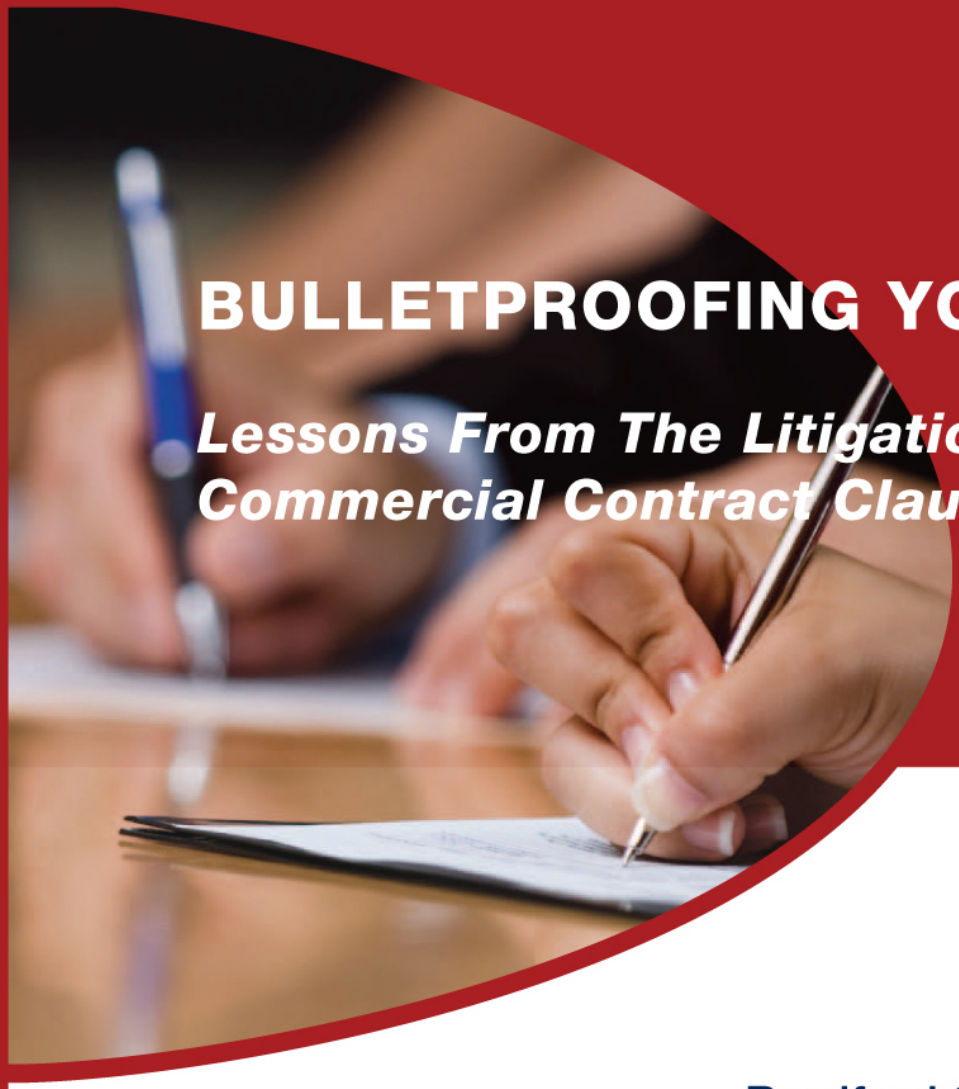

BULLETPROOFING YOUR DEALS 2010

Lessons From The Litigation Battlefield On Commercial Contract Clauses

Bradford S. Babbitt and William J. Egan

ROBINSON & COLE LLP
ATTORNEYS AT LAW

Commercial Contract Clauses

- The “rules of engagement”
- Disputes can delay and can determine outcome
- Risks posed by “boilerplate”

Limitations on Liability

Liability Limits – Goals

- **Prohibit certain forms of monetary relief**
  - Consequential or punitive damages
- **Cap damages**
  - Consideration paid under the contract
- **Prohibit non-monetary relief**
  - Injunctions, reformation, rescission

Liability Limits – Enforceability

- **Generally enforceable**
- **Exceptions:**
  - For intentional wrongdoing
  - Where Parties have special (e.g., fiduciary) relationship
- **Closely scrutinized in employment contracts and consumer transactions**

Liability Limits – Extension

- **"Himalaya Clauses"**
- **Extend liability limits to third parties, such as subcontractors and agents involved in performing the contract**
- **Typically enforced, provided the parties:**
  - Contemplated services of the third parties
  - Clearly intended to limit their liability to third parties

Liability Limits – Examples

- **Example 1:**
- **Client contracts with Service Provider to mine and reconcile the Client's customer data**
- **Client terminates the Service Provider**
- **Service Provider sues for breach seeking damages equal to the profits it would have earned had the contract been completed (i.e., expectation damages)**

Liability Limits – Examples

- **"In no event will Service Provider, its subcontractors, or Client be liable for consequential, incidental, indirect, punitive or special damages, or loss of profits, data, business or goodwill, regardless of whether such liability is based on breach of contract, tort, strict liability, breach of warranties, failure of essential purpose, or otherwise, and even if advised of the likelihood of such damages."**

Liability Limits – Examples

- **Example 2:**
- **Student loan guarantee corporation contracts with IT company to manage borrower data**
- **IT Company employee loses hard drive containing borrower social security numbers in an airport**
- **Student loan guarantee corporation sues IT Company to recover its out-of-pocket costs for mitigating the breach of privacy**

Liability Limits – Examples

- **"In no event shall IT Company be liable for any loss of profits, loss of business, or loss of data, or for special, incidental, indirect or consequential damages however arising even if IT Company has been advised of the possibility of such damages."**

- **IT Company moves for summary judgment**

Liability Limits – Examples

- **Motion denied**
- **Were the expenses indirect damages, which were barred, or direct damages, which weren't addressed?**

Liability Limits – Examples

- **Example 3:**
- **Private equity firm sold publishing company to another private equity firm**
- **Agreement created an indemnity fund and provided that buyer could only recover against the indemnity fund**

Liability Limits – Examples

- **Buyer sued for rescission**
- **Integration clause: buyer specifically represented that it was not relying on any representations or warranties other than those expressly provided in the sale agreement**
- **Limit of Liability:**
  - applied to claims arising out of the agreement as well as claims arising out of the transaction
  - excluded any judgment or award other than against the indemnity fund

Liability Limits – Examples

- **Buyer had to prove that Seller had lied about a representation contained in the four corners of the sale agreement**

Liability Limits – Drafting Considerations

- Governing law
- Potential damages for both sides
- Are lost profits consequential damages or direct/ expectation damages?
- Should equitable relief be precluded?
- Can damages be quantified?

Liability Limits – Drafting Considerations

- **Define the transaction to include both the written agreement and the deal itself**
- **Broadly identify the potential risks associated with the deal and the associated causes of action**
- **Identify each type of damage you are limiting/ prohibiting**

Liability Limits – Drafting Considerations

- **Identify each type of remedy you are precluding**
- **Limit arbitrator's power to relief authorized by contract**
- **Add the award of attorney's fees and costs where one party seeks damages or relief expressly barred by the contract**

Liability Limits – Drafting Considerations

- **Include a specific integration clause to mitigate against potential fraud exceptions**
- **Damage caps must be logically related to the deal**
- **Use recitals to support damage cap**

Arbitration Clauses

Goals of Arbitration

- **Avoid litigation costs and delays**
- **Arbitration clauses do not always achieve these desired results**
- **Careful consideration and drafting is a necessity**

Arbitration Clauses

- **An arbitration clause should at least include language that:**
  1. Any dispute arising out of or relating to this contract, or the breach thereof,
  2. shall be finally resolved by arbitration
  3. administered by (insert name of arbitration organization *e.g., JAMS, National Arbitration Forum or American Arbitration Association*) pursuant to its (insert type of case or rules *(e.g., AAA Commercial Arbitration Rules*),

Arbitration Clauses

4. and a judgment upon the award rendered by the arbitrator(s) may be entered in any court having proper jurisdiction.
5. The arbitration will be conducted in (select language – *e.g., English*)
6. in (insert location – may be a state, city, or specific address)
7. in accordance with the United States Federal Arbitration Act.
8. There shall be (insert number) arbitrators, named in accordance with such rules (or insert selection method).

Arbitration Clauses – Enforcement

- **Federal Arbitration Act ("FAA")**
  - Applies to any contract within the reach of the Commerce Clause that contains an arbitration clause
  - Provides for a stay of court litigation pending arbitration in accordance with the parties' agreement
  - Provides for summary confirmation of an arbitration award by the courts (*i.e.*, reducing the arbitration award to a judgment that can be enforced)
  - Severely limits the review by courts of an arbitration award

Arbitration Clauses

- **Standard Clause (Single Arbitrator)**
- **Standard Clause (Three Arbitrators)**
  - Pick three or pick one each and they pick third
- **Standard Clause (No administrator – detail own rules)**

Arbitration Clauses

- **Restrictions on types of awards (*e.g.*, no consequential or punitive damages – no injunctive relief)**
- **Baseball Arbitration**
- **High – Low**

Arbitration Clauses

- **Mediation**
  - Require that a dispute first be mediated prior to the commencement of an arbitration
  - Mediation can include an informal or structured non-binding dispute resolution meeting or series of escalating meetings

Arbitration Clauses

- **Class Actions may be expressly permitted or prohibited**
- **If not expressly permitted, then no consent exists for a class action arbitration**
- **Class action issues can arise in, for example,**
  - Franchise agreements
  - Vendor agreements
  - Customer contracts

Arbitration Clauses: Scope of Review under the FAA

- **The grounds for overturning an award under the FAA are:**
  - Where the award was procured by corruption, fraud, or undue means;
  - Partiality or corruption by the arbitrator;
  - Misconduct by the arbitrators in refusing to postpone the hearing or hear testimony or other misbehavior prejudicing the parties; or
  - The arbitrators exceeded their powers such that a mutual, final, and definite award was not made.

Arbitration Clauses: Scope of Review under the FAA

- **The grounds for modifying an award under the FAA are:**
  - An evident miscalculation of figures or material mistake in the description of a person, thing, or property referred to in the award;
  - Whether the arbitrators have awarded upon a matter not submitted to arbitration, unless it does not affect the merits of the decision; or
  - The award is imperfect in matter of form not affecting the merits of the controversy.

Arbitration Clauses – Recent Developments

- **Supreme Court precedent has confirmed that an attack on the validity of the arbitration clause itself may be entertained by the courts, but an attack on the agreement as a whole must be directed to the arbitrator**
- **But the issue of whether a matter is subject to arbitration may be reserved in an arbitration clause for the arbitrator to resolve, not the courts**

Arbitration Clauses – Recent Developments: Class Action Arbitration

- **Recent U.S. Supreme Court decision on class action arbitrations**
- ***Stolt-Nielson S.A. v. AnimalFeeds International Corp.*, 2010 U.S. Lexis 3672 (Apr. 27, 2010)**
- **Held that an arbitrator cannot impose a class action arbitration based on a simple arbitration provision in a contract that did not specifically authorize class action arbitrations**

Arbitration Clauses – Drafting Considerations

- When a third party arbitration service is selected in the contract, the parties, unless otherwise agreed, are stipulating to the service's rules
- The rules should be consulted at the time of drafting to determine whether exceptions should be taken

Arbitration Clauses – Drafting Considerations

- **Is it advisable to prohibit non-monetary relief, such as injunctive relief or rescission?**
- **Most arbitration rules (AAA and JAMS) provide for interim relief**
- **Courts have approved of injunctions issued by arbitrators to maintain the status quo and preserve the efficacy of the proceeding**

Arbitration Clauses – Drafting Considerations

- Courts may issue injunctions in aid of arbitration
- Absent a prohibition against injunctions in the agreement, the courts are authorized to issue these injunctions
- Therefore, there are two types of injunctions to consider when drafting arbitration clauses – court injunctions and arbitrator injunctions
- Both types must be excluded to be effective

Arbitration Clauses – Drafting Considerations

- **Other controls available:**
  - Allocation of expenses and attorney fees
  - Reasoned (*i.e.*, detailed opinion) vs. standard (*i.e.*, short form) awards
  - Availability of discovery (type and amount)
  - Deadline to conclude arbitration (the time for an award is set by some administrators, but the schedule for the arbitration as a whole can be set by the parties in their agreement)

Alternatives to Arbitration

- **Jury trial waivers**
- **Limits on discovery (enforceability issues)**

Indemnification Clauses

Indemnification

- **Claims made by third-parties**
- **Direct claims for losses**

Indemnification – Enforcement

- **Typically, cannot seek indemnification for losses due to one's own negligence**
- **Indemnitees will seek indemnification provisions that grant indemnification even where they were contributorily negligent**
  - See Sample Indemnification Clause C

Indemnification – Enforcement

- **Most jurisdictions only enforce indemnification clauses as to third-party claims**
- **Direct claims continue to be asserted**

Indemnification – Direct Claims

- **Key language:**
  - "indemnify"
  - "hold harmless"
- **Key definitions:**
  - "Loss"
  - "triggering event"
  - "occurrence"

Indemnification – Examples

Seller agrees to indemnify and hold harmless Buyer . . . for indemnification resulting from . . .

(a) any and all Loss (as defined below) resulting from any misrepresentation or breach of warranty by Seller . . .

(b) any and all Loss resulting from any non- fulfillment of any covenant or agreement on the part of Seller . . ., and

(c) any and all loss resulting from claims by any third party arising out of facts or circumstances relating to the Company or the Business

Indemnification – Examples

Loss: any and all loss, injury or damages incurred by Buyer in connection with any and all actions, suits, proceedings, hearings, investigations, charges, complaints, claims, demands, injunctions, judgments . . . Taxes, liens, expenses and fees (and including court costs and reasonable attorneys fees and expenses incident to any of the foregoing)

Indemnification – Examples

Seller indemnifies Buyer for 50% of any and all losses as a result of operation of the Business prior to the Closing Date including losses arising from events or occurrences prior to the Closing Date.

Buyer indemnifies Seller for 50% of any and all losses as a result of operation of the Business prior to the Closing Date including losses arising from events or occurrences prior to the Closing Date.

Indemnification – Examples

- Defective product manufactured pre-Closing Date
- Product sold and delivered to the customers post-closing
- Buyer bears expenses associated with defective product
- Seeks indemnity from Seller for 50% of expenses

Indemnification – Examples

- SPA created indemnities running for the benefit of both the Purchaser and Seller with no clear defining line for allocating responsibilities between the parties.
- The fatal drafting error was the absence of a defined term for “event” or “occurrence”
- The court imposed a definition under state law

Indemnification – Drafting Tips

- **Definitions can be outcome determinative**
- **Choice of law is critical: it will provide the law for interpreting the indemnification provisions**
- **Address notice provisions, right to select counsel, control of joint defense**

Ipso Facto Clauses

Ipso Facto Clauses

- ***Ipso facto*** **clauses allow one party to terminate the contract if the other party files for bankruptcy protection**
- **SAMPLE: "Upon the occurrence of any of the following events, Client/Buyer will be in material default under this agreement and Service Provider/Seller shall be entitled to terminate this agreement: (1) the dissolution, termination of existence, or business failure of Client/Buyer; or (2) any proceeding under any bankruptcy or insolvency laws is commenced by or against Client/Buyer or Client/Buyer makes an assignment for the benefit of its creditors."**

Ipso Facto Clauses

- **U.S. Bankruptcy Code generally prohibits the enforcement of *ipso facto* clauses**
- ***Ipso facto* clauses cannot be enforced to terminate "executory contracts"**
  - Executory contracts are defined as agreements under which the obligations of both parties remain due
- ***Ipso facto* clauses cannot be enforced to terminate a contract that is property of the bankruptcy estate**

Ipso Facto Clauses

- **Exceptions to the bar against *ipso facto* clauses include:**
  - Futures and other securities trading contracts
  - Certain contracts with individual debtors concerning financed personal property
  - Contracts that are deemed to not be part of the bankruptcy estate and that are non-executory (*e.g.*, some courts have held that *ipso facto* clauses in LLC operating agreements are enforceable while other courts have disagreed)

Ipso Facto Clauses

- **Independence Principle: An *ipso facto* clause may be invoked against a third party when a party to a contract files for bankruptcy**
- **Letter of credit**
- **Guaranty**

Ipso Facto Clauses

- **Including *ipso facto* clauses in an agreement is not a problem in and of itself**
- **However, the contracting party should make sure that the *ipso facto* clause is enforceable under a recognized exception to avoid a violation of the automatic stay**

Disclaimers of Warranties

Disclaimers of Warranties

- Typically enforced, provided they are conspicuous
- Cannot disclaim personal injury claims in the product liability context

Disclaimers of Warranties

- **Loosely drafted express warranties can undercut a well-drafted disclaimer of implied warranties**
- **Express representations and warranties can't be open-ended or vague**

Disclaimers of Warranties

- **Example: Sale of software package**
  - Contract: standard disclaimer of warranties, and limited liability to the purchase price
  - Contract: referenced other documents provided to the buyer, which included "puffing" re accuracy of the system, ease of use, and automation of system

Disclaimers of Warranties

- **Example: sale of disaster recovery business unit**
  - Asset deal, following extensive due diligence
  - Agreement: well drafted disclaimer of implied warranties and a strong merger clause
  - Agreement: express warranties concerning the business' assets and liabilities:
    - number of computers, servers, trailers
    - customer accounts
    - financial statements

Disclaimers of Warranties

- **Example: sale of disaster recovery business unit**
  - Express representation: assets sufficient to operate business
  - Buyer disagreed, thought more assets (*i.e.*, computers, servers) required to cover the customer obligations
  - Buyer sued the seller for breach

Disclaimers of Warranties

- **<u>Example</u>: sale of disaster recovery business unit**
  - Open-ended, non-specific express warranty defeated disclaimer of warranties, including that the assets were fit for a particular purpose

Disclaimers of Warranties

- **Drafting Considerations:**
  - Use both disclaimer and specific merger clause with anti-reliance representations
  - Avoid open-ended or vague representations
  - Language should be conspicuous

Survival Clauses

Survival Clauses

- **Historically, standard terms of art were used to draft Survival Clauses**
- **Courts in the 9th Circuit and 6th Circuit have refused to enforce Survival Clauses**
- **The majority of jurisdictions continue to enforce Survival Clauses**
- **But clear language is increasingly important**

Survival Clauses

- **Traditional and majority view: clauses shorten contractual limitations period for filing suit**
- **Majority position: party needs to actually file suit to avoid being time-barred – demand letter is insufficient**

Survival Clauses – Examples

- Often a contract will provide that representations and warranties expire upon the termination of the contract
- A three-year contract may be shorter than the statute of limitations for a claim
- A survival clause can alter the time limit to bring a claim

Survival Clauses – Examples

- **When an agreement provides that the representations and warranties survive but does not state a time period, then an action may be brought any time after the closing before the end of the statutory period**

Survival Clauses

- The majority view is that a Survival Clause extends and applies to related claims
- For example, a Survival Clause would extend to claims of fraud and negligent misrepresentation as well as the breach of contract claims
- The Survival Clause generally extends to the officers and directors of the Seller which is invoking the Survival Clause

Survival Clauses

- **Plaintiffs often sue officers/directors personally**
- **Typically allege that officers are personally liable for intentional torts and, because they are not signatories to the agreement, cannot benefit from the shortened limitations period**
- **Majority view: contractual limitations periods are periods of repose; therefore, claim-specific and not person-specific**

Survival Clauses

- **Most jurisdictions apply "reasonableness" standard to determine enforceability of the shortened limitations period**
- **No internal conflicts in contract (*e.g.*, No shorter limit to bring suit than time for claim to develop or arise)**
- **California applies "strict scrutiny" to agreements that shorten the limitations periods for filing suit**

Survival Clauses

- **Choose your choice of law very carefully**
- **Draft more explicit Survival Clauses as the trend appears to be moving away from the enforceability of the boilerplate language**
- **Use the word "file" to explicitly highlight the need to file suit within a shortened period**

Forum Selection Clauses

Forum Selection Clauses

- **Mandatory versus permissive**
- **Default: permissive**
- **Key words:**
  - "sole"
  - "only"
  - "exclusive"
  - "shall"

Forum Selection Clauses

- **Enforcement requires reasonable communication to opposing party in advance**
- **Inconvenience is not necessarily a bar**
- **Consumer contracts will be closely scrutinized**

Forum Selection Clauses – Example

- **Company located in Arizona**
- **High-level sales exec in Connecticut**
- **Services agreement**
  - Plaintiff can file suit in his/its home state
  - Parties waive doctrine of forum non conveniens

Contact

Bradford Babbitt
280 Trumbull Street
Hartford, CT 06103-3597
860-275-8209
bbabbitt@rc.com

William Egan
280 Trumbull Street
Hartford, CT 06103-3597
860-275-8365
wegan@rc.com

BULLETPROOFING YOUR DEALS 2010

Lessons From The Litigation Battlefield On Commercial Contract Clauses

Supplemental Materials

ROBINSON & COLE LLP
ATTORNEYS AT LAW

ROBINSON & COLE LLP
ATTORNEYS AT LAW

Bulletproofing Your Deals 2010

Lessons from the Litigation Battlefield on Commercial Contract Clauses

Bradford S. Babbitt and William J. Egan, ROBINSON & COLE LLP, www.rc.com

I. Limitations on Liability

In the context of commercial transactions, it is well settled that parties may limit their liability and limit the types of remedies available for breach of contract and negligence. *See, e.g., ABN Amro Verzekeringen BV v. Geologistics Americas, Inc.*, 485 F.3d 85 (2d Cir. 2007) (affirming judgment for plaintiff over plaintiff's objection in the amount of $50.00 when defendants tendered that sum in response to plaintiff's suit under a contract limiting the defendants' liability to $50 for simple negligence); *Tradex Europe SPRL v. Conair Corp*., No. 06 Civ. 1760 (KMW) (FM), 2008 U.S. Dist. LEXIS 37185 (S.D.N.Y. May 7, 2008) (limiting the defendant's liability to the fees paid by the plaintiff under the contract based on the parties' limitation on liability provision); *Abry Partners V, L.P. v. F&W Acquisition LLC*, 891 A.2d 1032 (De. Ch. Ct. 2006) (enforcing limitation of remedies provision to bar plaintiff's request for rescission based on anything less than actual fraud).

So called "Himalaya Clauses" can extend limitation on liability clauses to non-signatories to the agreement who act as a signatory's agent or independent contractor to perform under the contract. *See Norfolk Southern Rail co. v. Kirby*, 543 U.S. 14, 125 S. Ct. 385 (2004).

A liquidated damages provision does not bar equitable remedies such as specific performance unless there is express language in the contract that the liquidated damages provision shall be the sole remedy for breach. *See Vacold LLC v. Cerami*, 545 F.3d 114 (2d Cir. 2008).

Courts will not enforce limitation on liability provisions in cases of intentional wrongdoing, such as actual fraud. *See Metropolitan Life Insurance Co. v. Noble Lowndes International, Inc.*, 84 N.Y. 2d 430, 643 N.E. 2d 504 (1994).

II. Arbitration Clauses

A. Most arbitration services provide sample clauses. Examples include:

1. www.adr.org (American Arbitration Association);
2. www.finra.org (Financial Industry Regulatory Authority); and
3. www.jamsadr.com (JAMS).

A basic arbitration clause should have language addressing at least these eight terms:

1. Any dispute arising out of or relating to this contract, or the breach thereof,
2. shall be finally resolved by arbitration
3. administered by (insert name of arbitration organization e.g. JAMS, National Arbitration Forum or American Arbitration Association) pursuant to its (insert type of case or rules (e.g. AAA Commercial Arbitration Rules)),
4. and a judgment upon the award rendered by the arbitrator(s) may be entered in any court having proper jurisdiction.
5. The arbitration will be conducted in (select language – e.g. English)
6. in (insert location – may be a state, city, or specific address)
7. in accordance with the United States Arbitration Act.
8. There shall be (insert number) arbitrators, named in accordance with such rules.

B. Sample Clauses:

1. Standard clause (single arbitrator):

   Any dispute arising out of or relating to this agreement, which cannot be resolved by negotiation between the parties, must be settled by final and binding arbitration with one arbitrator in [*insert location*] pursuant to the rules of [*insert arbitration service*]. The costs of the arbitration shall be shared equally between the parties, except that each party shall be responsible for its own attorneys' fees and costs in preparing and

presenting its case. The arbitrator's award may be confirmed, entered, and enforced as a final judgment in any court of competent jurisdiction. Proceeding to arbitration and obtaining an award shall be a condition precedent to the bringing or maintaining of any action in any court with respect to any dispute arising out of or relating to this agreement, except for the institution of a civil action to maintain the status quo during the pendency of any arbitration proceeding.

2. Standard clause (three arbitrators):

Any dispute arising out of or relating to this agreement, which cannot be resolved by negotiation between the parties, must be settled by final and binding arbitration with a panel of three arbitrators in [*insert location*] pursuant to the rules of [*insert arbitration service*]. The costs of the arbitration shall be shared equally between the parties, except that each party shall be responsible for its own attorneys' fees and costs in preparing and presenting its case. The arbitrator's award may be confirmed, entered, and enforced as a final judgment in any court of competent jurisdiction. Proceeding to arbitration and obtaining an award shall be a condition precedent to the bringing or maintaining of any action in any court with respect to any dispute arising out of or relating to this agreement, except for the institution of a civil action to maintain the status quo during the pendency of any arbitration proceeding.

3. Standard clause (no third-party administrator):

Any dispute arising out of or relating to this agreement, which cannot be resolved by negotiation between the parties, must be settled by final and binding arbitration with one arbitrator in [*insert location*]. The costs of the arbitration shall be shared equally between the parties, except that each party shall be responsible for its own attorneys' fees and costs in preparing and presenting its case. The arbitrator's award may be confirmed, entered, and enforced as a final judgment in any court of competent jurisdiction. Proceeding to arbitration and obtaining an award shall be a condition precedent to the bringing or maintaining of any action in any court with respect to any dispute arising out of or relating to this agreement, except for the institution of a civil action to maintain the status quo during the pendency of any arbitration proceeding.

The arbitrator shall be selected pursuant to the following procedure: Within thirty (30) days of the receipt of a demand for arbitration, each party shall nominate five (5) potential arbitrators to generate a joint list of

ten (10) potential arbitrators. Each party shall be permitted to strike (regardless of cause) two (2) arbitrators from the list of ten (10) potential arbitrators. Each party shall then rank the remaining arbitrators on the list numbered from 1-6 in order of most preferred (No. 1) to least preferred (No. 6). The arbitrator with the lowest rank who was not stricken by either party shall be the arbitrator in the case. In the event of a tie, the parties can either break the tie by agreeing on an arbitrator or, in the absence of an agreement, the tied arbitrators shall be deemed stricken and the next lowest ranked arbitrator shall be selected as the arbitrator.

The arbitrator shall render his/her award within thirty (30) days from the final submission of evidence or argument from the parties.

4. Restricting arbitrator's power to award certain types of damages:

Any dispute arising out of or relating to this agreement, which cannot be resolved by negotiation between the parties, must be settled by final and binding arbitration with one arbitrator in [*insert location*] pursuant to the rules of [*insert arbitration service*]. The costs of the arbitration shall be shared equally between the parties, except that each party shall be responsible for its own attorneys' fees and costs in preparing and presenting its case. The arbitrator's award may be confirmed, entered, and enforced as a final judgment in any court of competent jurisdiction. Proceeding to arbitration and obtaining an award shall be a condition precedent to the bringing or maintaining of any action in any court with respect to any dispute arising out of or relating to this agreement, except for the institution of a civil action to maintain the status quo during the pendency of any arbitration proceeding. The arbitrator shall have no power or authority to render any award or issue any order at any time except as permitted in this agreement. In no event may the arbitrator have the power or authority to render any award or issue any order that provides for punitive damages, statutory double or treble damages, exemplary damages, incidental damages, consequential damages, or attorneys' fees.

5. Restricting arbitrator's power to award non-monetary relief:

Any dispute arising out of or relating to this agreement, which cannot be resolved by negotiation between the parties, must be settled by final and binding arbitration with one arbitrator in [*insert location*] pursuant to the rules of [*insert arbitration service*]. The costs of the arbitration shall be shared equally between the parties, except that each party shall be responsible for its own attorneys' fees and costs in preparing and

presenting its case. The arbitrator's award may be confirmed, entered, and enforced as a final judgment in any court of competent jurisdiction. Proceeding to arbitration and obtaining an award shall be a condition precedent to the bringing or maintaining of any action in any court with respect to any dispute arising out of or relating to this agreement. The arbitrator shall have no power or authority to render any award or issue any order at any time (whether final, interim, or temporary) except as permitted in this agreement. In no event may the arbitrator have the power or authority to render any award or issue any order that provides for equitable and/or other non-monetary relief, including, but not limited to, injunctive relief, declaratory relief, rescission, reformation of this agreement. In no event shall either party seek or be entitled to any such non-monetary relief (whether final, interim, or temporary) from any court.

6. Prohibiting class arbitration:

Any dispute arising out of or relating to this agreement, which cannot be resolved by negotiation between the parties, must be settled by individual final and binding arbitration with one arbitrator in [*insert location*] pursuant to the rules of [*insert arbitration service*]. The costs of the arbitration shall be shared equally between the parties, except that each party shall be responsible for its own attorneys' fees and costs in preparing and presenting its case. The arbitrator's award may be confirmed, entered, and enforced as a final judgment in any court of competent jurisdiction. Proceeding to arbitration and obtaining an award shall be a condition precedent to the bringing or maintaining of any action in any court with respect to any dispute arising out of or relating to this agreement, except for the institution of a civil action to maintain the status quo during the pendency of any arbitration proceeding.

There shall be no right or authority for any claims to be arbitrated on a class action or consolidated basis or on bases involving claims brought in a purported representative capacity on behalf of the general public (including, but not limited to, as a private attorney general), [*other customers/franchisees/vendors/etc.*], or other persons similarly situated.

7. Limiting discovery:

Presumption against discovery:

No discovery may be permitted in connection with the arbitration unless it is expressly authorized by the arbitrator upon a showing of substantial need by the party seeking discovery.

Discovery limited:

The parties may only engage in discovery to the following extent: Each party shall be entitled to serve twenty (20) document requests and each party shall only be entitled to notice and take no more than three (3) depositions of seven (7) hours or less each. No interrogatories or requests to admit shall be permitted. Under no circumstances shall either party be required to search for, mine, and/or produce any electronically-stored information other than such information stored in the ordinary course of business and readily available in active files. The parties agree that they are not required to resort to disaster recovery media or other methods of mining electronically-stored information not accessed in the ordinary course of business, such as back-up tapes, to locate and/or produce potentially responsive documents.

8. Attorney's fees / costs

Mandatory:

The arbitrator shall award the prevailing party all of its attorney's fees and costs incurred in connection with this arbitration.

Discretionary:

All costs and expenses of the arbitration, including actual attorney's fees, shall be allocated among the parties to this agreement according to the arbitrator's discretion.

9. Form of award

Standard (i.e., short form) award

The arbitrator's award shall be issued in writing and confined to a statement of the amount of damages (if any) awarded to either or both parties on the claims and counterclaims submitted to the arbitrator.

Reasoned (i.e., long form) award

The arbitrator's award shall be issued in writing with a recitation of the findings of facts and conclusions of law relied upon by the arbitrator in rendering his/her award.

10. Baseball arbitration:

Any dispute arising out of or relating to this agreement, which cannot be resolved by negotiation between the parties, must be settled by final and binding arbitration with one arbitrator in [*insert location*] pursuant to the rules of [*insert arbitration service*]. The costs of the arbitration shall be shared equally between the parties, except that each party shall be responsible for its own attorneys' fees and costs in preparing and presenting its case. The arbitrator's award may be confirmed, entered, and enforced as a final judgment in any court of competent jurisdiction. Proceeding to arbitration and obtaining an award shall be a condition precedent to the bringing or maintaining of any action in any court with respect to any dispute arising out of or relating to this agreement. The arbitrator shall have no power or authority to render any award or issue any order at any time (whether final, interim, or temporary) except as permitted in this agreement. In no event may the arbitrator have the power or authority to render any award or issue any order that provides for equitable and/or other non-monetary relief, including, but not limited to, injunctive relief, declaratory relief, rescission, reformation of this agreement. In no event shall either party seek or be entitled to any such non-monetary relief (whether final, interim, or temporary) from any court.

Fourteen (14) days before the commencement of the arbitration hearing, both sides will simultaneously submit to the arbitrator and exchange with each other a statement of the amount of the award that party will seek from the arbitrator. As the award in the arbitration, the arbitrator must choose one of the two submitted figures.

11. Mediation as a condition precedent:

If the parties have any dispute arising out of or relating to this agreement that they cannot resolve between themselves, then within fourteen (14) days from the request for mediation by either or both parties, the parties shall jointly select a mediator. The mediation shall be conducted within forty-five (45) days after the selection of the mediator. If the dispute is not resolved at the mediation, then not less than thirty (30) days after the mediation, the parties shall submit the dispute to binding arbitration in accordance with the following paragraph. Participation in mediation shall be a condition precedent to a demand for arbitration, unless one party refuses to participate in the mediation, in which case a request for mediation and the passage of thirty (30) days from the date of such request shall satisfy this condition precedent to arbitration. The parties agree that

the period from the request for mediation through and including the thirty-day period following the mediation, or the thirty (30) days following the request for mediation if one party refuses to participate in the mediation, shall not be asserted or relied upon in any way to compute the running of time under any statute of limitations or repose, or by way of laches or other time limit, whether statutory, contractual, common law or otherwise as to claims concerning the dispute identified in the request for mediation. The mediation shall be confidential, and no statements made during the mediation shall be admissible during any subsequent arbitration.

Any dispute arising out of or relating to this agreement, which cannot be resolved by negotiation or mediation between the parties, must be settled by final and binding arbitration with one arbitrator in [*insert location*] pursuant to the rules of [*insert arbitration service*]. The costs of the mediation and arbitration shall be shared equally between the parties, except that each party shall be responsible for its own attorneys' fees and costs in preparing and presenting its case. The arbitrator's award may be confirmed, entered, and enforced as a final judgment in any court of competent jurisdiction. Proceeding to arbitration and obtaining an award shall be a condition precedent to the bringing or maintaining of any action in any court with respect to any dispute arising out of or relating to this agreement, except for the institution of a civil action to maintain the status quo during the pendency of any arbitration proceeding.

C. Confidentiality:

All aspects of the arbitration shall be treated as confidential. Neither the parties nor the arbitrator may disclose the existence, content or results of the arbitration, except as necessary to comply with legal or regulatory requirements, including any pleading requirements with respect to an application to confirm, vacate, or modify any award rendered by the arbitrator. Before making any such disclosure, a party shall give written notice to all other parties and shall afford such parties a reasonable opportunity to seek protection of confidential information. Consent for the disclosure of information concerning this arbitration may not be unreasonably withheld.

D. Arbitration As A Binding Decision:

Generally provision for arbitration means that decision of arbitrator is final, as opposed to a mediation where a recommended outcome is obtained. A final decision from an arbitrator may be confirmed by a court, but will not be overturned absent a **manifest disregard for the law**, or evidence of bias or

misconduct by the arbitrator, or a misapplication of the law, or a finding in clear contradiction of the facts.

The courts give great deference to an arbitrator's ruling. "If the parties agreed to submit an issue for arbitration, we will uphold a challenged award as long as the arbitrator offers "a barely colorable justification for the outcome reached. . . .

In other words, as long as the arbitrator is even arguably construing or applying the contract and acting within the scope of his authority, a court's conviction that the arbitrator has committed serious error in resolving the disputed issue does not suffice to overturn his decision." *Reliastar Life Ins. Co. of New York v. EMC National Life Co.*, 564 F.3d. 81, 86 (2009) (internal quotations and citations omitted).

If a dispute proceeds to arbitration, be sure to provide the arbitrators with sufficient grounds to support the factual and legal finding sought from the panel. Do not assume that the arbitrator knows the law or is aware of any facts. Make your case obvious on the record as any attempt to overturn an arbitrator's decision is very difficult.

E. Arbitration Key Issues and Recent Decisions:

Background: By way of brief background, it is interesting to note that many courts did not support arbitration clauses until the last 80 or so years. Many courts felt that arbitrators were improperly taking the place of judges and that arbitration agreements were to be narrowly and strictly construed. But the trend shifted and a broader acceptance of arbitration was adopted as a policy change and enacted in legislation and adopted in court decisions. The Federal Arbitration Act ("FAA") that provides broad support for arbitration was enacted in its original form in 1925, and re-enacted and codified in 1947.

The key provisions of the FAA, codified as 9 U.S.C. § 1 *et seq*., are not difficult to understand, but there have been multiple issues that have arisen and which are subject to case law interpreting those statutes.

Some basic provisions of the FAA are that:

An agreement to arbitrate a contract involving commerce is valid, irrevocable and enforceable. 9 U.S.C. § 2.

A party may petition a U.S. District Court to stay litigation in federal court where there exists an agreement to arbitrate. 9 U.S.C. § 3.

A party may petition a U.S. District Court to enforce an agreement to arbitrate. 9 U.S.C. § 4.

A party may petition a U.S. District Court to confirm an arbitration award. 9 U.S.C. § 9.

A party may petition a U.S. District Court to vacate an arbitration award. 9 U.S.C. § 10.

An arbitration award may be vacated by the District Court in which the award was entered:

1. Where the award was procured by corruption, fraud or undue means;

2. Where there was evident partiality or corruption in the arbitrators, or either of them;

3. Where the arbitrators were guilty of misconduct (refusing to postpone a hearing for sufficient cause, or refusing to hear evidence or testimony, or other prejudicial behavior);

4. Where the arbitrators exceeded their powers or so imperfectly executed them that a mutual, final and definite award upon the subject matter submitted was not made.

Federal Court Jurisdiction: Remember that while the FAA validates and makes agreements to arbitrate enforceable as a matter of federal law, the federal courts do not have jurisdiction over all arbitration disputes.

In *Vaden v. Discover Bank*, 129 S.Ct. 1262, 2009 Lexis 1781 (2009), Discover Bank brought a state court action to collect on a $10,000 credit card debt, the debtor counterclaimed for usury under state law, and Discover Bank filed a petition to compel arbitration in federal court, saying that the Federal Deposit Insurance Act preempted the state usury statute, and therefore the federal court had jurisdiction over the matter to compel arbitration under 9 USC § 4.

The *Vaden* court held that the federal district court needed to "look through" the federal statute (providing for court ordered compulsion of arbitration) as the FAA is not jurisdictional, and see if the "well pleaded complaint" provided for federal jurisdiction (not the counterclaim or any preemption of the counterclaim). As it did not, the party seeking to compel arbitration is left to the state courts to issue such an order compelling arbitration. This may be done under FAA § 2 which

provides as a matter of federal law that agreements to arbitrate are valid and binding, and also may be ordered under state court arbitration statutes that allow for such stays or compulsion of arbitration. *Vaden*, 129 S.Ct. at 1278.

Similarly in *Perpetual Securities, Inc. v. Tang*, 290 F.3d. 132 (2002) the Second Circuit held that F.A.A. § 9 does not confer jurisdiction of the federal courts to confirm an arbitration award. The Court in *Perpetual* also noted that the district court correctly noted it did not have jurisdiction to vacate an award under F.A.A. § 10.

If federal jurisdiction does exist over the subject matter, however, a denial of a motion to stay federal litigation and compel arbitration by a court is immediately appealable under F.C.C. § 16(a). *See Powershare, Inc. v. Syntel*, Inc., 597 F.3d. 10 (2010) A party that wishes to proceed under an arbitration clause when a court improperly fails to stay court proceedings may take an immediate appeal of that ruling.

Class Actions and Arbitration: The recent U.S. Supreme Court decision of *Stolt-Nielson S.A. v. AnimalFeeds International Corp.*, 2010 U.S. Lexis 3672 (April 27, 2010) held that an arbitrator cannot impose a requirement that a party be subject to class action arbitration based on a simple arbitration provision in a contract that did not specifically address class actions absent other authority in the contract or at law.

"While the interpretation of an arbitration agreement is generally a matter of state law, the FAA imposes certain rules of fundamental importance, including the basic precept that arbitration "is a matter of consent, not coercion." *Stolt-Nielson* 2010 U.S. Lexis 3672 at *36.

Key issue in *Stolt-Nielson* was that AnimalFeeds argued that there was no agreement to preclude class arbitration, while the Court found that there needed to be an affirmative agreement to have a class action arbitration, beyond the simple arbitration clause. *Stolt-Nielson* 2010 U.S. Lexis 3672 at * 41.

The *Stolt-Nielson* court also covered several other areas of key areas of arbitration law including recognizing the distinction between a court's lack of authority to review an arbitrator's "interpretation" of the law, versus the arbitrator's "manifest disregard" for the law. Id. at * 14.

Who Decides Arbitrability: It is important to include language in the arbitration clause that the issue of arbitrability is to be decided by the arbitrator (if that is what you want to have happen). The Supreme Court held that the issue of whether a matter is arbitrable is for a court to determine, unless this issue is contractually

reserved for an arbitrator to decide by the parties. *See Awauah v. Coverall North America, Inc.*, 554 F.3d. 7 (2009), citing *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79, 83 (2002). Where the arbitration clause specifically incorporates the AAA rules or other terms which state that arbitrability is to be determined by an arbitrator, such an agreement is binding on the parties.

Choice of Law: Many contracts will include a clause directing the arbitrator or court to resolve disputes according to the laws of a particular state. To avoid time consuming disputes and grounds for challenging the validity of an arbitrator's ruling, a choice of law provision in a contract is important to direct the arbitrator to refer to the laws of a certain state. And as state law includes a conflict of law analysis, parties should specify that a state's law will be the governing law regardless of conflict of laws principals. This can be achieved through use of the following language:

Any arbitration and all disputes under this agreement shall be governed by the laws of the State of _____ without regard to its choice of law provisions.

Preliminary Hearings - *Pendente Lite* Issues: If the parties believe that there is a chance of irreparable harm occurring that they do not want to leave to the arbitrator to resolve, an arbitration clause can reserve the rights of the parties to seek immediate court relief to preserve the status quo or impose other equitable orders to protect the rights of the parties pending the outcome of the arbitration. It is not required that the parties seek such relief from the courts as an arbitrator may be empowered to grant equitable and preliminary relief as is the case under the AAA's Commercial Rules.

The advantage to reserving these issues for a court is that there is no extra step required to get a court order to enforce an arbiter's decision. The disadvantage is that such a preliminary remedy usually requires an evidentiary hearing that means putting on the case up front before a judge, and then putting on the case again later before an arbitrator, with concurrent proceedings open and running.

So if you are the party that is concerned about irreparable harm through the use of your company's information or other conduct, you may want to reserve the right to get into court for preliminary relief, but if this is not a primary concern, and if it is more important to limit the cost of dispute resolution, then having all issues resolved by the arbitrator may eliminate concurrent proceedings.

The sample clauses above provide for a civil action to preserve the status quo or obtain injunctive or equitable relief. If you wish for these types of decisions to be reserved for the arbitrator, then do not use that language from the sample clause but rather include the following:

The requirement that all disputes be submitted for arbitration includes the requirement that a resolution of any claim to preserve the status quo or obtain equitable or injunctive relief is reserved for the arbitrator who is empowered to address such issues and issue binding orders upon the parties.

If your contract is silent on this issue or contains no specific language allowing for the filing of a civil action or proceedings before "a court of competent jurisdiction" a court (or arbitrator) may find that the general arbitration language in the contract provides a grant of power to an arbitrator to issue equitable and injunctive relief. *Powershare, Inc. v. Syntel, Inc.*, 597 F.3d. 10 (2010) (held that where the parties agreed to allow for injunctive or other equitable relief in an arbitration clause, the district court improperly failed to stay the court proceedings seeking injunctive relief from the court. The provision in the arbitration clause that allowed for equitable and injunctive remedies was held to apply to the powers granted to the arbitrator and were not expressly reserved for the court.)

III. Indemnification Clauses

Parties continue to use indemnification clauses for both (1) direct claims; and (2) reimbursement of payments made on behalf of third-parties.

The majority position continues to be that indemnification clauses generally apply to actions for reimbursement of payments made to third-parties. *Amoco Oil Co. v. Liberty Auto & Electric Co.*, 262 Conn. 142 (2002); *Queen Villas Homeowners Assoc. v. TCB Property Mgmt.*, 149 Cal. App. 4th 1 (2007).

The key to drafting an agreement that bars indemnification for direct claims is using words clearly denoting its application to reimbursements for third-party claims such as "indemnify," "hold harmless" and defining "Loss." The notice procedures also indicate whether an indemnification provision extends to direct claims.

Attorneys should focus on the "triggering event" obligating an indemnitor to indemnify an indemnitee. *See MEMC Electronic Materials, Inc. v. Albemarle Corp.*, 241 S.W. 3d 67 (2007) (refusing to enforce indemnity because triggering event did not occur). Definitions can be outcome determinative in evaluating the meaning and scope of an indemnity. *See Smithkline Beecham Corp. v. Rohm & Haas Co.*, 89 F.3d 154 (3rd Cir. 1996) (holding that the definitions in the asset purchase agreement had the effect of limiting the scope of the indemnities); *see also Metropolitan Life Ins. v. AETNA Casualty and Surety*, 255 Conn. 295 (2001) (supplying state's own definition for the triggering event because agreement did not contain definitions for "occurrence").

Indemnitees generally cannot seek indemnification for losses resulting from their own negligence absent clear and unmistakable language in the indemnity agreement indicating otherwise. *See Haynes v. Kleinwefers*, No. 87-CV-2286 (ERK), 1990 U.S. Dist. Lexis 17872 (E.D.N.Y. Apr. 3, 1990) *aff'd*, *Haynes v. Kleinwefers*, 921 F.2d 453 (2nd Cir. 1990); *see also Heimbach v. Metropolitan Transp. Auth.*, 75 N.Y.S. 2d 387 (1990); *IU North America, Inc. v. Gage Co.*, No. 00-3361, 2002 U.S. Dist. Lexis 10275 (E.D.P.A. June 5, 2002) (all holding that indemnitees have no right to indemnification if the losses are a result in whole or in part from the indemnitees' own negligence in the absence of clear language in the agreements indicating otherwise). *But see Fountain v. Colonial Tupp Signs*, Nos. 86C-JA-117, 85C-DE-88, 1988 Del. Super. LEXIS 126 (Del. Super. Ct. Apr. 13, 1988) (holding that indemnitee was entitled to indemnification because the indemnity provision specifically referenced the indemnitee's own negligence among the covered occurrences); *see also Lone Mountain Processing, Inc. v. Bowser-Morner, Inc.*, No. 2:00cv00093, 2005 U.S. Dist. LEXIS 16340, 2005 WL 1894957 (W.D.Va. Aug. 10, 2005) (holding that indemnitee's contributory negligence did not prevent its claim for indemnification because losses to third-parties were not the result of its *sole* negligence per the agreement's indemnity requirements).

Indemnification and advancement of fees for a corporation's employees, officers and directors should be included in their employment agreements to better protect the individuals from any government action requiring the corporation to withhold or withdraw indemnification for its employees as a condition to a determination that the corporation is "cooperating" with the government investigation. *See* McNulty Memorandum from the Dept. of Justice and *U.S. v. Stein*, 435 F. Supp. 2d 330 (S.D.N.Y. 2006).

IV. Ipso Facto Clauses

Ipso Facto clauses are those that state that the occurrence of an event causes a default in a contract on its own. *Ipso facto* is literally translated: **by the fact itself**. It is commonly used to refer to a contractual provision that the filing of a bankruptcy or the insolvency of a party (or similar event) by itself is an event of default under that contract.

A. These clauses are normally included in a contract to protect a party from the difficulties in dealing with a bankrupt or insolvent party. When a party files for bankruptcy protection, its ability to perform contracts, make payments, enter into negotiations and otherwise conduct business as anticipated when the contract was made are often impaired or controlled by bankruptcy laws, courts and trustees.

B. Unless otherwise prohibited by applicable law, *ipso facto* clauses are enforceable. Some states prohibit the use of ipso facto clauses with regard to the insolvency or

bankruptcy of a party, but the most significant law that is nationally applied is the prohibition on such clauses under the Bankruptcy Code.

C. A typical *ipso facto* clause may read as follows:

"Upon the occurrence of any of the following events, Client/Buyer will be in material default under this agreement and Service Provider/Seller shall be entitled to terminate this agreement: (1) the dissolution, termination of existence, or business failure of Buyer/Client; or (2) any proceeding under any bankruptcy or insolvency laws is commenced against Client/Buyer or Client/Buyer makes an assignment for the benefit of its creditors."

D. The Bankruptcy Code generally prohibits the enforcement of *ipso facto* clauses. *See* 11 U.S.C. § 365(e) (*ipso facto* clauses cannot be used to terminate executory contracts and unexpired leases) and 11 U.S.C. § 541(c) (*ipso facto* clauses cannot deprive the debtor of estate property).

E. Some exceptions to this prohibition do exist.

i. **Financial Accommodations Contracts**: § 365(c)(2) of the Bankruptcy Code (11 U.S.C. § 365(c)(2)) provides that a bankruptcy trustee may not assume an executory contract if the contract is "a contract to make a loan, or to extend other debt financing or financial accommodations, to or for the benefit of the debtor . . ." and 11 U.S.C. § 365(e) which invalidates *ipso facto* clauses based on a party's bankruptcy does not apply if the contract is a financial accommodations contract. *See, e.g., In re Ernie Haire Ford, Inc.*, 403 B.R. 750 (2009); *see also In re Bownetree, LLC*, 2009 Bankr. Lexis 2295 (Bankr. E.D.N.Y. 2009) (held that where loan funds had already been advanced at 12% interest, subject to certain holdbacks, that the moneys had already been delivered and no further delivery of the holdback funds would be made, and therefore the contract at issue was not an executory contract to make a loan in the future such as to fall under the exception of 365(e)(2). The lender had sought to impose an additional 7% interest rate under an *ipso facto* clause upon the bankruptcy filing of the debtor and take advantage of the 365(e)(2) exception.)

ii. The Bankruptcy Code does not define what a "financial accommodation" is, but it has been fairly narrowly construed to be when the principal purpose of the contract is to "extend financing" or to "guaranty the financial obligations of the debtor" as opposed to generic obligations to make payment or incur obligations related to a contractual agreement such as to deliver goods or services. Most contracts involve some sort of

obligation to make future payments and to construe this exception broadly would have the effect of making the exception swallow the rule.

iii. **Personal Services Contracts**: Where applicable law excuses a party to a contract from accepting performance from someone other than the bankruptcy debtor, bankruptcy law does not bar *ipso facto* clauses in those circumstances. For example, if state law allows the termination of a limited liability company's member based on the filing of bankruptcy, the law will not require the other members to accept the trustee or trustee's assignee to become their fellow member. *See* 11 U.S.C. § 365(e)(1) and (2); *see, e.g., JD Factors, LLC v. Freightco, LLC*, 2009 U.S. Dist. Lexis 96705 (2009). Not all courts agree with this analysis and you should verify what kinds of personal services contracts are deemed to be within this exemption to the *ipso facto* clause prohibition.

iv. **Independence Principle:** Bankruptcy law recognizes that many contracts exist that have some relationship to the debtor, but are independent obligations that exist between two or more non-debtor entities. For example where a party obtains a letter of credit from a financial institution as security for the performance of another party to a contract, and where the contract has an *ipso facto* clause allowing for the termination of that contract upon the filing of a bankruptcy (and thereby allowing for the enforcement of the letter of credit), the non-bankruptcy party may enforce the letter of credit against the financial institution as an independent obligation, even though it was conditioned upon the bankruptcy filing by the debtor. *See In re Bender Shipbuilding & Repair Co., Inc.*, 2010 U.S. Dist. Lexis 18544 (S.D. Ala. 2010).

v. **Securities Safe Harbor Exception**: Section 560 of the Bankruptcy Code contains a safe harbor from the prohibition on bankruptcy *ipso facto* clauses. A non-defaulting "swap agreement" participant may enforce contractual rights upon the other party's bankruptcy to "(i) liquidate, terminate or accelerate one or more swap agreements because of condition of the kind specified in section 365(e)(1) or (ii) offset or net out any termination values or payment amounts arising under or in connection with the termination, liquidation, or acceleration of one or more swap agreements." *See In re Lehman Brothers Holdings, Inc.*, 422 B.R. 407 (2010) (internal quotations omitted) (also held that the court may look to the filing date of the initial Lehman entity for the operative bankruptcy filing rather than the later filing date of the related Lehman entity in analyzing the effective date of an ipso facto analysis. And further holding that the establishment of priority of payment rights (as opposed to

termination, liquidation or acceleration rights) is not within the safe harbor exception and the enforcement of those rights based upon *ipso facto* clauses is unenforceable under 365(e)(1) and 541(c)(1)(B).)

vi. "Section 559 of the Bankruptcy Code provides an exception to this general rule and allows a non-debtor counterparty to a 'repurchase agreement' (as defined by section 101(47) of the Bankruptcy Code) to exercise its contractual right under an ipso facto clause to liquidate, terminate or accelerate the repurchase agreement." *American Home Mortgage Investment Corp. v. Lehman Brothers, Inc. (In re American Mortgage Holdings, Inc.)*, 388 B.R. 69 (Bankr. D. DE 2008).

vii. In consumer transactions, the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 made some changes that are often seen in automobile repossession cases, but extend to all consumer transactions where an individual files a Chapter 7 petition, and a secured creditor files an allowed secured claim for the purchase price of an individual debtor's personal property. Under the new provisions of § 521(a) of the Bankruptcy Code, the debtor must turn in the collateral, pay off the loan, or reaffirm the debt (thereby reinstating his or her full liability for the debt). Failure assert the debtor's intentions to proceed as required and in accordance with the statutory time limits will result in the automatic stay under § 362 being terminated, the collateral will no longer be property of the estate, and the creditor can take whatever actions are allowed under non-bankruptcy law as to the collateral including the use of contractual provisions based on *ipso facto* clauses. *See, e.g., In re Antionette Dumont,* 581 F.3d. 1104 (9th Cir. 2009); *In re David Douglas Jones*, 591 F.3d 308 (4th Cir. 2010).

V. Disclaimers of Warranties

1. These provisions should be conspicuous, especially in a consumer contract.

2. Example (sale of business / business unit):

EXCEPT AS EXPRESSLY SET FORTH IN THIS AGREEMENT, THE COMPANY MAKES NO REPRESENTATION OR WARRANTY, EXPRESSED OR IMPLIED, AT LAW OR IN EQUITY IN RESPECT OF THE COMPANY OR THE COMPANY'S SUBSIDIARIES, OR ANY OF THEIR RESPECTIVE ASSETS, LIABILITIES OR

OPERATIONS, INCLUDING WITH RESPECT TO MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE, AND ANY SUCH OTHER REPRESENTATIONS OR WARRANTIES ARE HEREBY EXPRESSLY DISCLAIMED. BUYER HEREBY ACKNOWLEDGES AND AGREES THAT, EXCEPT TO THE EXTENT SPECIFICALLY SET FORTH IN THIS AGREEMENT, BUYER IS ACQUIRING THE COMPANY ON AN "AS IS, WHERE IS" BASIS. THE DISCLOSURE OF ANY MATTER OR ITEM IN ANY SCHEDULE HERETO SHALL NOT BE DEEMED TO CONSTITUTE AN ACKNOWLEDGEMENT THAT ANY SUCH MATTER IS REQUIRED TO BE DISCLOSED.

3. Example (sale of equipment):

Seller's sole liability under this agreement for failure of equipment shall be limited to the amount of actual seller charges incurred by buyer during a period of such interruption, provided that such interruption was caused solely by seller's willful act or omission or negligence. Seller shall not be liable for any interruption caused by the gross negligence or any act or omission of buyer or any third party furnishing any services to buyer. SELLER MAKES NO WARRANTIES, EXPRESS OR IMPLIED, INCLUDING BUT NOT LIMITED TO, ANY WARRANTY OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE. IN NO EVENT SHALL SELLER BE LIABLE TO BUYER OR ANY OTHER PERSON OR ENTITY FOR INDIRECT, CONSEQUENTIAL OR SPECIAL DAMAGES, INCLUDING BUT NOT LIMITED TO LOST REVENUES OR PROFITS, EVEN IF SELLER HAS BEEN ADVISED OF THE POSSIBILITY THEREOF.

VI. Survival Clauses

A. Traditional Survival Clauses That Have Been Enforced By Courts.

Survival of Representations and Warranties. All representations and warranties contained in this Agreement (including any certificate or exhibit hereto) shall survive any investigation made at any time with respect to any of the foregoing and shall survive the execution, delivery and performance of this Agreement for a period of 18 months from the Closing Date.

B. Traditional Survival Clauses That Certain Courts Have Declined To Enforce As A Matter Of Law

Survival of Representations and Warranties. The representations and warranties of Buyer and Seller in this Agreement shall survive the Closing for a period of one year, except the representations and warranties contained in Sections 3.1(a), (b), (c) and (f) and 3.2(a) and (b) shall ***survive indefinitely***.

Survival. The covenants, agreements, representations and warranties of the parties hereto contained in this Agreement or in any certificate or other writing delivered pursuant hereto or in connection herewith shall survive the Closing until the first anniversary of the Cosign Date or (i) in the case of Sections 6.05 and 7.02, for the period set forth therein, (ii) in the case of Sections 6.06 and 7.01, indefinitely, (iii) in the case of the items set forth in Section 11.02(f), for the periods set forth therein, and (iv) in the case of the covenants, agreements, representations and warranties contained in Sections 3.17 and 8.05, until the expiration of the applicable statutory period of limitations (giving effect to any waiver, mitigation and extension thereof), if later. No claim for indemnity under this Agreement with respect to any breach of any representations, warranties and/or covenants of the Company and/or Seller shall be made after the applicable period specified in the preceding sentence and all such claims shall be made in accordance with the applicable provision of the Escrow Agreement.

C. Recommended Sample Survival Clause

Survival of Representations and Warranties. Any lawsuit arising from the representations and warranties contained in this Agreement (including any certificate or exhibit hereto) must be filed within a year from the date of Closing.

D. Avoid Internal Conflicts And Impossible/Difficult Timing

Internal Consistency. When imposing a shorter time for bringing an action to enforce a right or claim under a contract, ensure that the party that needs to comply with the shorter time frame can do so in a reasonable manner. For example, where a construction contract provided that a subcontractor would be paid only when the general contractor was paid, and also required the subcontractor to file suit seeking payment within 90 days of completion of work, these two provisions were held to be inconsistent and the 90 day limitation on actions was not enforced by the court. Other courts have held that a reasonable amount of time must be provided to discover a claim and act upon it.

E. Survival Beyond Termination Of Contract

Certain issues, such as confidentiality, non-disclosure and other trade secret or related matters may be important to preserve beyond the termination of a contract. If there is a two year contract or license for the use of software or proprietary information, the provision in the contract that prohibits the use of the vendor's proprietary information by the buyer or user should extend beyond any termination or breach of the contract. In other words, if a party is allowed out of a contract early, or if there is a breach or other termination, that should not excuse the user from the requirements to maintain such information as confidential and not disseminate it or use it for improper purposes.

Sample Language:

The terms and conditions of Article V of this Agreement (Non-Disclosure and Confidentiality) shall survive any termination or breach of this Agreement and shall remain in full force and effect regardless of any termination, non-compliance, breach or other claims or actions of the parties.

F. Limitation On Tort Claims

A traditional survival clause will indicate that certain warranties or representations, or certain contract claims shall survive until a certain date, or beyond closing for a certain period of time. It is possible to also limit all claims between the parties, but broader language may be used to ensure that all claims are covered.

Sample Language:

Any alleged cause of action against (Party 1) for any claim arising under this Agreement or for any claim in contract, tort or otherwise that is related to the work to be performed, representations made, or otherwise related in any way to this Agreement and the circumstances that gave rise to this Agreement, shall be commenced no later than eighteen months from the effective date of this Agreement.

The majority position remains that a Survival Clause constitutes a contractual shortening of the limitations period and that it imposes a firm deadline for a party to file suit. *Lincoln National v. TakeCare, Inc.,* 1998 WL 281290 (N.D. Cal. 1998); *Garrison v. Bally Total Fitness Holding*, 2005 U.S. Dist. Lexis 31724 (D. Or. 2005); *Latek v. Lease America*, 1992 U.S. Dist. Lexis 10396 (N.D. Ill. 1992); *State Street Bank & Trust v. Denman Tire*, 240 F.3d 83 (1st Cir. 2001); *Graphic Technology v. Pitney Bowes*, 968 F. Supp. 602 (D. Kan. 1997).

The majority view is that Survival Clauses apply to related claims (e.g. fraud and negligent misrepresentation). *See Therma-Coustics Mfg v. Borden*, 167 Cal. App. 3d 282 (1985); *Campanelli v. Allstate Life Ins. Co.*, 322 F.3d 1086 (9th Cir. 2003); *Garrison v. Bally Total Fitness Holding*, 2005 U.S. Dist. Lexis 31724 (D. Or. 2005).

The Survival Clause generally extends to the officers and directors of the company invoking the protections offered by the Survival Clause. *Rohmtech v. Taylor*, 1997 WL 778669 (Mass. Super. Ct. Nov. 25,1997) ; *Southcenter View Condo. Owners Assn. v. Condominium Builders,* 47 Wash. App. 767 (1986); *Keiting v. Skauge*, 198 Wisc. 2d 887 (1995); *College of Notre Dame of Maryland v. Morabito Consultants*, 132 Md. App. 158 (2000).

Recently, there have been decisions refusing to interpret Survival Clauses as contractual limitations periods as a matter of law. *See Herring v. Teradyne*, 2007 U.S. App. Lexis 17175 (9th Cir. 2007); *Western Filter Corp. v. Argan, Inc. et al.*, 540 F.3d 947 (9th Cir. 2008). These decisions have found that Survival Clauses must be drafted clearly and explicitly so there can be no other reasonable interpretation as to the parties' intent to shorten the limitations period. Alternative explanations for the meaning of Survival Clauses have included that these provisions extend the time period in which a breach of the representation and warranty could occur. These interpretations are in the minority and have been rejected by most courts. *See Kaiser v. Bowlen*, 455 F.3d 1197 (10th Cir. 2006); *Latek v. Lease America*, 1992 U.S. Dist. Lexis 10396 (N.D. Ill. 1992) (both rejecting the interpretation that survival clauses extend the time for a breach of representation or warranty to occur).

VII. Forum Selection Clauses

Two types of Forum Selection Clauses exist: (1) mandatory; and (2) permissive.

If a party wants to ensure that any litigation takes place exclusively in a particular forum, it needs to draft a mandatory forum selection clause. A mandatory forum selection clause needs to contain explicit language indicating that the parties agree to litigate their claims in the selected forum exclusively. The better practice is to also include an accompanying venue provision indicating where all actions are to be filed. *Boutari and Son v. Attiki Importers*, 22 F.3d 51 (2nd Cir. 1994); *Docksider v. Sea Technologies*, 875 F.2d 762 (9th Cir. 1989); *JHB Resource Mgmt., LLC v. Henkel Corp.*, No. CV044001418, 2006 Conn. Super. LEXIS 1648 (Conn. Super. Ct. May 31, 2006).

A Forum Selection Clause stating only that the selected forum has jurisdiction over disputes between the parties is insufficient to prevent a plaintiff from filing suit in another forum which has personal jurisdiction over the parties.