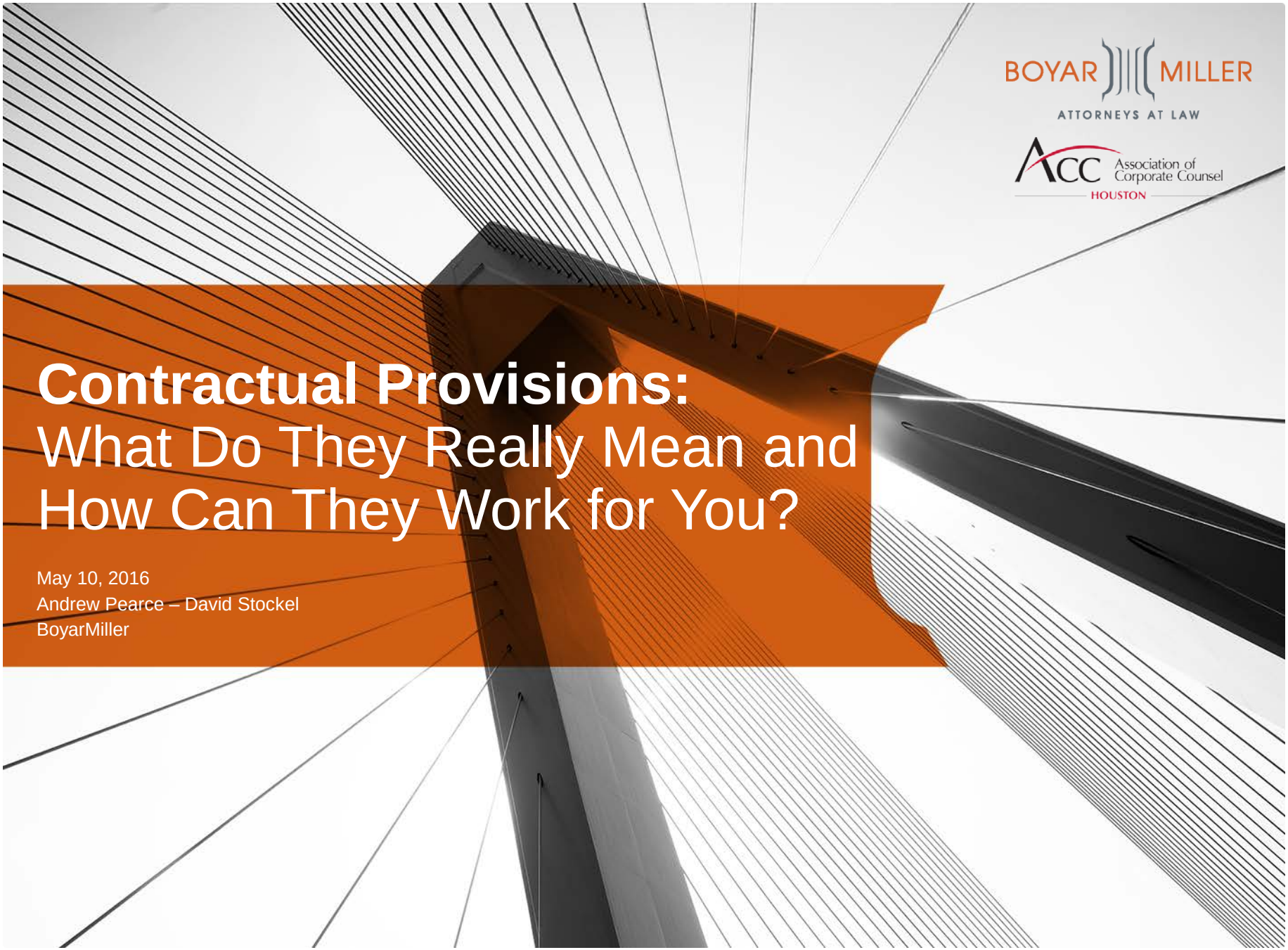

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Contractual Provisions: What Do They Really Mean and How Can They Work for You?

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Andrew Pearce – David Stockel
BoyarMiller

Overview

1. **Choice of Law**
2. **Arbitration**
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5. **Limitation of Damages**
6. **Confidentiality**
7. **Attorney's Fee Update**


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Choice of Law

Contractual Choice of Law

If the parties do not agree which law will apply to their transaction, Texas law will provide the law of the jurisdiction with the "most significant relationship" to the transaction.

***Duncan v. Cessna Aircraft Co.*, 665 S.W.2d 414 (Tex. 1984).**

But if the parties do choose, Texas courts apply the "party autonomy" rule of the Restatement (Second) of Conflict of Laws § 187.

***DeSantis v. Wackenhunt Corp.*, 793 S.W.2d 670 (Tex. 1990).**

The Party Autonomy Rule

To avoid uncertainty, the parties to a contract may express their own choice that the law of a specific jurisdiction apply to their agreement.

Judicial respect of the parties' choice advances the policy of protecting their expectations.

However, the parties' freedom to choose what jurisdiction's law will apply to their agreement is NOT unlimited.

What are the exceptions?

Parties cannot require that their contract be governed by the law of a jurisdiction which has no relation whatsoever to them or their agreement.

Parties cannot by agreement thwart or offend the public policy of the state who's law ought otherwise to apply

- Example: non-competition agreements involving Texas residents that call for the law of another state to govern

Qualified transactions over $1 million

The "fundamental public policy" exception does not apply.

TEXAS BUSINESS AND COMMERCE CODE 271.005(b).

As long as the transaction bears a reasonable relation to the state chosen, the chosen jurisdiction will apply.

What constitutes a “reasonable relation” to a jurisdiction?

TEX. BUSINESS AND COMMERCE CODE 271.004(b):

- **A party to the transaction is a resident of that jurisdiction;**
- **A party to the transaction has the party’s place of business in that jurisdiction or the party’s chief executive office or an office from which the party conducts a substantial part of the negotiations relating to the transaction is in that jurisdiction;**
- **All or part of the subject matter of the transaction is located in that jurisdiction;**
- **A party to the transaction is required to perform in that jurisdiction a substantial part of the party’s obligations relating to the transaction, such as delivering payments;**
- **A substantial part of the negotiations relating to the transaction occurred in or from that jurisdiction and an agreement relating to the transaction was signed in that jurisdiction by a party to the transaction; or**
- **All or part of the subject matter of the transaction is related to the governing documents or internal affairs of an entity formed under the laws of that jurisdiction.**


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Arbitration

Key Considerations in an Arbitration Provision

1. Scope of Arbitration Clauses
2. JAMS, AAA, or Outside of Formal Arbitration Forums
3. Exception for Injunctive Relief
4. One Person vs. Three Person Panels
5. Where to Arbitrate
6. Limited Discovery
7. Confidentiality of Process and Hearing
8. Costs Awarded to Prevailing Party
9. Right to Appeal

http://webcasts.acc.com/handouts/ADR_Rules_Comparison_7277059_1-c.PDF

Scope of Arbitration Clauses

- **The general rule is that the court decides the preliminary questions of arbitrability, including the validity and scope of the arbitration agreement.**

- **Usually, issues of validity and scope are initially raised in court via a motion to compel arbitration filed by a defendant in response to the plaintiff's lawsuit.**

- **"Arbitration. Any dispute, claim, or conflict of any kind *arising from, relating to, or in connection with* this Agreement, *including any question of whether a dispute, claim, or conflict is within the scope of this agreement to arbitrate*, or any questions regarding the existence, validity, enforceability, breach, termination, or waiver of this Agreement, or the construction or interpretation of this Agreement or any term or provision herein, including this agreement to arbitrate, shall be resolved by final and binding arbitration in accordance with any procedures set forth herein."**

Exception for Injunctive Relief?

- **The Texas cases that have considered whether or not a trial court can issue injunctive relief pending arbitration are in conflict.**
- **Some courts of appeal have held that injunctive relief is only proper if the parties' contract contemplated it.**
  - *See, e.g., Metra United Escalante, L.P., v. The Lynd Co.*, 158 S.W.3d 535, 539-40 (Tex. App.—San Antonio 2004, no pet.) (following "the general rule applied by federal courts in Texas and conclude that the issuance of a preliminary injunction is not appropriate when the underlying claims are subject to arbitration under the FAA").
- **Other courts have held that injunctive relief is improper altogether when arbitration is pending.**
  - *See, e.g., Feldman/Matz Interests, L.L.P. v. Settlement Capital Corp.*, 140 S.W.3d 879, 883 (Tex. App.—Houston [14th Dist.] 2004, no pet.) (acknowledging the split among federal courts but concluding that its precedent in *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. McCollum*, 666 S.W.2d 604, 608 (Tex. App.—Houston [14th Dist.] 1984, writ ref'd n.r.e.) and Fifth Circuit precedent compel the conclusion that injunctive relief is improper pending arbitration).
- **Some courts have held that injunctive relief is entirely proper.**
  - *See, e.g., Senter Invs., L.L.C. v. Veerjee*, 358 S.W.3d 841, 845 (Tex. App.—Dallas 2012, no pet.); Structured Capital Res. Corp. v. Arctic Cold Storage, LLC, 237 S.W.3d 890, 895 (Tex. App.—Tyler 2007, no pet.).

Right to Appeal?

- **The TAA provides that an award may be vacated in the following circumstances:**

  - If the award was obtained by **corruption, fraud, or other undue means**;
  - If the rights of a party were prejudiced by **evident partiality by a neutral arbitrator, corruption in an arbitrator, or misconduct or willful behavior of an arbitrator**;
  - If the arbitrators exceed their powers, refused to postpone the hearing after a showing of sufficient cause, refused to hear evidence material to the controversy, or conducted a hearing contrary to the TAA or in a manner that substantially prejudiced the rights of a party; or
  - If there was no agreement to arbitrate, the parties were not compelled by the court to arbitrate, and the party opposing the arbitration did not participate in the hearing without raising the objection.

Right to Appeal?

The Texas Supreme Court, in *Nafta Traders, Inc. v. Quinn* (2011), held that the Texas Arbitration Act (TAA) permits parties to contract for expanded judicial review of arbitration awards.

The parties in *Nafta Traders* attempted to contract around the statutory limitations in the FAA and the TAA—which preclude vacating arbitration awards for errors of law or fact—and agreed that "[t]he arbitrator does not have authority (i) to render a decision which contains a reversible error of state or federal law, or (ii) to apply a cause of action or remedy not expressly provided for under existing state or federal law."

Now, parties may avoid a choice between the risk of a wrong—and unreviewable—arbitration award or potentially cumbersome litigation in court.

Texas now recognizes a hybrid option—arbitration with an expanded scope of judicial review.


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Disclaimer of Reliance

Disclaimer of Reliance

Fraudulent inducement requires proof that the plaintiff justifiably relied on an alleged misrepresentation or non-disclosure.

Texas Supreme Court has held that "reliance disclaimer" provisions can, in certain circumstances, defeat this reliance element as a matter of law.

Unfortunately, the Texas Supreme Court has not provided a bright-line test for determining when such provisions are enforceable.

***Schlumberger Tech. Corp. v. Swanson*, 959 S.W.2d 171 (Tex. 1997).**

***Forest Oil Corp. v. McAllen*, 268 S.W.3d 51 (Tex. 2008).**

Reasons for and against enforcement

Reasons favoring enforcement of reliance disclaimers

- **Protects freedom of contract**
- **Fosters legal certainty and predictability in commercial transactions**
- **Fraud allegations are easily lodged**

Reasons against enforcement of reliance disclaimers

- **Contrary to public policy against fraud**
- **If you can lie convincingly enough to persuade someone to enter into a contract, you can also probably persuade them to agree that lies were never made or relied upon**

Schlumberger Tech Corp. v. Swanson

In enforcing a disclaimer of reliance provision in a settlement agreement, the Texas Supreme Court found the following factors to be significant:

- The parties were represented by highly competent and able legal counsel
- The parties were knowledgeable and sophisticated business players
- The parties dealt at arm's length
- The contract's sole purpose was to end the dispute once and for all
- The parties specifically disagreed and negotiated re: the allegedly fraudulent issue

But the Court did not indicate whether these factors were exhaustive and did not define any of the them.

Forest Oil Corporation v. McAllen

Texas Supreme Court made clear that *Schlumberger* applies broadly to contracts generally – not only to disclaimers intended to resolve the issue in dispute

The Court identified the following "*Schlumberger* factors" as the most relevant:

- The terms of the contract were negotiated, rather than boilerplate, and during negotiations the parties specifically discussed the issue which has become the topic of the subsequent dispute
- The complaining party was represented by counsel
- The parties dealt with each other in an arm's length transaction
- The parties were knowledgeable in business matters
- The release language was clear

Again, however, the Court did not provide a bright-line test or set forth the minimum requisite language.

What clear language should be used?

Don't do this: a standard merger clause or representation disclaimer does not provide the required "clear and unequivocal" language.

Do this:

- **A disclaimer of reliance clause that clearly provides that the plaintiff is not relying on any statement or extra-contractual representations in entering into the contract**
- **Language clearly stating that the contract contains all the parties' representations**
- **Language detailing the parties' arm's length negotiations, including specifically related to the reliance disclaimer**
- **Stipulate to the parties' knowledge and sophistication in business matters**
- **Identify the parties' competent counsel and advisors**
- **Ensure these provisions are conspicuous and initialed by the parties**

Reliance disclaimers are even better than you thought

A clear and unequivocal reliance disclaimer can bar any cause of action or defense which includes reliance as an element:

- **Common law fraud**
- **Statutory fraud (Section 27.01 of the Texas Business and Commerce Code)**
- **Negligent misrepresentation**
- **Deceptive Trade Practices Act violations**
- **Promissory estoppel**


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Jury Waiver

Arbitration clause vs. a contractual jury waiver?

Arbitration

- **Not as inexpensive as advertised**
- **Parties still conduct discovery**
- **Arbitrators typically do not grant pre-hearing dispositive motions**
- **No appellate review**

Jury waiver

- **Eliminates uncertainty of runaway jury finding**
- **Preserves appellate rights**

But are jury waivers constitutional?

Yes!

Texas Supreme Court has analogized contractual jury waivers to arbitration agreements and forum-selection clauses.

"Parties already have the power to agree to important aspects of how prospective disputes will be resolved. They can, with some restrictions, agree that the law of a certain jurisdiction will apply, designate the forum in which future litigation will be conducted, and waive in personam jurisdiction, a requirement of due process. Furthermore, parties can agree to opt out of the civil justice system altogether and submit future disputes to arbitration…Public policy that permits parties to waive trial altogether surely does not forbid waiver of trial by jury."

***In re Prudential Ins. Co. of Am.*, 148 S.W.3d 124, 131 (Tex. 2004).**

Jury waivers must be knowing and voluntary

"A waiver of constitutional rights must be voluntary, knowing, and intelligent, with full awareness of the legal consequences. We echo the United States Supreme Court's admonition that "[w]aivers of constitutional rights not only must be voluntary but must be knowing, intelligent acts done with sufficient awareness of the relevant circumstances and likely consequences."

***In re Prudential*, 148 S.W.3d at 132.**

What does “knowing and voluntary” mean?

- **Were both sides represented by counsel?**
- **Were there revisions to the contract?**
- **Was the waiver clear and unambiguous?**
- **Does it say “knowing and voluntary?”**

Conspicuousness shifts the burden

If the jury waiver is conspicuous, then the "knowing and voluntary" requirement must still be met.

But the burden is shifted to the other party to prove that the waiver was NOT voluntary or knowing.

A conspicuous jury waiver provision is prima facie evidence of a knowing and voluntary waiver and shifts the burden to the opposing party to rebut it.

Courts presume that "a party who signs a contract knows its contents."

***In re GE Capital*, 203 S.W.3d 314 (Tex. 2006).**

What does “conspicuous” mean?

The Texas Supreme Court addressed this in *In Re Bank of America*, 278 S.W.3d 342 (Tex. 2009)”

Section 1.201(b)(10) of the Texas Business and Commerce Code provides that “[c]onspicuous…means so written, displayed, or presented that a reasonable person against which it is to operate ought to have noticed it.”

In *Prudential*, we noted that the waiver provision was “crystal clear” because “it was not printed in small type or hidden in lengthy text” and “[t]he paragraph was captioned in bold type.”

Conspicuousness is not a requirement – it merely shifts the burden.


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Limitation of Damages

Damage Limitation Provisions

Direct vs. Consequential Damages

- Direct damages are those damages that flow naturally and necessarily from a breach of contract i.e. foreseen or contemplated by the parties.
- Example: benefit of the bargain

- Consequential damages are those damages which result, naturally, but not necessarily, from the alleged breach.
- Example: lost profits incidental to the performance of a contract

Limiting Damages

- Generally enforceable.
- Cannot violate public policy.
- Courts look to bargaining power between the parties.

Allright, Inc. v. Elledge, 515 S.W.2d 266 (Tex. 1974)

Conspicuousness of Limiting Provisions

Common Law

- Limitation of damages provisions are not required to be conspicuous.
- Regardless, courts will consider the conspicuousness of the provision when determining if it is enforceable.
- Language must be clear and unequivocal.
- Courts will strictly construe the provisions against the party they are intended to protect.

Liquidated Damages

***FPL Energy, LLC v. TXU Portfolio Mgmt. Co.*, 426 S.W.3d 59, 70 (Tex. 2014).**

- Texas energy providers, like TXU, were required to purchase a certain portion of the electricity they distribute from renewable sources.
- FPL was a renewable energy production company operating several windfarms.
- TXU contracted with FPL to purchase renewable electric energy, as well as the RECs generated from the production of that energy, in order to meet TXU's statutory renewable energy requirements.
- In the event that FPL failed to meet its obligations under the contract, the contract provided for liquidated damages of $50 per REC not produced. This $50 per REC figure was tied to the penalty TXU would be assessed by the Texas Public Utilities Commission for failing to meet its REC requirement.

Liquidated Damages

- TXU sued FPL for breach of contract and sought liquidated damages for FPL's failure to provide the agreed upon RECs and electricity.

- The trial court refused to enforce the liquidated damages provision because TXU was able to cover by obtaining substitute electricity elsewhere and because it determined that the stipulated amount of $50 per REC was not a realistic forecast of damages.

- The court of appeals, however, held that the liquidated damages provision was enforceable because the damages were difficult to estimate and the $50 per REC was a reasonable estimate of just compensation; thus, it assessed damages at $29 million based on a deficiency of 580,000 RECs and a deficiency rate of $50 per REC.

Liquidated Damages

Two indispensable findings a court must make to enforce contractual damages provisions: (1) the harm caused by the breach is incapable or difficult of estimation, and (2) the amount of liquidated damages called for is a reasonable forecast of just compensation.

- "Single-Look" Approach: compare the amount of damages stipulated in the contract to the amount of damages that could have reasonably been foreseen or anticipated based solely on what the parties knew at the time of contract formation.

- "Second-Look" Approach: compares the stipulated sum in the contract not only to the amount of damages that could reasonably be anticipated at the time of contract formation, but also to the amount of actual damages caused by a subsequent breach of the contract.

Trey Qualls, Note and Comment, *Take a Second-Look at Liquidated Damages in Texas (Regardless of What the Texas Supreme Court Says)*, 67 Baylor L. Rev. 666 (2016).

Liquidated Damages

- Ultimately, because the court found that actual damages would have been less than the stipulated amount of $50 per REC, the court held that the liquidated damages clause was an unenforceable penalty.

- The Texas Supreme Court appears to have interpreted the common law test for liquidated damages to apply a second-look approach to reasonableness, one in which actual damages can retrospectively invalidate a provision even if that provision was reasonable when viewed from the moment of contract formation.

What to do:

- Avoid "Shotgun" Clauses
- Avoid "Multiples" of Actual Damages
- Avoid "Damages-Plus" Clauses
- Consider a Bonus for Early Performance as an Alternative to Liquidated Damages


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Confidentiality

Confidentiality

Can a party condition settlement payments on adherence to a confidentiality clause?

- **Oksana Grigorieva received a $750,000 custody settlement from Mel Gibson following their highly publicized falling out. In October 2013, Grigorieva was interviewed by Howard Stern on his radio show. During that interview, Grigorieva comments were relatively brief and vague, and included references to her "painful and dark" experience and her desire to help others. Yet the court ruled her comments about Gibson during the interview violated the custody settlement's confidentiality agreement. The result is that Grigorieva forfeited the remaining installments of the original $750,000 settlement, which totaled close to $375,000.**

- **Patrick Snay sued his former employer, Gulliver Preparatory School in Miami, for age discrimination following the school's decision not to renew his contract as headmaster. The settlement of the suit was for $80,000 and contained a standard confidentiality clause. Snay's daughter, Dana, revealed the terms of the case on Facebook, posting: "Mama and Papa Snay won the case against Gulliver. Gulliver is now officially paying for my vacation to Europe this summer. SUCK IT." Many of Dana's 1,200 Facebook friends were current and former Gulliver students and the post eventually made its way to Gulliver's lawyers. The result? The court tossed out the $80,000 settlement.**


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Attorney's Fee Update

Attorney's Fee Update

Under the "American Rule," litigants may recover attorney's fees only if specifically provided for by statute or contract.

***Epps v. Fowler*, 351 S.W.3d 862, 865 (Tex. 2011).**

TEX. CIV. PRAC. & REM. CODE § 38.001(8) provides that a "person may recover reasonable attorney's fees from an individual or corporation, in addition to the amount of a valid claim, if the claim is for an oral or written contract."

In 2014, the Houston Court of Appeals (14th District) held that a limited liability partnership should not have to pay attorney's fees under § 38.001.

***Fleming & Associates, L.L.P. v. Barton*, 425 S.W.3d 560 (Tex. App.-Houston [14th Dist.] 2014, *pet. denied*).**

Attorney's Fee Update

In *Fleming*, the Court explained that neither "individual" nor "corporation" was defined in the Code Construction Act or Chapter 38, so the ordinary meaning of those terms should be applied in construing Section 38.001.

The legislature did not intend Section 38.001 to apply to partnerships because it did not use any term encompassing partnerships.

Just last month, the Court decided the same issue as to limited liability companies.

***Alta Mesa Holdings, L.P. v. Ives*, 2016 Tex. App. LEXIS 3872 (14th Dist. – April 14, 2016).**

Attorney's Fee Update

The Court admitted that the question of whether an LLC is contained within the term "corporation" is a closer call than whether partnership is included within "individual" or "corporation."

Sometimes "company" and "corporation" are sometimes used synonymously.

Regardless, under Texas statutes, the legal entities "corporation" and "limited liability company" are distinct entities with some but not all of the same features.

Final takeaway: LLCs (like partnerships) are not corporations, but are other legal entities against which Section 38.001 does not authorize the recovery of attorney's fees.

Questions?

David Stockel
BoyarMiller
dstockel@boyarmiller.com
(832) 615-4202

Andrew Pearce
BoyarMiller
apearce@boyarmiller.com
(832) 615-4263