

# REDUCING LITIGATION RISKS IN U.S. BUSINESS TRANSACTIONS

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During the excitement of closing a business transaction, the last thing participants often worry about is the deal going sour. But not doing so can be a serious oversight. A failed deal is bad enough; having to contend with the expense and uncertainty of litigation can be a catastrophe.

This is even more so for cross-border transactions, given the marked differences between the Canadian and U.S. legal systems. Fortunately, contracting parties can reduce litigation risks through choice of forum, choice of law, and arbitration clauses. These not only can reduce the expense and inconvenience of litigation but also ensure more productive business relationships by making dispute resolution more predictable.

## Why do choice of law and forum matter?

In the absence of a contractual provisions, choice of forum and law are governed by common law principles, which do not always make for predictable dispute resolution. The plaintiff often can bring suit in any one of several different localities whose courts have their own procedure and choice of law rules.

In turn, where a case is heard can determine its outcome, regardless of the merits. At every stage, litigants must constantly weigh the risk and benefits of pursuing a matter further. So even where the added expense and inconvenience of appearing in a distant court does not deter a litigant, other factors may. Differences in substantive law may give one party a distinct advantage. In other cases, the ability to retain counsel on a contingency basis, the relative burdens of pretrial discovery, the availability of third-party witnesses, or the prospect of facing a jury trial might influence the risk-benefit analysis.

Among the most significant differences between Canada and United States is the greater prevalence of jury trials and punitive damages in the States. These two factors result in considerable leverage for plaintiffs. Often defendants will prefer to pay a hefty "nuisance fee" rather than risk a devastating verdict. Given the experience of defendants such as the Loewen Group - the Canadian mortuary conglomerate that paid \$175 million in settlement after a Mississippi jury awarded \$500 million to a funeral director who accused the company of fraud - such caution is, indeed, often advisable. Thus, defendants frequently find themselves settling to

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avoid the risk of a run-away jury verdict, even though the plaintiff's case is weak and would hardly be worth suing, if brought elsewhere.

### Choice of forum and law provisions

By setting certain basic parameters, forum selection and choice of law clauses can eliminate much of the uncertainty associated with litigation. Equally important, these contractual provisions can contribute to the stability of a business relationship and discourage litigation in the first place. Perhaps most significantly, a forum selection clause eliminates a "race to the courthouse" between parties competing to ensure favorable forum. By removing pressure to bring suit first, a forum selection clause can thus allow parties time to negotiate. By the same token, a disgruntled party whose claim is marginal is less likely to turn to litigation if its ability to exact a nuisance settlement is limited by constraints on punitive damages.

Forum selection and choice of law provisions further help allocate risk between contracting parties during the course of their relationship. An appropriately crafted agreement creates incentives for parties to negotiate their differences by ensuring that legal proceedings are equally unattractive to everyone. A forum selection clause thus might designate a neutral forum or include provisions that minimize risks in a given forum that are disproportionate to one party. For example, a forum selection clause might permit bringing suit in a U.S. jurisdiction but preclude a jury trial.

The readiness of U.S. and Canadian courts to enforce forum selection clauses further ensures their utility. Significantly, U.S. courts favor such clauses as a means of promoting predictability in the international commercial system. To avoid a forum selection clause, a litigant must show that the clause is unreasonable and unjust, the result of fraud, or its enforcement would contravene a strong public policy.

### Arbitration clauses

Another important tool for limiting the uncertainty and inconvenience of cross-border dispute resolution is arbitration. Arbitration permits parties to have their dispute resolved through what is essentially a private trial before one or more neutral decision makers. The main advantages of this system are speed, economy, and higher predictability. Discovery is limited and the rules of evidence and other courtroom procedures are relaxed, so proceedings tend to be abbreviated and less expensive for the litigants. Arbitration decisions are often also more predictable than court adjudications because the arbitrators who hear the case are attorneys or other experts with experience in the relevant industry. The main disadvantage is that binding arbitration is final, and a court will only intervene under very limited circumstances. In short, a litigant sacrifices the procedural protections provided by traditional courts for efficiency and predictability.

Particularly in the international context, arbitration often makes sense. Several widely respected institutions, including the International Chamber of Commerce, the London Court of International Arbitration, and the American Arbitration Association are available as facilitators. Moreover, arbitration judgments are readily enforceable in dozens of countries, including both Canada and the United States, that are signatories of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. The parties can also specify the place of arbitration, the law, and the language.

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### Versatility

Yet another distinct advantage of forum selection, choice of law, and arbitration clauses is their versatility. Depending on the circumstances of the transaction, the parties can use virtually any combination. For example, in a complex joint venture, parties might agree to non-binding mediation as a prerequisite for commencing suit, while also including a choice of forum clause if a legal action proves necessary. In this way, the parties have at least an opportunity to resolve their differences in a cost-effective manner without sacrificing the protections of the judicial system. On a more routine transaction, however, the parties might agree to a binding arbitration clause, which bars recourse to the courts, as the sacrifice of full legal protections is justified by the efficiency gained. In yet another case, a party might request a non-exclusive forum selection clause to guarantee its ability to bring suit in a given jurisdiction, without precluding other jurisdictions. The possibilities are limited only by the needs of the parties.

### Conclusion

Generally recognized and broadly enforced by courts, forum selection, choice of law, and arbitration clauses are extremely valuable devices. Especially in cross-border transactions, these clauses can greatly limit the risks involved in potential litigation and create incentives for the parties to cooperate. While such clauses may seem an inconsequential detail during the heat of negotiations, they can literally save a business, if the once so promising deal ever sours.

