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## **Forum Selection Clauses and Their Effect in Commercial Collection Litigation**

### **Consideration of Where to Sue**

When a delinquent account receivable cannot be collected amicably, legal action is indicated. The initial issue is in what location will suit be filed? The answer is easy if both the creditor and debtor are located in the same state. The general rule is that the legal action may be commenced where the debtor resides or does business, or where the claim arose. The creditor's attorney should commence suit in the court that is most favorable to the creditor.

This is done for several reasons. Once the creditor starts suit in the court most favorable to the creditor, the debtor's counsel is often required to travel longer distances, thus increasing costs of litigation to the debtor. Additionally, a "hometown" court may be more favorable to the creditor and its position. Finally, it saves the creditor time and money by minimizing the travel distances of its lawyers and employees to appear for depositions and court hearings.

### **If the Debtor is in a Different State**

How does this play out if the debtor resides or is located outside the state where the creditor is located? Where can the suit be commenced? This question requires a detailed and complex examination of jurisdictional statutes, constitutional law and costs considerations. Generally, each state has a series of statutes providing the rules under which that state's courts may exercise its powers over an individual or business organization that is a debtor/defendant located outside its boundaries. However, these statutes must be interpreted in light of constitutional guarantees of due process protecting any debtor/defendant.

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A court may not exercise its jurisdiction over a nonresident individual or business entity, unless that nonresident has engaged in a series of "minimal contacts" within the respective state seeking to obtain or take jurisdiction over the debtor/defendant. In addition, the nonresident must have "purposefully availed" itself of the respective state and jurisdiction seeking to impose its court system on the subject nonresident. If these tests cannot be met, suit must be commenced in the state of the debtor's residence or domicile. If this occurs, then costs considerations must be considered.

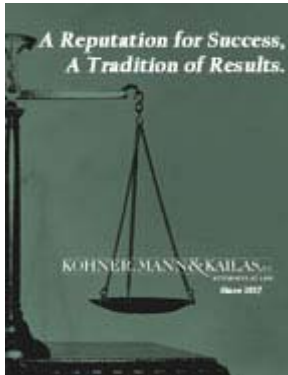
### Using the Forum Selection Clause

The smaller the amount of the claim involved, the less likely suit will be a viable option, since the costs of providing witnesses for depositions and/or trial in another state where the debtor/defendant is located may be prohibitive. This dilemma can often be avoided by the use of a "forum selection clause".

Simply stated, a forum selection clause is a provision in a written purchase order, sales agreement, credit application, personal guaranty, promissory note or any other form of agreement or contract between the debtor and creditor, which directs and provides for what law will apply, and what court or courts will have jurisdiction over any dispute that may arise between the parties, including the collection of any indebtedness owing. Such a clause typically reads:

"This agreement shall be governed by, and interpreted in accordance with the laws of the State of (creditor's choice of residence or domicile) and (customer, guarantor or debtor) agrees to submit at the option of (creditor), to the jurisdiction of the state or federal courts of (creditor's choice residence or domicile state) to determine any matter arising out of this (type of agreement)."

Generally, most state and federal courts have determined this provision to be enforceable. In addition, if the transaction involves a sale of goods and the Uniform Commercial Code has been adopted in the subject jurisdiction, most courts would permit the application of the choice of law provision (forum selection clause) provided the transaction is one that has a reasonable relation and/or connection to the jurisdiction that is selected for the legal action.



Both state and federal courts have carefully considered the jurisdiction aspects of these types of clauses. Generally these types of clauses will be given effect, provided they are not unfair or unreasonable.

The rationale for accepting such clauses is that parties should be free to contract with each other as to what forum will be convenient for them should a dispute arise. Such a clause, however, will not be enforced if the result is considered overreaching; its use is unfair and unequal in bargaining power; or if the forum chosen would be seriously inconvenient for one of the parties. These are a formidable number of "ifs", but the clause still has strong value for consideration.

### Conclusion

In dealing with a customer outside its state of residence or domicile, a creditor should consider the incorporation of a forum selection clause in any appropriate document utilized in its contracting. It will provide a valuable "insurance policy" for the creditor. If done properly, it will ensure that when any dispute arises in collection of the account, any litigation will be in a forum of the creditor's choosing, or in the location most favorable to the creditor. Legal counsel well versed in this consideration should be consulted in drafting such document language. The forum selection clause is a formidable tool for the creditor if considered and utilized correctly, properly and intelligently. *Don't accept the risk without it!* It is especially valuable in a well-drafted and state-of-the art credit application.

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**About Kohner, Mann & Kailas, S.C.**

Founded in 1937, KMKSC is a business and commercial law firm listed in Martindale-Hubbell's Bar Register of Preeminent Lawyers. KMKSC provides quality legal expertise across the areas of law encountered by businesses in the normal course of their operations and growth. Our services range from high-profile appellate representation and international business issues to ensuring that critical everyday needs, such as debt recovery, are fulfilled efficiently and expertly. Our purpose is to deliver excellent results for our clients, whether the issue is advice on the avoidance of legal disputes, closing a deal, protecting assets or winning in court. KMKSC is continually advancing the interests of its clients in negotiations, transactions, litigation and alternative dispute forums across North American and beyond. We help U.S. companies address the legal issues raised by trading across international borders and provide legal support and advice to foreign companies operating in American markets.

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