Bargaining on the Red-eye: New Light on Contract Theory

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Bargains on the Red-eye: 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 paper 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, is more willing to reform 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.
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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. Such firms are better off, according to this theory, when courts interpret contracts according to their terms and do not attempt to substitute their own concepts of reasonableness or fair dealing for bargains actually struck.

This theoretical work challenges conventional views in contract scholarship that favor looser, more contextual approaches. 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 which deviate, in some respects, from the more nuanced approach that would apply if the disputing parties brought their controversy before a court. Bernstein’s work suggests that industry actors,

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3 For discussion of the “new formalism” in contract theory, see Avery Katz, The Economics of Form and Substance in Contract Interpretation, 104 Colum. L. Rev. 496. 496-501 (2004) (distinguishing between “formalistic” and “substantive” approaches); 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).

4 In a study that complements the Schwartz-Scott theory, Avery Katz argues that formalistic rules may be useful for commercial parties which tend to be repeat players or have good (and relatively symmetric) information about the costs and benefits of performance. Avery Katz, The Economics of Form and Substance in Contract Interpretation, 104 Colum. L. Rev. 496 (2004). 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 context of individual transactions.

5 See Katz, supra note __, at 498 (“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”).

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.

The present paper 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. 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. 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.

This contrast between California and New York 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. And because the contracts in the Eisenberg-Miller study were, by definition, important to the financial results of large corporations, it can be presumed that they received scrutiny from well-qualified attorneys. Accordingly, there is reason to believe that, compared with California, New York may provide the more efficient regime

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8 The sample was taken from Form 8K reports, which are filed in connection with material events in the financial affairs of reporting companies.
for interpreting and enforcing commercial agreements.\(^9\) Analysis of the relevant differences between the two states’ contract law could then provide information on optimal contract rules.

This paper 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 which occasionally trump private agreements. Each state’s law grows out of 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 rewrite contracts to make them fairer or more equitable, and they look to the written agreement as the definitive source of interpretation. California, on the other hand, is more willing to reform or reject contracts in the service of morality or public policy; it places less emphasis on the written agreement of the parties and seeks instead to identify the contours of their commercial relationship within a broader context framed by principles of reason, equity and substantial justice.

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\(^9\) This observation is in line with Katz’s argument that sophisticated parties have the ability, by choice of law and forum and other strategies, to select the level of formalism that maximizes the value of their transactions. See Avery Katz, The Economics of Form and Substance in Contract Interpretation, 104 Colum. L. Rev. 496 (2004).
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.\textsuperscript{10}

II. General Approach

\textsuperscript{10} 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 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. These theories are discussed at length in Theodore Eisenberg & Geoffrey Miller, The Flight to New York, An Empirical Study of Choice of Law and Choice of Forum Clauses in Publicly-Held Companies’ Contracts, \textit{__} Cardozo Law Review \textit{__} (forthcoming 2009). Firms may select New York law and forum because of effective marketing and branding rather than any fundamental benefits offered by that state. See Theodore Eisenberg & Geoffrey Miller, The Market for Contracts, \textit{__} Cardozo Law Review \textit{__} (forthcoming 2009). 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 treatments of boilerplate, see, e.g., Omri Ben-Shahar, ed., Boilerplate: The Foundation of Market Contracts (2007); Omri Ben-Shahar, Forward: Freedom from Contract, 2004 Wis. L. Rev 261, 263 (2004); Omri Ben-Shahar, Forward: Freedom from Contract, 2004 Wis. L. Rev 261, 263 (2004); Stephen J. Choi & G. Mitu Gulati, Innovation in Boilerplate Contracts: An Empirical Examination of Sovereign Bonds, 53 Emory L.J. 929 (2004); David Gil\& 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.
Both New York and California recognize freedom of contract as fundamental although limited, at times, by other values. As between the two states, however, New York gives 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. New York’s tenderness for freedom of contract expresses itself, at times, in a seemingly atavistic pleasure in imposing the consequences of bad bargains. Thus, we are told that New York courts may not “alter the contract to reflect . . . personal notions of fairness and equity,” or reform a transaction to accomplish “notions of abstract justice or moral obligation.” Nor will morally 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. And New York’s reverence for freedom of contract is not waning; if


New York: New York courts are, if anything 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., 224 N.Y. 47, 51, 120 N.E. 86, 87 (N.Y. 1918) (“[t]he 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.”).

12 See, e.g., Zomba Recording LLC v. Williams, 15 Misc.3d 1118(A), 839 N.Y.S.2d 438 (Table) (N.Y. Sup. 2007).

13 Janian v. Barnes, 294 A.D.2d 787 (3rd Dept. 2002) (prudence or fairness of a contract is not the subject of judicial scrutiny in the absence of fraud or unconscionability); Dafnos v. Hayes, 264 A.D.2d 305 (3rd Dept. 1999) (same).


17 Jordan Panel Systems Corp. v. Turner Const. Co., 45 A.D.3d 165, 198, 841 N.Y.S.2d 561 (1st Dept. 2007) (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.”)
anything, the courts of that state are becoming even more inclined than heretofore to
deer to private agreements.\textsuperscript{18}

California courts rarely trumpet the virtues of holding parties to the consequences
of foolish bargains. California’s allegiance to freedom of contract, moreover, is
frequently tempered with concern for other values – providing compensation for harm,\textsuperscript{19}
facilitating job mobility,\textsuperscript{20} protecting parties against extortionate damages,\textsuperscript{21} preventing
“inequitable or unequal exchanges,”\textsuperscript{22} ensuring access to a civil jury,\textsuperscript{23} protecting
policyholders injured by uninsured motorists\textsuperscript{24} – even safeguarding the legislature’s
choice of venue for litigation.\textsuperscript{25} Unlike New York, California does not sharply
distinguish between consumer and commercial contracts, thus subjecting even business-
to-business contracts to potential invalidation or reform on ground of fairness, equity, or
substantial justice.\textsuperscript{26} Backing this complex structure of agreement-trumping policies is a
strong norm in California against waiver of rules implicating the public interest.\textsuperscript{27}

\textsuperscript{18} See, e.g., Zarsky v. Law Office of Maury B. Josephson, 14 Misc.3d 1207(A), 831 N.Y.S.2d 363
(Table) (N.Y.City Civ.Ct. 2006).
\textsuperscript{19} See City of Santa Barbara v. Superior Court, 41 Cal.4th 747, 754 n.5, 161 P.3d 1095 (Cal. 2007).
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).
\textsuperscript{21} See Calif. Civ. Code § 3358 (“[e]xcept 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.”)
\textsuperscript{22} See, e.g., Rich & Whillock, Inc. v. Ashton Development, Inc., 157 Cal.App.3d 1154, 204
Cal.Rptr. 86 (4th Dist. 1984) (“[o]n 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.”)
\textsuperscript{23} See Grafton Partners L.P. v. Superior Court, 36 Cal.4th 944, 116 P.3d 479 (Cal. 2005).
\textsuperscript{25} See Arntz Builders v. Superior Court, 122 Cal.App.4th 1195, 19 Cal.Rptr.3d 346 (1st Dist. 2004).
\textsuperscript{26} 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 notes __-__
and accompany text, infra.
\textsuperscript{27} See Cal. Civ. Code § 3513 (“[a]nyone 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. Both states require more than mere participation in contract negotiations in order to establish a legal obligation. Agreements to agree are not enforceable in either state. 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.* 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.” 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. 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

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bound;\textsuperscript{31} and the subject of negotiation must be both specific and backed by ascertainable indications of intent regarding the anticipated outcome of the process.\textsuperscript{32}

Recent California cases also recognize an obligation to negotiate in good faith. In \textit{Copeland v. Baskin Robbins U.S.A.},\textsuperscript{33} 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. After protracted discussions the defendant announced that it was terminating negotiations. 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.\textsuperscript{34} Although \textit{Copeland} appears similar to the \textit{Wolf} case, it is potentially broader in scope. The parties in \textit{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. 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.\textsuperscript{35} 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 will resist enforcing a contract if the parties intended to embody their

\begin{itemize}
\item \textsuperscript{31} See Teachers Ins. and Annuity Ass’n v. Tribune Co., 670 F.Supp. 491 (S.D.N.Y. 1987).
\item \textsuperscript{32} See L-3 Communications Corp. v. OSI Systems, Inc., 2004 WL 42276 (S.D.N.Y. 2004).
\item \textsuperscript{33} 96 Cal.App.4th 1251, 1255, 117 Cal.Rptr.2d 875 (2nd Dist. 2002).
\item \textsuperscript{34} The \textit{Copeland} decision has been followed by a number of other decisions. See, e.g., Coachella Valley Water Dist. v. Imperial Irr. Dist., 2007 WL 2822766 (4th Dist. 2007).
\item \textsuperscript{35} See, e.g., Rochlis v. Walt Disney Co., 19 Cal.App.4th 201 (1993)
\end{itemize}
agreement in a written form which was never executed. 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. In *Baird v. Gimbel Brothers, Inc.*, a well-known New York case, a general contractor obtained a contract in reliance on a subcontractor’s bid which was withdrawn prior to acceptance. The New York Court of Appeals rejected the contractor’s claim against the subcontractor: the parties had made no binding agreement and a theory of promissory estoppel could not fix the defect. Several New York decisions have subsequently endorsed the idea of promissory estoppel liability for subcontractor bids, but as yet New York has not definitively rejected the rule of the *Gimbel* case. Even when New York courts use promissory estoppel to impose liability for preliminary negotiations, moreover, the doctrine is hedged by limitations and qualifications. The promise on which the estoppel

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36 See, e.g., 1130 President St. Corp. v. Bolton Realty Corp., 300 N.Y. 63, 68, 89 N.E.2d 16 (N.Y. 1949) (phrase “Make up drawing”, which required further negotiations on the renovations plaintiff desired, rendered contract unenforceable); Chatterjee Fund Management, L.P. v. Dimensional Media Associates, 260 A.D.2d 159, 687 N.Y.S.2d 364 (1st Dept. 1999) (even if the parties agree to all essential terms, contract was not enforceable so long as the agreement has not been finalized with a sufficient manifestation of consent to the entire package.); Jordan Panel Systems Corp. v. Turner Const. Co., 45 A.D.3d 165, 841 N.Y.S.2d 561 (1st Dept. 2007); R.G. Group, Inc. v. Horn & Hardart Co., 751 F.2d 69, 75 (2d Cir. 1984) (“when a party gives forthright, reasonable signals that it means to be bound only by a written agreement, courts should not frustrate that intent.”).


38 64 F.2d 344 (2d Cir. 1933).


is based must be clear and unambiguous and cannot be established solely by course of conduct or vague reassurances. Promissory estoppel is unavailable in New York when the evidence shows that the parties intended not to be bound until the execution of a written document. Integration or merger clauses stipulating that the written document is the complete agreement of the parties will ordinarily preclude the use of promissory estoppel. The injury to the party claiming estoppel must be so severe as to be considered unconscionable. All the elements of a promissory estoppel claim must be specifically pleaded. 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, \textit{Drennan v. Star Paving Co.}, the California Supreme Court reached a result directly contrary to \textit{Baird v. Gimbel}, holding that promissory estoppel could substitute for consideration in situations where a contractor reasonably relied on a subcontractor’s bid. Subsequent California decisions have generalized this principle to other situations.

\begin{itemize}
  \item[49] The disagreement between the California and New York courts has provoked extensive scholarly commentary. See, e.g, J. Feinman, Promissory Estoppel and Judicial Method, 97 Harv.L.Rev. 678, 680-81,
in which reasonable reliance substitutes for a defect in contract formation. To be sure, California also limits the scope of promissory estoppel: there must be a clear and unambiguous promise\(^{50}\) rather than vague assurances;\(^{51}\) the promisor must reasonably expect the statement to induce reliance;\(^{52}\) the plaintiff must actually rely on the promise;\(^{53}\) the plaintiff must incur damage stemming from the reliance;\(^{54}\) and all the elements must be pleaded.\(^{55}\) Nevertheless it is clear that promissory estoppel will be available to enforce promises in California in situations where it will not be available in New York. Unconscionable injury is not usually required, for example, and the presence of a written agreement poses 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\(^{56}\) even at the expense of increasing the risk that parties will be trapped in unanticipated contractual obligations.

**B. Consideration**

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\(^{51}\) See Goines v. Wilkes, 2007 WL 1040979 (2d Dist. 2007).


\(^{54}\) See Massey v. Los Angeles Unified School Dist., 2008 WL 570792 (2\(^{nd}\) Dist. 2008).

\(^{55}\) See Smith v. City and County of San Francisco, 225 Cal.App.3d 38, 48, 275 Cal.Rptr. 17 (1\(^{st}\) Dist. 1990).

\(^{56}\) 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 Mobilehome Owners Assn. v. City of Poway, 149 Cal.App.4th 1460, 1470-1471 (4\(^{th}\) Dist. 2007), preserve “equity,” C & K Engineering Contractors v. Amber Steel Co., 23 Cal.3d 1, 6, 587 P.2d 1136, 151 Cal.Rptr. 323 (Cal. 1978), and do “right and justice,” Toscano v. Greene Music, 124 Cal.App.4th 685, 21 Cal.Rptr.3d 732 (4\(^{th}\) Dist. 2004). See Restatement (Second) of Contracts § 90(1): “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.”
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.\(^57\)

Again, however, a closer investigation reveals differences. New York adheres to traditional rules under which past consideration or moral obligation do not qualify.\(^58\) On the other hand, New York allows greater flexibility when a written instrument is involved. Recitals of “value received” are nearly conclusive evidence of consideration.\(^59\)

And the New York legislature has dispensed with the consideration requirement altogether for certain documents which appear frequently in business transactions. Promises based on past consideration or antecedent obligation, unenforceable if made orally, are binding if in writing and signed by the responsible party.\(^60\) So are modifications or releases,\(^61\) irrevocable assignments,\(^62\) firm offers,\(^63\) rewards for return of lost property,\(^64\) and certain promises by grantors of interests in real property.\(^65\)

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\(^{60}\) See N.Y. Gen. Obl. Law § 5-1105 (“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. City Bank v. Valentine, 61 Misc.2d 554, 306 N.Y.S.2d 227 (N.Y. Sup. 1969). The new promise must be in writing; an antecedent debt is not sufficient consideration for an oral promise. Beinett v. Becker, 34 A.D.3d 406, 824 N.Y.S.2d 155 (2nd Dept. 2006).

\(^{61}\) See N.Y. Gen. Obl. Law § 5-1103 (“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
California recognizes a moral element in consideration to a greater extent than New York. The traditional rules have been modified to enforce promises based on antecedent debts or obligations discharged in bankruptcy or barred by the statute of frauds or a statute of limitations. Conversely, value that would otherwise qualify as consideration does not support a contract if it is “contrary to good morals.” California also will not grant specific performance if the breaching party has not received “adequate consideration,” or if the contract is “not, as to him, just and reasonable.” Consideration here means more than the consideration to support a simple contract; the value conferred must be “fair and adequate.”

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. Matter of Maurer v. Erdheim, 292 A.D.2d 455, 738 N.Y.S.2d 885 (2nd Dept. 2002); Federal Deposit Ins. Corp. v. Hyer, 66 A.D.2d 521, 528-529, 413 N.Y.S.2d 939 (2nd Dept. 1979).

62   See N.Y. Gen. Obl. Law § 5-1107 (“a[n] 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.”)

63   See N.Y. Gen. Obl. Law § 5-1109 (except for merchant transactions under the UCC, “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.”)

64   See N.Y. Gen. Obl. Law § 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.”)

65   See N.Y. Gen. Obl. Law § 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, 135 A.D.2d 692, 522 N.Y.S.2d 591 (2nd Dept. 1987).

66   See Cal. Civ. Code § 1616 (“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.”).


68   Cal. Civ. Code § 3391 (specific performance is not available unless the defendant “received an adequate consideration for the contract”.)

69   Trup v. Manock, 2008 WL 889425 (4th Dist. 2008). 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.
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 weight but are never conclusive. Irrevocable options and firm offers, contract modifications, and other signed commitments enforceable in New York without consideration appear to require consideration under all circumstances in California. Overall, as compared with New York, California’s rules on consideration offer somewhat 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 which is both irreparable and of such magnitude that the victim is effectively deprived of free will. Mere financial pressure, even if

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70 Cal. Civ. Code § 1614 ("A written instrument is presumptive evidence of a consideration.")
71 Cal. Evid. Code § 622 ("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).
73 See Krobitsch v. Middleton, 72 Cal.App.2d 804, 165 P.2d 729 (1st Dist. 1946). Cal. Civ. Code § 1698(a), 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, especially since § 1698(c) specifically requires consideration for oral modifications of written contracts. The cases, however, does not appear to have endorsed this view.
“relentless,”\textsuperscript{76} is not enough; nor is duress present if the party experiencing the pressure has available means for response.\textsuperscript{77} The threat, moreover, must be intrinsically wrongful:\textsuperscript{78} a contract is not subject to challenge if the threatened action is something that the alleged wrongdoer was legally entitled to do.\textsuperscript{79} Even if an agreement is procured by duress, moreover, the victim must act promptly to repudiate it or suffer an inference of ratification;\textsuperscript{80} New York courts are not receptive to arguments that it is unfair to force a victim to elect promptly between accepting the benefit of contract procured through duress, however inadequate, or incurring the risk and expense of challenging the conditions under which the contract was made.\textsuperscript{81} California also recognizes a defense of duress.\textsuperscript{82} 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.\textsuperscript{83} Also, as in New York, the party

\begin{footnotesize}
\textsuperscript{81} See EEOC v. American Express Pub. Corp., 681 F Supp 216, 219 (S.D.N.Y. 1988) (“the 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.”).
\end{footnotesize}
must do more than merely inflict economic\textsuperscript{84} or social pressure.\textsuperscript{85} But in several respects California is more receptive than New York to claims of duress. Loss of free will is apparently not required; it is sufficient that the threat be “sufficiently coercive to cause a reasonably prudent person, faced with no reasonable alternative, to agree to an unfavorable contract.”\textsuperscript{86} California, moreover, recognizes certain duress-like defenses not found in New York.\textsuperscript{87} A contract may be invalidated if procured by “menace,” including threats of violence or injury to reputation.\textsuperscript{88} Also available as a ground for 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.”\textsuperscript{89} Although menace or undue influence are unlikely to be a ground for avoiding many business contracts, they, together with the state’s softer requirements for duress, 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,\textsuperscript{90} and do so on similar grounds.\textsuperscript{91} There are, however, significant

\textsuperscript{84} See, e.g., Doherty v. Regev, 2002 WL 1904435 (2\textsuperscript{nd} Dist. 2002) (party’s testimony that he felt “compelled” to execute an instrument held insufficient).
\textsuperscript{85} So, for example, the threat to publish politically embarrassing information may not be sufficient. See Philippine Export & Foreign Loan Guarantee Corp. v. Chuidian, 218 Cal.App.3d 1058, 1077-1081, 267 Cal.Rptr. 457 (6\textsuperscript{th} Dist. 1990).
\textsuperscript{86} CrossTalk Productions, Inc. v. Jacobson, 65 Cal.App.4th 631, 644, 76 Cal.Rptr.2d 615 (2\textsuperscript{nd} Dist. 1998).
\textsuperscript{87} Cal. Civ. Code § 1567.
\textsuperscript{88} Cal. Civ. Code § 1570.
\textsuperscript{89} Cal. Civ. Code § 1575.
\textsuperscript{90} New York’s law on unconscionability is largely judge-made. See, e.g., Gillman v. Chase Manhattan Bank, 73 N.Y.2d 1, 10, 537 N.Y.S.2d 787, 534 N.E.2d 824 (N.Y. 1988) (leading case setting forth the basic rules). California’s approach is embodied in a statute, Cal. Civ. Code § § 1670.5(a) (“[i]f 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
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. For a contract to be deemed procedurally unconscionable, a court must find that the complaining party was deprived of “meaningful choice.” This means more than mere inequality of bargaining power or that the contract term was offered on a “take it or leave it” basis. The complaining party must establish a lack of fundamental fairness in the contracting process, evidenced by a combination of factors such as marked differences in sophistication, “gross disparity” of bargaining power, “fine print” clauses hidden in a written contract, the vulnerability of the party seeking relief from the contract, or “high pressure” sales practices. New contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.”


Gillman v. Chase Manhattan Bank, 73 N.Y.2d 1, 10, 537 N.Y.S.2d 787, 534 N.E.2d 824 (N.Y. 1988), Rosiny v. Schmidt, 185 A.D.2d 727 (1st Dept 1992); Wachovia Securities, LLC v. Joseph, 14 Misc.3d 1228(A), 836 N.Y.S.2d 496 (Table) (N.Y.Sup. 2007). In “extreme” or “exceptional” cases, New York may dispense with the requirement of procedural unconscionability, see State v. Wolowitz, 96 A.D.2d 47, 468 N.Y.S.2d 131, 145 (2nd Dept. 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.”); Gillman v. Chase Manhattan Bank, N.A., 73 N.Y.2d 1, 10, 537 N.Y.S.2d 787, 534 N.E.2d 824, 829 (N.Y. 1988) (“There 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.” (citations omitted)).


For example, 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
York is even stricter when it comes to substantive unconscionability. The complaining party must show that the terms are “grossly unreasonable,”99 “exceptional,” or “oppressive,”100 – so deleterious that “no man in his senses and not under delusion” would agree to them.101 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 which awarded a lawyer firm $40 million for five months work following years of litigation which was fully compensated on an hourly basis.102 Given the stringency of its 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.103

California also requires a showing of both procedural and substantive unconscionability.104 Yet these requirements are interpreted differently than in New

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98  Matter of Friedman, 64 A.D.2d 70, 85 (2nd Dept. 1978).
100 Lawrence v. Miller, 48 A.D.3d 1, 853 N.Y.S.2d 1 (1st Dept. 2007) (“oppression”).
102 See, e.g., Lawrence v. Miller, 48 A.D.3d 1, 853 N.Y.S.2d 1 (1st Dept. 2007).
104 Armendariz v. Foundation Health Psychcare Services, Inc. 24 Cal.4th 83, 114, 99 Cal.Rptr.2d 745, 6 P.3d 669 (Cal. 2000).
York. As to procedural unconscionability, California cases sometimes indicate that “no-bargaining” contracts of adhesion are a prerequisite;\(^{105}\) but in practice the doctrine is employed in contexts where bargaining appears to have been possible\(^{106}\) as well as in cases of unilateral mistake.\(^{107}\) 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.”\(^{108}\) Unlike New York, California courts find substantive unconscionability in contracts which are one-sided, whether or not overly harsh.\(^{109}\) Also unlike New York, California does not limit the doctrine of unconscionability to contracts between consumers and businesses;\(^{110}\) any party, even a sophisticated business entity,\(^{111}\) can obtain relief,\(^{112}\) especially if the substantive terms complained of are onerous.\(^{113}\)

\(^{105}\) Graham v. Scissor-Tail, Inc., 28 Cal.3d 807, 817-819, 171 Cal.Rptr. 604 (Cal. 1981) ("[u]nconscionability analysis begins with an inquiry into whether the contract is one of adhesion.").


\(^{107}\) See, e.g., Donovan v. RRL Corp., 26 Cal.4th 261, 27 P.3d 702 (Cal. 2001) (relieving car dealership of consequences of error in advertised price term); M. F. Kemper Const. Co. v. City of Los Angeles, 37 Cal.2d 696, 235 P.2d 7 (Cal. 1951) (relieving contractor of consequences of mistaken bid).


\(^{109}\) See Armendariz v. Foundation Health Psychcare Services, Inc. 24 Cal.4th 83, 99 Cal.Rptr.2d 745, 6 P.3d 669 (Cal. 2000) (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 Medical Group, 100 Cal.App.3d 698, 161 Cal.Rptr. 146 (4th Dist. 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. See Little v. Auto Stiegler, Inc., 29 Cal.4th 1064, 1071, 130 Cal.Rptr.2d 892 (Cal. 2003) (rejecting a clause which allowed either party to appeal an arbitration award of more than $50,000).

\(^{110}\) See Harry 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”).

\(^{111}\) See Nagrampa v. MailCoups, Inc., 469 F.3d 1257, 1283 (9th Cir. 2006) (“sophistication of a party, alone, cannot defeat a procedural unconscionability claim.”).

\(^{112}\) See, e.g., A & M Produce Co. v. FMC Corp., 186 Cal. Rptr. 114, 122–26 (4th Dist. 1982) (small business); Donovan v. RRL Corp.26 Cal.4th 261, 27 P.3d 702 (Cal. 2001) (auto dealer); M. F. Kemper
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 below. The differences between the states are also manifested in ordinary commercial disputes. In *A & M Produce Company v. FMC Corporation*, 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. Even though the buyer was a commercial entity which had alternate sellers available and ample opportunity to read the conspicuous disclaimers, the court held that the terms were unconscionable: “experienced but legally unsophisticated businessmen may be unfairly surprised by unconscionable contract terms, and . . . even large business entities may have relatively little bargaining power.”

*Cayuga Harvester, Inc. v. Allis-Chalmers Corporation*, a New York case, involved a similar challenge to a clause excluding consequential damages in the sale of agricultural equipment. 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.
A similar contrast can be found in two cases from the entertainment industry. In *Graham v. Scissor-Tail, Inc.*\(^{120}\) a California court found a contract clause to be unconscionable even though the complaining party was a prominent music promoter who had signed numerous contracts of the same type and was aware of their provisions.\(^{121}\) In *Reznor v. J. Artist Management, Inc.*\(^{122}\) a New York case, the court refused to invalidate a contract between a struggling rock musician and his longtime manager, even though the musician arguably had much less bargaining power than the promoter in the California case,\(^{123}\) on the ground that as a participant in a commercial venture he had the power to negotiate over the terms.\(^{124}\)

C. Public Policy

Both New York and California refuse to enforce contracts that are deemed to violate public policy. Again, however, underneath the surface similarity are important differences. 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.\(^{125}\)

1. In General

New York only rarely trumps private agreements on public policy grounds. In part, New York’s resistance to public policy arguments is based on the state’s commitment to freedom of contract, which is inevitably frustrated when public policy is

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\(^{123}\) Although he subsequently became a major star as lead singer in the band Nine Inch Nails, the plaintiff (Michael Trent Rezor) had been a struggling artist when he signed the contract. 365 F.Supp.2d at 569.

\(^{124}\) 365 F.Supp.2d at 577 (“courts have rarely found a clause to be unconscionable in contracts involving two commercial entities, a situation in which negotiation is presumed possible.”).

\(^{125}\) See notes __-___ and accompanying text, infra.
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 rights: “efforts to use [public policy] as a sword for personal gain rather than a shield for the public good should not be countenanced.”

New York cases in which public policy trumps private agreement tend to involve specific statutory norms: laws against gambling, usury, insurance contracts benefiting parties without an insurable interest, contracts for the unauthorized practice of law, contracts based on bribery, and illegal agreements to split professional fees. 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 sex or promises to divorce. New York generally turns a deaf ear to broader policies

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126 See notes ___ and accompanying text, supra.
127 See Miller v. Continental Ins. Co., 40 N.Y.2d 675, 389 N.Y.S.2d 565, 358 N.E.2d 258 (N.Y. 1976), quoting Baltimore & Ohio Ry. Co. v. Voigt, 176 U.S. 498 (1900) (“the 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.”)
129 NY Gen. Obl. Law §§ 5-401, 5-411, 5-413, 5-115, 5-117, 5-119, 5-121, 5-123.
130 NY Gen. Obl. Law § 5-511.
131 See N.Y. Insurance Law § 3205(b)(2) (insurable interest required for life insurance policies).
such as protecting consumers, ensuring racial sensitivity, or guarding against “forfeitures.” Only occasionally do New York judges use public policy as a more general equitable tool for protecting the interests of vulnerable parties, and in such cases they apply the relevant policies sparingly.


139 The equitable distaste for forfeitures can be employed to deny enforcement of contract terms that deprive parties of substantial rights due to technical violations (more on this below). See notes ___-___ and accompanying text, infra. 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, 42 N.Y.2d 392, 397-398, 397 N.Y.S.2d 958, 960-961, 366 N.E.2d 1313 (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 Management Corp. v. Pioneer Auto Parks, Inc., 46 N.Y.2d 573, 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; because “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., 80 N.Y.2d 124, 589 N.Y.S.2d 396, 603 N.E.2d 246 (N.Y. 1992) (rejecting public policy claim, in part, on the ground that “forfeitures by operation of law are disfavored”).

140 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 Electric Contractors v. Aetna Casualty & Surety Co., 87 N.Y.2d 148, 661 N.E.2d 967 (N.Y. 1995). But cf. Welsbach Elec. Corp. v. MasTec North America, Inc., 7 N.Y.3d 624, 859 N.E.2d 498 (N.Y. 2006) (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 drives of the insured’s vehicle in situations where the insured had no reason to believe that the driver was unlicensed. See Conte v. Aprea, 23 A.D.3d 225, 803 N.Y.S.2d 557 N.Y.A.D. (1st Dept. 2005).

141 Thus, the mere fact that a contract or its consideration violates state law is not, in itself, enough to invalidate its enforcement. If the violation is merely technical, the contract may be enforced notwithstanding the illegality. See Lloyd Capital Corp. v. Pat Henchar, Inc., 80 N.Y.2d 124, 589 N.Y.S.2d 396, 603 N.E.2d 246 (N.Y. 1992) (“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.”); Denburg v. Parker Chapin Flattau & Kimpl, 82 N.Y.2d 375, 604 N.Y.S.2d 900, 624 N.E.2d 995 (N.Y. 1993); Wowaka & Sons, Inc. v. Pardell, 242 A.D.2d 1, 672 N.Y.S.2d 358 (2nd Dept. 1998); cf., Abramovitz v. Kew Realty Equities, Inc., 180 A.D.2d 568, 580 N.Y.S.2d 269, (1st Dept), lv. denied, 80 N.Y.2d 753, 587 N.Y.S.2d 905, 600 N.E.2d 632 (1992) (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, 50 N.Y.2d 481, 486, 429 N.Y.S.2d 592, 413 N.E.2d 1154 (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 England Mut. Life Ins. Co. v. Caruso, 73 N.Y.2d 74, 535 N.E.2d 270 (N.Y. 1989).
California courts enforce many of the same policies as those recognized under New York law, including norms against wagering contracts, contracts for sex, and fee-splitting agreements among attorneys. Also like New York, specific statutes in California establish overriding policies: prohibiting harassment and discrimination in employment, protecting clients of dating services, prohibiting deficiency judgments in purchase-money mortgages, and indemnifying employees for expenditures necessarily incurred within the scope of employment, 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.” California courts have power to reject contracts which tend to “undermine that sense of security for individual rights, whether of personal liberty or private property, which any citizen ought to feel.” And because public values are implicated, California looks with disfavor at attempts to waive these norms.

The breadth of California’s public policy rule is mitigated by the recognition of the risks associated with such an ill-defined power. 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.\textsuperscript{152} 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.\textsuperscript{153} Courts in that state may award a remedy when serious moral turpitude is not involved,\textsuperscript{154} the defendant is more at fault or would be unjustly enriched if the contract is invalidated, or the public interest would not be compromised by enforcement.\textsuperscript{155} 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 in important respects New York is more permissive. 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 undertaking. New York courts almost never employ their equitable power to prevent

\textsuperscript{152} Moran v. Harris, 131 Cal.App.3d 913, 919, 182 Cal.Rptr. 519 (4th Dist. 1982).
“forfeitures” as a tool for reforming private bargains which turn out poorly for a party, or which result in onerous outcomes because the party has failed to comply with some condition or requirement.\textsuperscript{156} 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,\textsuperscript{157} but waivers of liability for simple negligence among parties not in a fiduciary relationship are generally enforced so long as they are clearly articulated. Parties may also place ceilings on damages\textsuperscript{158} or preclude damages altogether.\textsuperscript{159} Exceptions to this permissive regime are specific and usually based on statute.\textsuperscript{160} New York is also receptive to settlements of disputes, and will enforce releases of claims absent a strong showing of fraud, illegality, duress or mutual mistake.\textsuperscript{161}

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, waivers of gross negligence or intentional misconduct are not allowed.\textsuperscript{162} But, more than New York,
California also disfavors clauses that waive liability for simple negligence. Such clauses are strictly construed because of the “harsh results” that they impose;\(^\text{163}\) liability for “active negligence” is not waived absent clear and specific language.\(^\text{164}\) Even if a clause covers simple negligence, moreover, it is may be challenged in situations extending beyond those recognized in New York. *Tunkl v. Regents of the University of California*,\(^\text{165}\) the leading case, announced that any “exculpatory clause which affects the public interest cannot stand.”\(^\text{166}\) The *Tunkl* court declined to define the “public interest,” contenting itself with vague standards summarizing prior decisions.\(^\text{167}\) The court, however, left little doubt as to the breadth of the concept: in rejecting a hospital’s disclaimer of negligence liability, it observed that

> “the 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


\(^\text{164}\) See Salton Bay Marina, Inc. v. Imperial Irrigation Dist., 172 Cal.App.3d 914, 933, 218 Cal.Rptr. 839 (4th Dist. 1985) (agreement which seeks to limit generally without mentioning negligence shields a party only for passive negligence.).

\(^\text{165}\) 60 Cal.2d 92, 32 Cal.Rptr. 33, 383 P.2d 441 (Cal. 1963).

\(^\text{166}\) 60 Cal.2d at 98.

\(^\text{167}\) 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.” 60 Cal.2d at 101.
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.\textsuperscript{168}

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 to 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.\textsuperscript{169} 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 with the debtor.”\textsuperscript{170} Although § 1542 can be waived, is not always strictly enforced,\textsuperscript{171} and arguably simply restates the law that would apply in any event,\textsuperscript{172} it remains a potential snare for the unwary.

3. Noncompete Clauses

\textsuperscript{168} 60 Cal.2d at 104.
\textsuperscript{169} See, e.g., Perez v. Uline, Inc., 157 Cal.App.4th 953, 68 Cal.Rptr.3d 872, 876 (4th Dist. 2007) (duress is available to invalidate a release only as a “last resort”).
\textsuperscript{170} Cal. Civ. Code § 1542.
\textsuperscript{172} Cf. Westlye v. Look Sports, Inc., 17 Cal. 1715, 1731, 22 Cal.Rptr.2d 781 (3rd Dist. 1993) (it must “appear that its terms were intended by both parties to apply to the particular conduct of the defendant which has caused the harm”).
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, a noncompete clause is enforced 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.” California, in contrast, treats noncompete and related clauses with extreme disfavor. Section 16600 of the California Civil 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.” This statute thus appears to impose a virtual per se ban on noncompete clauses, and some courts have viewed it as such, although others would recognize a reasonableness standard with an associated balancing test. In any event it is clear that the statute reflects an unusually strong public policy of the state, and that restraints on

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176 See, e.g., Edwards v. Arthur Andersen LLP, 47 Cal.Rptr.3d 788, 800 (2nd Dist. 2006) (“[i]n 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 to the employee.”).
177 See General Commercial Packaging v. TPS Package Engineering, Inc., 126 F.3d 1131, 1134 (9th Cir. 1997) (noncompetition agreement valid under § 16600 if the restriction is limited in scope and leaves a substantial portion of the market available to the employee).
competition, valid under the law of New York, would face a serious threat of being invalidated if subjected to California’s public policy.\textsuperscript{179}

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.\textsuperscript{180} 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 somewhat more predictable than in its sister state.\textsuperscript{181}

New York’s approach to employment contracts is illustrated in a 2003 decision by the Court of Appeals, \textit{Horn v. New York Times}.\textsuperscript{182} The plaintiff, an in-house physician, alleged that she was fired for resisting efforts by human relations managers to discover privileged medical information. 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


\textsuperscript{181} 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, supra note __, at __. The evidence might support an inference that sophisticated contracting parties prefer the more California’s protective 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 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, coupled with 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.

\textsuperscript{182} 100 N.Y.2d 85, 790 N.E.2d 753 (N.Y. 2003).
recognize a claim of retaliatory termination and declined the plaintiff’s request to use the covenant of good faith and fair dealing to provide a remedy in an at-will relationship. 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 cause and cases of legal employment implicating the rules of professional responsibility.

California’s approach is significantly less protective of the at-will presumption. In Foley v. Interactive Data Corp. the 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 “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.” 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 which, even if ultimately unsuccessful, enhance the employee’s bargaining leverage in disputes with former employers.

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184 58 N.Y.2d at 304-05.
188 47 Cal.3d at 680.
California also recognizes, as New York does not,\textsuperscript{189} 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.”\textsuperscript{190} Under this definition, plaintiffs may survive a motion to dismiss by alleging they suffered adverse employment action for refusing to commit a crime,\textsuperscript{191} reporting corporate misconduct,\textsuperscript{192} or otherwise acting in furtherance of the public interest.\textsuperscript{193}

D. Statute of Frauds

Both New York and California recognize and enforce versions of the statute of frauds.\textsuperscript{194} But New York, with its strong preference for written agreements, is more stringent in enforcing 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.\textsuperscript{195} Contracts otherwise barred can

\textsuperscript{189} See Horn v. New York Times, 100 N.Y.2d 85, 790 N.E.2d 753 (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. New York Telephone Company/NYNEX, 96 N.Y.2d 312, 727 N.Y.S.2d 383, 751 N.E.2d 462 (N.Y. 2001).
\textsuperscript{190} Stevenson v. Superior Court, 16 Cal.4th 880, 894, 66 Cal.Rptr.2d 888, 941 P.2d 1157 (Cal. 1997); Turner v. Anheuser-Busch, Inc., 7 Cal.4th 1238, 1256, 32 Cal.Rptr.2d 223, 876 P.2d 1022 (Cal. 1994).
\textsuperscript{191} See Tameny v. Atlantic Richfield Co., 27 Cal.3d 167, 164 Cal.Rptr. 839 (Cal. 1980).
\textsuperscript{192} See Garibaldi v. Lucky Food Stores, Inc., 726 F.2d 1367, 1374 (9th Cir. 1984).
\textsuperscript{193} 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., 85 Cal.App.4th 927, 929, 102 Cal.Rptr.2d 495 (2nd Dist. 2001).
\textsuperscript{194} 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 N.Y. Gen. Obl. Law §§ 5-701 (general contracts), 5-703 (real estate contracts); Cal. Civ. Code § 1624.
only rarely be salvaged. The doctrine of part performance is available for real estate contracts, but only where the performance in question “unequivocally” refers to the agreement, the complaining party detrimentally relies on the defendant’s actions, and failure to enforce the contract would result in an unconscionable injury. Outside the real estate context, part performance is not available. Promissory estoppel can defeat the statute, 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. 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. Some recent decisions suggest, however, that quantum meruit claims are categorically unavailable if the effect of recognizing them is to circumvent the statute.

196 See N.Y. Gen. Obl. Law § 5-703(4) (“[t]othing contained in this section abridges the powers of courts of equity to compel the specific performance of agreements in cases of part performance.”).
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.205

California is more receptive to efforts at avoiding the statute, especially where the result is perceived as unfair. The policy of the statute, as articulated by California courts, is to prevent fraud.206 This leads to an uncharitable attitude on the part of some judges who doubt the statute’s effectiveness at achieving that goal,207 and who worry that the statute itself might be used as a shield for fraud.208 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”209 – a sentiment that has been echoed in subsequent California cases.210

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 which would otherwise fall within the statute – not just real estate contracts.211 California cases also appear more

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206 See Sterling v. Taylor, 55 Cal.Rptr.3d 116, 40 Cal.4th 757, 152 P.3d 420 (Cal. 2007).


208 See, e.g., Juran v. Epstein, 28 Cal.Rptr.2d 588, 23 Cal.App.4th 882 (4th Dist. 1994); Seymour v. Oelrichs, 106 P. 88, 94-95 (Cal. 1909) (“[t]he 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.”).


210 See, e.g., Sterling v. Taylor, 6 Cal.Rptr.3d 836, 844 (2nd Dist. 2003) (suggesting that statute of frauds has “fallen into disfavor” in California, although since the statute remains in effect courts must enforce it); Estate of Housley, 56 Cal.App.4th 342, 65 Cal.Rptr.2d 628 (4th Dist. 1997) (same).

211 See, e.g., In re Marriage of Benson, 36 Cal.4th 1096, 116 P.3d 1152 (Cal. 2005) (general statute of frauds is subject to exception for part performance) (dictum).
generous in their application of the part performance rule’s requirement that the behavior in question unequivocally refer to the contract; they do not insist that the conduct in question be compatible with no other explanation. California courts are also receptive to the use of promissory estoppel as a basis for avoiding the statute.\textsuperscript{212} 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.\textsuperscript{213} California, unlike New York, may also permit fraud actions based on contracts which are otherwise unenforceable under the statute.\textsuperscript{214}

E. Mistake

Both California and New York recognize that parties may avoid performing contractual obligations upon 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 law permits rescission or reformation on the basis of mutual mistake of law only in limited circumstances. The mistake must have been present at the time of contract,\textsuperscript{215} must be mutual\textsuperscript{216} and substantial,\textsuperscript{217} must be shown by clear and convincing evidence,\textsuperscript{218}

\begin{footnotesize}
\begin{enumerate}
\item See Philip H. Wile, Kathleen Cordova-Lyon and Claude D. Rohwer, Estoppel to Avoid the California Statute of Frauds, 35 McGeorge L.Rev. 319 (2004) (arguing, however, the California promissory estoppel cases should be interpreted so as to avoid de facto repeal of the statute of frauds).
\item James G. Freeman & Associates, Inc. v. Tanner, 128 Cal.Rptr. 109, 56 Cal.App.3d (1\textsuperscript{st} Dist. 1976) (declining to apply statute of frauds where result would be unjust enrichment); Estate of Housley 56 Cal.App.4th 342, 65 Cal.Rptr.2d 628 (Cal.App. 1997).
\item Levin v. Knight, 780 F.2d 786 (9\textsuperscript{th} Cir. 1986) (approving fraud action based on misrepresentation in connection with unenforceable contract); Tenzer v. Superscope, Inc., 216 Cal.Rptr. 130, 39 Cal.3d 18, 702 P.2d 212 (Cal. 1985).
\item See Schultz v. Hourihan, 238 A.D.2d 818 (3\textsuperscript{rd} Dept.1997).
\item Brauer v. Central Trust Co., 77 A.D.2d 239, 243 (4\textsuperscript{th} Dept.1980), lv. den. 52 N.Y.2d 703 (1981) (“where 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.”)
\end{enumerate}
\end{footnotesize}
and must not be one that the party should have known about at the time he entered into
the contract.219 Parties may also be relieved of contractual obligation because of mutual
mistake of law,220 but here the requirements are even more stringent: the mistake must be
accompanied by “fraud or inequitable, unfair or deceptive behavior.”221 Rescission or
reformation based on unilateral, as opposed to mutual, mistake is uncommon in New
York;222 the proponent must establish and enforcing the contract as written would be
unconscionable223 or result in unjust enrichment of one party at the expense of the
other224 and the parties can be returned to the status quo ante without prejudice.225 In any
case of mistake, if reformation is sought, the party seeking relief must establish “exactly
what was really agreed upon the parties.”226

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.227 The necessity that the parties agree to the same thing at the same time228

1954).
220 NY CPLR § 3005 (“[w]hen 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.”).
1901).
1990).
228 See Cal. Civ. Code § 1580 (“Consent is not mutual, unless the parties agree upon the same thing in
the same sense.”); Weddington Productions, Inc. v. Flick, 60 Cal.App.4th 793, 811, 71 Cal.Rptr.2d 265 (2nd
Dist. 1998).
makes it relatively easy for parties to frame claims for relief under this theory.\textsuperscript{229} 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 relief 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.\textsuperscript{230} Proof of mistake is also facilitated, in California, by the state’s acceptance of extrinsic evidence on the question.\textsuperscript{231} Reformation is liberally available in California if mistake is shown, provided that the changed terms do not affect substantial rights of third parties.\textsuperscript{232}

V. Parol Evidence

Both California and New York administer a parol evidence rule.\textsuperscript{233} Both states recognize that if a contract is “integrated” – that is, if it expresses the full and complete

\textsuperscript{229} They must, however, a plead objective facts tending to negative the element of consent; mere allegations of subjective mistake will not do. Alexander v. Codemasters Group Limited, 104 Cal.App.4th 129, 127 Cal.Rptr.2d 145 (5th Dist. 1976).

\textsuperscript{230} See Cal. Civ. Code § 1577 (“Mistake of fact is a mistake, not caused by the neglect of a legal duty on the part of the person making the mistake, and consisting in . . . an 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., 26 Cal.4th 261, 27 P.3d 702 (Cal. 2001) (granting relief in case of unilateral mistake, despite the fact that the counterparty did not know of or suspect the mistake, when enforcement would be unconscionable).

\textsuperscript{231} See Cal. Code Civ. Proc., § 1856(e), (g); Casa Herrera, Inc. v. Beydoun, 32 Cal.4th 336, 343, 83 P.3d 497 (Cal. 2004).

\textsuperscript{232} Cal. Civ. Code § 3399 (“[w]hen, 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 v. Ford Motor Co., 27 Cal.4th 516, 524, 41 P.3d 46, 117 Cal.Rptr.2d 220 (Cal. 2002).

\textsuperscript{233} 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).
agreement of the parties – then evidence from outside the four corners of the contract may not be considered. 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 rule under which the court decides whether the contract is ambiguous from an analysis of the document itself. If the court concludes that the contract terms are unambiguous they do not consider extrinsic evidence bearing on the parties’ intent. Resort to extrinsic evidence is appropriate only if the agreement is subject to more than one interpretation. If the parties wish even greater protection against extra-contractual information being used to interpret their agreement, they are free to adopt merger or integration clauses, which are accorded nearly conclusive deference by the New York courts.

234 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.
239 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 would provide, for example, “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
California, in contrast, uses a “soft” parol evidence rule.\(^{241}\) Under a soft rule a lack of ambiguity in the explicit contractual language is not controlling. Instead, the court provisionally examines extrinsic evidence bearing on the threshold question of whether the contract is ambiguous.\(^{242}\) 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. If, however, the extrinsic evidence reveals ambiguity, then the court may consider all such extrinsic evidence as may be relevant to interpreting the contract. The parties can, of course, include merger or integration clauses in their contracts in an attempt to shore up the parol evidence rule; but while these are afforded substantial respect under California law,\(^{243}\) they are not conclusive\(^{244}\) but rather 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, PLI, Drafting Corporate Agreements 2004-2005 (December, 2004 - January, 2005).

\(^{240}\) See Norman Bobrow & Co., Inc. v. Loft Realty Co., 577 N.Y.S.2d 36, 36, 178 A.D.2d 175 (1st Dept. 1991) (“[p]arol evidence is not admissible to vary the terms of a written contract containing a merger clause.”); Balzano v. Lublin, 162 A.D.2d 252, 556 N.Y.S.2d 610, 611 (1st Dept. 1990) (same); Jones v. Trice, 202 A.D.2d 394, 608 N.Y.S.2d 688 (2nd Dept. 1994); Oppman v. IRMC Holdings, Inc., 14 Misc.3d 1219(A), (Sup. Ct., New York Co. 2007); Cornhusker Farms, Inc. v. Hunts Point Coop. Market, Inc., 2 A.D.3d 201, 203-204 (1st Dept. 2003); Tempo Shain Corp. v. Bertek, Inc., 120 F.3d 16, 21 (2d Cir. 1997) (“[o]rdinarily, 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, 95 N.Y.2d 665, 745 N.E.2d 1006, 1009 (N.Y. 2001) (“[t]he 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.”).


\(^{243}\) Banco Do Brasil, S. A. v. Latian, Inc., 234 Cal.App.3d 973, 285 Cal. Rptr. 870, 887 (2d Dist. 1991) (“obviously, the presence of an “integration” clause will be very persuasive”).

\(^{244}\) See, e.g., Specht v. Netscape Communications Corp., 306 F.3d 17, 36–37 (2d Cir. 2002) (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) (presence of merger clauses “not necessarily conclusive”).
considered along with other evidence of contract integration.\textsuperscript{245} Even if an integration clause is present and respected as regards the original terms of the contract, moreover, California recognizes relatively easy modification by course of dealing among the parties.\textsuperscript{246}

VI. Choice of Law and Forum

Both New York and California recognize wide latitude in the parties to determine the law applicable to their agreements and the forum in which disputes will be resolved.\textsuperscript{247} 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 (Second) of Conflict of Laws rule on choice-of-law clauses.\textsuperscript{248} The Restatement adopts “a strong

\textsuperscript{245} Sicor Ltd. v. Cetus Corp., 51 F.3d 848, 859 (9th Cir. 1995) (integration clause is “but one factor” in the analysis); Founding Members of the Newport Beach Country Club v. Newport Beach Country Club, Inc., 135 Cal. Rptr.2d 505, 512, 109 Cal.App.4th 944 (4th Dist. 2003) (“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, 138 Cal.App.3d 256, 187 Cal. Rptr. 845, 851–52 (4th Dist. 1982) (factors include 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.”).

\textsuperscript{246} See, e.g., Diamond Woodworks, Inc. v. Argonaut Ins. Co., 109 Cal.App.4th 1020, 1038, 135 Cal.Rptr.2d 736 (4th Dist. 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.”)


\textsuperscript{248} RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 (1996). See ABF Capital Corp. v. Osley, 414 F.3d 1061, 1065 (9th Cir. 2005) (California courts apply the Restatement approach for contractual choice-of-law provisions); Discover Bank v. Superior Court, 113 P.3d 1100, 1117 (Cal. 2005) (same);
policy favoring enforcement" of such provisions\(^{249}\) and recommends that choice-of-law clauses be respected unless 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.\(^{250}\) 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.\(^{251}\) As regards public policy, New York recognizes only limited circumstances in which choice-of-law clauses will be rejected: \(^{252}\) “those rare cases”\(^{253}\) where applying the parties’ choice would be “truly obnoxious”\(^{254}\) or “deeply abhorrent”\(^{255}\) 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.\(^{256}\) Applying the law must “violate some fundamental principle of justice, some prevalent conception of good morals, some deep-rooted tradition of the common

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\(^{249}\) Nedlloyd Lines B.V. v. Superior Court, 3 Cal.4th 459, 834 P.2d 1148, 1151 (Cal. 1992).

\(^{250}\) RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187(b) (1996).

\(^{251}\) See, e.g., Hackett v. Milbank, Tweed, Hadley & McCloy, 86 N.Y.2d 146, 154, 654 N.E.2d 95, 100, 630 N.Y.S.2d 274, 279 (N.Y. 1995) (explicit and unambiguous choice of law “must be given effect”).


The Court of Appeals offers only three examples of state policies fundamental enough to defeat choice-or-law clauses, all involving state anti-discrimination or human rights norms. New York courts, moreover, generally look to the policy of only New York when considering whether to reject a choice of New York law; conflicting policies of other jurisdictions that might trump the application of the parties’ chosen law will not be considered. This effectively gives an iron-clad 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 does contravene New York policy.

Provisions selecting New York law in commercial contracts receive even greater respect. A New York statute provides that parties to any contract worth at least $250,000 “may agree that the law of this state shall govern their rights and duties in whole or in

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part, whether or not such contract, agreement or undertaking bears a reasonable relation to this state." Thus, for qualifying commercial contracts, New York courts will respect choice-of-law provisions even if the parties or the transaction have no connections with the state. Such contracts, moreover, appear to be completely immune even from attack based on public policy considerations – or at least considerations that are implicitly overridden by the choice-of-law statute.

California is substantially less permissive towards choice-of-law clauses. The state has not enacted an analog to New York’s rule for large commercial contracts; thus choice-of-law provisions in all contracts, even among sophisticated parties, are subject to potential attack on the grounds they lack contacts with the state or violate important public policies. Moreover, as we have seen already, compared with New York, California uses expansive notions of public policy to reject contractual terms on grounds of public policy; these arguments are available for choice-of-law clauses as for other contractual terms. Thus, choice-of-law clauses may be invalidated whenever

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263 See text accompanying notes ___-___, supra.
“substantial legal rights” would be “significantly impaired”\textsuperscript{265} or “substantially diminished.”\textsuperscript{266} As a result, there are no “bright line rules”\textsuperscript{267} for applying the public policy doctrine to choice-of-law clauses. Further, California, unlike New York, is willing to look 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.\textsuperscript{268}

California’s approach to choice-of-law clauses is illustrated by Application Group, Inc. v. Hunter Group, Inc.,\textsuperscript{269} a 1998 case from the First District Court of Appeals. A California corporation recruited and hired an employee of a Maryland competitor in clear violation of a covenant not to compete. In a declaratory judgment action brought by the employee and her new employer, 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. 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 selecting Maryland law.\textsuperscript{270} 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, and further

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\item \textsuperscript{265} America Online, Inc. v. Superior Court, 90 Cal.App.4th 1, 108 Cal.Rptr.2d 699, 707 (1st Dist. 2001).
\item \textsuperscript{266} Klussman v. Cross Country Bank, 134 Cal.App.4th 1283, 36 Cal.Rptr.3d 728, 736 (1st Dist. 2005).
\item \textsuperscript{267} Discover Bank v. Superior Court, 36 Cal.Rptr.3d 456, 460 (2nd Dist. 2005) (citing \textsc{reSTATEMENT (SECOND) OF CONFLICT OF LAWS} § 187, cmt.g (1996) (“[w]e are not aware of any bright-line rules for determining what is and what is not contrary to a fundamental policy of California.”)).
\item \textsuperscript{268} See Discover Bank v. Superior Court, 36 Cal.Rptr.3d 456 (2nd Dist. 2005) (“Technically, the inquiry is not whether there is a conflict with a fundamental policy of \textit{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.”); Nedlloyd Lines B.V. v. Superior Court, 834 P.2d 1148, 1152 n.4 (Cal. 1992) (clarifying that California will look to the public policy of foreign states in applying Restatement approach).
\item \textsuperscript{269} 61 Cal.App.4th 881, 72 Cal.Rptr.2d 73 (1st Dist. 1998).
\item \textsuperscript{270} Id. at 899.
\end{itemize}
that California’s interests would be the more seriously impaired if its policy were subordinated to the policy of Maryland. Hence the court rejected the choice-of-law clause, applied California law, and invalidated the noncompete clause. Cases such as Application Group do not appear in New York jurisprudence.

B. Forum Selection Clauses

Consistently with the general trend in state and federal courts, 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.

The general law in New York is that forum selection clauses will not be set aside unless enforcement would be “so gravely difficult and inconvenient that challenging party would, for all practical purposes, be deprived of his or her day in court.” New York courts will deny enforcement to forum selection clauses only in unusual contexts, as where the clause is manifestly unreasonable and not prominently disclosed in the contract. 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.

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Commercial contracts receive even greater respect in New York. Part of the law adopted in 1984 requires New York courts to enforce a forum selection clause if the parties agree to submit to the jurisdiction of New York courts and choose New York law to govern their contract.\textsuperscript{275} To ensure that this rule only applies to commercial contracts, the legislation applies only to contracts for a value of more than one million dollars.\textsuperscript{276} Supplemented by this provision, New York waives the otherwise-applicable requirement that a foreign corporation must have minimum contacts with the state in order to bring suit in New York,\textsuperscript{277} and also precludes dismissal of such cases on \textit{forum non conveniens} grounds.\textsuperscript{278}

California courts enforce forum selection clauses in the absence of a showing the enforcement of such a clause would be unreasonable.\textsuperscript{279} They impose a “heavy burden” on parties seeking to escape such clauses.\textsuperscript{280} On the other hand, California precedent suggests that “take it or leave it” clauses may be closely scrutinized.\textsuperscript{281} California courts also display a willingness to reject forum selection clauses which work to deprive

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\textsuperscript{275} N.Y. Gen. Oblig. § 5-1402. \\
\textsuperscript{276} Id. \\
\textsuperscript{277} See N.Y General Obligation Law § 5-1402, waiving provisions of N.Y. Bus. Corp. Law § 1314(b). \\
\textsuperscript{278} N.Y.C.P.L.R. Rule 327(b) (“notwithstanding the provisions of subdivision (a) of this rule, the court shall not stay or dismiss any action on the ground of inconvenient forum, where the action arises out of or relates to a contract, agreement or undertaking to which section 5-1402 of the general obligations law applies, and the parties to the contract have agreed that the law of this state shall govern their rights or duties in whole or in part.”). \\
\textsuperscript{279} Smith, Valentino & Smith, Inc. v. Superior Court, 17 Cal.3d 491, 495-96, 131 Cal.Rptr. 374, 551 P.2d 1206 (Cal. 1976). “Unreasonable,” in this context, means more than inconvenience and expense. Id. at 496; America Online, Inc. v. Superior Court, 90 Cal.App.4th 1, 108 Cal.Rptr.2d 699 (1st Dist. 2001). \\
\textsuperscript{280} Miller-Leigh LLC v. Henson, 62 Cal.Rptr.3d 83, 152 Cal.App.4th 1143 (3rd Dist. 2007). \\
\textsuperscript{281} See Smith, Valentino & Smith, Inc. v. Superior Court, 17 Cal.3d 491, 496, 131 Cal.Rptr. 374, 551 P.2d 1206 (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 not upheld forum selection clauses in contracts of adhesion. See, e.g., Net2Phone, Inc. v. Superior Court, 109 Cal.App.4th 583, 135 Cal.Rptr.2d 14 (2nd Dist. 2003) (fact clause was in take-it-or-leave-it consumer contract did not preclude enforcement); Intershop Communications AG v. Superior Court, 104 Cal.App.4th 191, 201, 127 Cal.Rptr.2d 847 (1st Dist. 2002).
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litigants of substantial rights. Overall, California judges have greater flexibility than their peers in New York to reject forum choices freely-negotiated among the contracting parties.

VII. The Adjudicatory Process

I now compare New York and California law on 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. Even without an explicit jury waiver, New York courts vigorously enforce implied waivers, as where the parties to a contract agree to binding arbitration. 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, and California courts interpose limits on the ability of parties to waiver jury rights de facto by agreeing to mandatory arbitration clauses.

B. Attorneys’ Fees

\[\text{\footnotesize \textsuperscript{282} See text accompanying notes \_\_\_, infra.}\]
\[\text{\footnotesize \textsuperscript{284} See notes \_\_ and accompanying text, infra. New York courts developed the doctrine on jury waivers beginning in the 1920s and decided most of the early cases. See Stephen J. Ware, Arbitration Clauses, Jury-Waiver Clauses, and Other Contractual Waivers Of Constitutional Rights, Law and Contemporary Problems (Winter/Spring 2004).}\]
\[\text{\footnotesize \textsuperscript{285} Grafton Partners LP v. Superior Court, 9 Cal. Rptr. 3d 511 (Cal. Ct. App. 2004), rev. granted by 88 P.3d 24 (Cal. 2004).}\]
\[\text{\footnotesize \textsuperscript{286} See notes \_\_\_ and accompanying text, infra.}\]
Both New York and California apply the “American Rule” that each party to litigation pays his or her own attorney. 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.

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. In other respects, however, parties in New York are generally free to adopt “loser-pays” rules, “one-way” 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.

The rule is different in California. There, contracts containing one-way fee shifting provisions in contract cases are reformed by statute to award of fees to the prevailing party regardless of the nature of the parties. Unlike New York, therefore,

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288 NY Gen. Obl. Law § 5-327(2) (”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.”)
290 Cal. Civ. Code § 1717(a) (“[i]n 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.”). This policy of this statute is that “equitable considerations must
California extends its contract-trumping attorneys fee rule to all contacts, not just specified consumer contracts. Moreover, California’s statute, which is non-waivable, has been broadly interpreted to apply to actions that “involve” a contract, even if not directly framed as actions for breach.  

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.

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 or consumer goods and services (although this rule may be unenforceable for contracts affecting interstate commerce). In other respects, however, and especially in the case of commercial agreements, New York is among the national leaders in endorsing and enforcing arbitration agreements. New York
was the first American state to legalize pre-dispute arbitration clauses; its arbitration act, adopted in 1920, was the model for the Federal Arbitration Act of 1925. Its courts have also long encouraged arbitration, viewing the procedure as offering a speedy, flexible, inexpensive and sophisticated means for resolving disputes. Arbitration clauses are enforceable in New York 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. Alleged violations of public policy rarely defeat arbitration clauses in New York, and only for compelling reasons such as the need to protect the integrity of criminal investigations, to administer state antitrust law, to manage insurance company insolvencies, or to maintain judicial scrutiny over tenure

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297 See id.
302 See Port Jefferson Station Teachers Ass’n v. Brookhaven-Comsewogue Union Free School District, 45 N.Y.2d 898, 899, 411 N.Y.S.2d 1, 2, 383 N.E.2d 553, 554 (N.Y. 1978) (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. Board of Education, Union Free School, Dist. No. 3, Town of Huntington, 33 N.Y.2d 229, 235, 351 N.Y.S.2d 670, 675, 306 N.E.2d 791, 795 (N.Y. 1973) (issue must be “interlaced with strong public policy considerations”).
decisions for public school teachers. Parties in New York are free to devise their own arbitration procedures, may contract for enhanced judicial review of arbitral awards, and may adopt hybrids that combine elements of arbitration and litigation. Mutuality of remedy is not required: a contract may require only one of the parties to arbitrate a dispute. New York also strictly limits judicial review of awards in the absence of agreements expanding such review, requiring confirmation unless an award violates a “strong public policy,” is “totally irrational,” or “clearly exceeds a specifically enumerated limitation on the arbitrator’s power” – a standard that may be even more deferential than the “manifest disregard” rule under the Federal Arbitration Act.

California courts, like their New York peers, endorse arbitration and recognize its advantages as a speedy and expeditious means to resolve disputes. Nonetheless

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310 See, e.g., County of Nassau v. Sheriff’s Officers Ass’n, Inc.294 A.D.2d 31, 743 N.Y.S.2d 503 (2d Dept. 2002) (refusing to upset an award favoring policeman who had engaged in patently offensive, racially provocative public conduct).
312 See Wien & Malkin LLP v. Helmsley-Spear, Inc.12 A.D.3d 65, 783 N.Y.S.2d 339 (1st Dept. 2004) (court first upheld an award under New York’s standard for judicial review, but then, applying the federal standard, rejected it on the ground that the arbitrators exhibited “manifest disregard” of the law).
314 See Cal. Code Civ. Pro. § 1281 (”[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, providing that arbitration agreements are “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, e.g., Vandenberg v. Superior Court, 21 Cal.4th 815, 830, 88 Cal.Rptr.2d 366, 982 P.2d 229 (Cal. 1999); Adajar v. RWR Homes, Inc., 160 Cal.App.4th 563, 73 Cal.Rptr.3d 17, 21 (4th Dist. 2008).
arbitration agreements face significant obstacles. \footnote{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 (1985) (FAA held to preempt California rule prohibiting arbitration of claims under state franchise statute). As yet, however, the federal courts have not definitively addressed this matter. Cf. Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ., 489 U.S. 468 (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).} 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. \footnote{See Armendariz v. Foundation Health Psychcare Services, Inc., 24 Cal.4th 83, 102-103, 99 Cal.Rptr.2d 745 (Cal. 2000); Abramson v. Juniper Networks, Inc., 115 Cal.App.4th 638, 9 Cal.Rptr.3d 422 (6th Dist. 2004).} Party-crafted procedures and limitations of remedy which fail to afford the requisite procedural rights will be struck down. \footnote{See Armendariz v. Foundation Health Psychcare Services, Inc., 24 Cal.4th 83, 120, 6 P.3d 669 (Cal. 2000) ("an 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., 29 Cal.4th 1064, 1071, 63 P.3d 979 (Cal. 2003); Abramson v. Juniper Networks, Inc., 115 Cal.App.4th 638, 9 Cal.Rptr.3d 422 (6th Dist. 2004); O’Hare v. Municipal Resource Consultants, 107 Cal.App.4th 267, 273-79, 132 Cal.Rptr.2d 116 (2nd Dist. 2003).} Arbitration clauses are also frequently invalidated in California on grounds of unconscionability. Clauses contained in contracts of adhesion are suspect, even if the party contesting enforcement knew of the terms at the time of contract \footnote{See Kinney v. United HealthCare Services, Inc., 70 Cal.App.4th 1322, 1329, 83 Cal.Rptr.2d 348 (4th Dist. 1999).} and enjoyed protections such as a cooling-off period. \footnote{See Gentry v. Superior Court, 42 Cal.4th 443, 165 P.3d 556 (Cal. 2007).} In contrast with New York, California rejects agreements deemed to lack mutuality if the result is to disadvantage the weaker party. \footnote{See Armendariz v. Foundation Health Psychcare Services, Inc., 24 Cal.4th 83, 103, 99 Cal.Rptr.2d 745 (Cal. 2000) (arbitration agreement may not limit statutorily imposed remedies such as punitive damages and attorney fees); Azteca Construction, Inc. v. ADR Consulting, Inc., 121 Cal.App.4th 1156, 18 Cal.Rptr.3d 142 (3rd Dist. 2004) (right to disqualify an arbitrator).} Even...
clauses neutral on their face may be invalidated if their effect would be one-sided.\textsuperscript{321}

California courts are also ill-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.\textsuperscript{322}

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.\textsuperscript{323}

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.\textsuperscript{324} New York and California adopt different approaches to such waivers. In New York they are presumptively valid and regularly

\textsuperscript{321} See Saika v. Gold, 49 Cal.App.4th 1074, 56 Cal.Rptr.2d 922 (4th Dist. 1996) (invalidating provision that 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).


\textsuperscript{323} But see Greenbriar Homes Communities, Inc. v. Superior Court, 117 Cal.App.4th 337, 11 Cal.Rptr.3d 371 (3rd Dist. 2004) (upholding arbitration clause that required consumers to share forum costs).

\textsuperscript{324} 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-SPG 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, and Emily L. Sherwin, Arbitration’s Summer Soldiers: An Empirical Study of Arbitration Clauses in Consumer and Nonconsumer Contracts (manuscript on file with the author).
enforced against claims that they are unconscionable or violate public policy.\textsuperscript{325}

California, in contrast, generally invalidates these clauses on grounds of public policy or unconscionability.\textsuperscript{326}

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).\textsuperscript{327} Both New York and California resist attempts to substitute a tort regime for contract remedies, but New York is the more consistent in requiring 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, requiring that some legal duty separate from the

\textsuperscript{325} See Ranieri v. Bell Atlantic Mobile, 304 A.D.2d 353, 354, 759 N.Y.S.2d 448, 449 (1st Dept. 2003) (“given the strong public policy favoring arbitration, and the absence of a commensurate policy favoring 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., 193 Misc. 2d 721, 751 N.Y.S.2d 722 (N.Y. Sup. 2002) (“[t]he 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”); Brower v. Gateway 2000, Inc., 246 A.D.2d 246, 676 N.Y.S.2d 569 (1st Dept. 1998).

\textsuperscript{326} See Discover Bank v. Superior Court, 36 Cal.4th 148, 113 P.3d 1100 (Cal. 2005) (class action waiver unenforceable under California law); Gentry v. Superior Court, 42 Cal.4th 443, 165 P.3d 556 (Cal. 2007) (class arbitration waivers in employment agreements could not be enforced if class arbitration would be significantly more effective way of vindicating rights); America Online, Inc. v. Superior Court, 90 Cal.App.4th 1, 108 Cal. Rptr. 2d 699 (1st Dist. 2001) (rejecting choice-of-law and forum selection clauses that would have precluded class action treatment under California consumer protection law); Aral v. Earthlink, Inc., 134 Cal.App.4th 544, 36 Cal.Rptr.3d 229 (2nd Dist. 2005) (class action waiver invalidated as unconscionable); Lee v. AT & T Wireless Services, Inc., 2006 WL 1452936 (2nd Dist 2006) (same); Klussman v. Cross Country Bank, 134 Cal.App.4th 1283, 36 Cal.Rptr.3d 728 (1st Dist. 2005) (same); Gatton v. T-Mobile USA, Inc., 152 Cal.App.4th 571, 61 Cal.Rptr.3d 344 (1st Dist. 2007) (same).

\textsuperscript{327} 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).
contract must be infringed before extra-contractual relief will be granted. New York rejects contract-based claims of unjust enrichment, either for failed preliminary negotiations or breach of an executed contract. Employees claiming that their employers tortiously interfered with contractual relations are summarily shown the door. New York courts sometimes recognize claims for fraud in the inducement, but require more than the allegation that the defendant did not intend to perform his promises. 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

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330 Clark-Fitzpatrick v. Long Island Rail Road Co., 521 N.Y.S.2d 653, 70 N.Y.2d 382, 389 (N.Y. 1987) (“[W]here 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”, a party may not maintain an action in both quasi-contract and breach of contract); Cooper, Bamundo, Hecht, & Longworth, LLP v. Kuczinski, 14 A.D.3d 644, 14 A.D.3d 644 (2nd Dept. 2005).


New York courts require the plaintiff both seek different relief\textsuperscript{334} and make specific factual allegations separate from those associated with the contract.\textsuperscript{335} 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.\textsuperscript{336} Even in the absence of a no-reliance clause, moreover, a New York court might well dismiss claims of fraud if the alleged misrepresentation is contrary to the terms of the express contract, on the theory that plaintiff could not prove justifiable reliance in such a circumstance.\textsuperscript{337}

California law is more receptive to the alchemy of transmuting contract claims into torts. The general rule is that a tort claim can be made out if “the 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.”\textsuperscript{338} While this formulation appears forbidding, it does not forbid actions for fraud in the inducement that overlap contract claims.\textsuperscript{339} In \textit{Linza v. Diamond}

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{334} Rockefeller University v. Tishman Const. Corp. of New York, 240 A.D.2d 341, 659 N.Y.S.2d 460 (1st Dept. 1997) (tort claim rejected where contractual benefit-of-the-bargain recovery was sought).
\item \textsuperscript{335} Gotham Boxing Inc. v. Finkel, 18 Misc.3d 1114(A), 2008 WL 104155 (Table) (N.Y.Sup. 2008) (summarizing cases).
\item \textsuperscript{338} Erlich v. Menezes, 21 Cal.4th 543, 553-554, 87 Cal.Rptr.2d 886, 981 P.2d 978 (Cal. 1999).
\end{itemize}
\end{footnotesize}
Center, Inc.,\textsuperscript{340} 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. The same court found 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. California is also receptive to other non-contractual remedies. It judges do not enforce a cause of action for negligent breach of contract,\textsuperscript{341} yet they recognize that parties to a contract have a duty to perform their obligations with reasonable care, skill, expediency and faithfulness.\textsuperscript{342} Accordingly, the “same wrongful act may constitute both a breach of contract and an invasion of an interest protected by the law of torts.”\textsuperscript{343} While a negligence claim may not survive if it merely replicates allegations of contractual breach, it may succeed if the plaintiff is able to include relevant allegations that are not fairly encompassed in the contract claim. California is also receptive to claims of unjust enrichment associated with breaches of 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.\textsuperscript{344}

IX. 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

\textsuperscript{340} 2005 WL 3560800 (1st Dist. 2005).
\textsuperscript{341} Erlich v. Menezes, 21 Cal.4th 543, 551, 552, 87 Cal.Rptr.2d 886, 981 P.2d 978 (Cal. 1999).
\textsuperscript{343} North American Chemical Co. v. Superior Court, 59 Cal.App.4th 764, 774, 69 Cal.Rptr.2d 466 (2nd Dist. 1997).
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: contracts are enforced as written, not reformed or rejected to satisfy ideas of fairness or equity. Doctrines such as promissory estoppel and unjust enrichment are disfavored. Tort actions that duplicate claims a breach of contract claim are rejected in favor of the contract remedies.

California law is different 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 paper 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.