

Dispute Resolution Provisions: What to Include & Why They Matter

When entering into a business agreement, parties typically have high hopes regarding the success of their relationship and are hesitant to discuss what should happen if an issue arises over the course of their relationship. But there are key questions that need to be addressed in the contract about potential disputes. Those questions include:

How will disputes between the parties be settled?

Who will determine the appropriate remedy?

What state's laws will govern the agreement?

It is important to make these decisions at the beginning of the business relationship before tensions arise between the parties.

Litigation and arbitration are the most common forms of dispute resolution found in contracts. Contracts may also include mechanisms for parties to attempt to resolve issues internally before turning to external dispute resolution mechanisms, such as by having executives meet to discuss the issues and negotiate a compromise for a certain amount of time. In this paper, we focus on the litigation and arbitration mechanisms for dispute resolution, as well as the choice of governing law.

Litigation

Litigation is the default mechanism for dispute resolution. This means that even if a contract is silent on dispute resolution, the parties will be able to use litigation to resolve disputes under the contract. A decision reached through litigation is binding and enforceable on the parties, but it is also appealable. Litigation is *typically* longer, more expensive, and less predictable than arbitration.

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Jurisdiction

A court can only decide a case if it has jurisdiction over the parties or property involved. For example, if one party is based in Massachusetts and the other party in Rhode Island, and the contract governs services provided in Massachusetts, courts in Oregon would not have proper jurisdiction to hear the parties' disputes under the contract. However, parties to the agreement may consent to the jurisdiction of courts in a chosen state (and if they desire, a specific county within that state).

Venue

Venue refers to the state, county and/or district where the lawsuit is to be tried. For certainty, the parties to an agreement should include a provision in the agreement that identifies the specific venue in which lawsuits arising under the contract must be brought. Venue and jurisdiction can be dealt with in the same provision. In the following example, the parties are identifying Massachusetts as the venue for any lawsuits arising under the contract and consenting to the jurisdiction of Massachusetts courts:

Exclusive jurisdiction and venue for any action arising under this Agreement is in the federal and state courts located in Massachusetts, and both Parties consent to the jurisdiction of, and irrevocably waive any objection to venue in (on the basis of an inconvenient forum or otherwise), those courts for this purpose.

Judge vs. Jury

In the litigation context, the parties can decide if they want a judge (called a "bench trial") or a jury ("jury trial") to decide the outcome of the litigation. A bench trial may be preferable to a trial by jury because juries can be unpredictable. A jury swayed by emotional testimony may award exorbitant damages that neither party foresaw. Furthermore, for complex business issues, a jury may not be the best choice – a judge experienced in business disputes and contract law might be better suited to decide on the issues. Because parties to a contract are automatically entitled to

a jury trial, if the parties want a bench trial, the contract should include a provision waiving the right to trial by jury.

Arbitration

Unlike the court system, arbitration proceedings are able to be held in private and issues can be resolved confidentially. The parties can choose arbitrators with expertise related to their dispute. Arbitration hearings are usually conducted by one or three arbitrators. While one arbitrator can make the process faster and less expensive, three arbitrators is often thought to lead to a fairer outcome. Compared to litigation, arbitration *typically* is faster, less expensive, and leads to more predictable outcomes because the arbitrators are experts in the fields relevant to the dispute.

Arbitration Services

Typically, when parties agree to arbitration, they identify a particular arbitration organization to manage the proceedings. The International Chamber of Commerce (“ICC”), the American Arbitration Association (“AAA”), and JAMS (formerly known as Judicial Arbitration and Mediation Services) are popular choices to guide parties through arbitration, provide arbitrators for proceedings, and administer hearings. Each of these organizations has procedural rules that govern the arbitrations it administers. For contracts in which the parties are based in different countries, the ICC may be the best option. For contracts in which the parties are based in the US, AAA and JAMS are both good options.

Arbitration Provisions

An arbitration clause should state that all claims and disputes arising under the agreement will be settled by *binding* arbitration and that an arbitration award may be confirmed in a court of competent jurisdiction. This means that the results of the arbitration are final and that if a party refuses to pay damages, the other party can go to a court and have the arbitration award converted into an enforceable judgement. The parties should also include the following in an arbitration clause:

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- the arbitration organization that will administer the arbitration
- how many arbitrators will be appointed
- where the arbitration will take place

Governing Law

Whether the parties opt for litigation, arbitration, or another method of dispute resolution, the agreement should contain a governing law provision. A governing law provision (also known as a “choice of law provision”), identifies which state’s laws govern the contract. Law varies from state to state on business issues, contract interpretation, and damages. If no governing law is chosen, the judge/arbitrator must conduct a factual analysis to determine the appropriate governing law. This analysis includes questions like where the contract was performed, where the contract was signed, and where the parties are based. This analysis can be expensive and time consuming and the uncertainty is not desirable for either party.

A governing law clause can be simple, such as the following:

This Agreement shall be governed by and construed in accordance with the laws of the Commonwealth of Massachusetts, without regard to its conflict of law provisions.

Federal Claims

Although contractual disputes are largely governed by state law, the topics addressed in contracts may sometimes also be governed by federal law. Even though federal statutes do not vary from state to state, federal courts in different states may develop different tests and ways to analyze those statutes. With that in mind, the choice of venue (discussed above) can act as a de facto “choice of law” with respect to the interpretation of federal law.

For example, in the context of patent claims, federal courts in Massachusetts and in the larger New England area have developed their own tests and methods for assessing patent infringement claims that may be slightly different than the tests and methods used by federal

courts in other parts of the country. If those approaches are seen as favorable to a patent licensor or licensee, that party might want to select Massachusetts as the venue, knowing that a patent claim (which is governed by federal law) will be resolved by a Massachusetts federal court.

Conclusion

While it may seem pessimistic to discuss at the outset of a contractual relationship what to do if a dispute occurs or an issue arises, it is important that parties to a contract negotiate dispute resolution terms while relations between them are amicable. Although it may be an uncomfortable discussion, in the long run it will save time and money, and make navigating issues in the relationship down the road simpler and more predictable.

The information in this white paper is just an introduction to dispute resolution. If you are eligible for the Startup Law Clinic's services and you are looking to enter into an agreement with another business, we may be able to draft the contract for you and walk you through the considerations for the dispute resolution provisions.