SHUMAKER
Shumaker, Loop & Kendrick, LLP

Winning Commercial Litigation: Terms and Conditions, Strategy and Execution

Business Information for Clients and Friends of Shumaker, Loop & Kendrick, LLP

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Manufacturing • Customers • Vendors • Supply Chain
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Commercial litigation is an inevitable part of the business world. Companies make efforts to prevent and avoid disputes with customers, suppliers or counterparties to commercial contracts. However, when such disputes are unavoidable, companies seek to eliminate, or at least minimize, loss and risk.

A recent case we handled makes this point. Our client was a global manufacturing company with a diverse customer base and supply chain. For business reasons, the company elected to terminate a supply agreement with a customer. Not wanting to lose the business opportunities associated with the supply contract, the customer sued the company for wrongful termination.

The customer challenged what the company believed to be a by-the-book contract termination. Moreover, the customer sought to extract value from the company by using its alleged wrongful termination to avoid paying a substantial outstanding account receivable owed to the company.

In a reasonable period of time, the company collected 100% of the account receivable owed, and avoided all liability for the claims asserted by the customers. How did the company win?

A GOOD CONTRACT

The primary contract document was a 25-year-old, one-and-a-half page, letter agreement, which expressly incorporated the company's "terms of sale." Provisions in the terms of sale that made a difference included:

- Interest upon default at a materially above-market contract rate, and
- Attorneys' fees arising from the company's loss in connection with the customer's default.

A GOOD STRATEGY

The customer's strategy was to assert allegations of wrongful termination of the supply agreement, seeking damages that would offset what the customer owed to the company on the account receivable. The customer might end up paying some of the account receivable but would avoid paying as agreed. **The company needed a counter strategy.**

A. Removal

The customer filed the suit in its own state court. However, to avoid "home cooking" and given the "diversity of citizenship" of the parties (citizens of different states), the company removed the lawsuit to United States Federal Court in New York, to obtain a balanced forum.

B. Teeing up the Incentives

In Federal Court, the Company denied the wrongful termination allegations, and also filed a counterclaim seeking recovery of the substantial account receivable owed. Faced with a certain account receivable obligation, and with the additional obligation of interest at the contract rate until the account receivable was paid, plus paying the company's legal fees, it would be virtually impossible for the customer to "be in the money" on its claims. Facing this reality, the customer would have no incentive to continue the litigation.

A GOOD EXECUTION: EARLY SUMMARY JUDGMENT

To execute the strategy, rather than get bogged down in "motions practice" and protracted discovery, the company moved for partial summary judgment on its accounts receivable claim at the outset.

While the allegations regarding the alleged wrongful termination of the supply agreement were fact intensive and not resolvable on a summary judgment basis (material fact disputes), the accounts receivable claim was clear and undisputed. The customer received the goods, utilized the goods in its business and received full value from its customers on account of the goods supplied. The accounts receivable claim and the wrongful termination of supply agreement claims were unrelated. The company moved for partial summary judgment in the case to reduce its account receivable claim to a judgment, which would include interest and attorneys' fees.

Once the Federal Court entered partial summary judgment on the account receivable, the value of the customer's wrongful termination claim was neutralized. The customer's incentive to continue the litigation was largely eliminated, particularly in light of mounting interest on the judgment and attorneys' fees. It would be virtually impossible for the customer to achieve a damage claim greater than the amount of the accounts receivable judgment. Especially since the customer would be liable for the company's attorneys' fees defending the counterclaim.

Under Federal Rule of Civil Procedure 62(h) regarding "Stay with Multiple Claims or Parties," a court may stay the enforcement of a judgment until it enters a later judgment, and "may prescribe terms necessary to secure the benefit of the stayed judgment for the party in whose favor it was entered." The customer sought to stay enforcement of the judgment until its claims for wrongful termination were fully adjudicated. The company successfully countered that the Federal Court should require a cash bond in the amount of the company's accounts receivable judgment to protect its value for the company.

In light of the court's ruling requiring a cash bond, the customer capitulated and paid its obligations owed to the company in full, and dismissed the wrongful termination provisions with prejudice.

With a good contract and a well-planned and swiftly executed litigation strategy, the company was successful in getting paid in full for its goods and avoiding all liability asserted by the customer.

We hope you found this useful and informative. Please contact us if you have any questions about this or any other matter.

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