

BARGAINS BICOASTAL: NEW LIGHT ON CONTRACT THEORY

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ABSTRACT

Recent research has shown that large companies select New York law and New York courts to govern disputes under commercial contracts. Because these parties make choice-of-law and forum selection decisions before conflicts arise, there is reason to believe that their preference for New York reflects an effort to select efficient terms. This Article compares New York's contract law with that of its most natural competitor, California. It turns out that New York strictly enforces bargains and displays little tolerance for efforts to rewrite deals ex post. California, in contrast, more willingly reforms contracts for reasons of fairness, equity, morality, or public policy. The revealed preferences of sophisticated parties support arguments by Schwartz, Scott, and others that formalistic rules offer superior value for the interpretation and enforcement of commercial contracts.

TABLE OF CONTENTS

I.	Introduction	1476
II.	General Approach	1479
III.	Formation	1481
	A. Preliminary Negotiations	1481
	B. Consideration	1485
IV.	Validity	1487
	A. Duress	1487
	B. Unconscionability	1489
	C. Public Policy	1493
	1. In General	1493
	2. Exculpatory Clauses	1496
	3. Noncompete Clauses	1499

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4. Wrongful Discharge.....	1500
D. Statute of Frauds	1502
E. Mistake.....	1504
V. Parol Evidence.....	1506
VI. Choice of Law and Forum.....	1508
A. Choice-of-Law Clauses.....	1508
B. Forum Selection Clauses.....	1512
VII. The Adjudicatory Process	1513
A. Waivers of Jury Trial	1513
B. Attorneys' Fees	1513
C. Arbitration Clauses	1515
D. Class Action Waivers.....	1518
VIII. Extra-Contractual Liabilities	1519
Conclusion.....	1522

I. INTRODUCTION

Recent work in contract theory, epitomized by an influential article by Alan Schwartz and Robert Scott, suggests that business entities benefit from formal rather than contextual rules of contract law.¹ Such firms are better off, according to this theory, when courts interpret contracts according to their terms and do not attempt to substitute the courts' own concepts of reasonableness or fair dealing for bargains actually struck.²

¹ See Alan Schwartz & Robert E. Scott, *Contract Theory and the Limits of Contract Law*, 113 YALE L.J. 541 (2003). For other work by these authors identifying advantages to a formalistic approach, see Robert E. Scott, *A Theory of Self-Enforcing Indefinite Agreements*, 103 COLUM. L. REV. 1641 (2003); Robert E. Scott, *The Case for Formalism in Relational Contract*, 94 NW. U. L. REV. 847, 864-65 (2000); Alan Schwartz, *Relational Contracts in the Courts: An Analysis of Incomplete Agreements and Judicial Strategies*, 21 J. LEGAL STUD. 271, 316-18 (1992). For a critique, see James W. Bowers, *Murphy's Law and the Elementary Theory of Contract Interpretation: A Response to Schwartz and Scott*, 57 RUTGERS L. REV. 587 (2005), which argues, contra Schwartz and Scott, that many commercial parties would favor a contextualist approach.

For discussion of the "new formalism" in contract theory, see Avery Weiner Katz, *The Economics of Form and Substance in Contract Interpretation*, 104 COLUM. L. REV. 496, 496-501 (2004), which distinguishes between "formalistic" and "substantive" approaches; see also David Charny, *The New Formalism in Contract*, 66 U. CHI. L. REV. 842 (1999). The current debate in contract theory roughly tracks the longstanding disagreement between the two giants of traditional contract scholarship, Samuel Williston (who advocated a formalistic approach) and Arthur Corbin (who supported a more contextual analysis).

² In a study that complements the Schwartz-Scott theory, Avery Katz argues that formalistic rules may be useful for commercial parties that tend to be repeat players or have good (and relatively symmetric) information about the costs and benefits of performance. Katz, *supra* note 1, at 527-28. Katz, however, does not take a position on which style of contract law is more efficient, preferring instead to let the contracting parties themselves make this decision in the

This theoretical work challenges conventional views in contract scholarship that favor looser, more contextual approaches.³ But does it accurately describe the real world? Lisa Bernstein's important studies of internal industry dispute resolution practices find that private arbitration tribunals employ bright-line rules; these rules deviate, in some respects, from the more nuanced approach that would apply if the disputing parties brought their controversy before a court.⁴ Bernstein's work suggests that industry actors, when given the freedom to devise their own procedures, opt for a system of rules much like that predicted in Schwartz and Scott's theory.

This Article offers a more general test of the proposition that formal rules are efficient means for governing commercial contracts. It draws on Eisenberg and Miller's empirical study of dispute resolution clauses in major transactions.⁵ Nearly half of the contracts in Eisenberg and Miller's sample chose New York law to govern disputes, and nearly half of the contracts that contained forum selection clauses opted for New York state or federal courts.⁶ California, on the other hand, was distinctly unpopular with the parties represented in Eisenberg and Miller's study. Many fewer contracts opted for California law or a California forum than would be expected given the size and commercial importance of that state.⁷

The contrast between California and New York law has implications for contract theory. Since choice-of-law and forum selection clauses are negotiated *ex ante*, they likely represent efforts by the contracting parties to maximize the joint value of the undertaking.⁸ And because the contracts in the Eisenberg-Miller study were, by definition, important to the financial results of large corporations,⁹ it can be presumed that they received scrutiny from well-qualified attorneys.

context of individual transactions. *See id.* at 502-12.

³ *See* Katz, *supra* note 1, at 498 (“[F]or the past one hundred years or so the historical trend across the board has been to water down such formal doctrines in favor of a more all-things-considered analysis of what the parties may have meant in the individual case.”).

⁴ *See* Lisa Bernstein, *Private Commercial Law in the Cotton Industry: Creating Cooperation Through Rules, Norms, and Institutions*, 99 MICH. L. REV. 1724 (2001); Lisa Bernstein, *Merchant Law in a Merchant Court: Rethinking the Code's Search for Immanent Business Norms*, 144 U. PA. L. REV. 1765 (1996).

⁵ Theodore Eisenberg & Geoffrey P. Miller, *The Flight to New York: An Empirical Study of Choice of Law and Choice of Forum Clauses in Publicly-Held Companies' Contracts*, 30 CARDOZO L. REV. 1457 (2009) [hereinafter Eisenberg & Miller, *Flight to New York*] (finding that parties to contracts included as exhibits to SEC reports strongly preferred New York law and forum); *see also* Theodore Eisenberg & Geoffrey Miller, *Ex Ante Choices of Law and Forum: An Empirical Analysis of Corporate Merger Agreements*, 59 VAND. L. REV. 1975 (2006) (finding that parties to corporate mergers prefer New York law over all states other than Delaware).

⁶ Eisenberg & Miller, *Flight to New York*, *supra* note 5.

⁷ *See* Eisenberg & Miller, *Flight to New York*, *supra* note 5.

⁸ *See* Schwartz & Scott, *supra* note 1, at 552.

⁹ The sample was taken from Form 8K reports, which are filed in connection with material events in the financial affairs of reporting companies.

Accordingly, compared with California, New York may provide the more efficient regime for interpreting and enforcing commercial agreements.¹⁰ Analysis of the relevant differences between the two states' contract law could then provide information on optimal contract rules.

This Article performs such an analysis. It compares New York and California across a range of contract law issues. As would be expected, the laws are similar in broad outline. Each state respects freedom of contract and each recognizes other social and moral objectives that occasionally trump private agreements. Each state's law grows out of a dialectic process in which competing values are reconciled in different settings. Yet a closer analysis reveals substantial differences in tone and substance. New York and California are close siblings—children of the common law and a shared legal and political tradition. But they are far from identical twins.

The differences between New York and California contract law turn out to align with the formalist-contextualist distinction in contract theory. New York judges are formalists. Especially in commercial cases, they have little tolerance for attempts to re-write contracts to make them fairer or more equitable, and they look to the written agreement as the definitive source of interpretation. California judges, on the other hand, more willingly reform or reject contracts in the service of morality or public policy; they place less emphasis on the written agreement of the parties and seek instead to identify the contours of their commercial relationship within a broader context framed by principles of reason, equity, and substantial justice.

Both approaches to contract law are commendable. Both serve important social goals and employ sophisticated and well-reasoned doctrines in the service of those ends. This article takes no position on whether one is better than the other. What is clear, however, is that contracting parties do take a position on this question. The testimony of the marketplace—the verdict of thousands of sophisticated parties whose incentives are to maximize the value of contract terms—is that New York's formalistic rules win out over California's contextualist approach. As predicted by theory, sophisticated parties prefer formalistic rules of contract law.¹¹

¹⁰ This observation is in line with Katz's argument that sophisticated parties have the ability—by choice of law, choice of forum and other strategies—to select the level of formalism that maximizes the value of their transactions. *See* Katz, *supra* note 1, at 508-11.

¹¹ The results of the present study are not conclusive. They depend in part on the reliability of Eisenberg and Miller's empirical analysis. Perhaps the contracts in their sample are not representative of commercial contracts generally, either because the time period under study (six months) was insufficient to generate reliable results because the SEC-reporting firms in the sample are not representative of commercial firms generally, or for other reasons. Further, Eisenberg and Miller's finding that commercial parties prefer New York law and forum is not

II. GENERAL APPROACH

Both New York and California recognize freedom of contract as fundamental,¹² although limited at times by other values;¹³ however New York gives comparatively more weight to contractual freedom. In the absence of severe inequality of bargaining power, New York courts almost never upset private arrangements, no matter how inequitable they may appear *ex post*.¹⁴ New York's tenderness for freedom of contract expresses itself, at times, in a seemingly atavistic pleasure in imposing the consequences of bad bargains.¹⁵ Thus, we are told that New York courts may not "alter the contract to reflect . . . personal notions of fairness and equity"¹⁶ nor reform a transaction to accomplish "notions of abstract justice or moral obligation."¹⁷ Nor will morally

tantamount to a conclusion that they do so out of concern to maximize the joint value of the contract. Network effects, agency costs, or bargaining problems could conceivably explain the data in the Eisenberg-Miller study without implying that the observed terms are efficient. For further discussion of these issues, see Eisenberg & Miller, *Flight to New York*, *supra* note 5. Firms may select New York law and forum because of effective marketing and branding rather than any fundamental benefits offered by that state. *See id.* Perhaps the contract provisions observed in Eisenberg's and Miller's data are simply boilerplate, reflecting nothing more than adherence to convention by people who give little or no thought to the consequences. (For examples of treatment of boilerplate, see BOILERPLATE: THE FOUNDATION OF MARKET CONTRACTS (Omri Ben-Shahar ed. 2007); Omri Ben-Shahar, *Freedom from Contract*, 2004 WIS. L. REV. 261, 265 (2004); Stephen J. Choi & G. Mitu Gulati, *Innovation in Boilerplate Contracts: An Empirical Examination of Sovereign Bonds*, 53 EMORY L.J. 929 (2004); David Gilo & Ariel Porat, *The Hidden Roles of Boilerplate and Standard-Form Contracts: Strategic Imposition of Transaction Costs, Segmentation of Consumers, and Anticompetitive Effects*, 104 MICH. L. REV. 983, 1030 (2006).) If accurate, these observations would affect the relevance of the present study to the question of formalism versus contextualism in contract law (although the comparison between New York and California would still be of interest). However, as one of the authors of the Eisenberg-Miller study, I believe it is robust to such criticisms.

¹² California: *See, e.g.*, *Fries v. Save Mart Supermarkets, Inc.*, No. F050104, 2007 WL 3151609, at *6 (Cal. Ct. App. Oct. 30, 2007) (characterizing value of freedom of contract as "fundamental"), *cert. denied*, (Cal. 2008). The California legislature, likewise, has declared that "[i]t is the public policy of the state and fundamental to the commerce and economic development of the state to enable and facilitate freedom of contract by the parties to commercial real property leases." CAL. CIV. CODE § 1995.270(a)(1) (West 2008).

New York: If anything, New York courts are even more enthusiastic, sometimes speaking as if freedom of contract were the only relevant concern. *See, e.g.*, *Bird v. St. Paul F. & M. Ins. Co.*, 120 N.E. 86, 87 (N.Y. 1918) ("The inquiry for us is how far the parties to this contract intended us to go. The causes within their contemplation are the only causes that concern us.").

¹³ *See, e.g.*, *Zomba Recording LLC v. Williams*, No. 600639/06, 2007 WL 1063869, at *5 (N.Y. Sup. Ct. Feb. 19, 2007).

¹⁴ *See Janian v. Barnes*, 742 N.Y.S.2d 445 (App. Div. 2002) (holding that prudence or fairness of a contract is not the subject of judicial scrutiny in the absence of fraud or unconscionability); *Dafnos v. Hayes*, 694 N.Y.S.2d 42, 44 (App. Div. 1999).

¹⁵ *See Oppenheimer & Co. v. Oppenheim, Appel, Dixon & Co.*, 660 N.E.2d 415, 421 (N.Y. 1995).

¹⁶ *Greenfield v. Philles Records, Inc.* 780 N.E.2d 166, 171 (N.Y. 2002).

¹⁷ *Breed v. Ins. Co. of N. Am.*, 385 N.E.2d 1280, 1283 (N.Y. 1978).

objectionable behavior by a counterparty excuse performance or confer rights of recovery on the victim, at least where the conduct is not so egregious as to be unconscionable.¹⁸ And New York's reverence for freedom of contract is not waning; if anything, the courts of that state are becoming even more inclined than heretofore to defer to private agreements.¹⁹

In contrast, California's allegiance to freedom of contract is frequently tempered with concern for other values: providing compensation for harm;²⁰ facilitating job mobility;²¹ protecting parties against extortionate damages;²² preventing "inequitable or unequal exchanges";²³ ensuring access to a civil jury;²⁴ protecting policyholders injured by uninsured motorists;²⁵ even safeguarding the legislature's choice of venue for litigation.²⁶ Unlike New York, California does not sharply distinguish between consumer and commercial contracts, subjecting even business-to-business contracts to potential invalidation or reform on grounds of fairness, equity, or substantial justice.²⁷ A strong norm in California against waiver of rules implicating the public interest backs this complex structure of agreement-trumping policies.²⁸

¹⁸ *Jordan Panel Sys. Corp. v. Turner Constr. Co.*, 841 N.Y.S.2d 561, 573 (App. Div. 2007) (noting that even though the defendant's actions left "much to be desired" and would probably have led to a different result under principles of equity jurisprudence, "we did not write those rules of engagement, and we are not empowered either to ignore or rewrite them").

¹⁹ *See, e.g., Zarsky v. Law Office of Maury B. Josephson*, No. 1764CV2005, 2006 WL 3751486, at *4 (N.Y. Civ. Ct. Dec. 20, 2006).

²⁰ *See City of Santa Barbara v. Superior Court*, 161 P.3d 1095, 1099 n.5 (Cal. 2007).

²¹ *See VL Sys., Inc. v. Unisen, Inc.*, 61 Cal. Rptr. 3d 818, 821-22 (Ct. App. 2007) (recognizing that freedom of contract is an "important principle," but striking down a contract on the ground that it impermissibly interfered with employee job mobility).

²² *See CAL. CIV. CODE* § 3358 (West 2008) ("Except as expressly provided by statute, no person can recover a greater amount in damages for the breach of an obligation, than he could have gained by the full performance thereof on both sides.").

²³ *See, e.g., Rich & Whillock, Inc. v. Ashton Dev., Inc.*, 204 Cal. Rptr. 86, 89 (Ct. App. 1984) ("On the one hand, courts are reluctant to set aside agreements because of the notion of freedom of contract and because of the desirability of having private dispute resolutions be final. On the other hand, there is an increasing recognition of the law's role in correcting inequitable or unequal exchanges between parties of disproportionate bargaining power and a greater willingness to not enforce agreements which were entered into under coercive circumstances." (quoting *Totem Marine Tug & Barge, Inc. v. Alyeska Pipeline Serv. Co.*, 584 P.2d 15, 21 (Alaska 1978))).

²⁴ *See Grafton Partners L.P. v. Superior Court*, 116 P.3d 479 (Cal. 2005).

²⁵ *Daun v. USAA Cas. Ins. Co.*, 23 Cal. Rptr. 3d 44, 48 (Ct. App. 2005).

²⁶ *See Arntz Builders v. Superior Court*, 19 Cal. Rptr. 3d 346 (Ct. App. 2004).

²⁷ California courts, for example, are willing to invalidate commercial contracts on unconscionability grounds, even when severe inequality of bargaining power does not appear to be present. *See infra* notes 121-124 and accompanying text.

²⁸ *See CAL. CIV. CODE* § 3513 (West 2008) ("Any one may waive the advantage of a law intended solely for his benefit. But a law established for a public reason cannot be contravened by a private agreement.").

III. FORMATION

A. *Preliminary Negotiations*

California and New York articulate generally similar rules on contract formation.²⁹ Both states require more than mere participation in contract negotiations in order to establish a legal obligation.³⁰ Neither state enforces agreements to agree. Behind this similarity, however, lurk subtle differences.

One of these differences concerns the contractual obligation to negotiate in good faith. The New York Court of Appeals recognized such an obligation in *American Broadcasting Companies, Inc. v. Wolf*.³¹ Sportscaster Warner Wolf's contract with ABC required him to "enter into good faith negotiations . . . for the extension of this agreement on mutually agreeable terms."³² All the judges of the New York Court of Appeals agreed that this language obligated Wolf to bargain in good faith for the extension of his contract.³³ Although a broad reading of the *Wolf* case could gut the traditional rule against agreements to agree, the case has not had a broad impact. The reason is that New York courts have strictly limited its application. The obligation to negotiate in good faith applies only when the parties use definite language indicating a present intent to be bound,³⁴ and the subject of negotiation is both specific and backed by ascertainable indications of intent regarding the anticipated outcome of the process.³⁵

Recent California cases also recognize an obligation to negotiate in good faith. In *Copeland v. Baskin Robbins U.S.A.*,³⁶ the parties agreed that the plaintiff would acquire a manufacturing plant from the defendant and further agreed that the defendant would purchase product from the plant at a price to be negotiated.³⁷ After protracted discussions

²⁹ For interesting analyses of the policy issues surrounding the imposition of liability for actions or statements made in preliminary negotiations, see Kevin Davis, *Licensing Lies: Merger Clauses, the Parol Evidence Rule and Pre-contractual Misrepresentations*, 33 VAL. U. L. REV. 485, 485, 534 (1999); Jason Scott Johnston, *Communication and Courtship: Cheap Talk Economics and the Law of Contract Formation*, 85 VA. L. REV. 385 (1999).

³⁰ See, e.g., *Teachers Ins. & Annuity Ass'n v. Tribune Co.*, 670 F. Supp. 491, 497 (S.D.N.Y. 1987) (noting that New York seeks to avoid "trapping parties in surprise contractual obligations that they never intended"); *Kruse v. Bank of Am.*, 248 Cal. Rptr. 217, 229 (Ct. App. 1988) (finding that preliminary negotiations or agreements for future negotiations do not create binding obligations).

³¹ 420 N.E.2d 363 (N.Y. 1981).

³² *Id.* at 364.

³³ *Id.* at 365, 369.

³⁴ See *Tribune Co.*, 670 F. Supp. at 499-500.

³⁵ See *L-3 Commc'ns Corp. v. OSI Sys., Inc.*, No. 02 Civ. 9144, 2004 WL 42276, at *10 (S.D.N.Y. Jan. 8, 2004).

³⁶ 117 Cal. Rptr. 2d 875 (Ct. App. 2002).

³⁷ *Id.* at 878.

the defendant announced that it was terminating negotiations.³⁸ The California Court of Appeal, in a case of first impression, held that the complaint set forth a cause of action for damages for breach of a promise to negotiate in good faith.³⁹ Although *Copeland* appears similar to the *Wolf* case, it is potentially far broader in scope. The parties in *Copeland* did not manifest an unequivocal intent to negotiate in good faith and the contract lacked specific indications of the parties' expectations regarding the outcome of negotiations.⁴⁰ California law thus arguably imposes risks of being inadvertently caught up in contractual obligations that are not present under New York law.

California and New York also differ in the reasons given for imposing liability for preliminary negotiations. California cases tend to emphasize the lack of agreement among the parties on a material term of the contract when they refuse to recognize contractual obligations based on preliminary negotiations.⁴¹ New York cases, in contrast, focus more on the form of the purported agreement. Even if the key terms are agreed to, New York courts resist enforcing contracts if the parties intended to embody their agreement in a written form that was never executed.⁴² The New York cases reflect a significant emphasis, not nearly as pronounced in California, on the importance of a definitive written agreement for determining the intent of the parties.

New York and California also differ in their willingness to use promissory estoppel to impose liability for pre-contractual negotiations.⁴³ In *James Baird Co. v. Gimbel Brothers, Inc.*,⁴⁴ a well-known New York case, a general contractor obtained a contract in reliance on a subcontractor's bid that was withdrawn prior to acceptance.⁴⁵ The New York Court of Appeals rejected the contractor's

³⁸ *Id.*

³⁹ *Id.* at 879-85. The *Copeland* decision has been followed by a number of other decisions. See, e.g., *Coachella Valley Water Dist. v. Imperial Irrigation Dist.*, 2007 WL 2822766, at *8-10 (Cal. Ct. App. Oct. 1, 2007) (No. D049610, 2004 term; renumbered No. D049636, 2006 term).

⁴⁰ See *Copeland*, 117 Cal. Rptr. 2d at 878.

⁴¹ See, e.g., *Rochlis v. Walt Disney Co.*, 23 Cal. Rptr. 2d 793, 797 (Ct. App. 1993).

⁴² See, e.g., *R.G. Group, Inc. v. Horn & Hardart Co.*, 751 F.2d 69, 75 (2d Cir. 1984) ("[W]hen a party gives forthright, reasonable signals that it means to be bound only by a written agreement, courts should not frustrate that intent."); *Jordan Panel Sys. Corp. v. Turner Constr. Co.*, 841 N.Y.S.2d 561, 565-66 (App. Div. 2007); *Chatterjee Fund Mgmt., L.P. v. Dimensional Media Assocs.*, 687 N.Y.S.2d 364, 365 (App. Div. 1999) (mem.) (declining to enforce contract so long as the agreement had not been finalized with a sufficient manifestation of consent to the entire package even though the parties agreed to all essential terms); *Deli of Latham, Inc. v. Freije*, 475 N.Y.S.2d 652 (App. Div. 1984) (holding that phrase "Make up drawing," which required further negotiations on the renovations plaintiff desired, rendered contract unenforceable), *aff'd*, 472 N.E.2d 1041 (N.Y. 1984).

⁴³ For a historical analysis focusing on the leading cases, see Alfred S. Konefsky, *Freedom and Interdependence in Twentieth-Century Contract Law: Traynor and Hand and Promissory Estoppel*, 65 U. CIN. L. REV. 1169 (1997).

⁴⁴ 64 F.2d 344 (2d Cir. 1933).

⁴⁵ *Id.* at 345.

claim against the subcontractor: The parties had made no binding agreement and a theory of promissory estoppel could not fix the defect.⁴⁶ Several New York decisions have subsequently endorsed the idea of promissory estoppel liability for subcontractor bids,⁴⁷ but as yet New York has not definitively rejected the rule of the *Gimbel* case.⁴⁸ Moreover, even when New York courts do use promissory estoppel to impose liability for preliminary negotiations, the doctrine is hedged by limitations and qualifications. The promise on which the estoppel is based must be clear and unambiguous,⁴⁹ and it cannot be established solely by course of conduct⁵⁰ or vague reassurances.⁵¹ New York disallows promissory estoppel when the evidence shows that the parties intended not to be bound until the execution of a written document.⁵² Integration or merger clauses stipulating that the written document is the complete agreement of the parties will ordinarily preclude the use of promissory estoppel to enforce oral promises.⁵³ The injury to the party claiming estoppel must be so severe as to be considered unconscionable.⁵⁴ All the elements of a promissory estoppel claim must be specifically pleaded.⁵⁵ Overall, New York offers only a limited and grudging acceptance of the promissory estoppel theory as a means for imposing liability for preliminary negotiations.

California is more receptive to promissory estoppel claims. In the leading case, *Drennan v. Star Paving Co.*,⁵⁶ the California Supreme Court reached a result directly contrary to *Baird v. Gimbel*. It held that promissory estoppel could substitute for consideration in situations

⁴⁶ *Id.* at 345-46.

⁴⁷ *See, e.g.,* Bunkoff General Contractors, Inc. v. Dunham Elec., Inc., 753 N.Y.S.2d 156, 157-58 (App. Div. 2002).

⁴⁸ *See* LAHR Constr. Corp. v. J. Kozel & Son, Inc., 640 N.Y.S.2d 957, 959-61 (Sup. Ct. 1996) (expressing doubts that the state has repudiated the *Gimbel* rule and describing New York's adoption of promissory estoppel principles as "tentative"); Arthur B. Schwartz, *The Second Circuit "Estopped": There Is No Promissory Estoppel in New York*, 19 CARDOZO L. REV. 1201 (1997).

⁴⁹ *Asgahar v. Tringali Realty, Inc.*, 795 N.Y.S.2d 68, 70 (App. Div. 2005) (rejecting promissory estoppel claim for lack of a clear and unambiguous promise).

⁵⁰ *S. Fed. Sav. & Loan Ass'n of Ga. v. 21-26 E. 105th St. Assocs.*, 145 B.R. 375, 383 (S.D.N.Y. 1991), *aff'd*, 978 F.2d 706 (2d Cir. 1992).

⁵¹ *See Kelly v. Chase Manhattan Bank*, 717 F. Supp. 227, 236 (S.D.N.Y. 1989).

⁵² *See, e.g.,* Telecom Int'l Am., Ltd. v. AT & T Corp., 67 F. Supp. 2d 189, 206 (S.D.N.Y. 1999); *Jordan Panel Sys., Corp. v. Turner Constr. Co.*, 841 N.Y.S.2d 561, 565-66, 572 (App. Div. 2007) (declining to recognize reliance when defendant explicitly disclaimed an intent to be bound prior to signing of formal contract); *Wiscovitch Assocs., Ltd. v. Philip Morris Cos.*, 598 N.Y.S.2d 193, 194 (App. Div. 1993) (mem.).

⁵³ *See Gebbia v. Toronto-Dominion Bank*, 762 N.Y.S.2d 38, 38 (App. Div. 2003).

⁵⁴ *Readco, Inc. v. Marine Midland Bank*, 81 F.3d 295, 301 (2d Cir. 1996); *Zucker v. Katz*, 708 F. Supp. 525, 533 (S.D.N.Y. 1989); *Spier v. Southgate Owners Corp.*, 833 N.Y.S.2d 459, 460 (App. Div. 2007) (rejecting estoppel claim because injury was not unconscionable).

⁵⁵ *See Special Event Entm't v. Rockefeller Ctr., Inc.*, 458 F. Supp. 72, 76-77 (S.D.N.Y. 1978).

⁵⁶ 333 P.2d 757 (Cal. 1958).

where a contractor reasonably relied on a subcontractor's bid.⁵⁷ Subsequent California decisions have generalized this principle to other situations in which reasonable reliance substitutes for a defect in contract formation.⁵⁸ To be sure, California also limits the scope of promissory estoppel: There must be a clear and unambiguous promise⁵⁹ rather than vague assurances;⁶⁰ the promisor must reasonably expect the statement to induce reliance;⁶¹ the plaintiff must actually rely on the promise;⁶² the plaintiff must incur damage stemming from the reliance;⁶³ and all the elements must be pleaded.⁶⁴ Nevertheless, California makes promissory estoppel available to enforce promises in situations where New York does not. For example, California does not usually require unconscionable injury, and it views the presence of a written agreement as less of an obstacle to recognition of the theory. The California approach, in contrast to New York's, seeks to impose a principle of fairness and morality in business conduct,⁶⁵ even at the expense of increasing the risk that parties will be trapped in unanticipated contractual obligations.

⁵⁷ See *id.* at 760. The disagreement between the California and New York courts has provoked extensive scholarly commentary. See, e.g., Jay M. Feinman, *Promissory Estoppel and Judicial Method*, 97 HARV. L. REV. 678, 680-81, 692-94, 700-01 (1984); Friedrich Kessler & Edith Fine, *Culpa in Contrahendo, Bargaining in Good Faith, and Freedom of Contract: A Comparative Study*, 77 HARV. L. REV. 401, 422-24 (1964); Charles L. Knapp, *Reliance in the Revised Restatement: The Proliferation of Promissory Estoppel*, 81 COLUM. L. REV. 52, 63-64 (1981); Kofesky, *supra* note 43.

⁵⁸ See, e.g., *Aronowicz v. Nalley's, Inc.*, 106 Cal. Rptr. 424, 434 (Ct. App. 1972); *French v. Bd. of Educ.*, 71 Cal. Rptr. 713 (Ct. App. 1968); *Hilltop Props., Inc. v. State*, 43 Cal. Rptr. 605, 612-13 (Ct. App. 1965).

⁵⁹ *Cal. Cancer Specialists Med. Group, Inc. v. Health Net of Cal., Inc.*, No. B182557, 2006 WL 2468069, at *9 (Cal. Ct. App. Aug. 28, 2006).

⁶⁰ See *Sarafa v. PC Quote, Inc.*, No. D036652, 2001 WL 1506659, at *10-11 (Cal. Ct. App. Nov. 28, 2001); *Ladas v. Cal. State Auto. Ass'n*, 23 Cal. Rptr. 2d 810, 815-16 & n.4 (Ct. App. 1993).

⁶¹ *Poway Royal Mobilehome Owners Ass'n v. City of Poway*, 58 Cal. Rptr. 3d 153, 160 (Ct. App. 2007).

⁶² See *Millbrae Serra Sanitrium, Inc. v. State*, No. D050273, 2008 WL 903091, at *7 (Cal. Ct. App. Apr. 4, 2008).

⁶³ See *Massey v. L.A. Unified Sch. Dist.*, No. B193106, 2008 WL 570792, at *11-12 (Cal. Ct. App. Mar. 4, 2008).

⁶⁴ See *Smith v. City and County of S.F.*, 275 Cal. Rptr. 17, 23 (Ct. App. 1990).

⁶⁵ The purpose of the device in California is fundamentally moral: Following the *Restatement (Second) of Contracts*, the California courts see the doctrine as a means to prevent "injustice," *Poway Royal*, 58 Cal. Rptr. 3d at 160, preserve "equity," *C & K Eng'g Contractors v. Amber Steel Co.*, 587 P.2d 1136, 1138-39 (Cal. 1978), and do "right and justice," *Toscano v. Greene Music*, 21 Cal. Rptr. 3d 732, 738 (Ct. App. 2004). See *RESTATEMENT (SECOND) OF CONTRACTS* § 90 (1981) ("A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise.").

B. *Consideration*

Both New York and California recognize the doctrine of consideration: In general, parties are not bound unless something of value is exchanged. Neither state insists on equivalence in value: Any benefit to the promisor or detriment to the promisee will do.⁶⁶

Again, however, a closer investigation reveals differences. New York adheres to traditional rules under which past consideration or moral obligation do not qualify.⁶⁷ On the other hand, New York allows greater flexibility when a written instrument is involved. Recitals of “value received” are presumptive evidence of consideration.⁶⁸ And the New York legislature has dispensed with the consideration requirement altogether for certain documents that appear frequently in business transactions. Promises based on past consideration or antecedent obligations, unenforceable if made orally, are binding if in writing and signed by the responsible party.⁶⁹ So are modifications or releases,⁷⁰

⁶⁶ California: *See, e.g.*, *Melican v. Regents of Univ. of Cal.*, 59 Cal. Rptr. 3d 672, 679 (Ct. App. 2007) (declining to scrutinize adequacy of consideration so long as some benefit was received); *A.J. Indus., Inc. v. Ver Halen*, 142 Cal. Rptr. 383, 389 (Ct. App. 1977); *Bank of Cal. v. Connolly*, 111 Cal. Rptr. 468, 482 n.7 (Ct. App. 1973).

New York: *See, e.g.*, *Rooney v. Tyson*, 697 N.E.2d 571, 580-81 (N.Y. 1998) (Smith, J., dissenting) (declining to scrutinize adequacy of consideration so long as some benefit was received); *Weiner v. McGraw-Hill, Inc.*, 443 N.E.2d 441, 445 (N.Y. 1982); *Laham v. Chambi*, 753 N.Y.S.2d 34, 35 (App. Div. 2002).

⁶⁷ *See Ripley v. Int'l Rys. of Cent. Am.*, 171 N.E.2d 443, 447 (N.Y. 1960) (explaining that promise to do what one is under a legal obligation to do is not consideration); *Pershall v. Elliot*, 163 N.E. 554 (N.Y. 1920) (noting that moral obligation is insufficient consideration); *Strong v. Sheffield*, 39 N.E. 330 (N.Y. 1895).

⁶⁸ *See Vernon v. Winikoff*, 582 N.Y.S.2d 758 (App. Div. 1992) (mem.); *Noreaster Real Estate Servs. & Holding Inc. v. Vasquez*, No. 2002-1474, 2003 WL 23191090 (N.Y. App. Term Dec. 10, 2003).

⁶⁹ N.Y. GEN. OBLIG. LAW § 5-1105 (McKinney 2008) (“A promise in writing and signed by the promisor or by his agent shall not be denied effect as a valid contractual obligation on the ground that consideration for the promise is past or executed, if the consideration is expressed in the writing and is proved to have been given or performed and would be a valid consideration but for the time when it was given or performed.”); *see First Nat'l. City Bank v. Valentine*, 306 N.Y.S.2d 227, 231 (Sup. Ct. 1969). The new promise must be in writing; an antecedent debt is not sufficient consideration for an oral promise. *Beitner v. Becker*, 824 N.Y.S.2d 155, 157 (App. Div. 2006).

⁷⁰ N.Y. GEN. OBLIG. LAW § 5-1103 (McKinney 2008) (“An agreement, promise or undertaking to change or modify, or to discharge in whole or in part, any contract, obligation, or lease, or any mortgage or other security interest in personal or real property, shall not be invalid because of the absence of consideration, provided that the agreement, promise or undertaking changing, modifying, or discharging such contract, obligation, lease, mortgage or security interest, shall be in writing and signed by the party against whom it is sought to enforce the change, modification or discharge, or by his agent.”). Oral modifications or releases do require consideration. *See Maurer v. Erdheim*, 738 N.Y.S.2d 885, 886 (App. Div. 2002); *Fed. Deposit Ins. Corp. v. Hyer*, 413 N.Y.S.2d 939, 943-44 (App. Div.), *appeal dismissed*, 47 N.Y.2d 951 (1979).

irrevocable assignments,⁷¹ firm offers,⁷² rewards for return of lost property,⁷³ and certain promises by grantors of interests in real property.⁷⁴

California recognizes a moral element in consideration to a greater extent than does New York. The traditional rules have been modified to enforce promises based on antecedent debts, obligations discharged in bankruptcy, or those barred by the statute of frauds or a statute of limitations.⁷⁵ Conversely, value that would otherwise qualify as consideration does not support a contract if it is “contrary to good morals.”⁷⁶ California also will not grant specific performance if the breaching party has not received “adequate consideration”⁷⁷ or if the contract is “not, as to him, just and reasonable.”⁷⁸ Consideration here means more than the consideration to support a simple contract—the value conferred must be “fair and adequate.”⁷⁹

On the other hand, California does not go as far as New York when it comes to recognizing the special status of written instruments. Written recitals of consideration are given presumptive weight⁸⁰ but are

⁷¹ N.Y. GEN. OBLIG. LAW § 5-1107 (McKinney 2008) (“An assignment shall not be denied the effect of irrevocably transferring the assignor’s rights because of the absence of consideration, if such assignment is in writing and signed by the assignor, or by his agent.”).

⁷² *See id.* § 5-1109 (“Except as otherwise provided in . . . the uniform commercial code . . . when an offer to enter into a contract is made in a writing signed by the offeror, or by his agent, which states that the offer is irrevocable during a period set forth or until a time fixed, the offer shall not be revocable during such period or until such time because of the absence of consideration for the assurance of irrevocability.”).

⁷³ *Id.* § 5-1113 (“A promise to pay a reward for return of lost or mislaid property is not unenforceable because of absence of consideration if the promise was made in writing or the promisor caused it to be published.”).

⁷⁴ *See id.* § 5-1115 (“A promise or warranty by the grantor in a deed or conveyance of an estate or interest in real property and acknowledged or proved in the manner prescribed by law to entitle it to be recorded shall not be denied effect because of the absence of consideration, if no consideration was intended.”). Among other things, this statute provides a means for recognizing that people often grant property to beneficiaries as gifts. *See Moczan v. Moczan*, 522 N.Y.S.2d 591, 593 (App. Div. 1987) (mem.).

⁷⁵ *Dow v. River Farms Co. of Cal.*, 243 P.2d 95, 99 (Cal. Dist. Ct. App. 1952); *see CAL. CIV. CODE* § 1606 (West 2008) (“An existing legal obligation resting upon the promisor, or a moral obligation originating in some benefit conferred upon the promisor, or prejudice suffered by the promisee, is also a good consideration for a promise, to an extent corresponding with the extent of the obligation, but no further or otherwise.”).

⁷⁶ CAL. CIV. CODE §§ 1607, 1667 (West 2008).

⁷⁷ *Id.* § 3391 (providing that specific performance is not available unless the defendant “received an adequate consideration for the contract”).

⁷⁸ *Id.*

⁷⁹ *Trup v. Manock*, No. D050134, 2008 WL 889425, at *9 (Cal. Ct. App. Apr. 3, 2008) (quoting *Gilbert v. Mercer*, 3 Cal. Rptr. 456, 457 (Ct. App. 1960)). Presumably, the purpose of this rule is the desire, based on moral principles, to protect parties against demands for specific relief where the cost of performance to the breaching party far exceeds the benefit of performance to the nonbreaching party. *See Dore v. S. Pac. Co.*, 124 P. 817, 822 (Cal. 1912).

⁸⁰ CAL. CIV. CODE § 1614 (West 2008) (“A written instrument is presumptive evidence of a consideration.”).

2010]

BARGAINS BICOASTAL

1487

never conclusive.⁸¹ Irrevocable options and firm offers,⁸² contract modifications,⁸³ and other signed commitments enforceable in New York without consideration appear to require consideration under all circumstances in California.⁸⁴ Overall, as compared with New York's, California's rules on consideration offer less certainty to commercial parties that their contracts will be enforced as written.

IV. VALIDITY

I now turn to an analysis of specific doctrines that may be employed to challenge the validity of contracts otherwise proper in form and substance: duress, unconscionability, public policy, statute of frauds, and mistake.

A. Duress

New York courts recognize duress as a defense to the enforcement of a contract but impose significant limitations on its use. The threat must be credible and its execution must inflict harm that is both irreparable⁸⁵ and of such magnitude that the victim is effectively deprived of free will.⁸⁶ Mere financial pressure, even if "relentless," is not enough;⁸⁷ nor is duress present if the party experiencing the pressure

⁸¹ CAL. EVID. CODE § 622 (West 2008) ("The facts recited in a written instrument are conclusively presumed to be true as between the parties thereto, or their successors in interest; *but this rule does not apply to the recital of a consideration.*" (emphasis added)).

⁸² See *City of Orange v. S.D. County Employees Ret. Ass'n*, 126 Cal. Rptr. 2d 405, 410 (Ct. App. 2002) ("[A]n irrevocable option is a contract made for consideration, to keep an offer open for a prescribed period." (quoting *Palo Alto Town & Country Vill., Inc. v. BBTC Co.*, 521 P.2d 1097, 1100 (1974))).

⁸³ See *Krobitzsch v. Middleton*, 165 P.2d 729, 731 (Cal. Dist. Ct. App. 1946). Section 1698(a) of the California Civil Code, providing that "[a] contract in writing may be modified by a contract in writing," might be read to dispense with a requirement of new consideration for written modifications; this is especially true because section 1698(c) specifically requires consideration for oral modifications of written contracts. CAL CIV. CODE § 1698(a), (c) (West 2008). The cases, however, do not appear to have endorsed this view. See *In re Mediscan Research*, 109 B.R. 392, 394-95 (B.A.P. 9th Cir. 1989), *aff'd*, 940 F.2d 558 (9th Cir. 1991); *Motown Record Corp. v. Brockert*, 207 Cal. Rptr. 574, 581 (Ct. App. 1984).

⁸⁴ See, e.g., ELIZABETH A. SMITH ET AL., CALIFORNIA CIVIL PRACTICE REAL PROPERTY LITIGATION § 1:5 (2008) (declaring consideration a central element of real property contracts and listing no exceptions).

⁸⁵ *Sosnoff v. Carter*, 568 N.Y.S.2d 43, 46 (App. Div. 1991); *Boglioli v. Advantage Diagnostics Inc.*, No. 06-019637, 2007 WL 4686228, at *3 (N.Y. Sup. Ct. Dec. 27, 2007); *Kurtz v. Lelchuk*, No. 7585-04, 2006 WL 1982598, at *7 (N.Y. Sup. Ct. July 10, 2006).

⁸⁶ *805 Third Ave. Co. v. M.W. Realty Assocs.*, 448 N.E.2d 445, 447 (N.Y. 1983); *Austin Instrument Inc. v. Loral Corp.*, 272 N.E.2d 533, 535 (N.Y. 1971).

⁸⁷ See *Morad v. Morad*, 812 N.Y.S.2d 126, 128 (App. Div. 2006); *accord Beutel v. Beutel*,

has available means for response.⁸⁸ The threat, moreover, must be intrinsically wrongful⁸⁹: A contract is not subject to challenge if the threatened action is something that the alleged wrongdoer was legally entitled to do.⁹⁰ Even if an agreement is procured by duress, moreover, the victim must act promptly to repudiate it or suffer an inference of ratification.⁹¹

California also recognizes a defense of duress.⁹² As in New York, the threat must be wrongful. Thus, a good faith threat to exercise legal rights is not duress in California even if the party is mistaken about his entitlements.⁹³ Also, as in New York, the party must do more than merely inflict economic⁹⁴ or social pressure.⁹⁵ But in several respects California is more receptive than New York to claims of duress. It does not require loss of free will; a threat that is “sufficiently coercive to cause a reasonably prudent person, faced with no reasonable alternative, to agree to an unfavorable contract” suffices.⁹⁶ California, moreover, recognizes certain duress-like defenses not found in New York.⁹⁷ A contract may be invalidated if procured by “menace,” including threats of violence or injury to reputation.⁹⁸ Also available as a ground for

434 N.E.2d 249, 250 (N.Y. 1982) (mem.).

⁸⁸ See *Austin Instrument*, 272 N.E.2d at 535; *Finserv Computer Corp. v. Bibliographic Retrieval Servs., Inc.*, 509 N.Y.S.2d 187, 189 (App. Div. 1986).

⁸⁹ See *Stewart M. Muller Constr. Co. v. N.Y. Tel. Co.*, 359 N.E.2d 328 (N.Y. 1976) (mem.). For example, a party acts wrongfully by threatening to withhold performance of clear contractual obligation. See, e.g., *Friends Lumber Inc. v. Cornell Dev. Corp.*, 663 N.Y.S.2d 327, 329 (App. Div. 1997); *Sosnoff*, 568 N.Y.S.2d at 46 (App. Div. 1991).

⁹⁰ See *Marine Midland Bank v. Hallman's Budget Rent-a-Car of Rochester, Inc.*, 613 N.Y.S.2d 92, 92-93 (App. Div. 1994) (holding that pursuit of a legal right does not constitute economic duress); *Philips S. Beach LLC v. ZC Specialty Ins. Co.*, No. 103021/07, 2007 WL 2915600, at *2 (N.Y. Sup. Ct. Oct. 3, 2007).

⁹¹ E.g., *Cosh v. Cosh*, 847 N.Y.S.2d 136, 138 (App. Div. 2007); *Stoerchle v. Stoerchle*, 475 N.Y.S.2d 489, 490-91 (App. Div. 1984) (mem.); *Wachovia Sec., LLC v. Joseph*, No. 104326/06, 2007 WL 419366, at *5 (N.Y. Sup. Ct. Feb. 7, 2007). Arguments that it is unfair to force a victim to elect promptly between accepting the benefit of a contract procured through duress, however inadequate, or incurring the risk and expense of challenging the conditions under which the contract was made fail to sway New York courts. See *EEOC v. Am. Express Pub. Corp.*, 681 F. Supp. 216, 219 (S.D.N.Y. 1988) (“[T]he fact that a party faces a difficult choice—between additional benefits or pursuing his [or her] legal rights—does not alone indicate lack of free will.”).

⁹² See CAL. CIV. CODE § 1567 (West 2008).

⁹³ See *River Bank Am. v. Diller*, 45 Cal. Rptr. 2d 790, 804 (Ct. App. 1995); *London Homes, Inc. v. Korn*, 44 Cal. Rptr. 262, 266 (Ct. App. 1965) (holding party did not impose duress when it asserted an erroneous claim of contract rights).

⁹⁴ See, e.g., *Doherty v. Regev*, No. BC220282, 2002 WL 1904435, at *1, *9 (Cal. Ct. App. Aug. 20, 2002) (failing to find duress even though party testified that his company's financial troubles led him to believe he had no other choice than to execute the instrument).

⁹⁵ So, for example, the threat to publish politically embarrassing information may not be sufficient. See *Philippine Exp. & Foreign Loan Guar. Corp. v. Chuidian*, 267 Cal. Rptr. 457, 466-68 (Ct. App. 1990).

⁹⁶ *CrossTalk Prods., Inc. v. Jacobson*, 76 Cal. Rptr. 2d 615, 623 (Ct. App. 1998).

⁹⁷ See CAL. CIV. CODE § 1567 (West 2008).

⁹⁸ *Id.* § 1570.

upsetting a contract is “undue influence”—“taking an unfair advantage of another’s weakness of mind; or . . . taking a grossly oppressive and unfair advantage of another’s necessities or distress.”⁹⁹ Menace or undue influence are unlikely to be grounds for avoiding many business contracts; but, together with the state’s softer requirements for duress, they represent a wild-card in California jurisprudence that parties may seek to use in order to avoid performing on losing deals.

B. *Unconscionability*

Both New York and California refuse to enforce contract terms deemed to be unconscionable,¹⁰⁰ and they do so on similar grounds.¹⁰¹ There are, however, significant differences of nuance and application—differences that reduce certainty of contract enforcement in California as compared with New York.

New York’s standards for unconscionability are demanding. A determination of unconscionability generally requires a showing that the transaction was both procedurally and substantively unconscionable when made.¹⁰² For a contract to be deemed procedurally unconscionable, a court must find that the complaining party was deprived of “meaningful choice.”¹⁰³ This means more than mere inequality of bargaining power or that the contract term was offered on a “take it or leave it” basis.¹⁰⁴ The complaining party must establish a

⁹⁹ *Id.* § 1575.

¹⁰⁰ New York’s law on unconscionability is largely judge-made. *See, e.g.*, *Gillman v. Chase Manhattan Bank*, 534 N.E.2d 824, 828 (N.Y. 1988). California’s approach is embodied in a statute. CAL. CIV. CODE § 1670.5(a) (West 2008) (“If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.”).

¹⁰¹ The similarity is not accidental. Both state’s unconscionability doctrines are outgrowths of the Uniform Commercial Code’s unconscionability rule. *See* CAL. CIV. CODE § 1670.5 (enacting U.C.C. § 2-302 (1962)); *Gillman*, 534 N.E.2d at 828 (citing § 2-302).

¹⁰² *Gilman*, 534 N.E.2d at 828; *Rosiny v. Schmidt*, 587 N.Y.S.2d 929, 930 (App. Div. 1992); *Wachovia Sec., LLC v. Joseph*, No. 104326/06, 2007 WL 419366, at *2 (N.Y. Sup. Ct. Feb. 7, 2007). In “extreme” or “exceptional” cases, New York may dispense with the requirement of procedural unconscionability. *Gillman*, 534 N.E.2d at 829 (“[T]here have been exceptional cases where a provision of the contract is so outrageous as to warrant holding it unenforceable on the ground of substantive unconscionability alone.”); *State v. Wolowitz*, 468 N.Y.S.2d 131, 145 (App. Div. 1983) (“While there may be extreme cases where a contractual term is so outrageous and oppressive as to warrant a finding of unconscionability irrespective of the contract formation process, such cases are the exception.” (citation omitted)).

¹⁰³ *See* *State v. Avco Fin. Serv. of N.Y. Inc.*, 406 N.E.2d 1075, 1078 (N.Y. 1980) (“[A]n absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party.” (quoting *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445, 449 (D.C. Cir. 1965))).

¹⁰⁴ *See, e.g.*, *Ranieri v. Bell Atl. Mobile*, 759 N.Y.S.2d 448, 449 (App. Div. 2003) (“Inequality

lack of fundamental fairness in the contracting process, evidenced by a combination of factors such as: marked differences in sophistication;¹⁰⁵ “gross inequality” of bargaining power;¹⁰⁶ “fine print” clauses hidden in a written contract;¹⁰⁷ the vulnerability of the party seeking relief from the contract;¹⁰⁸ or “high pressure” sales practices.¹⁰⁹ New York is even stricter when it comes to substantive unconscionability. The complaining party must show that the terms are “grossly unreasonable,”¹¹⁰ “unjust,” “oppressive,”¹¹¹ or so deleterious that “no man in his senses and not under delusion” would agree to them.¹¹² Even terms that appear objectively unfair can pass muster under New York’s approach: In one case the court found no unconscionability in a retainer agreement that awarded a law firm \$40 million for five months’ work following years of litigation that was fully compensated on an hourly basis.¹¹³ Given the stringency of New York’s unconscionability rule, New York decisions recognize that the doctrine of unconscionability has little or no application to commercial contracts between business entities or sophisticated parties.¹¹⁴

of bargaining power alone does not invalidate a contract as one of adhesion when the purchase can be made elsewhere.” (citation omitted)); *Brower v. Gateway 2000, Inc.*, 676 N.Y.S.2d 569, 573 (App. Div. 1998) (failing to find a take it or leave it contract procedurally unconscionable); *Gelbman v. ValleyCrest Prod.*, 732 N.Y.S.2d 528, 533 (Sup. Ct. 2001).

¹⁰⁵ See *Scotts Co., LLC v. Ace Indem. Ins. Co.*, 858 N.Y.S.2d 121, 122 (App. Div. 2008); *Suffolk Laundry Servs., Inc. v. Redux Corp.*, 656 N.Y.S.2d 372, 374 (App. Div. 1997) (mem.); *Day Op of N. Nassau, Inc. v. Viola*, No. 005018/2007, 2007 WL 2305035, at *6 (N.Y. Sup. Ct. Aug. 1, 2007).

¹⁰⁶ *Blake v. Biscardi*, 403 N.Y.S.2d 544, 547 (App. Div. 1978).

¹⁰⁷ See *Gillman*, 534 N.E.2d at 828-29.

¹⁰⁸ See *Harrington v. Atl. Sounding Co.*, No. 06-CV-2900, 2007 WL 2693529, at *4 (E.D.N.Y. Sept. 11, 2007). The New York legislature has enacted special legislation designed to protect sellers of structured settlements on the theory that these individuals may be particularly vulnerable to sharp practices. See *Settlement Funding of N.Y., LLC v. Solivan*, No. 2708/05, 2005 WL 1498217, at *2, *3 (N.Y. Sup. Ct. June 23, 2005) (citing N.Y. GEN. OBLIG. LAW § 5-1076(b) (McKinney 2008)).

¹⁰⁹ *Gillman*, 534 N.E.2d at 828; *In re Estate of Friedman*, 407 N.Y.S.2d 999, 1008 (App. Div. 1978).

¹¹⁰ *Gillman*, 534 N.E.2d at 828.

¹¹¹ *Day Op of N. Nassau, Inc. v. Viola*, No. 005018/2007, 2007 WL 2305035, at *7 (N.Y. Sup. Ct. Aug. 1, 2007).

¹¹² *Avildsen v. Prystay*, 574 N.Y.S.2d 535, 535 (App. Div. 1991), *appeal dismissed*, 588 N.E.2d 91 (N.Y. 1991).

¹¹³ See, e.g., *Lawrence v. Miller*, 853 N.Y.S.2d 1, 12-15 (App. Div. 2007).

¹¹⁴ See *Reznor v. J. Artist Mgmt., Inc.*, 365 F. Supp. 2d 565, 577 (S.D.N.Y. 2005) (“[C]ourts ‘have rarely found a clause to be unconscionable’ in contracts involving two commercial entities, a situation in which negotiation is presumed possible.” (quoting *Am. Dredging Co. v. Plaza Petroleum, Inc.*, 799 F. Supp. 1335 (E.D.N.Y. 1992))); *Chateaugay Corp. v. N. States Contracting Co.*, 162 B.R. 949, 960 (Bankr. S.D.N.Y. 1994) (“It is extremely rare for a court to find an unconscionable limitation on consequential damages in a contract between experienced businessmen arising in a commercial setting.”); *Oppenheimer & Co. v. Oppenheim, Appel, Dixon & Co.*, 660 N.E.2d 415, 421 (N.Y. 1995) (presuming unconscionability inapplicable to commercial transactions among sophisticated business entities absent countervailing public policy concerns); *Gillman*, 521 N.Y.S.2d at 732 (App. Div. 1987) (“[T]he doctrine of

California also requires a showing of both procedural and substantive unconscionability.¹¹⁵ Yet California courts interpret the requirements differently than do New York's. As to procedural unconscionability, California cases sometimes indicate that "no-bargaining" contracts of adhesion are a prerequisite;¹¹⁶ but in practice the courts employ the doctrine in contexts where bargaining appears to have been possible¹¹⁷ as well as in cases of unilateral mistake.¹¹⁸ As to substantive unconscionability, California decisions suggest that the level of unfairness necessary to invalidate a contract term need not be extreme or outrageous; it is enough if the terms are "overly harsh."¹¹⁹ Unlike New York, California courts find substantive unconscionability in contracts that are one-sided, whether or not they are overly harsh.¹²⁰ Also unlike New York, California does not limit the doctrine of unconscionability to contracts between consumers and businesses;¹²¹ any party, even a sophisticated business entity,¹²² can obtain relief,¹²³

unconscionability has little applicability in the commercial setting because it is presumed that businessmen deal at arm's length with relative equality of bargaining power. Apparently the doctrine is primarily a means with which to protect the "commercially illiterate consumer beguiled into a grossly unfair bargain by a deceptive vendor or finance company." (citations omitted) (quoting *Equitable Lumber Corp. v. I.P.A. Dev. Corp.*, 344 N.E.2d 391, 396 (N.Y. 1976)), *aff'd*, 534 N.E.2d 824 (N.Y. 1988); *Chrysler Credit Corp. v. Kosal*, 518 N.Y.S.2d 162, 164 (App. Div. 1987) (mem.) (presuming unconscionability inapplicable to commercial transactions among sophisticated business entities); *Scotts Co., LLC v. Ace Indem. Ins. Co.*, No. 602712/05, 2007 WL 4954442, at *3 (N.Y. Sup. Ct. Feb. 28, 2007), *aff'd*, 858 N.Y.S.2d 121 (App. Div. 2008) (same).

¹¹⁵ *Armendariz v. Found. Health Psychcare Servs., Inc.*, 6 P.3d 669, 690 (Cal. 2000).

¹¹⁶ *See id.* at 689 ("Unconscionability analysis begins with an inquiry into whether the contract is one of adhesion.")

¹¹⁷ *See Estate of Dito v. Dito*, No. A116815, 2008 WL 821694, at *13 (Cal. Ct. App. Mar. 28, 2008); *Greenbear Techs., Inc. v. ABC Rentals, Inc.*, No. B192041, 2007 WL 3173291, at *1, *5 (Cal. Ct. App. Oct. 31, 2007).

¹¹⁸ *See, e.g., Donovan v. RRL Corp.*, 27 P.3d 702, 723-24 (Cal. 2001) (relieving car dealership of consequences of error in advertised price term); *M. F. Kemper Constr. Co. v. City of L.A.*, 235 P.2d 7, 11 (Cal. 1951) (relieving contractor of consequences of mistaken bid).

¹¹⁹ *Little v. Auto Stiegler, Inc.*, 63 P.3d 979, 983 (Cal. 2003); *Armendariz*, 6 P.3d at 690.

¹²⁰ *See id.* at 772 (rejecting as unconscionable a clause requiring mandatory arbitration of an employee's claims against an employer but not an employer's claims against an employee); *Beynon v. Garden Grove Med. Group*, 161 Cal. Rptr. 146, 150 (Ct. App. 1980) (rejecting a clause entitling physician, but not patient, to obtain a second arbitration). California courts even reject facially neutral clauses found to be overly one-sided in practice. *Compare Little*, 63 P.3d at 983-85 (rejecting a clause that allowed either party to appeal an arbitration award of more than \$50,000), *with Reznor v. J. Artist Mgmt., Inc.*, 365 F. Supp. 2d 565, 577 (S.D.N.Y. 2005) (rejecting substantive unconscionability claim where no disparity in bargaining power between artist and manager), *and Rowe v. Great Atl. & Pac. Tea Co.*, 385 N.E.2d 566, 569 (N.Y. 1978) (finding no unconscionability in assignment of supermarket lease), *and Christian v. Christian*, 365 N.E.2d 849, 855 (N.Y. 1977) (finding no cause for court interference in separation agreement made with full disclosure), *and O'Lear v. O'Lear*, 652 N.Y.S.2d 1008 (App. Div. 1997) (same).

¹²¹ *See Hary G. Prince, Unconscionability in California: A Need for Restraint and Consistency*, 46 HASTINGS L.J. 459, 500-01 (1995) (arguing that "California courts have been unduly indulgent of merchant-like parties claiming unconscionability" and referring to the state's jurisprudence on this point as "notorious").

¹²² *See Nagrampa v. MailCoups, Inc.*, 469 F.3d 1257, 1283 (9th Cir. 2006) ("[S]ophistication

especially if the substantive terms complained of are onerous.¹²⁴

These differences are not merely theoretical. California and New York courts have reached widely different results in challenges to arbitration clauses and class action waivers—matters discussed *infra*.¹²⁵ The differences between the states are also manifested in ordinary commercial disputes. In *A & M Produce Co. v. FMC Corp.*,¹²⁶ a California case, a farming company challenged the enforceability of disclaimers of warranty and consequential damages in a sales contract with an agricultural equipment manufacturer.¹²⁷ Even though the buyer was a commercial entity that had alternate sellers available and ample opportunity to read the conspicuous disclaimers, the court held that the terms were unconscionable: “[E]xperienced but legally unsophisticated businessmen may be unfairly surprised by unconscionable contract terms, and . . . even large business entities may have *relatively* little bargaining power”¹²⁸ *Cayuga Harvester, Inc. v. Allis-Chalmers Corp.*,¹²⁹ a New York case, involved a similar challenge to a clause excluding consequential damages in the sale of agricultural equipment.¹³⁰ Here the outcome was different. Noting that the contract was “unquestionably commercial” and that alternative sellers were available, the court denied the unconscionability claim and held the buyer to the consequence of its bargain.¹³¹

A similar contrast can be found in two cases from the entertainment industry. In *Graham v. Scissor-Tail, Inc.*,¹³² the complaining party was a prominent music promoter who had signed numerous contracts of the same type and was aware of their provisions; still, a California court found the contract clause unconscionable.¹³³ In *Reznor v. J. Artist Management, Inc.*,¹³⁴ a New York court refused to invalidate a contract between a struggling rock musician and his longtime manager. Even though the musician arguably had much less

of a party, alone, cannot defeat a procedural unconscionability claim.”)

¹²³ See, e.g., *Donovan*, 27 P.3d at 724 (auto dealer); *Graham v. Scissor-Tail, Inc.*, 623 P.2d 165, 178 (Cal. 1981) (music promoter and producer); *M. F. Kemper Constr., Co.*, 235 P.2d at 11 (contractor); *A & M Produce Co. v. FMC Corp.*, 186 Cal. Rptr. 114, 122-26 (Ct. App. 1982) (small business).

¹²⁴ Cf. *Woodside Homes of Cal., Inc. v. Superior Court*, 132 Cal. Rptr. 2d 35, 39 (Ct. App. 2003) (noting that necessary showing of procedural unconscionability diminishes if contract is significantly unfair as a matter of substance).

¹²⁵ See *infra* Parts VII.C-VII.D.

¹²⁶ 186 Cal. Rptr. 114 (Ct. App. 1982).

¹²⁷ *Id.* at 117-18.

¹²⁸ *Id.* at 124 (citations omitted). For a critique, see Prince, *supra* note 121, at 513-24.

¹²⁹ 465 N.Y.S.2d 606 (App. Div. 1983).

¹³⁰ *Id.* at 609, 616.

¹³¹ *Id.* at 617-18.

¹³² 623 P.2d 165 (Cal. 1981).

¹³³ See Prince, *supra* note 121, at 506-07.

¹³⁴ 365 F. Supp. 2d 565 (S.D.N.Y. 2005).

bargaining power than the promoter in the California case,¹³⁵ the court held that, as a participant in a commercial venture, he had the power to negotiate over the terms.¹³⁶

C. Public Policy

Both New York and California refuse to enforce contracts that are deemed to violate public policy. Again, however, important differences underlie the surface similarity. I first examine general public policy questions and then turn to the specific issues of exculpatory clauses, covenants not to compete, and wrongful discharge claims. Reserved for later is the treatment of arbitration clauses and class action waivers.¹³⁷

1. In General

New York only rarely trumps private agreements on public policy grounds. In part, New York bases its resistance to public policy arguments on the state's commitment to freedom of contract,¹³⁸ which is inevitably frustrated when public policy is the basis for denying enforcement. In addition, New York courts display an understandable suspicion of litigants who seek to avoid complying with their promises on the ground that keeping their word would impair public rights¹³⁹: “[E]fforts to use [public policy] as a sword for personal gain rather than a shield for the public good should not be countenanced”¹⁴⁰

New York cases in which public policy trumps private agreement tend to involve specific statutory norms: laws against gambling,¹⁴¹ usury,¹⁴² insurance contracts benefiting parties without an insurable

¹³⁵ Although he subsequently became a major star as lead singer in the band Nine Inch Nails, the plaintiff (Michael Trent Reznor) was a struggling artist when he signed the contract. *Id.* at 568-69.

¹³⁶ *See id.* at 577 (“[C]ourts have rarely found a clause to be unconscionable in contracts involving two commercial entities, a situation in which negotiation is presumed possible.”).

¹³⁷ *See infra* Parts VII.C-VII.D.

¹³⁸ *See supra* notes 14-19 and accompanying text.

¹³⁹ *See Miller v. Cont'l Ins. Co.*, 358 N.E.2d 258 (N.Y. 1976) (“[T]he right of private contract is no small part of the liberty of the citizen, and the usual and most important function of courts of justice is rather to maintain and enforce contracts than to enable parties thereto to escape from their obligation on the pretext of public policy, unless it clearly appears that they contravene public right or the public welfare.” (quoting *Balt. & Ohio Ry. Co. v. Voight*, 176 U.S. 498 (1900))).

¹⁴⁰ *Charlebois v. J.M. Weller Assocs.*, 531 N.E.2d 1288, 1292 (N.Y. 1988).

¹⁴¹ *See* N.Y. GEN. OBLIG. LAW §§ 5-401, 5-411, 5-413, 5-415, 5-417, 5-419, 5-421, 5-423 (McKinney 2008).

¹⁴² *See id.* § 5-511.

interest,¹⁴³ contracts for the unauthorized practice of law,¹⁴⁴ contracts based on bribery,¹⁴⁵ and illegal agreements to split professional fees.¹⁴⁶ Where a statutory norm is absent, the public policy sword usually serves traditional moral values: New York courts, for example, will not enforce contracts for sex¹⁴⁷ or promises to divorce.¹⁴⁸ New York generally turns a deaf ear to broader policies such as protecting consumers,¹⁴⁹ ensuring racial sensitivity,¹⁵⁰ or guarding against “forfeitures.”¹⁵¹ Only occasionally do New York judges use public policy as a more general equitable tool for protecting the interests of vulnerable parties,¹⁵² and in such cases they apply the relevant policies sparingly.¹⁵³

¹⁴³ See N.Y. INS. LAW § 3205(b)(2) (McKinney 2008) (insurable interest required for life insurance policies).

¹⁴⁴ See *Spivak v. Sachs*, 211 N.E.2d 329, 330-31 (N.Y. 1965).

¹⁴⁵ See *McConnell v. Commonwealth Pictures Corp.*, 166 N.E.2d 494, 496-97 (N.Y. 1960).

¹⁴⁶ See *Ungar v. Matarazzo Blumberg & Assocs., P.C.*, 688 N.Y.S.2d 588, 589-90 (App. Div. 1999) (legal fees); *LoMugno v. Koh*, 667 N.Y.S.2d 280 (App. Div. 1998) (medical fees); *United Calendar Mfg. Corp. v. Huang*, 463 N.Y.S.2d 497, 500 (App. Div. 1983) (medical fees).

¹⁴⁷ See *Anonymous v. Anonymous*, 740 N.Y.S.2d 341 (App. Div. 2002); *Rose v. Elias*, 576 N.Y.S.2d 257 (App. Div. 1991) (mem.); *Kastil v. Carro*, 536 N.Y.S.2d 63 (App. Div. 1988) (mem.), *appeal dismissed*, 540 N.E.2d 714 (N.Y. 1989) (mem.).

¹⁴⁸ See *McCall v. Frampton*, 438 N.Y.S.2d 11, 13 (App. Div. 1981) (mem.).

¹⁴⁹ See, e.g., *Slayko v. Sec. Mut. Ins. Co.*, 774 N.E.2d 208, 213 (N.Y. 2002) (holding that New York public policy does not require insurance companies to provide coverage for risks that policyholders would reasonably expect to be included).

¹⁵⁰ See *N.Y. State Corr. Officers & Police Benevolent Ass’n, Inc. v. State*, 726 N.E.2d 462, 464, 467 (N.Y. 1999) (refusing to upset arbitration award reinstating police officer who displayed Nazi flag outside his home on Hitler’s birthday).

¹⁵¹ The equitable distaste for forfeitures can be employed to deny enforcement of contract terms that deprive parties of substantial rights due to technical violations. See *infra* note 167 and accompanying text. New York has occasionally employed the equitable hostility to forfeitures for this purpose. See, e.g., *J.N.A. Realty Corp. v. Cross Bay Chelsea, Inc.*, 366 N.E.2d 1313, 1316 (N.Y. 1977). But the trend of recent New York cases has been to enforce forfeitures in the absence of some other grounds for invalidity, such as unconscionability. See *Fifty States Mgmt. Corp. v. Pioneer Auto Parks, Inc.*, 389 N.E.2d 113 (N.Y. 1979) (approving provision under which tenant forfeited possessory rights upon failing to tender rent payments for two months); *id.* at 115 (“As . . . there is no claim of fraud or exploitive overreaching on the part of the plaintiff in compelling performance of its bargained-for right, the agreement of the parties must be enforced in accordance with its terms.”). Ironically, the distaste of forfeitures has been converted, in some New York cases, into a reason for not using public policy reasons to deprive parties of contractual rights. See *Lloyd Capital Corp. v. Pat Henchar, Inc.*, 603 N.E.2d 246, 248 (N.Y. 1992) (rejecting public policy claim, in part, on the ground that “forfeitures by operation of law are disfavored”).

¹⁵² New York will not enforce clauses that impose on a subcontractor the risk of nonpayment or delay in payment to the general contractor. *West-Fair Elec. Contractors v. Aetna Cas. & Sur. Co.*, 661 N.E.2d 967, 971 (N.Y. 1995), *enforced*, 78 F.3d 61 (2d Cir. 1996). *But cf.* *Welsbach Elec. Corp. v. MasTec N. Am., Inc.*, 859 N.E.2d 498, 501-03 (N.Y. 2006) (holding that policy against “pay-if-paid” construction contracts was not fundamental enough to override parties’ choice of Florida law, even though Florida did not enforce such a policy). Another example of New York’s use of public policy to accomplish general social objectives is the rule against automobile lease clauses denying coverage for accidents involving unlicensed drivers of the insured’s vehicle in situations where the insured had no reason to believe that the driver was unlicensed. See *Conte v. Aprea*, 803 N.Y.S.2d 557, 558 (App. Div. 2005).

¹⁵³ Thus, the mere fact that a contract or its consideration violates state law is not, in itself,

California courts enforce many of the same policies as those recognized under New York law, including norms against wagering contracts,¹⁵⁴ contracts for sex,¹⁵⁵ and fee-splitting agreements among attorneys.¹⁵⁶ Also as in New York, specific statutes in California establish overriding policies: prohibiting harassment and discrimination in employment;¹⁵⁷ protecting clients of dating services;¹⁵⁸ prohibiting deficiency judgments in purchase-money mortgages;¹⁵⁹ and indemnifying employees for expenditures necessarily incurred within the scope of employment,¹⁶⁰ for example. Unlike New York, however, California recognizes very broad authority to reject contracts on grounds of general unfairness. Consideration for a contract is illegal if it is “contrary to good morals.”¹⁶¹ California courts have the power to reject contracts that tend to “undermine that sense of security for individual rights, whether of personal liberty or private property, which any citizen ought to feel.”¹⁶² And because public values are implicated, California looks with disfavor at attempts to waive these norms.¹⁶³

enough to invalidate its enforcement. If the violation is merely technical, the contract may be enforced notwithstanding the illegality. *See* *Denburg v. Parker Chapin Flattau & Klimpl*, 624 N.E.2d 995, 1001 (N.Y. 1993); *Lloyd Capital*, 603 N.E.2d at 247 (“If the statute does not provide expressly that its violation will deprive the parties of their right to sue on the contract, and the denial of relief is wholly out of proportion to the requirements of public policy . . . the right to recover will not be denied.” (quoting *John E. Rosasco Creameries Inc. v. Cohen*, 11 N.E.2d 908, 909 (N.Y. 1937))); *Wowaka & Sons, Inc. v. Pardell*, 672 N.Y.S.2d 358, 360 (App. Div. 1998); *cf.* *Abramovitz v. Kew Realty Equities, Inc.*, 580 N.Y.S.2d 269, (App. Div. 1992) (mem.) (applying equitable principles to permit recovery on criminally usurious loan). Contracts among co-habiting partners are enforceable, even if the couple is sexually intimate, so long as the sex is not the consideration for the contract. *Morone v. Morone*, 413 N.E.2d 1154, 1156 (N.Y. 1980). Contracts that violate the rule against procuring an insurance policy without an insurable interest will be enforced after the statutory contestability period expires. *New Eng. Mut. Life Ins. Co. v. Caruso*, 535 N.E.2d 270, 271, 273 (N.Y. 1989).

¹⁵⁴ *See, e.g., Kelly v. First Astri Corp.*, 84 Cal. Rptr. 2d 810, 819, 827-28 (Ct. App. 1999).

¹⁵⁵ California, however, is somewhat more willing to enforce contracts among co-habiting parties. *See Marvin v. Marvin*, 557 P.2d 106, 112 (Cal. 1976).

¹⁵⁶ *See Chambers v. Kay*, 106 Cal. Rptr. 2d 702, 714-15 (Ct. App. 2001), *aff'd*, 56 P.3d 645 (Cal. 2002).

¹⁵⁷ *See* CAL. GOV'T. CODE § 12940 (West 2008).

¹⁵⁸ *See Duffens v. Valenti*, 74 Cal. Rptr. 3d 311, 325-26 (Ct. App. 2008).

¹⁵⁹ CAL. CIV. PROC. CODE § 580b (West 2008).

¹⁶⁰ CAL. LAB. CODE § 2802 (West 2008).

¹⁶¹ CAL. CIV. CODE § 1667 (West 2008).

¹⁶² *Moran v. Harris*, 182 Cal. Rptr. 519, 522 (Ct. App. 1982) (quoting *Noble v. City of Palo Alto*, 264 P. 529, 531 (Cal. Ct. App. 1928)).

¹⁶³ *See* CAL. CIV. CODE § 3513 (“Anyone may waive the advantage of a law intended solely for his benefit. But a law established for a public reason cannot be contravened by a private agreement.”); *County of Riverside v. Superior Court*, 42 P.3d 1034, 1042-43 (Cal. 2002) (holding that statutory labor rights of peace officers are generally not waivable); *DeBerard Props., Ltd. v. Lim*, 976 P.2d 843, 849 (Cal. 1999) (holding that a party may waive a statutory provision only if the statute does not prohibit doing so, the statute’s public benefit is merely incidental to its main purpose, and waiver does not seriously compromise any public purpose fostered by the statute); *Edwards v. Arthur Andersen LLP*, 47 Cal. Rptr. 3d 788, 792 (Ct. App. 2006) (declining to permit waivers of employer indemnity for necessary expenses), *cert. granted*, 147 P.3d 1013 (Cal.

Recognition of the risks associated with such an ill-defined power mitigates the breadth of California's public policy rule. Thus, we find admonitions that "it is exactly because of this subjective, amorphous definition [of the public good] and the variations in human response to the same facts, depending upon the philosophical or psychological perceptions of those involved, that courts have been cautious in blithely applying public policy reasons to nullify otherwise enforceable contracts."¹⁶⁴ California courts also limit the impact of public policy by exercising equitable authority to accomplish effective justice when a contract provision is found to be illegal on public policy grounds.¹⁶⁵ They may award a remedy when serious moral turpitude is not involved, the defendant is more at fault and would be unjustly enriched if the contract is invalidated, and the public interest would not be compromised by enforcement.¹⁶⁶ Nevertheless, the breadth of the public policy doctrine impairs the certainty and predictability of contractual enforcement in California relative to that which obtains in New York.

2. Exculpatory Clauses

New York and California both recognize the ability of parties to limit their liability by contract. But New York is more permissive in important respects. California law thus creates greater uncertainty in the enforcement of private agreements limiting liability.

Subject to the general rules on unconscionability and good faith, parties under New York law enjoy broad authority to distribute the risks and rewards of their undertakings. New York courts almost never employ their equitable power to prevent "forfeitures" as a tool for reforming private bargains that turn out poorly for one party. Nor do New York courts reform bargains that result in onerous outcomes because a party has failed to comply with some condition or requirement.¹⁶⁷ Accordingly, parties may, within limits, agree to clauses exculpating liability due to fault. New York does not recognize waivers of liability for gross negligence or intentional misconduct,¹⁶⁸

2006); *Covino v. Governing Bd.*, 142 Cal. Rptr. 812, 817 (Ct. App. 1977) (holding teacher's right to probationary status unwaivable).

¹⁶⁴ *Moran*, 182 Cal. Rptr. at 522.

¹⁶⁵ See *Cho v. Chi*, No. D038607, 2002 WL 454302, at *6-7 (Cal. Ct. App. Mar. 26, 2002); *Dunkin v. Boskey*, 98 Cal. Rptr. 2d 44, 61-62 (Ct. App. 2000); *Arya Group, Inc. v. Cher*, 91 Cal. Rptr. 2d 815, 819-21 (Ct. App. 2000).

¹⁶⁶ See *Tri-Q, Inc. v. Sta-Hi Corp.*, 404 P.2d 486, 497-98 (Cal. 1965); *Kelton v. Stravinski*, 41 Cal. Rptr. 3d 877, 883 (Ct. App. 2006).

¹⁶⁷ See *supra* note 151 and accompanying text.

¹⁶⁸ *Sommer v. Fed. Signal Corp.*, 593 N.E.2d 1365, 1370-71 (N.Y. 1992); *Kalisch-Jarcho, Inc. v. City of N.Y.*, 448 N.E.2d 413, 416-17 (N.Y. 1983); *Rector v. Calamus Group, Inc.*, 794

but it does enforce clearly articulated waivers of liability for simple negligence among parties not in a fiduciary relationship. Parties may also place ceilings on damages¹⁶⁹ or preclude damages altogether.¹⁷⁰ Exceptions to this permissive regime are specific and usually based on statute.¹⁷¹ New York—generally receptive to settlements of disputes—will enforce releases of claims absent a strong showing of fraud, illegality, duress, or mutual mistake.¹⁷²

California law allows parties to waive or limit legal rights by contract, but it imposes greater obstacles in the path of doing so. As in New York, California does not allow waivers of gross negligence or intentional misconduct.¹⁷³ But, more than New York, California also disfavors clauses that waive liability for simple negligence. California courts strictly construe such clauses because of the “harsh results” that they impose.¹⁷⁴ Liability for “active negligence” is not waived absent clear and specific language.¹⁷⁵ Even if a clause covers simple negligence, moreover, it may be challenged in situations extending beyond those recognized in New York. *Tunkl v. Regents of the*

N.Y.S.2d 470, 471 (App. Div. 2005); *Peluso v. Tauscher Cronacher Prof'l Eng'rs, P.C.*, 704 N.Y.S.2d 289, 291 (App. Div. 2000).

¹⁶⁹ *Alleyne v. Four Seasons Hotel*, No. 99 CIV. 3432, 2001 WL 135770, at *17 (S.D.N.Y. Feb. 15, 2001), *aff'd*, No. 01-7347, 2002 WL 109353 (2d Cir. Jan. 23, 2002); *Schietinger v. Tauscher Cronacher Prof'l Eng'rs, P.C.*, 838 N.Y.S.2d 95, 96 (App. Div. 2007).

¹⁷⁰ Thus in commercial leases, it is permissible under New York law to limit the tenant's remedies for bad faith withholding of consent to actions for declaratory or equitable relief. *Gladlitz, Inc. v. Castiron Court Corp.*, 677 N.Y.S.2d 662, 666 (Sup. Ct. 1998).

¹⁷¹ Thus, New York invalidates clauses waiving negligence liability for landlords, N.Y. GEN. OBLIG. LAW § 5-321 (McKinney 2008), caterers and catering establishments, *id.* § 5-322, construction or demolition contractors, *id.* § 5-322.1, building service or maintenance contractors, *id.* § 5-323, pools, gyms, and places of recreation, *id.* § 5-326, and agreements to indemnify architects and other professionals for defects in maps, designs, plans and specifications, *id.* § 5-324.

¹⁷² *See, e.g., Mitchell v. N.Y. Hosp.*, 461 N.E.2d 285, 288 (N.Y. 1984); *Young v. Williams*, 850 N.Y.S.2d 262, 264 (App. Div. 2008); *Scotts Co. v. Ace Indem. Ins. Co.*, No. 602712/05, 2008 WL 518062, at *4 (N.Y. Sup. Ct. Feb. 26, 2008).

¹⁷³ *See* CAL. CIV. CODE § 1668 (West 2008) (“All contracts which have for their object, directly or indirectly, to exempt any one from responsibility for his own fraud, or willful injury to the person or property of another, or violation of law, whether willful or negligent, are against the policy of the law.”); *City of Santa Barbara v. Superior Court*, 161 P.3d 1095, 1115 (Cal. 2007) (invalidating agreement disclaiming liability for “even a *minimal* standard of care”); *Neubauer v. Goldfarb*, 133 Cal. Rptr. 2d 218, 224-25 (Ct. App. 2003); *Cohen v. Kite Hill Cmty. Ass'n*, 191 Cal. Rptr. 209, 216 (Ct. App. 1983).

¹⁷⁴ *See, e.g., Westlye v. Look Sports, Inc.*, 22 Cal. Rptr. 2d 781, 788 (Ct. App. 1993) (noting that liability-limiting agreements are strictly construed because of “harsh results”); *Ferrell v. S. Nev. Off-Road Enthusiasts, Ltd.*, 195 Cal. Rptr. 90, 95 (Ct. App. 1983) (requiring release of negligence liability to be “clear, explicit, and comprehensible in each of its essential details”); *Basin Oil Co. v. Baash-Ross Tool Co.*, 271 P.2d 122, 131 (Cal. Ct. App. 1954) (noting that law does not look favorably on attempts to waive negligence liability).

¹⁷⁵ *See Salton Bay Marina, Inc. v. Imperial Irrigation Dist.*, 218 Cal. Rptr. 839, 848 (Ct. App. 1985) (holding that agreement which seeks to limit generally without mentioning negligence shields a party only for passive negligence).

University of California,¹⁷⁶ the leading case, announced that any “exculpatory clause which affects the public interest cannot stand.”¹⁷⁷ The *Tunkl* court declined to define the “public interest,” contenting itself with vague standards summarizing prior decisions.¹⁷⁸ The court, however, left little doubt as to the breadth of the concept. In rejecting a hospital’s disclaimer of negligence liability, it observed:

[T]he integrated and specialized society of today, structured upon mutual dependency, cannot rigidly narrow the concept of the public interest. From the observance of simple standards of due care in the driving of a car to the performance of the high standards of hospital practice, the individual citizen must be completely dependent upon the responsibility of others. The fabric of this pattern is so closely woven that the snarling of a single thread affects the whole. We cannot lightly accept a sought immunity from careless failure to provide the hospital service upon which many must depend. Even if the hospital’s doors are open only to those in a specialized category, the hospital cannot claim isolated immunity in the interdependent community of our time. It, too, is part of the social fabric, and prearranged exculpation from its negligence must partly rend the pattern and necessarily affect the public interest.¹⁷⁹

Based on this language, many contracting parties, with the exercise of a little creativity, may frame complaints presenting non-frivolous arguments for avoiding an exculpatory clause purporting to disclaim liability for negligent acts.

California, like New York, adopts a generally favorable stance toward releases of claims once a dispute has arisen, enforcing them liberally in the absence of duress, illegality, or other defenses to the enforcement of a simple contract.¹⁸⁰ In some respects, however, California law is less favorable to enforcement of litigation releases. Section 1542 of the Civil Code provides a limiting rule of construction for releases in debtor-creditor contracts, under which a “general release does not extend to claims which the creditor does not know or suspect to exist in his or her favor at the time of executing the release, which if known by him or her must have materially affected his or her settlement

¹⁷⁶ 383 P.2d 441 (Cal. 1963).

¹⁷⁷ *Id.* at 444.

¹⁷⁸ For example, indicia of situations where waivers of simple negligence would violate the public interest include the circumstances that “the releasing party does not really acquiesce voluntarily in the contractual shifting of the risk,” that the “service is one which each member of the public, presently or potentially, may find essential to him,” and that the party granting the release “faces, despite his economic inability to do so, the prospect of a compulsory assumption of the risk of another’s negligence.” *Id.* at 446-47.

¹⁷⁹ *Id.* at 448-49.

¹⁸⁰ See, e.g., *Perez v. Uline, Inc.*, 68 Cal. Rptr. 3d 872, 876 (Ct. App. 2007) (holding that duress is available to invalidate a release only as a “last resort”); *Timney v. Lin*, 131 Cal. Rptr. 2d 387, 391 (Ct. App. 2003); *Huens v. Tatum*, 60 Cal. Rptr. 2d 438, 442 (Ct. App. 1997).

with the debtor.”¹⁸¹ Although § 1542 can be waived¹⁸², is not always strictly enforced,¹⁸³ and arguably simply restates the law that would apply in any event,¹⁸⁴ it remains a potential snare for the unwary.

3. Noncompete Clauses

Both New York and California place limits on covenants not to compete and related clauses, but California is significantly more willing to reject agreements on this ground.

Under New York law, covenants not to compete are not per se invalid. Instead, courts enforce a noncompete clause to the extent that “it is reasonable in time and area, necessary to protect the employer’s legitimate interests, not harmful to the general public and not unreasonably burdensome to the employee.”¹⁸⁵ California, in contrast, treats noncompete and related clauses with extreme disfavor. Section 16600 of the California Business and Professions Code provides that “[e]very contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void.”¹⁸⁶ This statute thus appears to impose a virtual per se ban on noncompete clauses,¹⁸⁷ and some courts have viewed it as such,¹⁸⁸ although other opinions are more qualified.¹⁸⁹ In any event the statute reflects an unusually strong public policy of the state.¹⁹⁰ The statute ensures that restraints on competition, valid under the law of New York,

¹⁸¹ CAL. CIV. CODE § 1542 (West 2008).

¹⁸² See *Kaufman & Broad-South Bay v. Unisys Corp.*, 822 F. Supp. 1468, 1474 (N.D. Cal. 1993); *Winet v. Price*, 6 Cal. Rptr. 2d 554, 560-62 (Ct. App. 1992).

¹⁸³ See, e.g., *Perez*, 68 Cal. Rptr. 3d at 872, 875-76 (upholding general release despite lack of explicit § 1542 waiver).

¹⁸⁴ Cf. *Westlye v. Look Sports, Inc.*, 22 Cal.Rptr.2d 781, 788 (Ct. App. 1993) (“[It must] ‘appear that . . . [a liability limiting agreement’s] terms were intended by both parties to apply to the particular conduct of the defendant which has caused the harm.’” (quoting *Bennett v. U.S. Cycling Fed’n*, 239 Cal. Rptr. 55, 58 (Ct. App. 1987))).

¹⁸⁵ *BDO Seidman v. Hirshberg*, 712 N.E.2d 1220, 1223 (N.Y. 1999) (quoting *Reed, Roberts Assoc. v. Strauman*, 353 N.E.2d 590, 593 (N.Y. 1976)).

¹⁸⁶ CAL. BUS. & PROF. CODE § 16600 (West 2008).

¹⁸⁷ The same policy works to invalidate agreements not to solicit employees. See *VL Sys., Inc. v. Unisen, Inc.*, 61 Cal. Rptr. 3d 818, 821-24 (Ct. App. 2007).

¹⁸⁸ See, e.g., *Edwards v. Arthur Andersen LLP*, 47 Cal. Rptr. 3d 788, 800 (Ct. App. 2006) (“In our view, section 16600 prohibits noncompetition agreements between employers and employees even where the restriction is narrowly drawn and leaves a substantial portion of the market available for the employee.”), *aff’d in relevant part*, 189 P.3d 285, 290-93 (Cal. 2008).

¹⁸⁹ See *Gen. Commercial Packaging, Inc. v. TPS Package Eng’g, Inc.*, 126 F.3d 1131, 1134 (9th Cir. 1997) (holding that a noncompetition agreement is valid under § 16600 if the restriction is limited in scope and leaves a substantial portion of the market available to the employee).

¹⁹⁰ See *Scott v. Snelling & Snelling, Inc.*, 732 F. Supp. 1034, 1042 (N.D. Cal. 1990); *Kelton v. Stravinski*, 41 Cal. Rptr. 3d 877, 881 (Ct. App. 2006); *KGB, Inc. v. Giannoulas*, 164 Cal. Rptr. 571, 577 (Ct. App. 1980); *Frame v. Merrill Lynch, Pierce, Fenner & Smith Inc.*, 97 Cal. Rptr. 811, 814 (Ct. App. 1971).

would face a serious threat of being invalidated if subjected to California's public policy.¹⁹¹

4. Wrongful Discharge

Both California and New York assume that, unless specifically agreed otherwise, contracts for employment are at-will and terminable by either party at any time.¹⁹² But while New York rigorously enforces this principle, California recognizes exceptions based on public policy that, at times, threaten to swallow the rule. The consequence is that employment contracts in New York are more predictable than in its sister state.¹⁹³

A 2003 decision by the Court of Appeals, *Horn v. New York Times*,¹⁹⁴ illustrates New York's approach to employment contracts. The plaintiff, an in-house physician, alleged that she was fired for resisting efforts by human relations managers to discover privileged medical information.¹⁹⁵ Even accepting these allegations as true, the court held that the plaintiff had not made out a claim for wrongful discharge. The court refused to recognize a claim of retaliatory termination¹⁹⁶ and declined the plaintiff's request to use the covenant of

¹⁹¹ See Michael J. Garrison & John T. Wendt, *The Evolving Law of Employee Noncompete Agreements: Recent Trends and an Alternative Policy Approach*, 45 AM. BUS. L.J. 107, 120 (2008) (noting that the state's restrictive policy on covenants not to compete is "vigorously protected" by the California courts).

¹⁹² California: CAL. LAB. CODE § 2922 (West 2008) ("An employment, having no specified term, may be terminated at the will of either party on notice to the other."); *Guz v. Bechtel Nat'l, Inc.*, 8 P.3d 1089, 1100 (Cal. 2000) (holding that California provides a "strong" presumption of at-will employment); *Foley v. Interactive Data Corp.*, 765 P.2d 373, 384 (Cal. 1988) ("We begin by acknowledging the fundamental principle of freedom of contract: employer and employee are free to agree to a contract terminable at will or subject to limitations.")

New York: *Horn v. N.Y. Times*, 790 N.E.2d 753, 755 (N.Y. 2003) (citing *Martin v. N.Y. Life Ins. Co.*, 42 N.E. 416 (N.Y. 1895)).

¹⁹³ Contracts of employment are the only category of agreement in Eisenberg and Miller's data where California law and forum were chosen more often than New York. See Eisenberg & Miller, *Flight to New York*, *supra* note 5. The evidence might support an inference that sophisticated contracting parties prefer California's more protective law over the strong norm of at-will employment found in New York. However, the frequent use of California law in employment agreements in the Eisenberg-Miller data might be due to two related circumstances: first, the fact that many of the companies reporting employment agreements are in the high-tech sector, where contracts with senior managers are arguably more often material to a firm's financial results; and second, the fact that if the employer and employee are both in California, the courts of that state would probably refuse to honor a choice-of-law or forum selection clause opting into some other state.

¹⁹⁴ 790 N.E.2d 753 (N.Y. 2003).

¹⁹⁵ *Id.* at 754.

¹⁹⁶ *Id.* at 756, 759 (citing *Murphy v. Am. Home Prods. Corp.*, 448 N.E.2d 86, 89 (N.Y. 1983)). However, New York law prohibits retaliatory termination when an employee is fired for disclosing a violation which creates a "substantial and specific danger to the public health or safety." N.Y. LAB. LAW § 740(2)(a) (McKinney 2008).

good faith and fair dealing to provide a remedy in an at-will relationship.¹⁹⁷ The *Horn* case acknowledged only two exceptions to the at-will rule: situations where the employer's handbook or other literature promised not to terminate the employee except for cause¹⁹⁸ and cases of legal employment implicating the rules of professional responsibility.¹⁹⁹ Neither exception was present on the facts of the case.

California's approach is significantly less protective of the at-will presumption. In *Foley v. Interactive Data Corp.*,²⁰⁰ the California Supreme Court set forth liberal rules for implying a non-at-will employment relationship in the absence of express contract. Among the "totality of the circumstances" deemed relevant are "the personnel policies or practices of the employer, the employee's longevity of service, actions or communications by the employer reflecting assurances of continued employment, and the practices of the industry in which the employee is engaged."²⁰¹ Because of the open-textured nature of this test and the fact that a disgruntled employee can almost always point to some behavior by the employer or its agents purporting to assure continuation of employment, the *Foley* case is a fruitful source of complaints for wrongful discharge. These complaints, even if ultimately unsuccessful, enhance employees' bargaining leverage in disputes with former employers.²⁰²

California also recognizes, while New York does not,²⁰³ a tort action for discharge in violation of public policy. "Public policy," in this context, is a broad and flexible concept. California decisions indicate that the policy must be delineated in either constitutional or statutory provisions, "public" in the sense that it inures to the benefit of the public, well established at the time of the discharge, and substantial and fundamental.²⁰⁴ Under this definition, plaintiffs may survive a motion to dismiss by alleging they suffered adverse employment action

¹⁹⁷ 790 N.E.2d at 756, 759 (citing *Murphy*, 448 N.E. at 91).

¹⁹⁸ *Id.* at 755, 759 (citing *Weiner v. McGraw-Hill, Inc.*, 443 N.E.2d 441 (N.Y. 1982)).

¹⁹⁹ *Id.* at 757, 759 (citing *Wieder v. Skala*, 609 N.E.2d 105, 108 (N.Y. 1992)).

²⁰⁰ 765 P.2d 373 (Cal. 1988); *see also* *Guz v. Bechtel Nat'l, Inc.*, 8 P.3d 1089 (Cal. 2000).

²⁰¹ *Foley*, 765 P.2d at 387-88 (quoting *Pugh v. See's Candies, Inc.*, 171 Cal. Rptr. 917, 925-26 (Ct. App. 1981)).

²⁰² *See, e.g., Guz*, 8 P.3d at 1101-02; *Scott v. Pac. Gas & Elec. Co.*, 904 P.2d 834, 838-40 (Cal. 1995); *Nelson v. United Techs.*, 88 Cal. Rptr. 2d 239, 250-51 (Ct. App. 1999); *Haycock v. Hughes Aircraft Co.*, 28 Cal. Rptr. 2d 248, 258-59 (Ct. App. 1994).

²⁰³ *See Horn v. N.Y. Times*, 790 N.E.2d 753, 759 (N.Y. 2003) ("We have consistently declined to create a common-law tort of wrongful or abusive discharge, or to recognize a covenant of good faith and fair dealing to imply terms grounded in a conception of public policy into employment contracts, as the dissent would have us do, and we again decline to do so."); *Lobosco v. N.Y. Tel. Co./NYNEX*, 751 N.E.2d 462, 464 (N.Y. 2001).

²⁰⁴ *Stevenson v. Superior Court*, 941 P.2d 1157, 1165 (Cal. 1997); *Turner v. Anheuser-Busch, Inc.*, 876 P.2d 1022, 1032-33 (Cal. 1994), *overruled on other grounds by Romano v. Rockwell Int'l, Inc.*, 926 P.2d 1114 (Cal. 1996).

for refusing to commit a crime,²⁰⁵ reporting corporate misconduct,²⁰⁶ or otherwise acting in furtherance of the public interest.²⁰⁷

D. *Statute of Frauds*

Both New York and California recognize and enforce versions of the statute of frauds.²⁰⁸ But New York, with its strong preference for written agreements, more stringently enforces the statute's requirements.

New York courts enforce the statute of frauds with a view towards ensuring that only genuine agreements are subject to enforcement.²⁰⁹ Contracts otherwise barred by the statute can only rarely be salvaged. The doctrine of part performance is available for real estate contracts,²¹⁰ but only where the performance in question "unequivocally" refers to the agreement,²¹¹ the complaining party detrimentally relies on the defendant's actions,²¹² and failure to enforce the contract would result in an unconscionable injury.²¹³ Outside the real estate context, part performance is not available.²¹⁴ Promissory estoppel can defeat the

²⁰⁵ See *Tameny v. Atl. Richfield Co.*, 610 P.2d 1330, 1332 (Cal. 1980).

²⁰⁶ See *Garibaldi v. Lucky Food Stores, Inc.*, 726 F.2d 1367, 1374 (9th Cir. 1984), *abrogated on other grounds*, *Allis Chambers Corp. v. Lueck*, 471 U.S. 202 (1985).

²⁰⁷ California's rules on covenants not to compete also provide an avenue for recovery in wrongful termination cases. In California, an employer cannot condition the renewal of an employment agreement on the employee signing an unenforceable covenant not to compete; if the employment is not renewed after the employee refuses such a demand, the employee may obtain damages for wrongful discharge. See *D'sa v. Playhut, Inc.*, 102 Cal. Rptr. 2d 495, 499-500 (Ct. App. 2001).

²⁰⁸ The statute of frauds is a rule of evidence which requires proof of a written document or documents as a condition for the enforcement of certain types of contracts. See CAL. CIV. CODE § 1624 (West 2008); N.Y. GEN. OBLIG. LAW § 5-701 (McKinney 2008) (general contracts); *id.* § 5-703 (real estate contracts).

²⁰⁹ See *Sonnenschein v. Douglas Elliman-Gibbons & Ives*, 713 N.Y.S.2d 9 (App. Div. 2000), *aff'd*, 753 N.E.2d 857 (N.Y. 2001).

²¹⁰ See N.Y. GEN. OBLIG. LAW § 5-703(4) (McKinney 2008) ("Nothing contained in this section abridges the powers of courts of equity to compel the specific performance of agreements in cases of part performance.").

²¹¹ *Woolley v. Stewart*, 118 N.E. 847, 848 (N.Y. 1918); *Burns v. McCormick*, 135 N.E. 273, 273 (N.Y. 1922). Part performance unequivocally refers to the agreement, in New York, only in extreme cases: the actions in question must be "unintelligible or at least extraordinary" under any other explanation. *Anostario v. Vicinanza*, 450 N.E.2d 215, 216 (N.Y. 1983) (mem.) (quoting *Burns*, 135 N.E. at 273).

²¹² *Messner Vetere Berger McNamee Schmetterer Euro RSCG Inc. v. Aegis Group PLC*, 711 N.E.2d 953, 956 (N.Y. 1999), *enforced*, 186 F.3d 135 (2d Cir. 1999).

²¹³ *E.g., id.*

²¹⁴ The New York Court of Appeals has specifically refused to recognize the doctrine of part performance in other contexts, *see id.* at 956 n.1, a comment which is generally seen as denying the application of part performance to other types of agreement, *see Sea Trade Co. Ltd. v. FleetBoston Fin. Corp.*, No. 03 Civ. 10254, 2004 WL 2029399, at *4-5 (S.D.N.Y. Sept. 9, 2004); *Spencer Trask Software & Info. Servs. LLC v. RPost Int'l Ltd.*, 383 F. Supp. 2d 428, 450

statute,²¹⁵ but only where the defendant makes a clear and unambiguous promise on which the plaintiff reasonably relies and enforcing the statute would work an unconscionable injury.²¹⁶ Claims in quantum meruit have been allowed where the plaintiff has conferred a benefit on the defendant by performing an agreement subject to the statute.²¹⁷ Some recent decisions suggest, however, that quantum meruit claims are categorically unavailable if the effect of recognizing them is to circumvent the statute.²¹⁸ Attempts to avoid the statute by recasting the claim as a tort action are unavailing. No action for fraud will lie if proof of the unenforceable contract is essential to establish an element of the claim.²¹⁹

California is more receptive to efforts at avoiding the statute of frauds, especially where the result is perceived as unfair. The policy of the statute, as articulated by California courts, is to prevent fraud.²²⁰ This leads to an uncharitable attitude on the part of some judges who doubt the statute's effectiveness at achieving that goal²²¹ and who worry that the statute, itself, might be used as a shield for fraud.²²² In a notable opinion from 1964, the California Supreme Court, pointing to these concerns, endorsed calls for a "restricted application of the statute of frauds, if not its total abolition"²²³—a sentiment that has been echoed in subsequent California cases.²²⁴

(S.D.N.Y. 2003); *Pevner, Inc. v. Ensler*, 766 N.Y.S.2d 183, 184 (App. Div. 2003); *Valentino v. Davis*, 703 N.Y.S.2d 609, 611-12 (App. Div. 2000).

²¹⁵ See, e.g., *Pearce v. Manhattan Ensemble Theater, Inc.*, 528 F. Supp. 2d 175, 181 (S.D.N.Y. 2007).

²¹⁶ E.g., *Pacesetter Motors, Inc. v. Nissan Motor Corp. in U.S.A.*, 913 F. Supp. 174, 182-83 (W.D.N.Y. 1996); *Fleet Bank v. Pine Knoll Corp.*, 736 N.Y.S.2d 737, 742 (App. Div. 2002).

²¹⁷ See *Farash v. Sykes Datatronics, Inc.*, 452 N.E.2d 1245, 1246-47 (N.Y. 1983).

²¹⁸ See *Sugerman v. MCY Music World, Inc.*, 158 F. Supp. 2d 316, 326 (S.D.N.Y. 2001); *Am.-European Art Assocs., Inc. v. Trend Galleries, Inc.*, 641 N.Y.S.2d 835, 845 (App. Div. 1996) ("[P]laintiffs may not utilize a quantum meruit theory of recovery to circumvent the Statute of Frauds." (citation omitted)); *Meyers Assocs., L.P. v. Conolog Corp.*, No. 600824/07, 2008 WL 711702, at *3 (N.Y. Sup. Ct. Mar. 5, 2008). These decisions do not clearly distinguish the prior Court of Appeals decision in *Farash*, 452 N.E. 1245, but perhaps can be reconciled on the theory that a plaintiff may make out a claim for unjust enrichment to the extent that the claim is not based on the unenforceable contract. See, e.g., *RTC Props., Inc. v. Bio Res., Ltd.*, 744 N.Y.S.2d 173, 175 (App. Div. 2002), *appeal dismissed*, 782 N.E. 568 (N.Y. 2002).

²¹⁹ See, e.g., *Nifty Foods Corp. v. Great Atl. & Pac. Tea Co.*, 614 F.2d 832, 837-38 (2d Cir. 1980) (barring claims for fraud); *Nelson Bagel Bakery Co. v. Moshcorn Realty Corp.*, 734 N.Y.S.2d 134 (App. Div. 2001); *Weitz v. Smith*, 647 N.Y.S.2d 236 (App. Div. 1996) (mem.).

²²⁰ See *Sterling v. Taylor*, 152 P.3d 420, 425 (Cal. 2007).

²²¹ See *Sunset-Sternau Food Co. v. Bonzi*, 389 P.2d 133, 136 (Cal. 1964).

²²² See, e.g., *Seymour v. Oelrichs*, 106 P. 88, 94 (Cal. 1909) ("The right of courts of equity to hold a person estopped to assert the statute of frauds, where such assertion would amount to practicing a fraud, cannot be disputed."); *Juran v. Epstein*, 28 Cal. Rptr. 2d 588, 594-95 (Ct. App. 1994).

²²³ *Sunset-Sternau*, 389 P.2d at 136 n.3 (Tobriner, J.).

²²⁴ See, e.g., *Sterling*, 152 P.3d at 420 n.11; *Estate of Housley v. Haywood*, 65 Cal. Rptr. 2d 628, 633 (Ct. App. 1997) (suggesting that the statute of frauds "has fallen into disfavor" in California, although continuing to enforce it (citing 1 WITKIN, SUMMARY OF CAL. LAW,

California's grudging attitude toward the statute of frauds is mirrored in a receptive approach to strategies for avoiding it. Unlike New York, California recognizes part performance as a means for salvaging all contracts that would otherwise fall within the statute—not just real estate contracts.²²⁵ California courts are also receptive to the use of promissory estoppel as a basis for avoiding the statute.²²⁶ Even in the absence of detrimental reliance, they may allow enforcement of a contract under a promissory estoppel theory if failing to do so would result in unjust enrichment to the counterparty.²²⁷ California, unlike New York, may also permit fraud actions based on contracts that are otherwise unenforceable under the statute.²²⁸

E. *Mistake*

Both California and New York recognize that parties may avoid performing contractual obligations upon a suitable showing of mistake. As between the two, however, New York is less willing to relieve parties of their commitments on this basis.

Consistent with its general philosophy of holding parties to their bargains, New York allows rescission or reformation on the basis of mutual mistake of fact only in limited circumstances. The mistake must have been present at the time of contract,²²⁹ must be mutual²³⁰ and substantial,²³¹ must be shown by clear and convincing evidence,²³² and must not be one that the party should have known about at the time he entered into the contract.²³³ Parties may also be relieved of contractual

CONTRACTS § 261, at 259 (9th ed. 1987)).

²²⁵ See, e.g., *In re Marriage of Benson*, 116 P.3d 1152, 1160 (Cal. 2005) (noting in dicta that general statute of frauds is subject to exception for part performance).

²²⁶ See Philip H. Wile, Kathleen Cordova-Lyon & Claude D. Rohwer, *Estoppel to Avoid the California Statute of Frauds*, 35 MCGEORGE L. REV. 319 (2004). The authors argue, however, that California promissory estoppel cases should be interpreted so as to avoid a de facto repeal of the statute of frauds. See *id.*

²²⁷ *Estate of Housley*, 65 Cal. Rptr. 2d at 632-33; *James G. Freeman & Assocs., Inc. v. Tanner*, 128 Cal. Rptr. 109, 115 n.10 (Ct. App. 1976) (declining to apply statute of frauds where result would be unjust enrichment).

²²⁸ *Levin v. Knight*, 780 F.2d 786, 788 (9th Cir. 1986) (approving fraud action based on misrepresentation in connection with unenforceable contract); *Tenzer v. Superscope, Inc.*, 702 P.2d 212, 218-19 (Cal. 1985).

²²⁹ *Schultz v. Hourihan*, 656 N.Y.S.2d 526 (App. Div. 1997).

²³⁰ See, e.g., *Marsh v. Labella*, No. 11039/07, 2008 WL 920988, at *5 (N.Y. Sup. Ct. Apr. 3, 2008).

²³¹ *Brauer v. Cent. Trust Co.*, 433 N.Y.S.2d 304, 307 (App. Div. 1980) (“[W]here a mistake in contracting is both mutual and substantial, there is an absence of the requisite ‘meeting of the minds’ to the contract, and the relief will be provided in the form of rescission.”).

²³² *Lacoparra v. Bellino*, 745 N.Y.S.2d 693 (App. Div. 2002); see *Nash v. Kornblum*, 186 N.E.2d 551, 553 (N.Y. 1962).

²³³ See *In re Schenck Tours, Inc.*, 69 B.R. 906, 914 (Bankr. E.D.N.Y. 1987), *aff’d*, 75 B.R.

obligation because of mutual mistake of law,²³⁴ but here the requirements are even more stringent: The mistake must be accompanied by “fraud, or inequitable, unfair, or deceptive conduct.”²³⁵ Rescission or reformation based on unilateral, as opposed to mutual, mistake is uncommon in New York;²³⁶ the proponent must establish that enforcing the contract as written would be unconscionable²³⁷ or would result in unjust enrichment of one party at the expense of the other,²³⁸ or that the parties can be returned to the status quo ante without prejudice.²³⁹ In any case of mistake where reformation is sought, the party seeking relief must establish “exactly what was really agreed upon between the parties.”²⁴⁰

California follows the same general rules but is more receptive to pleas for relief from unwanted bargains. Instead of emphasizing the importance of respecting the parties’ written agreement, California courts focus on the statutory requirement of mutual consent.²⁴¹ The necessity that the parties agree to the same thing at the same time²⁴² makes it relatively easy for parties to frame claims for relief under this theory.²⁴³ California courts do not emphasize the restrictions that limit the availability of mutual mistake under New York law, such as the lack of fault on the part of the party seeking relief²⁴⁴ or the need for clear and convincing evidence to establish the claim. California is also more generous in offering relief based on unilateral mistake; the supplicant must show that the counterparty knew of or suspected the error, but the elements of unconscionability or unjust enrichment are not required unless the counterparty’s fault cannot be shown.²⁴⁵ California’s

249 (E.D.N.Y. 1987); *P.K. Dev., Inc. v. Elvem Dev. Corp.*, 640 N.Y.S.2d 558, 560 (App. Div. 1996).

²³⁴ N.Y. C.P.L.R. § 3005 (McKinney 2008) (“When relief against a mistake is sought in an action or by way of defense or counterclaim, relief shall not be denied merely because the mistake is one of law rather than one of fact.”).

²³⁵ *Trotter v. Brevoort*, 69 N.Y.S. 1028, 1031 (App. Div. 1901); *see* *Greene v. Smith*, 55 N.E. 212, 212 (N.Y. 1899).

²³⁶ *See* *Cox v. Lehman Bros., Inc.*, 790 N.Y.S.2d 16 (App. Div. 2005).

²³⁷ *Morey v. Sings*, 570 N.Y.S.2d 864, 872 (App. Div. 1991).

²³⁸ *Weissman v. Bondy & Schloss*, 660 N.Y.S.2d 115, 118 (App. Div. 1997), *appeal dismissed*, 691 N.E.2d 637 (N.Y. 1998).

²³⁹ *Broadway-111th St. Assocs. v. Morris*, 553 N.Y.S.2d 153, 155 (App. Div. 1990) (mem.).

²⁴⁰ *See* *Chimart Assocs. v. Paul*, 489 N.E.2d 231, 234 (N.Y. 1986).

²⁴¹ *See* CAL. CIV. CODE §§ 1550, 1565, 1580 (West 2008).

²⁴² *See* § 1580 (“Consent is not mutual, unless the parties all agree upon the same thing in the same sense.”); *Weddington Prods., Inc. v. Flick*, 71 Cal. Rptr. 2d 265, 277 (Ct. App. 1998).

²⁴³ They must, however, plead objective facts tending to negate the element of consent; mere allegations of subjective mistake will not do. *Alexander v. Codemasters Group Ltd.*, 127 Cal. Rptr. 2d 145, 159 (Ct. App. 2002).

²⁴⁴ *See* *Mutual Life Ins. Co. of N.Y. v. Simon*, 151 F. Supp. 408, 412 (S.D.N.Y. 1957); *Hess v. Ford Motor Co.*, 41 P.3d 46, 55 (Cal. 2002); *Van Meter v. Bent Constr. Co.*, 297 P.2d 644, 647 (Cal. 1956); *Nat’l Auto & Cas. Ins. Co. v. Indus. Accident Comm’n*, 206 P.2d 841, 844 (Cal. 1949).

²⁴⁵ *See* CAL. CIV. CODE § 1577 (West 2008) (“Mistake of fact is a mistake, not caused by the

acceptance of extrinsic evidence on the question also facilitates proof of mistake.²⁴⁶ California makes reformation liberally available if mistake is shown, provided that the changed terms do not affect substantial rights of third parties.²⁴⁷

V. PAROL EVIDENCE

Both California and New York administer a parol evidence rule.²⁴⁸ Both states recognize that if a contract is “integrated”—that is, if it expresses the full and complete agreement of the parties—then evidence from outside the four corners of the contract may not be considered.²⁴⁹ Both accept that a contract is integrated if the language of the agreement is clear and unambiguous.

Beyond these uncontroversial propositions, the states diverge. New York, consistent with its preference for written agreements and contractual clarity, employs a “hard” parol evidence rule²⁵⁰ under which the court decides whether the contract is ambiguous from an analysis of the document itself.²⁵¹ If the court concludes that the contract terms are unambiguous, it does not consider extrinsic evidence bearing on the parties’ intent.²⁵² Courts only resort to extrinsic evidence if the

neglect of a legal duty on the part of the person making the mistake, and consisting in . . . [a]n unconscious ignorance or forgetfulness of a fact past or present, material to the contract; or . . . [b]elief in the present existence of a thing material to the contract, which does not exist, or in the past existence of such a thing, which has not existed.”); *Donovan v. RRL Corp.*, 27 P.3d 702, 716 & n.6 (Cal. 2001) (granting relief when counterparty had reason to know of the mistake or when enforcement would be unconscionable).

²⁴⁶ CAL. CIV. PROC. CODE § 1856(e), (g) (West 2008); see *Casa Herrera, Inc. v. Beydoun*, 83 P.3d 497, 503 (Cal. 2004).

²⁴⁷ CAL. CIV. PROC. CODE § 3399 (“When, through fraud or a mutual mistake of the parties, or a mistake of one party, which the other at the time knew or suspected, a written contract does not truly express the intention of the parties, it may be revised on the application of a party aggrieved, so as to express that intention, so far as it can be done without prejudice to rights acquired by third persons, in good faith and for value.”); *Hess*, 41 P.3d at 52 (Cal. 2002).

²⁴⁸ The parol evidence rule is a principle for identifying the information that will be admitted to prove the meaning of a contract. For an interesting economic analysis of the parol evidence rule, seeing it as an efficient means for smoking out information from better-informed parties, see Albert H. Choi, *Integrating an Agreement to Induce Information Disclosure* (Working Paper) (on file with the author).

²⁴⁹ See generally 2 E. ALLEN FARNSWORTH, *CONTRACTS* § 7.3 (1990). If the contract is final but does not express the complete agreement of the parties, it is partially integrated and the court may allow extrinsic evidence to the extent it is consistent with the written terms.

²⁵⁰ The distinction between “hard” and “soft” rules is from Eric A. Posner, *The Parol Evidence Rule, the Plain Meaning Rule, and the Principles of Contractual Interpretation*, 146 U. PA. L. REV. 533, 534 (1998).

²⁵¹ See, e.g., *Morgan Stanley High Yield Sec., Inc. v. Seven Circle Gaming Corp.*, 269 F. Supp. 2d 206, 214 (S.D.N.Y. 2003).

²⁵² See *Crane Co. v. Coltec Indus., Inc.*, 171 F.3d 733, 737 (2d Cir. 1999); *W.W.W. Assocs. v. Giancontieri*, 566 N.E.2d 639, 642 (N.Y. 1990); *Chimart Assocs. v. Paul*, 489 N.E.2d 231, 233 (N.Y. 1986); *Katz v. Am. Mayflower Life Ins. Co. of N.Y.*, 788 N.Y.S.2d 15, 19 (App. Div.

agreement is subject to more than one interpretation.²⁵³ If the parties desire even greater protection from extra-contractual information being used to interpret their agreement, they are free to adopt merger or integration clauses;²⁵⁴ these clauses are accorded nearly conclusive deference by the New York courts.²⁵⁵

California, in contrast, uses a “soft” parol evidence rule.²⁵⁶ Under a soft rule, a lack of ambiguity in the explicit contractual language does not control. Instead, the court provisionally examines extrinsic evidence bearing on the threshold question of whether the contract is ambiguous.²⁵⁷ If, after such an investigation, the contract is found to be unambiguous, the rule then excludes all extrinsic evidence, including the evidence considered at the threshold stage.²⁵⁸ If, however, the extrinsic evidence reveals ambiguity, then the court may consider all such extrinsic evidence as may be relevant to interpreting the contract.²⁵⁹ The parties can, of course, include merger or integration

2004), *aff’d*, 841 N.E.2d 742 (N.Y. 2005).

²⁵³ See, e.g., *CV Holdings v. Artisan Advisors*, 780 N.Y.S.2d 425, 427 (App. Div. 2004); *Besicorp Group, Inc. v. Enowitz*, 652 N.Y.S.2d 366, 368 (App. Div. 1997).

²⁵⁴ Merger clauses provide that all prior agreements and understandings between the parties related to the transaction are merged into the final contract. The effect of merger clauses is to exclude any claims based on precontractual negotiations or understandings between the parties. Integration clauses provide that the written contract reflects the full and complete understanding of the parties. Integration clauses have a similar effect and purpose as merger clauses, but their scope is larger: They apply to all extra-contractual evidence of the parties’ intent, not merely prior agreements or understandings. An example of a typical merger/integration clause might provide: “This Agreement contains the entire understanding between the parties and supersedes any prior understanding and agreements between them respecting the subject matter hereof. There are no representations, agreements, arrangements or understandings, oral or written, between the parties hereto relating to the subject matter of this Agreement which are not fully expressed herein.” For discussion of the drafting considerations pertinent to such clauses, see Brad S. Karp, *The Litigation Angle in Drafting Commercial Agreements*, 1459 PRACTICING L. INST. CORP. L. & PRAC. COURSE HANDBOOK SERIES 343 (2004).

²⁵⁵ See *Tempo Shain Corp. v. Bertek, Inc.*, 120 F.3d 16, 21 (2d Cir. 1997) (“Ordinarily, a merger clause provision indicates that the subject agreement is completely integrated, and parol evidence is precluded from altering or interpreting the agreement.”); *Jarecki v. Shung Moo Louie*, 745 N.E.2d 1006, 1009 (N.Y. 2001) (“The purpose of a merger clause is to require the full application of the parol evidence rule in order to bar the introduction of extrinsic evidence. . . . The merger clause accomplishes this purpose by evincing the parties’ intent that the agreement ‘is to be considered a completely integrated writing.’” (citation omitted)); *Cornhusker Farms, Inc. v. Hunts Point Coop. Mkt., Inc.*, 769 N.Y.S.2d 228, 230-31 (App. Div. 2003); *Jones v. Trice*, 608 N.Y.S.2d 688 (App. Div. 1994) (mem.); *Norman Bobrow & Co. v. Loft Realty Co.*, 577 N.Y.S.2d 36, 36 (App. Div. 1991) (mem.) (“Parol evidence is not admissible to vary the terms of a written contract containing a merger clause.”); *Balzano v. Lublin*, 556 N.Y.S.2d 610 (App. Div. 1990) (mem.); *Oppman v. IRMC Holdings, Inc.*, No. 600929/2006, 2007 WL 151355, at *4 (N.Y. Sup. Ct. Jan. 23, 2007).

²⁵⁶ See Posner, *supra* note 250, at 539-40 & n.15 (noting that “soft” parol evidence rule has been the law in California since the 1960s).

²⁵⁷ See *Winet v. Price*, 6 Cal. Rptr. 2d 554, 557 (Ct. App. 1992); Schwartz & Scott, *supra* note 1, at 591.

²⁵⁸ *Winet*, 6 Cal. Rptr. 2d at 557.

²⁵⁹ *Id.*

clauses in their contracts in an attempt to shore up the parol evidence rule; but, while these are afforded substantial respect under California law,²⁶⁰ they are not conclusive²⁶¹ but rather considered along with other evidence of contract integration.²⁶² Moreover, even if an integration clause is present and respected regarding the original terms of the contract, California recognizes relatively easy modification by course of dealing among the parties.²⁶³

VI. CHOICE OF LAW AND FORUM

Both New York and California recognize wide latitude of the parties to determine the law applicable to their agreements and the forum in which disputes will be resolved.²⁶⁴ As between the two, however, New York is substantially more receptive to party autonomy.

A. *Choice-of-Law Clauses*

New York and California both endorse versions of the Restatement

²⁶⁰ *Banco Do Brasil, S.A. v. Latian, Inc.*, 285 Cal. Rptr. 870, 887 (Ct. App. 1991) (“[O]bviously, the presence of an ‘integration’ clause will be very persuasive . . .”).

²⁶¹ *See, e.g., Specht v. Netscape Commc’ns Corp.*, 306 F.3d 17, 36-37 (2d Cir. 2002) (noting that merger and integration clauses are recognized by California courts, but the presence of merger clauses is not dispositive); *Enrico Farms, Inc. v. H. J. Heinz Co.*, 629 F.2d 1304, 1306 (9th Cir. 1980) (noting presence of merger clauses “not necessarily conclusive”).

²⁶² *Sicor Ltd. v. Cetus Corp.*, 51 F.3d 848, 859 (9th Cir. 1995) (stating integration clause is “but one factor” in the analysis); *Founding Members of Newport Beach Country Club v. Newport Beach Country Club, Inc.*, 135 Cal. Rptr. 2d 505, 512 (Ct. App. 2003) (“[T]he court must consider the writing itself, including whether the written agreement appears to be complete on its face; whether the agreement contains an integration clause; whether the alleged parol understanding on the subject matter at issue might naturally be made as a separate agreement; and the circumstances at the time of the writing.”); *Mobil Oil Corp. v. Rossi*, 187 Cal. Rptr. 845, 851-52 (Ct. App. 1982) (“[A] court must consider such factors as the language and completeness of the written agreement and whether it contains an integration clause, the terms of the alleged oral agreement and whether they contradict those in the writing, whether the oral agreement might naturally be made as a separate agreement, and whether the jury might be misled by the introduction of the parole testimony.”).

²⁶³ *See, e.g., Diamond Woodworks, Inc. v. Argonaut Ins. Co.*, 135 Cal. Rptr. 2d 736, 747 (Ct. App. 2003) (“[W]here the subsequent conduct of parties is inconsistent with and clearly contrary to provisions of the written agreement, the parties’ modification setting aside the written provisions will be implied.”).

²⁶⁴ A number of recent studies emphasize the importance of contractual choice-of-law clauses in modern business transactions. *See* Erin Ann O’Hara, *Opting Out of Regulation: A Public Choice Analysis of Contractual Choice-of-Law*, 53 VAND. L. REV. 1551 (2000); Larry E. Ribstein & Erin Ann O’Hara, *Corporations and the Market for Law*, 2008 U. ILL. L. REV. 661 (2008); Larry E. Ribstein, *Delaware, Lawyers, and Contractual Choice-of-Law*, 19 DEL. J. CORP. L. 999, 1003-04 (1994); William J. Woodward, Jr., *Contractual Choice-of-Law: Legislative Choice in an Era of Party Autonomy*, 54 SMU L. REV. 697, 698-700 (2001) (discussing different states’ laws that are designed to attract different businesses and persons).

(Second) of Conflict of Laws rule on choice-of-law clauses.²⁶⁵ The Restatement adopts “a strong policy favoring enforcement” of such provisions.²⁶⁶ It recommends that choice-of-law clauses be respected unless one of two conditions are met: either the state has no “substantial relationship” with the transaction and there is no reasonable basis for the parties’ choice, or application of the chosen law would be contrary to a fundamental policy of a state with a materially greater interest in the issue and whose law would apply absent the clause.²⁶⁷ Behind this surface agreement, however, substantial differences can be discerned as between the states: New York, overall, is more willing to respect contractual choice.

New York courts regularly enforce choice-of-law provisions, especially in commercial contracts.²⁶⁸ Regarding public policy, New York recognizes only limited circumstances in which choice-of-law clauses will be rejected²⁶⁹: “those rare cases”²⁷⁰ where applying the parties’ choice would be “truly obnoxious”²⁷¹ or “deeply abhorrent”²⁷² to fundamental New York policy. Accordingly, the party seeking to show a violation of public policy to defeat a choice-of-law clause bears a “heavy burden” of proof.²⁷³ Applying the law must “violate some fundamental principle of justice, some prevalent conception of good morals, some deep-rooted tradition of the common weal.”²⁷⁴ The Court of Appeals offers only three examples of state policies fundamental

²⁶⁵ RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 (1971); *see* ABF Capital Corp. v. Osley, 414 F.3d 1061, 1065 (9th Cir. 2005) (noting that California courts apply the Restatement approach for contractual choice-of-law provisions); *Hartford Fire Ins. Co. v. Orient Overseas Containers Lines Ltd.*, 230 F.3d 549, 556 (2d Cir. 2000) (“Absent fraud or violation of public policy, a court is to apply the law selected in the contract as long as the state selected has sufficient contacts with the transaction.”); *Discover Bank v. Superior Court*, 113 P.3d 1100, 1117 (Cal. 2005).

²⁶⁶ *Nedlloyd Lines B.V. v. Superior Court*, 834 P.2d 1148, 1151 (Cal. 1992).

²⁶⁷ RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 (1971).

²⁶⁸ *See, e.g., Hackett v. Milbank, Tweed, Hadley & McCloy*, 654 N.E.2d 95, 100 (N.Y. 1995) (“[E]xplicit and unambiguous choice of law . . . must be given effect.”).

²⁶⁹ The following are rare cases where courts in New York refused to respect choice-of-law clauses on grounds of public policy. *See* *Prod. Res. Group, L.L.C. v. Oberman*, No. 03 Civ. 5366, 2003 WL 22350939, at *8-10 (S.D.N.Y. Aug. 27, 2003) (declining to enforce New York choice-of-law clause to uphold California’s policy against covenants not to compete); *Caribbean Wholesales & Serv. Corp. v. US JVC Corp.*, No. 93 Civ. 8197, 1996 WL 140251, at *3 (S.D.N.Y. Mar. 27, 1996) (rejecting New York choice-of-law clause due to Puerto Rico’s policy of disregarding choice of law clauses in distribution agreements); *Triad Fin. Establishment v. Tumpane Co.*, 611 F. Supp. 157, 162-64 (N.D.N.Y. 1985) (rejecting choice-of-law clause and applying Saudi Arabian law due to Saudi policies to prevent corruption in military contracts); *N. Am. Bank, Ltd. v. Schulman*, 474 N.Y.S.2d 383, 385-87 (N.Y. Co. Ct. 1984) (declining enforcement to preserve New York policy against usury).

²⁷⁰ *Hamilton v. Accu-Tek*, 47 F. Supp. 2d 330, 337 (E.D.N.Y. 1999).

²⁷¹ *Cooney v. Osgood Mach., Inc.*, 612 N.E.2d 277, 285 (N.Y. 1993).

²⁷² *Hamilton*, 47 F. Supp. 2d at 337.

²⁷³ *Schultz v. Boy Scouts of Am., Inc.*, 480 N.E.2d 679, 688 (N.Y. 1985).

²⁷⁴ *Cooney*, 612 N.E.2d at 284 (1993) (quoting *Loucks v. Standard Oil Co.*, 120 N.E. 198, 202 (N.Y. 1918)).

enough to defeat choice-of-law clauses, all involving state anti-discrimination or human rights norms.²⁷⁵ New York courts, moreover, generally look to the policy of only New York when considering whether to reject a choice of New York law; they do not consider conflicting policies of other jurisdictions that might trump the application of the parties' chosen law.²⁷⁶ This effectively gives an ironclad assurance if New York law is selected, since New York courts are very unlikely to find that New York public policy is violated by the application of New York law. Conversely, if the parties have selected the law of some other state, New York courts are loath to upset that decision even if substantive terms of the contract contravene New York policy.²⁷⁷

California is substantially less permissive towards choice-of-law clauses. As we have seen already, compared with New York, California uses expansive notions of public policy to reject contractual terms;²⁷⁸ these arguments are available for choice-of-law clauses as they are for other contractual terms.²⁷⁹ Thus, courts may invalidate choice-of-law

²⁷⁵ *Welsbach Elec. Corp. v. MasTec N. Am., Inc.*, 859 N.E.2d 498, 501 (N.Y. 2006).

²⁷⁶ *See Barkanic v. Gen. Admin. of Civil Aviation of the P.R.C.*, 923 F.2d 957, 964 n.7 (2d Cir. 1991) (“[W]e do not believe that New York courts would consider the public policies of jurisdictions other than New York in choice of law decisions.”); *Woodling v. Garrett Corp.*, 813 F.2d 543, 551 (2d Cir. 1987) (noting that New York honors choice of law clauses “so long as fundamental policies of New York law are not thereby violated”); *Home Ins. Co. v. Appleton Papers, Inc.*, No. 99 Civ. 3169, 2002 WL 22024, at *6 (S.D.N.Y. Jan. 8, 2002) (“New York courts consider only New York public policy when making choice of law decisions, not the public policies of other jurisdictions.”); *Hugh O’Kane Elec., Co. v. MasTec N. Am., Inc.*, 797 N.Y.S.2d 45, 46 (App. Div. 2005) (noting that New York courts enforce choice-of-law clauses so long as they do not violate “a fundamental public policy of New York”). There is some contrary authority however—i.e., some cases in which New York courts have looked to public policies other than that of New York itself—though typically only in unreported federal district-level cases. *See, e.g.*, *Prod. Res. Group, L.L.C. v. Oberman*, No. 03 Civ. 5366, 2003 WL 22350939, at *8-10 (S.D.N.Y. Aug. 27, 2003) (considering public policy of California in declining to enforce New York choice-of-law clause); *Caribbean Wholesales & Serv. Corp. v. US JVC Corp.*, No. 93 Civ. 8197, 1996 WL 140251, at *3 (S.D.N.Y. Mar. 27, 1996) (considering public policies of Puerto Rico in declining to enforce New York choice-of-law clause).

²⁷⁷ *See Welsbach Elec. Corp.*, 859 N.E.2d 498, 500-03 (finding that New York’s policy against “pay-if-paid” construction contracts was not so fundamental that it overrode parties’ choice of Florida law to govern construction subcontract).

²⁷⁸ *See supra* notes 154-166 and accompanying text.

²⁷⁹ *Compare Am. Online, Inc. v. Superior Court*, 108 Cal. Rptr. 2d 699, 707 (Ct. App. 2001) (holding California public policy applies whenever enforcement of choice-of-law clause causes “substantial legal rights [to be] significantly impaired”), *and Hall v. Superior Court*, 197 Cal. Rptr. 757, 761-63 (Ct. App. 1983) (holding that California’s policy in regulating securities prevented enforcing Nevada choice-of-law provision), *with Hamilton v. Accu-Tek*, 47 F. Supp. 2d 330, 337 (E.D.N.Y. 1999) (holding that public policy exception in New York is reserved for “rare cases in which choice of a foreign jurisdiction’s law would be deeply abhorrent from the point of view of fundamental New York policy”), *and Welsbach Elec. Corp.*, 859 N.E.2d at 500-03 (holding that New York policy against enforcing “pay-if-paid” subcontractor provisions did not prevent enforcement of Florida choice-of-law clause), *and Cooney v. Osgood Mach., Inc.*, 612 N.E.2d 277, 284-85 (N.Y. 1993) (stressing limited nature of New York’s public policy exception, which is reserved for foreign law that is “truly obnoxious” and “violate[s] some

clauses whenever “substantial legal rights” would be “significantly impaired”²⁸⁰ or “substantially diminish[ed].”²⁸¹ As a result, there are no “bright line rules”²⁸² for applying the public policy doctrine to choice-of-law clauses. Further, California, unlike New York, looks to the public policies of any state whose law would apply in the absence of the choice-of-law clause, even when California law is selected.²⁸³

Application Group, Inc. v. Hunter Group, Inc.,²⁸⁴ a 1998 case from the First District Court of Appeal, illustrates California’s approach to choice-of-law clauses. A California corporation recruited and hired an employee of a Maryland competitor in clear violation of a covenant not to compete.²⁸⁵ The employee and her employer brought a declaratory judgment action claiming that the covenant violated California public policy. The former employer argued that it was valid under the law of Maryland, which had been selected in the prior employment contract.²⁸⁶ Applying California’s choice-of-law jurisprudence, the appellate court recognized that Maryland had a substantial relationship to the parties and the transaction and that there was a reasonable basis for selecting Maryland law.²⁸⁷ But citing to the importance of California’s policy favoring free competition in employment relationships, the court held that California had a materially greater interest in applying its law to the dispute; it further held that California’s interests would be the more seriously impaired if its policy were subordinated to the policy of Maryland.²⁸⁸ Hence the court rejected the choice-of-law clause, applied California law, and invalidated the noncompete clause.²⁸⁹ Cases like *Application Group* do not appear in New York jurisprudence.

fundamental principle of justice”).

²⁸⁰ *Am. Online*, 108 Cal. Rptr. 2d at 707.

²⁸¹ *Klussman v. Cross Country Bank*, 36 Cal. Rptr. 3d 728, 736 (Ct. App. 2005) (quoting *Am. Online*, 108 Cal. Rptr. 2d at 708).

²⁸² *Discover Bank v. Superior Court*, 36 Cal. Rptr. 3d 456, 460 (Ct. App. 2005) (“We are not aware of any bright-line rules for determining what is and what is not contrary to a fundamental policy of California.” (citing RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187, cmt. g (1996))).

²⁸³ *See Nedlloyd Lines B.V. v. Superior Court*, 834 P.2d 1148, 1152 & n.6 (Cal. 1992) (clarifying that California will look to the public policy of foreign states in applying Restatement approach); *Discover Bank*, 36 Cal. Rptr. 3d at 458 n.1 (“Technically, the inquiry is not whether there is a conflict with a fundamental policy of *California*, but whether there is a conflict with a fundamental policy of the state whose law would apply under Restatement section 188 in the absence of a contractual choice of law.”).

²⁸⁴ 72 Cal. Rptr. 2d 73 (Ct. App. 1998).

²⁸⁵ *Id.* at 75-77.

²⁸⁶ *Id.* at 77, 81-82.

²⁸⁷ *Id.* at 84.

²⁸⁸ *Id.* at 86.

²⁸⁹ *Id.*

B. *Forum Selection Clauses*

Consistent with the general trend in state and federal courts,²⁹⁰ both New York and California respect and enforce forum selection clauses. As between the two, however, New York is more willing to defer to party autonomy.

Generally, New York courts do not set aside forum selection clauses unless enforcement would be “so gravely difficult and inconvenient that the challenging party would, for all practical purposes, be deprived of his or her day in court.”²⁹¹ New York courts deny enforcement of forum selection clauses only in unusual contexts, such as where the clause is manifestly unreasonable and not prominently disclosed in the contract.²⁹² They give short shrift to arguments that the contracts are adhesive, that the complaining party lacked bargaining power, or that the disputed clause was never brought to the party’s attention.²⁹³

California courts enforce forum selection clauses in the absence of a showing the enforcement of such a clause would be unreasonable.²⁹⁴ They impose a “heavy burden” on parties seeking to escape such clauses.²⁹⁵ On the other hand, California precedent suggests that “take it or leave it” clauses may be closely scrutinized.²⁹⁶ California courts also display a willingness to reject forum selection clauses that work to deprive litigants of substantial rights.²⁹⁷ Overall, California judges have

²⁹⁰ The leading case is *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585, 593-95 (1991) (upholding forum selection clause in cruise line contract, a classic consumer contract of adhesion); see also *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 15 (1972).

²⁹¹ *Fidelity & Deposit Co. of Md. v. Altman*, 618 N.Y.S.2d 286 (App. Div. 1994) (mem.) (quoting *British W. Indies Guar. Trust Co. v. Banque Internationale*, 567 N.Y.S.2d 731 (App. Div. 1991) (mem.)).

²⁹² See *In re Assicurazioni Generali S.P.A. Holocaust Ins. Litig.*, 228 F. Supp. 2d 348, 373 (S.D.N.Y. 2002) (denying enforcement to forum selection clauses in insurance contracts for Holocaust victims, issued between 1920 and 1945, which specified various European locations for adjudication of disputes); *Oxman v. Amoroso*, 659 N.Y.S.2d 963, 967 (City Ct. 1997) (invalidating forum selection clause in contract for au pair services performed in New York which required suits to be brought in Utah).

²⁹³ *Fidelity & Deposit Co.*, 618 N.Y.S.2d at 287.

²⁹⁴ *Smith, Valentino & Smith, Inc. v. Superior Court*, 551 P.2d 1206, 1209 (Cal. 1976). “Unreasonable,” in this context, means more than inconvenience and expense. *Id.*; Am. Online, *Inc. v. Superior Court*, 108 Cal. Rptr. 2d 699, 707 (Ct. App. 2001).

²⁹⁵ *Miller-Leigh LLC v. Henson*, 62 Cal. Rptr. 3d 83, 87 (Ct. App. 2007).

²⁹⁶ See *Smith, Valentino*, 551 P.2d at 1209 (Cal. 1976) (endorsing forum selection clauses where the contract was “entered into freely and voluntarily by parties who have negotiated at arm’s length”). Later cases, however, have upheld forum selection clauses in contracts of adhesion. See, e.g., *Net2Phone, Inc. v. Superior Court*, 135 Cal. Rptr. 2d 149, 153 (Ct. App. 2003) (holding unenforceable forum selection clause accessible via hyperlink in take-it-or-leave-it consumer contract); *Intershop Commc’ns, AG v. Superior Court*, 127 Cal. Rptr. 2d 847, 855 (Ct. App. 2002).

²⁹⁷ See *infra* notes 329-337 and accompanying text.

greater flexibility than their peers in New York to reject forum choices that were freely negotiated among the contracting parties.

VII. THE ADJUDICATORY PROCESS

I now compare New York and California law regarding attempts by private parties to control aspects of the adjudicatory process by means of *ex ante* contractual agreements: waivers of jury trial; provisions allocating liability for attorneys' fees; mandatory arbitration clauses; and class action waivers.

A. *Waivers of Jury Trial*

New York courts enforce and respect waivers of jury trials in the absence of fraud, oppression, or overreaching.²⁹⁸ Even without an explicit jury waiver, New York courts vigorously enforce implied waivers, as where the parties to a contract agree to binding arbitration.²⁹⁹ California is less receptive to jury waivers. A Supreme Court case from 2005 held that pre-dispute contractual waivers of jury trial are unenforceable under the state constitution.³⁰⁰ California courts also impose limits on the ability of parties to waive jury rights *de facto* by agreeing to mandatory arbitration clauses.³⁰¹

B. *Attorneys' Fees*

Both New York and California apply the "American Rule" that each party to litigation pays his or her own attorney.³⁰² The two states differ, however, in the degree to which they will respect contractual modifications of the rule. As between them, New York is more willing to respect the parties' voluntary choices in commercial transactions.

²⁹⁸ See *Barclays Bank of N.Y., N.A. v. Heady Elec. Co.*, 571 N.Y.S.2d 650, 653 (App. Div.) (explaining that contract provisions waiving a jury trial are generally valid and enforceable, unless adequate basis to deny enforcement is set forth by the challenging party), *appeal dismissed*, 582 N.E. 604 (N.Y. 1991); *Fordham Univ. v. Mfrs. Hanover Trust Co.*, 534 N.Y.S.2d 993 (App. Div. 1988). Jury waivers are not permitted for suits for personal injury or property damages in leases. N.Y. REAL PROP. LAW § 259-c (McKinney 2008).

²⁹⁹ See *infra* notes 311-326 and accompanying text. New York courts developed the doctrine on jury waivers beginning in the 1920s and decided most of the early cases. See Stephen J. Ware, *Arbitration Clauses, Jury-Waiver Clauses, and Other Contractual Waivers of Constitutional Rights*, 67 LAW & CONTEMP. PROBS. 167, 198 (2004).

³⁰⁰ *Grafton Partners LP v. Superior Court*, 116 P.3d 479 (Cal. 2005).

³⁰¹ See *infra* notes 327-337 and accompanying text.

³⁰² See *Alyeska Pipeline Serv. Co. v. Wilderness Soc'y*, 421 U.S. 240, 247 (1975).

New York, to be sure, is not entirely receptive to private fee arrangements. A statute requires that if a consumer contract imposes liability for attorneys' fees, the counterparty is also liable for fees to the same extent, regardless of whether the contract imposes such a liability.³⁰³ In other respects, however, New York generally leaves parties free to adopt "loser-pays" rules, "one-way" rules requiring only one of the contracting parties to pay the other's fees, or any other system they like, subject only to the general rules regarding enforcement of contracts.³⁰⁴

The rule is different in California. There, contracts containing one-way fee shifting provisions are reformed by statute to award fees to the prevailing party regardless of the nature of the parties.³⁰⁵ Unlike New York, therefore, California extends its contract-trumping attorneys' fee rule to *all* contracts, not just specified consumer contracts. Moreover, the state's courts broadly interpret California's statute, which is non-waivable, to apply to actions that "involve" a contract, even if not directly framed as actions for breach.³⁰⁶

³⁰³ N.Y. GEN. OBLIG. LAW § 5-327 (McKinney 2008) ("Whenever a consumer contract provides that the creditor, seller or lessor may recover attorney's fees and expenses incurred as the result of a breach of any contractual obligation by the debtor, buyer or lessee, it shall be implied that the creditor, seller or lessor shall pay the attorney's fees and expenses of the debtor, buyer or lessee incurred as the result of a breach of any contractual obligation by the creditor, seller or lessor, or in the successful defense of any action arising out of the contract commenced by the creditor, seller or lessor. Any limitations on attorney's fees recoverable by the creditor, seller or lessor shall also be applicable to attorney's fees recoverable by the debtor, buyer or lessee under this section. Any waiver of this section shall be void as against public policy.").

³⁰⁴ See *Chapel v. Mitchell*, 642 N.E.2d 1082, 1084 (N.Y. 1994) ("[A]ttorney's fees are incidents of litigation and a prevailing party may not collect them unless an award of such fees is authorized by an agreement between the parties, statute, or court rule." (emphasis added)) (quoting *Hooper Assocs. v. AGS Computers*, 548 N.E.2d 903, 904 (N.Y. 1989)); *In re A.G. Ship Maint. Corp. v. Lezak*, 503 N.E.2d 681, 683 (N.Y. 1986); *Mighty Midgets, Inc. v. Centennial Ins. Co.*, 389 N.E.2d 1080, 1085 (N.Y. 1979).

³⁰⁵ CAL. CIV. CODE § 1717(a) (West 2008) ("In any action on a contract, where the contract specifically provides that attorney's fees and costs, which are incurred to enforce that contract, shall be awarded either to one of the parties or to the prevailing party, then the party who is determined to be the party prevailing on the contract, whether he or she is the party specified in the contract or not, shall be entitled to reasonable attorney's fees in addition to other costs."). "[E]quitable considerations must prevail over both the bargaining power of the parties and the technical rules of contractual construction." *PLCM Group v. Drexler*, 997 P.2d 511, 515 (Cal. 2000) (quoting *Int'l Indus. v. Olen*, 577 P.2d 1031, 1034 (Cal. 1978)).

³⁰⁶ See *Dell Merk, Inc. v. Franzia*, 33 Cal. Rptr. 3d 694, 703 n.13 (Ct. App. 2005); *Cal. Wholesale Material Supply, Inc. v. Norm Wilson & Sons, Inc.*, 117 Cal. Rptr. 2d 390, 394 (Ct. App. 2002). The statute does not extend, however, to tort actions arising out of contract. *Reynolds Metals Co. v. Alpers*, 599 P.2d 83, 86 (Cal. 1979); *Excess Electronix v. Heger Realty Corp.*, 75 Cal. Rptr. 2d 376, 384 (Ct. App. 1998).

C. Arbitration Clauses

Both New York and California respect and enforce pre-dispute mandatory arbitration clauses. As between the two, however, New York is more deferential to the parties' choices.³⁰⁷

New York is positively disposed towards arbitration as a means for resolving disputes. This attitude is not unqualified: New York purports to prohibit mandatory arbitration clauses in contracts for the sale of consumer goods³⁰⁸ and services³⁰⁹ (although this rule may be unenforceable for contracts affecting interstate commerce).³¹⁰ In other respects, however, and especially in the case of commercial agreements, New York ranks among the national leaders in endorsing and enforcing arbitration agreements. New York was the first American state to legalize pre-dispute arbitration clauses;³¹¹ its arbitration act, adopted in 1920, was the model for the Federal Arbitration Act of 1925.³¹² Its courts have also long encouraged arbitration,³¹³ viewing the procedure as offering a speedy, flexible, inexpensive, and sophisticated means for resolving disputes.³¹⁴ New York enforces arbitration clauses even if a party alleges fraud in the underlying contract, unless the fraud is so pervasive as to constitute a "grand scheme" of which the arbitration agreement is a part.³¹⁵ Alleged violations of public policy rarely defeat

³⁰⁷ Arbitration clauses are important in commercial dealings, especially when international parties are involved, although they are used surprisingly infrequently in business-to-business contracts involving large public companies. See Theodore Eisenberg & Geoffrey P. Miller, *The Flight from Arbitration: An Empirical Study of Ex Ante Arbitration Clauses in the Contracts of Publicly Held Companies*, 56 DEPAUL L. REV. 335, 335 (2007).

³⁰⁸ N.Y. GEN. BUS. LAW § 399-c (McKinney 2008) ("No written contract for the sale or purchase of consumer goods . . . to which a consumer is a party, shall contain a mandatory arbitration clause.").

³⁰⁹ The term "consumer goods" includes "services purchased or paid for by a consumer, the intended use or benefit of which is intended for the personal, family or household purposes of such consumer." *Id.*

³¹⁰ See *Citizens Bank v. Alafabco, Inc.*, 539 U.S. 52, 55-56 (2003) (per curiam) (holding that the Federal Arbitration Act controls the issue of the enforcement of arbitration agreements in which the subject matter would have an effect on interstate commerce).

³¹¹ For background, see Geoffrey Miller & Theodore Eisenberg, *The Market for Contracts*, 30 CARDOZO L. REV. 2073 (2009).

³¹² See *id.*

³¹³ See *Smith Barney Shearson Inc. v. Sacharow*, 689 N.E.2d 884, 888 (N.Y. 1997) (noting that New York courts have "long promoted" liberal enforcement of agreements to arbitrate); *Weinrott v. Carp*, 298 N.E.2d 42, 47 (N.Y. 1973).

³¹⁴ See, e.g., *Sablosky v. Edward S. Gordon Co.* 535 N.E.2d 643, 646 (N.Y. 1989) ("Arbitrators customarily have an expertise over a particular subject matter and are able to offer parties a relatively expeditious and inexpensive forum to resolve their disputes."); *Weinrott*, 298 N.E.2d at 47 (N.Y. 1973) ("[A]rbitration's primary virtues . . . [include] speed and finality.").

³¹⁵ *Riverside Capital Advisors, Inc. v. Winchester Global Trust Co.*, 800 N.Y.S.2d 754, 756 (App. Div. 2005); *Amoroso v. Metropolitan Life Ins. Co.*, No. 104008/2007, 2008 WL 1724002, at *3 (N.Y. Sup. Ct. Apr. 14, 2008).

arbitration clauses in New York,³¹⁶ and then only for compelling reasons³¹⁷ such as the need to protect the integrity of criminal investigations,³¹⁸ to administer state antitrust law,³¹⁹ to manage insurance company insolvencies,³²⁰ or to maintain judicial scrutiny over tenure decisions for public school teachers.³²¹ Parties in New York are free to devise their own arbitration procedures, may contract for enhanced judicial review of arbitral awards,³²² and may adopt hybrids that combine elements of arbitration and litigation.³²³ New York does not require mutuality of remedy: A contract may require only one of the parties to arbitrate a dispute.³²⁴ New York also strictly limits judicial review of awards in the absence of agreements expanding such review;³²⁵ it requires confirmation unless an award violates a “strong public policy, is totally irrational or clearly exceeds a specifically enumerated limitation on the arbitrator’s power.”³²⁶

³¹⁶ See *United Fed’n of Teachers, Local 2 v. Bd. of Educ.*, 801 N.E.2d 827, 832 (N.Y. 2003) (“[T]he scope of the public policy exception to an arbitrator’s power to resolve disputes is . . . extremely narrow.”).

³¹⁷ See *Port Jefferson Station Teachers Ass’n v. Brookhaven-Comsewogue Union Free Sch. Dist.*, 383 N.E.2d 553, 554 (N.Y. 1978) (per curiam) (noting that when an arbitration agreement is invalidated on policy grounds, it is nearly always because an important constitutional or statutory duty or responsibility is involved); *Associated Teachers of Huntington, Inc. v. Bd. of Educ.*, 306 N.E.2d 791, 795 (N.Y. 1973) (“[An issue] interlaced with strong public policy considerations . . . [may be] placed beyond the reach of the arbitrator’s discretion.”).

³¹⁸ See *City of N.Y. v. Uniformed Fire Officers Ass’n, Local 854*, 739 N.E.2d 719, 722 (N.Y. 2000) (noting that enforcing arbitration clause could interfere with the ability of state officials to conduct a criminal investigation).

³¹⁹ *Aimcee Wholesale Corp. v. Tomar Prods., Inc.*, 237 N.E.2d 223, 224 (N.Y. 1968).

³²⁰ *Corcoran v. Ardra Ins. Co.*, 567 N.E.2d 969, 972-73 (N.Y. 1990).

³²¹ *Candor Cent. Sch. Dist. v. Candor Teachers Ass’n*, 366 N.E.2d 826, 828 (N.Y. 1977); *Cohoes City Sch. Dist. v. Cohoes Teachers Ass’n*, 358 N.E.2d 878, 880 (N.Y. 1976).

³²² See *Nab Constr. Corp. v. Metro. Transp. Auth. ex rel. N.Y. City Transit Auth.*, 579 N.Y.S.2d 375 (App. Div. 1992) (mem.).

³²³ See *Instructional Television Corp. v. Nat’l Broad. Co.*, 357 N.Y.S.2d 915 (App. Div. 1974) (mem.) (upholding arbitration solely of questions of fact, leaving application of law for judicial determination).

³²⁴ *Sablosky v. S. Gordon Co.*, 535 N.E.2d 643, 646 (N.Y. 1989).

³²⁵ See, e.g., *N.Y. State Corr. Officers & Police Benevolent Ass’n v. State*, 726 N.E.2d 462, 464, 467 (N.Y. 1999) (refusing to upset an award favoring policeman who had engaged in patently offensive, racially provocative public conduct).

³²⁶ *Town of Callicoon v. Civil Serv. Employees Ass’n*, 519 N.E.2d 300 (N.Y. 1987) (mem.). New York’s standard may be even more deferential than the “manifest disregard” rule under the Federal Arbitration Act. See *Wien & Malkin LLP v. Helmsley-Spear, Inc.* 783 N.Y.S.2d 339, 340-41, 343-44 (App. Div. 2004) (applying federal standard to reject an award, first upheld under New York’s standard for judicial review, on the ground that the arbitrators exhibited “manifest disregard” of the law), *rev’d*, 846 N.E.2d 1201 (N.Y. 2006); *N.Y. State Corr. Officers*, 726 N.E.2d at 465 (N.Y. 1999) (“[E]ven in circumstances where an arbitrator makes errors of law or fact, courts will not assume the role of overseers to conform the award to their sense of justice.”); *Allstate Ins. Co. v. Nicolosi*, 643 N.Y.S.2d 164, 165 (App. Div. 1996) (mem.) (“[A]n arbitrator’s interpretation may even disregard ‘the apparent, or even the plain, meaning of the words’ of the contract before him and still be impervious to challenge in the courts.” (quoting *Rochester City Sch. Dist. v. Rochester Teachers Ass’n*, 362 N.E. 977, 981 (N.Y. 1977))).

California courts, like their New York peers, endorse arbitration³²⁷ and recognize its advantages as a speedy and expeditious means to resolve disputes.³²⁸ Nonetheless, arbitration agreements face significant obstacles.³²⁹ Public policy provides a fruitful avenue for challenging arbitration agreements in California. Judicial-type procedures are required for arbitrations involving non-waivable rights; these procedures include discovery, written findings, remedies that would be available outside arbitration, and protection against forum costs.³³⁰ Party-crafted procedures and limitations of remedies that fail to afford the requisite procedural rights will be struck down.³³¹ California also frequently invalidates arbitration clauses on grounds of unconscionability. Clauses contained in contracts of adhesion are suspect, even if the party contesting enforcement knew of the general terms at the time of contracting³³² and enjoyed protections such as a cooling-off period.³³³ In contrast with New York, California rejects agreements deemed to lack mutuality if the result is to disadvantage the weaker party.³³⁴ Even clauses neutral on their face may be invalidated if their effect would be one-sided.³³⁵ California courts are also ill-

³²⁷ See, e.g., *Blake v. Ecker*, 113 Cal. Rptr. 2d 422, 432 (Ct. App. 2001) (“There is a strong public policy in favor of arbitration agreements.”).

³²⁸ See CAL. CIV. PRO. CODE § 1281 (West 2008) (“A written agreement to submit to arbitration an existing controversy or a controversy thereafter arising is valid, enforceable and irrevocable, save upon such grounds as exist for the revocation of any contract.”). California’s state tracks the language of the Federal Arbitration Act, 9 U.S.C. § 2 (2006), providing that arbitration agreements are “valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.” On the California courts’ sense of the virtues of arbitration, see, for example, *Vandenberg v. Superior Court*, 982 P.2d 229, 238 (Cal. 1999); *Adajar v. RWR Homes, Inc.*, 73 Cal. Rptr. 3d 17, 21 (Ct. App. 2008).

³²⁹ Many of the rules hostile to arbitration described in this paragraph are potentially vulnerable to challenge on grounds of pre-emption under the Federal Arbitration Act. See *Southland Corp. v. Keating*, 465 U.S. 1, 16 (1985) (holding that FAA preempts California rule prohibiting arbitration of claims under state franchise statute). As yet, however, the federal courts have not definitively addressed this matter. Cf. *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ.*, 489 U.S. 468, 478-89 (1989) (upholding anti-arbitration rule of California against pre-emption challenge on the ground that the parties had opted for the application of California law).

³³⁰ See *Armendariz v. Found. Health Psychcare Servs., Inc.*, 6 P.3d 669, 682 (Cal. 2000); *Abramson v. Juniper Networks, Inc.*, 9 Cal. Rptr. 3d 422, 433-34 (Ct. App. 2004).

³³¹ See *Armendariz*, 6 P.3d at 682 (requiring arbitration agreement not limit statutorily imposed remedies such as punitive damages and attorney fees); *Azteca Constr., Inc. v. ADR Consulting, Inc.*, 18 Cal. Rptr. 3d 142, 147-150 (Ct. App. 2004) (holding that statutory right to disqualify an arbitrator is not waivable).

³³² See *Kinney v. United HealthCare Servs., Inc.*, 83 Cal. Rptr. 2d 348, 353 (Ct. App. 1999).

³³³ See *Gentry v. Superior Court*, 165 P.3d 556, 571, 573-74 (Cal. 2007).

³³⁴ See *Armendariz*, 6 P.3d at 694 (“[A]n arbitration agreement imposed in an adhesive context lacks basic fairness and mutuality if it requires one contracting party, but not the other, to arbitrate all claims arising out of the same transaction or occurrence or series of transactions or occurrences.”). Many California cases are in accord. See, e.g., *Little v. Auto Stiegler, Inc.*, 63 P.3d 979, 985 (Cal. 2003); *Abramson*, 9 Cal. Rptr. at 422, 436-47; *O’Hare v. Mun. Res. Consultants*, 132 Cal. Rptr. 2d 116, 121-25 (Ct. App. 2003).

³³⁵ See *Saika v. Gold*, 56 Cal. Rptr. 2d 922, 923 (Ct. App. 1996) (invalidating provision that

disposed toward attempts by parties to “home-make” procedures in arbitration, at least when the assistance of the judiciary is required; thus, clauses providing for enhanced judicial review of arbitral awards may not be respected.³³⁶ While the foregoing rules have primarily been developed in the employment context, they appear transferable to other settings, especially where important statutory or common-law rights are involved.³³⁷

D. *Class Action Waivers*

Waivers of aggregate dispute resolution (class actions and class-wide arbitration) are closely interwoven with the issues concerning enforcement of arbitration agreements discussed in the previous section. The reason is that arbitration clauses can also operate as de facto waivers of aggregate dispute resolution. However, the issues are conceptually distinct insofar as arbitration agreements occur in many situations where aggregate treatment is not feasible and aggregate dispute resolution waivers can be included in contracts without an arbitration clause.³³⁸ New York and California adopt different approaches to such waivers. In New York they are presumptively valid and regularly enforced against claims that they are unconscionable or violate public policy.³³⁹ California, in contrast, generally invalidates

allowed either party to reject an arbitration award of \$25,000 or greater and obtain trial de novo in court, on ground that the clause would only serve the interests of the health care provider).

³³⁶ See *Crowell v. Downey Cmty. Hosp. Found.*, 115 Cal. Rptr. 2d 810, 815-17 (Ct. App. 2002); *Old Republic Ins. Co. v. St. Paul Fire & Marine Ins. Co.*, 53 Cal. Rptr. 2d 50, 53 (Ct. App. 1996).

³³⁷ See *Duffens v. Valenti*, 74 Cal. Rptr. 3d 311, 326-27 (Ct. App. 2008) (striking arbitration clause in dating service contract that violated statute); *Baker v. Osborne Dev. Corp.*, 71 Cal. Rptr. 3d 854, 864 (Ct. App. 2008) (striking one-sided arbitration agreement between builder and home purchaser); *Higgins v. Superior Court*, 45 Cal. Rptr. 3d 293, 304-05 (Ct. App. 2006); *Sehulster Tunnels v. Traylor Bros. Inc.*, 4 Cal. Rptr. 3d 655, 667 (Ct. App. 2003) (refusing to enforce arbitration contract between general contractor and subcontractor that violated fundamental notions of fairness); *Goodrich, Goodyear & Hinds v. Conkle & Oleston*, No. G028844, 2002 WL 2005678, at *4 (Cal. Ct. App. Aug. 29, 2002). *But see* *Greenbriar Homes Cmty., Inc. v. Superior Court*, 11 Cal. Rptr. 3d 371, 375 (Ct. App. 2004) (upholding arbitration clause that required consumers to share forum costs).

³³⁸ For general treatment of the issues, and a discussion of class-wide arbitration, see Jean R. Sternlight & Elizabeth J. Jensen, *Arbitration to Eliminate Consumer Class Actions: Efficient Business Practice or Unconscionable Abuse?*, 67 LAW & CONTEMP. PROBS. 75 (2004); Jean R. Sternlight, *As Mandatory Binding Arbitration Meets the Class Action, Will the Class Action Survive?*, 42 WM. & MARY L. REV. 1 (2000). For an empirical study providing evidence that companies use arbitration clauses in order to thwart consumer class actions, see Theodore Eisenberg, Geoffrey P. Miller & Emily L. Sherwin, *Arbitration's Summer Soldiers: An Empirical Study of Arbitration Clauses in Consumer and Nonconsumer Contracts* (unpublished manuscript, on file with the author).

³³⁹ See *Ranieri v. Bell Atl. Mobile*, 759 N.Y.S.2d 448, 449 (App. Div. 2003) (“[G]iven the strong public policy favoring arbitration, and the absence of a commensurate policy favoring

these clauses on grounds of public policy or unconscionability.³⁴⁰

VIII. EXTRA-CONTRACTUAL LIABILITIES

Litigants who face difficulties prevailing on contract theories, or who seek damages greater than those available for breach, often frame their actions under some non-contractual theory: tort (fraud in the inducement, negligent misrepresentation, conversion); quasi-contract (unjust enrichment); equitable remedies (constructive trust or quantum meruit); or statutory rights (e.g., unfair business practice laws).³⁴¹ Both New York and California resist attempts to substitute a tort regime for contract remedies, but New York more consistently requires litigants to seek remedies under contract law.

New York courts regularly rebuff attempts to couch contract and contract-related actions as torts or equitable remedies; they require that some legal duty separate from the contract must be infringed before extra-contractual relief will be granted.³⁴² New York rejects contract-based claims of unjust enrichment, either for failed preliminary negotiations³⁴³ or breach of an executed contract.³⁴⁴ Employees

class actions, we are in accord with authorities holding that a contractual proscription against class actions, such as contained in the Agreements, is neither unconscionable nor violative of public policy.” (citations omitted)); *Flynn v. Labor Ready, Inc.*, 751 N.Y.S.2d 722 (Sup. Ct. 2002) (“The fact that a class action lawsuit, as plaintiffs contemplate, may be a less costly alternative to arbitration (which is generally less costly than litigation) does not alter the binding effect of the valid arbitration clause . . .”), *aff’d as modified*, 775 N.Y.S.2d 357, 359 (App. Div. 2004).

³⁴⁰ See *Gentry v. Superior Court*, 165 P.3d 556, 568 (Cal. 2007) (holding that class arbitration waivers in employment agreements could not be enforced if class arbitration would be significantly more effective way of vindicating rights); *Discover Bank v. Superior Court*, 113 P.3d 1100, 1110 (Cal. 2005) (holding class action waiver unenforceable under California law when it is found in consumer contracts of adhesion and acts to exculpate party from alleged willful misconduct); *Gatton v. T-Mobile USA, Inc.*, 61 Cal. Rptr. 3d 344, 356-58 (Ct. App. 2007) (invalidating class action waiver as unconscionable), *cert. denied*, 128 S. Ct. 2501 (U.S. 2008); *Lee v. AT & T Wireless Servs., Inc.*, No. B186240, 2006 WL 1452936, at *4-5 (Cal. Ct. App. May 26, 2006); *Klussman v. Cross Country Bank*, 36 Cal. Rptr. 3d 728, 739, 741 (Ct. App. 2005); *Aral v. Earthlink, Inc.*, 36 Cal. Rptr. 3d 229, 238 (Ct. App. 2005); *Am. Online, Inc. v. Superior Court*, 108 Cal. Rptr. 2d 699, 710-12 (Ct. App. 2001) (rejecting choice-of-law and forum selection clauses that would have precluded class action treatment under California consumer protection law).

³⁴¹ For a general analysis focusing on the tort of promissory fraud, see Kevin E. Davis, *Promissory Fraud: A Cost-Benefit Analysis*, 2004 WIS. L. REV. 535 (2004).

³⁴² See *Clark-Fitzpatrick, Inc. v. Long Island R.R.*, 516 N.E.2d 190, 193-94 (N.Y. 1987); *Megarix Furs, Inc. v. Gimbel Bros., Inc.*, 568 N.Y.S.2d 581, 583 (App. Div. 1991).

³⁴³ See *Chatterjee Fund Mgmt., L.P. v. Dimensional Media Assocs.*, 687 N.Y.S.2d 364 (App. Div. 1999) (mem.).

³⁴⁴ *Clark-Fitzpatrick*, 516 N.E.2d at 193 (N.Y. 1987) (“It is impermissible . . . to seek damages in an action sounding in quasi contract where the suing party has fully performed on a valid written agreement, the existence of which is undisputed, and the scope of which covers the dispute between the parties.”); see *Cooper, Bamundo, Hecht, & Longworth, LLP v. Kuczinski*,

claiming that their employers tortiously interfered with contractual relations are summarily shown the door.³⁴⁵ New York courts sometimes recognize claims for fraud in the inducement,³⁴⁶ but they require more than the allegation that the defendant did not intend to perform his promises.³⁴⁷ Although the line between allegations that merely duplicate contract claims and those that set forth a separate cause of action is sometimes thin, it appears that the New York courts require the plaintiff both seek different relief³⁴⁸ and make specific factual allegations separate from those associated with the contract.³⁴⁹ New York also generally accepts contractual limitations of fraud liability, including clauses that disclaim reliance on statements or representations not contained in the written agreement.³⁵⁰ A New York court might well dismiss claims of fraud, even in the absence of a no-reliance clause, if the alleged misrepresentation is contrary to the terms of the express contract.³⁵¹

789 N.Y.S.2d 508, 510 (App. Div. 2005).

³⁴⁵ *Negron v. JP Morgan Chase/Chase Manhattan Bank*, 789 N.Y.S.2d 257 (App. Div. 2005).

³⁴⁶ *See, e.g., Black Rock, Inc. v. Z Best Car Wash, Inc.*, 809 N.Y.S.2d 918 (App. Div. 2006); *Sterling Nat'l Bank v. Chang*, No. 570513/05, 2005 WL 3313023 (N.Y. App. Div. Dec. 7, 2005) (per curiam); *Zaro Bake Shop, Inc. v. David*, 574 N.Y.S.2d 803 (App. Div. 1991) (mem.); *Imaging Int'l v. Hell Graphic Sys., Inc.*, No. 005062/1992, 2007 WL 3227245, at *1 (N.Y. Sup. Ct. Oct. 29, 2007).

³⁴⁷ *See Rong Rong Jiang v. Tan*, 783 N.Y.S.2d 557, 557 (App. Div. 2004) (“[A] contract action cannot be converted into one for fraud by merely alleging that the contracting party did not intend to satisfy a contractual obligation.”); *Coppola v. Applied Elec. Corp.*, 732 N.Y.S.2d 402 (App. Div. 2001); *Egan v. N.Y. Care Plus Ins. Co.*, 716 N.Y.S.2d 430, 431-32 (App. Div. 2000); *Page v. Muze, Inc.*, 705 N.Y.S.2d 383 (App. Div. 2000) (mem.); *Morgan v. A.O. Smith Corp.*, 697 N.Y.S.2d 152 (App. Div. 1999) (mem.); *Steinberg v. DiGeronimo*, 680 N.Y.S.2d 93 (App. Div. 1998) (mem.); *Alamo Contract Builders, Inc. v. CTF Hotel Co.*, 663 N.Y.S.2d 42 (App. Div. 1997) (mem.); *Modell's N.Y. Inc. v. Noodle Kidoodle, Inc.*, 662 N.Y.S.2d 24, 26 (App. Div. 1997) (holding that “mere . . . allegations that the contracting parties did not intend to meet their contractual obligations” are insufficient to state a claim for fraud in the inducement (quoting *Devlin v. 645 First Ave. Manhattan Co.*, 645 N.Y.S.2d 476 (App. Div. 1996))); *Rockefeller Univ. v. Tishman Constr. Corp. of N.Y.*, 659 N.Y.S.2d 460, 462 (App. Div. 1997) (mem.) (holding that a building owner’s fraudulent misrepresentation claims against a construction company were duplicative of the owner’s breach of contract cause of action, so as to warrant dismissal of the fraud claims, where identical contractual benefit-of-the-bargain recovery was sought); *Weitz v. Smith*, 647 N.Y.S.2d 236 (App. Div. 1996) (mem.); *Rocco v. Town of Smithtown*, 645 N.Y.S.2d 187 (App. Div. 1996) (mem.), *appeal dismissed*, *Rocco v. Town of Smithtown*, 674 N.E.2d 338 (N.Y. 1996); *CBW Fin. Corp. v. Computer Consoles, Inc.*, 504 N.Y.S.2d 179, 182 (App. Div. 1986) (holding promises to develop a new computer system subject to contract law rather than fraud concepts); *Chase v. United Hosp.*, 400 N.Y.S.2d 343 (App. Div. 1977) (holding allegation that defendant never intended to honor contractual promise insufficient to make out a claim of fraud in the inducement).

³⁴⁸ *See Rockefeller*, 659 N.Y.S.2d at 462 (rejecting tort claim where contractual benefit-of-the-bargain recovery was sought).

³⁴⁹ *Gotham Boxing Inc. v. Finkel*, No. 601497/2007, 2008 WL 104155, at *9 (N.Y. Sup. Ct. 2008) (summarizing cases).

³⁵⁰ *See Stanley v. Bray Terminals, Inc.*, 197 F.R.D. 224, 228 (N.D.N.Y. 2000).

³⁵¹ *Stone v. Schulz*, 647 N.Y.S.2d 822 (App. Div. 1996); *In re N. Hills Office Servs. v. Bevona*, 635 N.Y.S.2d 16 (App. Div. 1995); *Pinney v. Beckwith*, 608 N.Y.S.2d 738, 739 (App. Div. 1994).

California law is more receptive to the alchemy of transmuted contract claims into torts. Generally a claimant can make such tort claims in three circumstances:

[T]he breach is accompanied by a traditional common law tort, such as fraud or conversion; the means used to breach the contract are tortious, involving deceit or undue coercion; or one party intentionally breaches the contract intending or knowing that such a breach will cause severe, unmitigable harm in the form of mental anguish, personal hardship, or substantial consequential damages.³⁵²

While this formulation appears forbidding, it does not bar actions for fraud in the inducement that overlap contract claims.³⁵³ In *Linza v. Diamond Center, Inc.*,³⁵⁴ for example, a California court upheld a fraud claim based on allegations that the defendant, plaintiff's employer, had promised a bonus without intending to pay it.³⁵⁵ The same court held that punitive damages were available under the tort claim, even though they would be barred in an action for breach of contract, if the defendant acted with the requisite degree of fault.³⁵⁶ California also makes other non-contractual remedies available. Its judges do not enforce a cause of action for negligent breach of contract,³⁵⁷ yet they recognize that parties to a contract have a duty to perform their obligations with reasonable care, skill, expedience, and faithfulness.³⁵⁸ Accordingly, the "same wrongful act may constitute both a breach of contract and an invasion of an interest protected by the law of torts."³⁵⁹ A negligence claim may not survive if it merely replicates allegations of contractual breach; it may succeed, however, if the plaintiff includes relevant allegations that are not fairly encompassed in the contract claim.³⁶⁰ California is also receptive to claims of unjust enrichment associated with breaches of

³⁵² *Erlich v. Menezes*, 981 P.2d 978, 984 (Cal. 1999) (numbering omitted) (quoting *Freeman & Mills v. Belcher Oil Co.*, 900 P.2d 669, 681 (Cal. 1995)).

³⁵³ For decisions allowing such overlapping claims, see, for example, *Baker v. Superior Court*, 197 Cal. Rptr. 480, 483 (Ct. App. 1983); *Glendale Fed. Sav. & Loan Ass'n v. Marina View Heights Dev. Co.*, 135 Cal. Rptr. 802, 823 (Ct. App. 1977); *Symcox v. Zuk*, 34 Cal. Rptr. 462, 466-67 (Ct. App. 1963).

³⁵⁴ 2005 WL 3560800 (Cal. Ct. App. Dec. 30, 2005) (No. A101407, 2005 term; renumbered No. A101408, 2006 term).

³⁵⁵ *Id.* at *6-8.

³⁵⁶ *See id.* at *9.

³⁵⁷ *Erlich*, 981 P.2d at 983.

³⁵⁸ *Moreno v. Sanchez*, 131 Cal. Rptr. 2d 684, 692 (Ct. App. 2003) (home inspection services); *N. Am. Chem. Co. v. Superior Court*, 69 Cal. Rptr. 2d 466, 470 (Ct. App. 1997); *Allred v. Bekins Wide World Van Serv., Inc.*, 120 Cal. Rptr. 312, 315 (Ct. App. 1975) (moving services); *Roscoe Moss Co. v. Jenkins*, 130 P.2d 477, 482 (Cal. Dist. Ct. App. 1942) (well drilling).

³⁵⁹ *N. Am. Chem. Co.*, 69 Cal. Rptr. 2d at 774.

³⁶⁰ *See Freeman & Mills, Inc. v. Belcher Oil Co.*, 900 P.2d 669, 674 (Cal. 1995); *Applied Equip. Corp. v. Litton Saudi Arabia Ltd.*, 869 P.2d 454 (Cal. 1994); *Stop Loss Ins. Brokers, Inc. v. Brown & Toland Med. Group*, 49 Cal. Rptr. 3d 609, 614 (Ct. App. 2006); *Benavides v. State Farm Gen. Ins. Co.*, 39 Cal. Rptr. 3d 650, 657 (Ct. App. 2006); *Moreno*, 131 Cal. Rptr. 2d at 698.

contract: There does not appear to be any general prohibition against awarding damages for unjust enrichment in a contract case, so long as the requirements for that remedy are otherwise met.³⁶¹

CONCLUSION

New York's contract jurisprudence is formalistic, literalistic, nonjudgmental, and deferential to the freedom of parties to bargain for mutual advantage. The job of the courts is not to intrude into the contractual relationship but rather to enforce the deal the parties actually struck. To this end New York courts place a high value on clarity and predictability, especially in commercial contracts: Courts enforce contracts as written and do not reform or reject them to satisfy ideas of fairness or equity. They disfavor doctrines such as promissory estoppel and unjust enrichment. They reject, in favor of contract remedies, tort actions that duplicate breach of contract claims.

California law differs in spirit, nuance, and detail. California judges are more concerned with defining relationships among the parties on the basis of fairness, equity, and the public interest. California courts are more willing to impose obligations on the basis of preliminary negotiations; to reject bargains deemed unfair to one of the parties; to repudiate contracts on grounds of duress, unconscionability, or mistake; to consider evidence on contractual meaning from outside the four corners of the document; and to ignore the parties' choices of law or forum, waivers of jury trial, allocations of attorneys' fees, agreements to arbitrate disputes, and waivers of aggregate dispute resolution. Extra-contractual liabilities based on tort theories are more available in California than in New York. Overall, California administers a regime of contract law that, compared with New York, places greater emphasis on context, morality, and fairness and gives less importance to the written agreement of the parties. The purpose of this Article has been to identify these differences and to suggest that the demonstrated preference of sophisticated contracting parties for the more formalistic New York approach may provide evidence on basic questions of contract theory.

³⁶¹ See *Middleton v. L&J Assets, LLC*, No. B198133, 2008 WL 2764582, at *3 (Cal. Ct. App. July 17, 2008).