that state.[4] The fundamental policy prong of the equation is less clear and subject to an issue-by-issue and state-versus-state analysis. For an instance of where a court eschewed a California choice of law clause and instead applied New Jersey law based upon policy considerations, *see Instructional Sys. Inc. v. Computer Curriculum Corp.*[5]

By way of example, where a business with a New Jersey headquarters institutes a breach of contract action in the District of New Jersey against a New York counterparty and the agreement at issue contains an Alaska choice of law clause, the party espousing the application of Alaska law (without more) will have an uphill battle convincing the court to give effect to the choice of law. Indeed, in this law school exam-type hypothetical, Alaska has no relationship to the parties or the subject matter of their agreement. When preparing a cross-state asset purchase or other transactional agreement, it is important for the drafters not to overreach in their choice of law. Approaching the issue from a practical perspective is advisable. Certainly, under New Jersey law, more than a passing connection to a state likely is required for the application of that state's law, even if the applicable law is designated in the agreement.

Forum Selection Clauses

Being forced to litigate in a jurisdiction far from home can be a daunting experience for a number of reasons. Notwithstanding technological advances or multi-law office firms/capable local counsel, just the mere time commitment involved in witness travel to and from a foreign jurisdiction can cause immeasurable business disruption to a client. Selecting a reasonable forum in advance of a dispute and memorializing it in the agreement should neutralize this upheaval before it occurs.

Generally, forum selection clauses will be enforced by New Jersey courts.[6] However, such clauses *will not be given effect* if they are the result of fraud or the exercise of coercive bargaining power.[7] It is not enough to allege that one was induced generally to enter into the agreement at issue as a result of fraud.[8] Instead, fraud or overreaching are only grounds for setting aside a forum selection clause where it has been determined that the *inclusion of the clause itself* was the product of deception or coercion.[9]

Another factor New Jersey courts will consider is whether enforcement of the forum selection clause would be "seriously inconvenient for the trial."[10] The inconvenience prong of the analysis will come into play only where a "trial in the contractual forum will be so gravely difficult and inconvenient that [the party] will for all practical purposes be deprived of his day in court."[11] Finally, New Jersey courts will apply the familiar touchstone of whether the cause at issue violates a strong public policy.[12] Like the public policy analysis related to choice of law clauses, the impact of this prong is determined on a case-by-case basis.

Recently, the U.S. Supreme Court came down strongly in favor of the enforcement of forum selection clauses. In *Atlantic Marine Construction Co. v. United States Dist. Court*, the Court held that in the context of a motion to change venue, "[w]hen the parties have agreed to a valid forum-selection clause," it should be enforced, unless there are "extraordinary circumstances unrelated to the convenience of the parties."[13] The enforcement of such "bargained for" clauses, the Court noted, protects the parties' "legitimate expectations and furthers the vital interests of the justice system."[14] The Court's rationale behind this ruling was crystal clear:

> When parties have contracted in advance to litigate a dispute in a particular forum, courts should not unnecessarily disrupt the parties' settled expectations. A forum-selection clause, after all, may have figured centrally in the parties' negotiations and may have affected how they set monetary and other contractual terms; it may, in fact, have been a critical factor in their agreement to do business together in the first place. In all but the most unusual cases, therefore, 'the interest of justice' is served by holding parties to their bargain.[15]

Of course, the Supreme Court's analysis in *Atlantic Marine* assumed the validity of the clause at issue therein; however, such a strongly worded decision is sure to reverberate through those lower courts faced with determining whether to enforce a forum selection clause.

Dispute Resolution Clauses

Given the cost of litigation in the current legal environment (especially since the advent of e-discovery and its related potentially burdensome litigation holds) and the overwhelming backlog in the courts, it is advantageous for contracting parties to include some type of dispute resolution clause in their agreements, whether it be a straightforward arbitration clause or one requiring the parties to submit to non-binding mediation as a condition precedent to filing a lawsuit or arbitration. Against that backdrop, the benefits of alternative dispute resolution mechanisms are legion both from a cost-saving and time-saving perspective.

Arbitration is a favored mechanism pursuant to federal and New Jersey statutes.[16] Notwithstanding the well-established preference toward arbitration, New Jersey courts will not simply rubber-stamp the process and order the parties to arbitration. An agreement to arbitrate is a contract, and is subject to the legal rules of contract construction. Put another way, a court must satisfy itself that an agreement exists (*i.e.*, in the absence of a consensual understanding, neither party is entitled to force the other to arbitrate a dispute).[17] The consensual nature of an arbitration agreement will be less of a concern in a dispute involving two sophisticated commercial parties.

Next, the court will evaluate whether the particular claims at issue fall within the clause's scope.[18] In doing so, the court will look to the language of the clause itself to establish its boundaries—without rewriting the contract to broaden the scope of arbitration.[19] Nevertheless, given their favored status, agreements to arbitrate are read liberally in favor of arbitration.[20]

Depending upon the scope of the clause, certain legal claims may not be arbitrable. For example, in a case involving an asset purchase agreement containing a clause instructing the parties to arbitrate disputes relating to the "interpretation of [the] Agreement," a court refused to refer to arbitration claims sounding in fraudulent inducement and negligent misrepresentation.[21] Similarly, a claim for unjust enrichment was not arbitrable because it was predicated on the absence of a valid contract that by its essence could not involve the interpretation of a definite agreement.[22] It is important for drafters of these clauses to appreciate their client's motivations and expectations in preparing the scope of the provisions.

Conclusion

This article highlights some of the issues that may arise with respect to choice of law, forum selection and dispute resolution clauses in transaction agreements. The impact of these provisions may have far-reaching effects on the results of a client's dispute and overall deal. Involving an attorney in the drafting process who has experience litigating these clauses could minimize future uncertainty in their interpretation, or at least provide a client with an understanding of the implications of various drafting options. ■

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Endnotes

1. *See Hoffer v. Infospace.com, Inc.,* 102 F. Supp. 2d 556, 562 (D.N.J. 2000).
2. *See North Bergen Rex Transp. v. Trailer Leasing Co.,* 158 N.J. 561, 568-69 (1999).
3. *Id.*
4. *Id.* at 569.
5. 130 N.J. 324, 342-46 (1992) (recognizing New Jersey's strong policy of protecting its franchises).
6. *See Copelco Capital v. Shapiro*, 331 N.J. Super. 1, 4 (App. Div. 2000).
7. *Id.*
8. *See Hoffer,* 102 F. Supp. 2d at 563-64.
9. *Id.* at 563.
10. *See Copelco Capital*, 331 N.J. Super. at 4.
11. *Id.*
12. *See Id.* at 4.
13. 134 S. Ct. 568, 581 (2013).
14. *Id.*
15. *Id.* at 583.
16. *See* Federal Arbitration Act, 9 *U.S.C.A.* §§1-16; Arbitration Act, N.J.S.A. 2A:23B-1 to 32.
17. *See Moore v. Woman to Woman Obstetrics & Gynecology, L.L.C.,* 416 N.J. Super. 30, 37 (App. Div. 2010).
18. *See Hirsch v. Amper Fin. Servs.,* 215 N.J. 174, 179 (2013).
19. *Id.*
20. *See Garfinkel v. Morristown Obstetrics & Gynecology Assocs., P.A.,* 168 N.J. 124, 132 (2001).
21. *See RCM Tech., Inc. v. Constr. Servs. Assocs.,* 149 F. Supp. 2d 109, 113-14 (D.N.J. 2001).
22. *Id.* at 114.