



# THE BEST LAID PLANS OFTEN GO AWRY: LITIGATION STORIES ON THE UNINTENDED CONSEQUENCES OF CONTRACTS

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**PFM**  
**ROYER COOPER COHEN BRAUNFELD LLC**  
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# Presenters

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# Agenda

- How well-drafted contracts can still lead to unexpected and unwelcome outcomes in litigation
- Real-life “war stories”
- How will your drafted documents hold up in court?
  - Integration Clauses
  - Forum Selection Clauses
  - Arbitration Clauses
  - Choice of Law Clauses
  - Practical/Administrative Provisions
  - Indemnification Clauses
  - Fee-shifting Clauses
  - Non-Compete Clauses



# Unintended Consequences: Integration Clauses

Despite the integration clause, I'd like to show the existence of a whole separate agreement.



La, la, la...  
I'm not listening.



# Integration Clauses

- An “integration clause” or a “merger clause”
  - Where parties agree that their agreement is their “entire” agreement and that it wipes out any earlier agreements
- *Diskriter, Inc. v. Baker*, No. 524 WDA 2013, 2014 WL 10805972, at \*2 (Pa. Super. Ct. Aug. 1, 2014)
  - This PA Superior Court decision is a warning to companies that the non-compete agreement they think they have with their top executive could be unintentionally wiped out by a few words in a later agreement



# Integration Clauses

- **Learning Outcome:**
  - Integration clauses may only be a few words and look like contract boilerplate, but they can have powerful and unintended consequences
  - Companies should consider their impact carefully before including them in agreements of any kind – including employment, severance and separation agreements



# Unintended Consequences: Forum Selection Clauses



# Forum Selection Clauses

- *Sompo Japan Ins., Inc. v. Alarm Detection Sys., Inc.*, No. 03 C 2322, 2003 WL 21877615, at \*2 (N.D. Ill. Aug. 6, 2003)
  - Forum selection clause specified venue "in Kane County, Illinois."
  - The court held that this only included the state courts in Kane County because "venue in the federal system is stated in terms of judicial districts, not counties. Thus, where a forum selection clause merely designates a particular county, venue lies only in the state courts in that county."
- **But see:**
  - In *City of W. Palm Beach v. Visionair, Inc.*, 199 F. App'x 768, 769 (11th Cir. 2006), the forum selection clause provided for litigation "in Palm Beach County, Florida."
    - The court held that the clause permitted venue in either the state or federal courts located in Palm Beach County

# Forum Selection Clauses

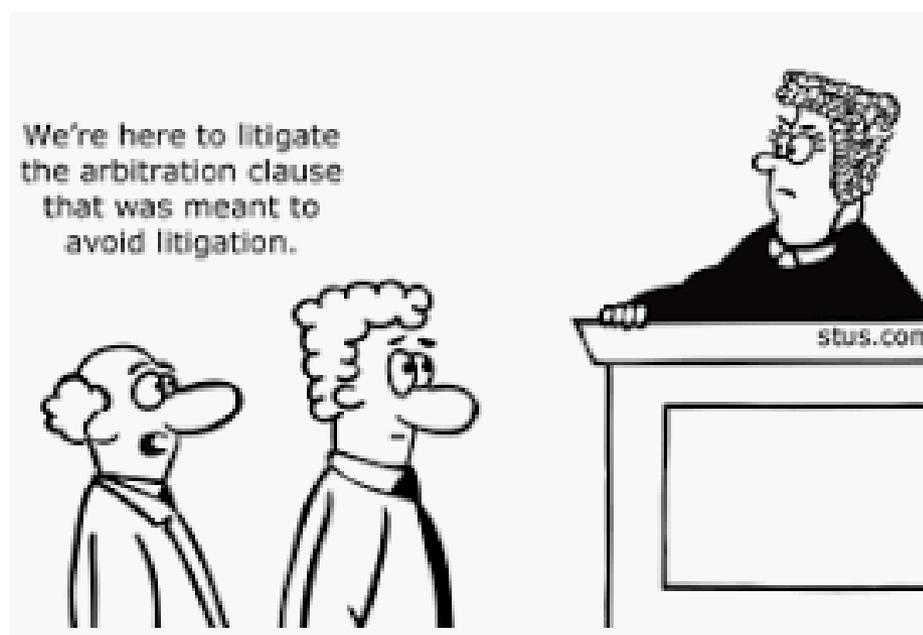
- In many instances, the federal district court that has jurisdiction over a specific county does not have a physical courthouse in that county.
- *Cornett v. Carrithers*, No. 3:11-CV-191-J-37TEM, 2011 WL 13175066, at \*2 (M.D. Fla. Aug. 16, 2011)
  - The forum selection clause stated that "venue shall be Suwanee County, Florida." Suwanee County is part of the U.S. District Court for the Middle District of Florida, but there is no federal courthouse in that county
  - Thus, the court held that the forum selection clause did not include federal courts.

# Forum Selection Clauses

- **Learning Outcome:**

- When drafting forum selection clauses, lawyers should be as precise as possible
- If the clause is intended to be mandatory, it should state that any dispute "shall be litigated" in the designated venue.
- The clause can provide for "exclusive jurisdiction" in a particular venue
- The best practice is to designate a particular court (i.e., Superior Court of Fulton County, Georgia, or U.S. District Court for the Northern District of Georgia) as opposed to particular counties or states
- If the forum selection clause does refer to a geographic locale, it is best to refer to courts "having jurisdiction over" the specific state or county, or specify whether the venue is "state courts" or "state or federal courts" in the locale

# Unintended Consequences: Arbitration Clauses



# Arbitration Clauses

- **Sample Provision:**

- “All disputes arising in connection with this Agreement shall be resolved by binding arbitration in accordance with the Commercial Arbitration Rules of the American Arbitration Association (‘AAA’) then in effect (the ‘Rules’). There shall be three arbitrators. One arbitrator shall be selected by the Person or Persons initiating the demand for arbitration and one arbitrator shall be selected by the Person or Persons responding to the demand within twenty (20) days of the receipt by the respondent(s) of a copy of the demand for arbitration. The third arbitrator, who shall chair the arbitral tribunal, shall be selected by the two party-appointed arbitrators within twenty (20) days of the appointment of the second arbitrator. Any arbitrator not timely appointed shall be appointed by the AAA in accordance with the listing, striking, and ranking provisions of the Rules.”

# Arbitration Clauses

- Seems simple enough, right?
  - **WRONG.**
- Seems like a fair way to get a neutral Chair and overall Panel, right?
  - **WRONG.**
- What could possibly go wrong?
  - **A LOT!**

# Arbitration Clauses

- AAA Rules state that although there is generally no *ex parte* communications with arbitrators, a party “may communicate *ex parte* with a candidate for direct appointments pursuant to R-13 in order to advise the candidate of the general nature of the controversy and of the anticipated proceedings and to discuss the candidate’s qualifications, availability, or independence in relation to the parties **or to discuss the suitability of candidates for selection as a third arbitrator** where the parties or party-designated arbitrators are to participate in that selection.” AAA, R-19 (emphasis added).
  - In practice, what this means is that the parties will be actively communicating with their designee until the Chair is selected.
  - If the parties disagree about the Chair (which is likely), then the party-designated arbitrators won’t be able to agree and you will be left with the potential that AAA appoints the Chair.
  - Or, the parties “agree” to some other random way to choose the Chair so as to not be at the whim of AAA.

# Arbitration Clauses

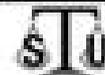
- **Drafting considerations:**
  - How will a panel be selected?
  - Is arbitration intended to be the exclusive method of dispute resolution?
  - Will the parties be entitled to discovery?
    - If so, how much? What kind?



# Unintended Consequences: Choice of Law Provisions

Stu's Views

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Children,  
let's settle this  
like adults.



# Choice of Law

- **Initial questions:**
  - Does the law of the chosen state have a substantial relationship to the parties or the transaction?
  - Is there a reasonable basis for the parties' choice?
- **Contract vs. Tort Law:** The breadth of the clause may preclude its application to tort claims, as opposed to those based in contract
  - ***Miguel v. Pro and David Landscape (D.N.J. 2008)*:** The court noted that choice of law clauses using the language “govern and construed by” are broad enough to capture tort and contract, but clauses that simply say “construed under” are limited to contract claims
  - ***Caton v. Leach Corp., 896 F.2d 939, 942 (5th Cir. 1990)*:** “[this] Agreement shall be construed under the laws of the State of California” did not include tort claims.

# Choice of Law

- **Learning Outcome:**

- Must be a reasonable basis for the parties' choice
- Many clauses are dependent upon the particular choice of law
- Scope: tort and contract, “relating to and arising out of” versus “interpretation” versus “governed by”
- Applies in arbitration as well as court
- If absent, courts do their own analysis
- Can affect ability to terminate contract or amount of damages, entitlement to interest, modify restrictive covenants, and others

# Unintended Consequences: Practical / Administrative Provisions



"The paper and ink content is within acceptable norms, but the contract itself appears to have too many clauses."

# Practical / Administrative Provisions

- **Sample Confidentiality Provision:**

- “All information and data furnished to the Recipient by the Discloser and all other documents to which the Recipient’s Representatives have access during the term of the business arrangement shall be safeguarded by Recipient as required by this Agreement in perpetuity.”

- **Sample Provision Regarding Advance Consent for Removing Personnel:**

- “Company shall submit, prior to project assignment, the name, position description, resumes, and duration of assignment for each key professional employee to be assigned to any project on a regular basis. No employee assigned to a project shall be removed prior to completion of assignment without prior approval of the Client.”

# Practical / Administrative Provisions

- **Sample Arbitration Provision:**

- “All claims, disputes and other matters in question between Contractor, Client, and subcontractors arising out of, or relating to, this Agreement or the breach thereof, shall be decided by arbitration in accordance with the Arbitration Rules of the American Arbitration Association then existing, as modified herein, unless the parties mutually agree otherwise.
- Client, Contractor (or any other architect, engineer, or construction manager), subcontractors, contractors, surety, subcontractors, or any material suppliers who have an interest in the dispute shall be joined as parties to the arbitration. Client will endeavor to require any appropriate third party to be subject to joinder. Contractor's contracts with its subcontractors shall also require such joinder.

...

# Practical / Administrative Provisions

- **Sample Arbitration Provision (continued):**

- The arbitrator(s) shall have authority to decide all issues between the parties including, but not limited to, claims for extras, delay and liquidated damages, matters involving defects in the work, rights to payment, and whether the necessary procedures for arbitration have been followed. The parties expressly agree that the arbitrator(s)' authority is limited to interpretation and application of the specific terms of the Agreement between the parties and the applicable laws of the State of [\_\_\_\_\_] and to deviate from same constitutes a manifest disregard of the law. The arbitrator(s) shall have no authority to add to, take from, or modify any of the provisions of the contract between the parties.
- The foregoing agreement to arbitrate and any other agreement to arbitrate with an additional person or persons duly consented to by the parties to this Agreement, shall be specifically enforceable under the prevailing arbitration law. The award rendered by the arbitrator shall be final, and judgment may be entered upon it in accordance with applicable law in any court having jurisdiction thereof.”

# Practical / Administrative Provisions

- **Sample Provision Regarding Reporting Requirements:**
  - “During the term of this Agreement and to the extent permitted by law, the Contractor agrees to promptly notify the Client in writing of the commencement of existence of any known or threatened Proceeding or Internal Investigation.”

# Unintended Consequences: Indemnification vs. Coverage for Additional Insured



*“And, for what we don’t cover, there’s insurance insurance.”*

# Indemnification

## Indemnification Agreements :

- Transfer the payment responsibility for the indemnitee's negligence from the indemnitee to the indemnitor
- Constitute a non-insurance transfer
- **Three basic types:**
  - Limited
  - Intermediate
  - Broad



SO, NOW WE HAVE ASCERTAINED WHO IS RESPONSIBLE....

# Indemnification

- **Limited:**

- Sample Language: “. . . only to the extent caused by the negligent acts or omissions of the party providing indemnification.”
  - Does not cover indemnitee’s own negligent acts

- **Intermediate:**

- Sample Language: “. . . even for, and if caused in part by, any act, omission, or negligence of the Indemnified Parties.”
  - Covers indemnitee’s negligent acts *so long as* indemnitee is not solely negligent

- **Broad:**

- Sample Language: “. . . even for, and if caused in whole or in part by, any act, omission, or negligence of the Indemnified Parties.”
  - Covers indemnitee’s negligent acts



# Indemnification

- **Example:**
  - *Mace v. Atlantic Refining Marketing Corp.*, 785 A.2d 491 (Pa. 2001)
    - Indemnification provision: “Franchisee agrees to indemnify and defend Atlantic Refining from and against all Claims, losses and damages arising out of Franchisee’s use and operation. . . , excepting any damage or loss caused solely by the negligence of Atlantic.”
    - This is a **LIMITED PROVISION**: The court ruled the “excepting” clause does nothing to expand the indemnification obligation and refused to allow the inference that the excepting clause implicated a promise of Franchisee to provide indemnification for Atlantic Refining’s own partial negligence.

# Indemnification

- **Learning Outcome**

- Use clear and unequivocal language
- Consider enforceability issues & potential limits under Anti-Indemnity Statutes
  - Broad indemnification is not permitted under certain circumstances in many states



"Sign here to indicate you have no idea what you've signed."

# Coverage for Additional Insured

- **Additional Insured Coverage:** One party to a contract obtains coverage under other party's policy
  - The additional insured has direct access to the policy holder's general liability policy
  - Scope of coverage may be broader than indemnification
  - Frequently involves upfront payment of defense fees and costs for the additional insured
  - Additional insured is not able to choose own defense counsel
  - Protection to additional insured is only as good as the underlying insurance policy
  - May erode policy holder's limits for other claims
  - Potential deductibles

# Coverage for Additional Insured

- **Three Basic Types of Additional Insured Coverage:**
  - **Vicarious Liability**: coverage only for additional insured's vicarious liability for acts of policy holder
  - **Partial Negligence**: coverage for the additional insured's partial negligence
    - Often the default
  - **Sole Negligence**: coverage for additional insured's sole negligence

# Unintended Consequences: Fee Shifting Provisions

- Prepare for David and Goliath situations
- What is a “win”?



# Unintended Consequences: Non-Compete Clauses

- **M&A Considerations:**

- Nexus between restrictive covenant and consideration paid

- **Employment Considerations:**

- *Socko v. Mid-Atlantic Systems of CPA, Inc.*, No. 142 MAP 2014, 633 Pa. 555 (Nov. 18, 2015)
  - An employee is not bound by a non-compete agreement signed during the course of his employment if he was not offered additional consideration, even though the agreement expressly stated the parties “intend to be legally bound”



# Non-Compete Clauses

- Will be enforceable only if new and valuable consideration, beyond mere continued employment, is provided and is sufficient to support the restrictive clause



# Non-Compete Clauses

- Examples of a “benefit or a favorable change in employment status” include:
  - A promotion;
  - A change from part-time to full-time status;
  - A salary increase;
  - A favorable change in other aspects of the compensation package – bonuses, stock options, enhanced benefits, and the like; or
  - A one-time bonus payment or severance payment to which the employee was not previously or otherwise entitled



# QUESTIONS AND COMMENTS



*"Any questions?"*

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# THANK YOU

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