

GEORGE MASON AMERICAN INN OF COURT



A LITIGATOR'S PERSPECTIVE ON CONTRACTS

September 26, 2017

Pupilage Team Members:

Randall K. Miller, Esq.
Nicholas M. DePalma, Esq.

Michelle Owen West (Student Member)
Jessica L. Hannah (Student Member)

AGENDA

- Introduction (7:00-7:05)
 - Introduction of subject matter, presenters, and student members
- Need for clarity in contract drafting (7:05-7:15)
 - Vignette 1
 - *Cox v. Snap*, 859 F.3d 304 (4th Cir. 2017).
- Conditions precedent or promises (7:15-7:25)
 - Vignette 2
 - *MASTR Asset Backed Securities Trust 2006-HE3*, 843 F. Supp. 2d 996 (D. Minn. 2012).
 - Vignette 3
 - *Cox v. SNAP, Inc.*, 859 F.3d 304 (4th Cir. 2017)
- Forum selection and governing law (7:25-7:35)
 - Vignette 4
 - *Excell, Inc. v. Sterling Boiler & Mechanical, Inc.*, 106 F.3d 318 (10th Cir. 1997)
- Avoiding fraud claims (focus on settlement agreements) (7:35-7:45)
 - Vignette 5
 - *Jared & Donna Murayama 1997 Trust v. NISC Holdings, LLC*, 284 Va. 234 (2012)
- Arbitration or litigation (7:45-7:55)
- Question and Answer Session: 7:55-8:00
- If time permits, we will cover the other topics and vignettes included in the written materials.



GEORGE MASON UNIVERSITY AMERICAN INN OF COURT

“A LITIGATOR’S PERSPECTIVE ON CONTRACTS”

Lessons Learned from Breach of Contract Lawsuits to Help Draft Better Contracts

September 26, 2017



Randy K. Miller
Partner, Litigation
Venable LLP
rkmill@Venable.com
703.905.1449



Nicholas M. DePalma
Partner, Litigation
Venable LLP
ajcowett@Venable.com
703.905.1455




Michelle Owen West (student member)

Jessica L. Hannah (student member)

Topics

1. **Need for clarity in contract drafting**
2. **Conditions precedent?**
3. **Forum Selection and Governing Law**
4. **Avoiding fraud claims (focus on settlement agreements)**
5. **Arbitration or litigation?**
6. **Question and answer**

1. Need for clarity in contract drafting



Make clear in plain language what you think each provision is intended to accomplish

- “If only the contract said ‘X’ we could have saved a ton of money in the litigation”
- Others (litigators, judge, jury, arbitrator) will decide what the deal is based on the words that you write
- People who drafted the contract may no longer be managing the contract or available to explain what was intended

Otherwise...



Strategies

- Don't talk in short hand or in jargon
- **Define** terms
- Illustrate:
 - provide various examples
 - use formulas
- Ask, "where can this go south?" and manage that risk upfront
- Make sure you have the right subject-matter experts on the team
 - remembering the big picture without forgetting the minutiae
- Ask a litigator to review the contract

CVP Calculations for a Single Product

$$\text{Sales \$ required to achieve target pretax profit} = \frac{F + \text{Profit}}{CMR}$$

where F = total fixed costs

CMR = contribution margin ratio

$$= (P - V)/P$$

Note that CMR can be computed as

$$CMR = \frac{\text{Total Revenue} - \text{Total Variable Costs}}{\text{Total Revenue}}$$

To find the breakeven point in sales \$, set Profit = 0.

Vignette 1

- Summary judgment argument.
 - Legal issue: is it .8 times actual sales or \$12M?

“For purposes of determining the strike price of the options issued pursuant to paragraph 1, the value of [SNAP] will be based on a valuation of .8 times [SNAP’s] sales in calendar year 2005. This amount is estimated to be approximately \$12,000,000.”

- *Cox v. Snap*, 859 F.3d 304 (4th Cir. 2017)

2. Conditions precedent or promises?

Conditions

- Conditions precedent can be powerful
 - condition does not occur?
 - **performance is excused!**

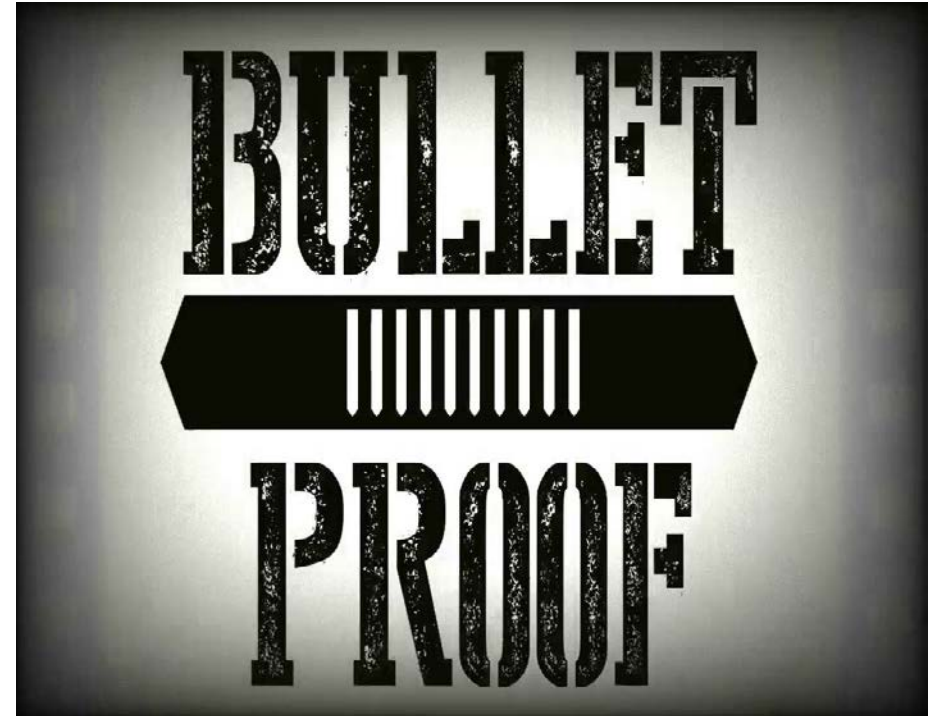


Promises

- If someone does not fulfill a promise then you can sue them for breach, but performance is not excused.

How can you tell the difference?

- Best practice: use the word: "condition precedent."
- Virginia law does not permit conditions precedent unless the parties "clearly understood these terms to assert a condition precedent."
 - *Galloway Corp. v. S.B. Ballard Const. Co.*, 250 Va. 493, 503 (1995)



Vignette 2

- Motion to dismiss argument.
 - Legal issue: is this a condition precedent?

“Upon discovery by the Company or purchaser of a breach of any of the foregoing representations and warranties which materially and adversely affects the value of the Mortgage Loans..., the party discovering such breach shall give prompt (but in no event later than within sixty (60) days after the date on which a responsible officer of the discovery party with direct responsibility for the related transaction has actual knowledge of such reach) written notice to the other.”

- *MASTR Asset Backed Securities Trust 2006-HE3*, 843 F. Supp. 2d 996 (D. Minn. 2012).

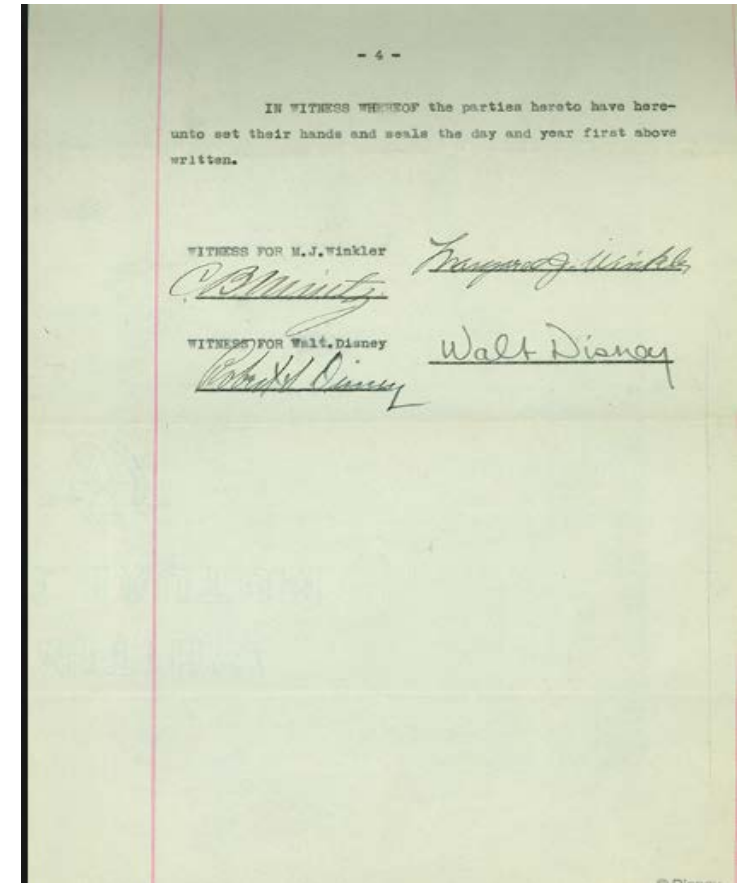
Vignette 3

- Summary judgment. Is this a promise or a condition?
SNAP “will issue a non-qualified stock option to Mr. Cox granting him the right to purchase 308 shares, representing five (5%) percent of the total authorized shares of stock of SNAP.”
 - *Cox v. SNAP, Inc.*, 859 F.3d 304 (4th Cir. 2017).

3. Forum Selection and Governing Law

Litigators Go to The Back of the Contract First

- Litigators love fights that are collateral:
 - is forum selection is mandatory?
 - what governing law applies to the fraud count?
 - are all disputes are covered by the arbitration clause?
- Using clear, mandatory terms forestalls the waste of time and money fighting such claims



Forum Selection Clauses

- Go ahead and say “this is a mandatory forum selection clause and all parties covenant and agree that they will not argue that the provision is a permissive forum selection clause.”



Governing Law

Standard provision

This contract is governed by and interpreted in accordance with the laws of Pennsylvania without regard to that State's conflict of law principles.

- Potential problem: Doesn't expressly address law applicable to tort claims

How a litigator might redraft

- This Agreement **shall** be governed and construed in accordance with the substantive law of Pennsylvania, excluding that State's choice-of-law principles, and this law applies to all claims **arising out of or relating to** the Agreement contract, whether sounding in contract, tort or otherwise. The parties covenant and agree that they will not argue for application of any substantive law other than Pennsylvania's law.

Vignette 4

- Argument on motion to transfer venue.
 - Legal issue: is this mandatory? If you think it is mandatory, can I lay venue in the United States District Court in the County of El Paso, Colorado?

In the event that any dispute shall arise with regard to any provision or provisions of this Agreement, this agreement shall be subject to, and shall be interpreted in accordance with, the laws of the State of Colorado. Jurisdiction shall be in the State of Colorado, and venue shall be in the County of El Paso, Colorado.

- *Excell, Inc. v. Sterling Boiler & Mechanical, Inc.*, 106 F.3d 318 (10th Cir. 1997)



4. Avoiding fraud claims (focus on settlement agreements)

Litigators Love Fraud Claims

- Easier to argue breach of duties **outside** the contract
 - Punitive damages available
 - Avoid contractual limitation on liability
 - Avoidance of merger / integration clause
- Fraud allegations have power!
 - “I was **deceived!**”
 - “I never would have entered the contract if I knew X, which was **concealed from me**”



Protections

- Consider provisions that may limit availability of fraud claims
 - Consider whether the integration clause is sufficient in the context of other contract provisions
 - Consider whether to include a standalone “no reliance” clause



No Reliance Clause


"The parties acknowledge that they have relied upon their own judgment and the advice of their own counsel and financial advisors in making this agreement and represent that they are **not relying on any representation not contained in the agreement**. The parties covenant and agree that they will **not make any claim based on fraud** or similar causes of action based on representations not contained in this agreement."



Vignette 5.

Client meeting. Clients wants to get rid of minority shareholder so they can do a deal selling the Company for a much higher valuation. The other side is willing to do a deal. How can you protect the client against fraudulent inducement?

Jared & Donna Murayama 1997 Trust v. NISC Holdings, LLC, 284 Va. 234 (2012)



Murayama and the Trust “acknowledge and agree that they are fully aware that NISC is considering and pursuing a range of strategic alternatives, including a sale of the company or a qualified public offering, that could ultimately result in a different valuation” of the Class A shares than the \$2,000,000 being paid pursuant to the agreement.”

Murayama and the Trust “irrevocably and unconditionally release and forever discharge NISC from all claims known or unknown, arising at any time before execution of this agreement, whether based on fraud or any other theory of recovery....”

5. Arbitration or litigation?

Benefits of arbitration

- Put the arbitrator qualifications in the contract.
- Provide for discovery in the contract if you want discovery.
- Privacy.
- Cost prohibitive.



Costs of arbitration

- Cost prohibitive
 - Protects wealthier entities from weak claims.
 - Protects wealthier entities from meritorious claims held by entities without sufficient funding.
- No right to discovery.
- Discovery is limited.
- Decision is not made by a judge or jury—but by another lawyer.
- Limited appeal rights.

Argument against arbitration

- Judges are better (no repeat business concerns)
- Judges are free
- Established rules of procedure
- Established substantive law
- Robust appellate rights





Questions?

6. Integration, Ambiguity and Parol Evidence

Parol Evidence?

- Ambiguities allow parol evidence comes slopping into the case
- Ambiguities can eviscerate a merger / integration clause
- Litigators like to depose the deal lawyers
- Techniques to avoid this
 - Define terms
 - Don't talk in shorthand



7. Contract Formation / Agreements To Agree

One Day (Maybe) We Will Build a New World!

- Was the contract even formed?
- Examples:
 - Teaming Agreements
 - Agreements to Agree
 - Term Sheets
- Address whether it is binding
- Have definitive material terms



Vignette 6.

- Motion to dismiss argument. Is this enforceable?

Teaming agreement would be terminated if there was a “failure of the parties to reach agreement on a subcontract after a reasonable period of good faith negotiations.”

- *Cyberlock Consulting, Inc. v. Information Experts, Inc.*, 939 F. Supp. 2d 572 (E.D. Va. 2013)

8. Privilege in M&A Deals

But that's privileged! (No it's actually not)

- Seller's privileged communications are part of what buyer gets in deal
- Unless the contract says otherwise

