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Special Report of the TriBar Opinion Committee: The Remedies Opinion—Deciding When to Include Exceptions and Assumptions

By the TriBar Opinion Committee*

I. INTRODUCTION

The TriBar Opinion Committee's report on *Third-Party "Closing" Opinions*¹ (the "1998 TriBar Report") describes customary practice² in preparing and interpreting third-party closing opinions.³ This Report augments the analysis of the remedies

*The TriBar Opinion Committee (the "Committee" or "TriBar") currently includes designees of the following organizations functioning as a single Committee: (i) Special Committee on Legal Opinions in Commercial Transactions, New York County Lawyers' Association; (ii) Corporation Law Committee, The Association of the Bar of the City of New York, and (iii) Special Committee on Legal Opinions of the Business Law Section, New York State Bar Association. Members of the Allegheny County (Pa.), Atlanta, Boston, Chicago, District of Columbia and Ontario Bar Associations and of the state bars of California, Delaware, Georgia, North Carolina, Pennsylvania, and Texas are also members of the Committee. The members of the Committee and the Reporter and Editorial Group for this Report are listed in Appendix A.

This Report has not been approved by the governing body or membership of any of the bar associations whose committees or members were involved in its preparation. Accordingly, the views expressed are solely those of TriBar. This Report reflects a consensus of the Committee. It does not, however, necessarily reflect the views of individual members or their firms, organizations, or associations on any particular point.

1. TriBar Opinion Committee, *Third-Party "Closing" Opinions: A Report of The TriBar Opinion Committee*, 53 BUS. LAW. 591, 592 (1998). Terms used in this Report have the meanings given them in the 1998 TriBar Report. See generally *id.* Art. I, at 595–608. Like the 1998 TriBar Report, this Report refers to the lawyer or law firm rendering the closing opinion as the "opinion giver" and the lawyer or lawyers who prepare the opinion as the "opinion preparers."

2. See 1998 TriBar Report, *supra* note 1, § 1.4, at 600–03. See also RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS §§ 51 cmt. e, 95(2) cmt. b (2000) [hereinafter RESTATEMENT OF LAW GOVERNING LAWYERS]; The Committee on Legal Opinions of the American Bar Association's Section of Business Law (the "ABA Section"), *Legal Opinion Principles*, 53 BUS. LAW. 831, § I.B, at 832 (1998) [hereinafter ABA Principles] (stating "[T]he scope and nature of the work counsel is expected to perform are based (whether or not so stated) on the customary practice of lawyers who regularly give, and lawyers who regularly advise opinion recipients regarding, opinions of the kind involved."); The Committee on Legal Opinions of the American Bar Association's Section of Business Law, *Guidelines for the Preparation of Closing Opinions*, 57 BUS. LAW. 875, § 1.7, at 876 (2002) [hereinafter ABA Guidelines] (stating "An opinion giver is entitled to assume, without so stating, that in relying on a closing opinion the opinion recipient (alone or with its counsel) is familiar with customary practice concerning the preparation and interpretation of closing opinions."); 1998 TriBar Report, *supra* note 1, §§ 1.4(a), 1.6, at 601 n.24, 604.

3. A third-party closing opinion (a "closing opinion") is an opinion letter delivered at the closing of a business transaction by counsel for one party to another party. In most jurisdictions, an opinion giver has the obligation to the opinion recipient to exercise care in preparing a closing opinion. An opinion giver, however, does not owe the recipient the broader responsibilities lawyers owe to their

opinion contained in that report.⁴ The remedies opinion addresses the enforceability of each of the undertakings of the opinion giver's client (the "Company") in the agreement between the Company and the opinion recipient.⁵ These undertakings include affirmative and negative covenants of the Company and the remedies specified in the agreement for breaches by the Company of its contractual obligations. They also include provisions for interpreting and administering the agreement and resolving disputes under it.⁶

The meaning of the remedies opinion is based on the customary practice of lawyers who regularly give, and lawyers who regularly advise clients regarding, opinions of the kind involved.⁷ Customary practice allows the opinion to be expressed in only a few words and permits the opinion preparers to rely on many unstated exceptions, assumptions, and limitations.⁸ By amplifying the meaning of abbreviated opinion language, customary practice provides the framework for preparing and interpreting the opinion, thus facilitating the process by which opinions are given and received and reducing cost.

Like other opinions typically included in a closing opinion, the remedies opinion requires the opinion preparers to make professional judgments regarding application of the law covered by the opinion to the provisions of the agreement.⁹

own clients. The responsibilities of an opinion giver in delivering a closing opinion are limited to the opinions rendered, as interpreted in accordance with customary practice. See 1998 TriBar Report, *supra* note 1, § 1.2(a), at 595–97. An opinion giver should not, however, render an opinion that it believes will be misleading to the recipient under the circumstances. See *id.* § 1.4(d), at 602–03.

4. The remedies opinion (also called the "enforceability opinion") is discussed in Article III of the 1998 TriBar Report. The following example of a remedies opinion is included in that Report: "The Agreement is a valid and binding obligation of the Company enforceable against the Company in accordance with its terms." *Id.* § 3.1, at 619.

5. See *id.* § 3.1, at 619–21. This Report assumes that the Company is a corporation; for its application to other entities, see *id.* § 1.2(g), at 599.

6. For a discussion of the categories of contractual undertakings addressed by the remedies opinion, see *id.* § 3.1, at 619–21.

7. See *supra* note 2. The customary practice relevant to any particular opinion is the customary practice applicable on the date of the opinion. Customary practice is described and discussed in the 1998 TriBar Report and other bar association reports and scholarly writings. See, e.g., ABA Principles, *supra* note 2; ABA Guidelines, *supra* note 2. See generally DONALD W. GLAZER ET AL., GLAZER AND FITZGIBBON ON LEGAL OPINIONS: DRAFTING, INTERPRETING AND SUPPORTING CLOSING OPINIONS IN BUSINESS TRANSACTIONS (2d ed. 2001), which reproduces many of the bar association reports and includes a bibliography of scholarly writings. Customary practice is not static; rather, it changes over time as opinion practice evolves and new issues emerge and are addressed.

8. See 1998 TriBar Report, *supra* note 1, §§ 1.2(a), 1.4(a), at 595–97, 600–01. See also RESTATEMENT OF LAW GOVERNING LAWYERS, *supra* note 2, § 95, reporter's note to cmt. c, which states: "In giving 'closing' opinions, lawyers typically use custom and practice to provide abbreviated opinions that facilitate the closing. Such opinions may not recite certain assumptions, limitations, and standards of diligence because they are understood between counsel."

Like the law, closing opinions are the product not only of logic but of experience. See generally Oliver Wendell Holmes, Jr., THE COMMON LAW (Little, Brown and Co. 1963) (1881). The words of closing opinions, were they to be read literally and taken to their logical extreme, would not always square with the way they are understood in practice. Molded by experience, customary practice tempers logic with practicality, reflecting a realistic assessment of what lawyers can be expected to do, from the standpoint of expertise and cost, to support the opinions they render.

9. The opinion does not cover limitations on enforceability that arise under bodies of law that are excluded from the opinion either expressly by the coverage limitation (see *infra* note 25) or implicitly as a matter of customary practice. See ABA Principles, *supra* note 2, Part II: Law; 1998 TriBar Report,

That law includes both statutory law and case law. In the absence of statute or controlling precedent, opinion preparers look to general principles of contract law and, in particular, the principle that accords contracting parties broad latitude to order their affairs by agreement.¹⁰

The enforceability of contractual provisions is subject to the effect of bankruptcy and insolvency laws and the availability of equitable defenses. These matters are excluded from the opinion by the standard bankruptcy exception and equitable principles limitation which, although usually stated in the opinion, are understood to be applicable whether stated or not.¹¹ Furthermore, enforceability may depend on various factual matters that, as a matter of customary practice, are covered by assumptions of general application that apply even if not stated.¹² These include factual assumptions regarding the genuineness of signatures and conformity of copies with the originals.¹³ They also include assumptions regarding good faith and the absence of fraud, coercion, duress, and similar inequitable conduct preventing formation of an agreement.¹⁴

Some matters that affect enforceability do not fit neatly within the limitations described above but nevertheless, as a matter of customary practice, are understood not to be covered by the opinion. This may be, for example, because of the practical inability of lawyers to make the necessary determination of the reasonableness of an economic remedy¹⁵ or because of the discretion courts have under applicable law to decline to enforce an otherwise enforceable forum selection clause.¹⁶ Customary practice as to such matters reflects a practical assessment of what opinion recipients can reasonably expect lawyers to do in preparing the opinion.

supra note 1, § 3.5.1, at 627–28 (stating that opinion covers only law that a lawyer would reasonably recognize as being applicable), and § 3.5.2, at 629–30 (stating that certain specific laws are understood not to be covered unless expressly identified).

10. See RESTATEMENT (SECOND) OF CONTRACTS ch. 8, introductory note (1981) [hereinafter RESTATEMENT OF CONTRACTS]. See also E. ALLEN FARNSWORTH, CONTRACTS §§ 1.6, 1.7, and 5.1 (3d ed. 1999), which states:

The principle of freedom of contract rests on the premise that it is in the public interest to accord individuals broad powers to order their affairs through legally enforceable agreements. In general, therefore, parties are free to make such agreements as they wish, and courts will enforce them without passing on their substance. Occasionally, however, a court will decide that this interest in party autonomy is outweighed by some other interest and will refuse to enforce the agreement or some part of it.

11. See 1998 TriBar Report, *supra* note 1, § 3.3, at 622–25.

12. See *id.* § 2.3(a), at 615. See also *id.* § 2.3, at 616 (stating “Opinion preparers should not rely on an unstated assumption if it is unreliable.”).

13. See *id.* § 2.3(a), at 615.

14. See *id.* § 3.3.4, at 625 n.77.

15. See *infra* section III.B., “Economic Remedies Provisions,” at notes 46–50. Although the Committee believes the preferred course is usually to deal with the issue of reasonableness explicitly in the opinion, many lawyers do not take an express exception unless they have serious doubts about the reasonableness of a particular economic remedy.

16. See *infra*, section III.F., “Forum Selection Clause,” at notes 87–88. Although an express exception with regard to these matters is not required, some lawyers include one to avoid any risk of misunderstanding.

When an express exception or assumption¹⁷ is included in an opinion, its purpose should be to highlight a legal issue that could affect enforceability.¹⁸ Sometimes an express exception or assumption will be necessary for an opinion to be correct. At other times, it will be unnecessary but will help clarify how the opinion should be interpreted.

To maintain the opinion's effectiveness as a communication tool, the opinion preparers should consider, each time they give an opinion, which exceptions and assumptions are appropriate. The value of an opinion is undercut when the opinion preparers include exceptions and assumptions that relate to issues that are not covered by the opinion or that are not raised by the agreement.¹⁹ The inclusion of such exceptions and assumptions burdens the opinion process, requiring often protracted discussion over the opinion's meaning and coverage and obscuring the issues the opinion is intended to bring to the recipient's attention.²⁰

Part II of this Report describes a process for determining when the opinion preparers should include express exceptions or assumptions. Part III examines customary practice in giving opinions on the enforceability of several common contractual provisions.

II. DETERMINING WHEN TO INCLUDE EXPRESS EXCEPTIONS OR ASSUMPTIONS

In determining when to include express exceptions or assumptions, opinion preparers may wish to ask themselves one or more of the following questions:²¹

Do any of the Company's undertakings raise legal issues of concern?

To determine whether any of the undertakings of the Company in the agreement raise legal issues that call into question their enforceability,²² opin-

17. See 1998 TriBar Report, *supra* note 1, § 3.2, at 622. This Report uses the terms "express exception" to refer to any exception in an opinion other than the standard bankruptcy exception or equitable principles limitation, and "express assumption" to refer to any assumption set forth explicitly in an opinion other than an assumption of general application, which may be unstated. An express assumption may serve as a substitute for an express exception. See *id.* § 2.3, at 615-16. For example, when an agreement provides for a floating interest rate, the opinion preparers, rather than taking an exception for usury laws, might expressly assume that the interest rate will never exceed a specified level.

18. An opinion that is limited in a way that is not customary for transactions of the type involved is referred to as a "qualified opinion." See *id.* §§ 1.2(a), 1.9(i), at 595-97, 606-07. Sometimes opinion preparers conclude that an opinion can be given but should not be stated apart from its underlying reasoning. A reasoned (or explained) opinion may or may not be qualified. See *id.* See also *id.* § 1.6, at 604.

19. Nevertheless, when the size of the transaction or the significance of the issue does not justify the cost of fully researching the question, exceptions and assumptions that might have proven unnecessary after further inquiry are sometimes included and accepted by opinion recipients.

20. See ABA Guidelines, *supra* note 2, at 876 ("Closing opinions should not include assumptions, exceptions, and limitations that do not relate to the transaction and the opinions given.") See also Arthur Norman Field, *One Size Doesn't Fit All: Reject 'Kitchen-Sink' Responses in Opinion Letters*, BUS. LAW TODAY, May/June 2002, at 61-62.

21. The questions do not have to be asked in any particular order. For example, some opinion preparers may begin their inquiry with the law covered by the opinion rather than legal issues generally.

22. See 1998 TriBar Report, *supra* note 1, § 3.1, at 619-21. The principal focus of the remedies opinion is the legal effect of the agreement's provisions as a matter of contract law. The opinion, however, also covers issues arising under some other bodies of law. For example, to give a remedies

ion preparers review the law of each jurisdiction (state or federal) whose law is applicable²³ and make a professional judgment²⁴ whether under that law the highest court of that jurisdiction would enforce those undertakings. For state law, that court will be the highest court of the state in question and, for federal law, the United States Supreme Court.

The opinion preparers normally will not have to conduct legal research on every contractual provision each time they render an opinion. For many common provisions, the opinion preparers' existing knowledge and experience typically will be sufficient without further research to permit them to address the legal issues presented.

Does the legal issue arise under the law covered by the opinion?

When they have identified a legal issue of concern, the opinion preparers should consider whether it arises under the law covered by the opinion.²⁵

opinion, the opinion preparers normally need to satisfy themselves that the agreement has been properly authorized and executed, even if a separate opinion is not rendered on those matters. For a corporation, due authorization is a function of corporation law and due execution a function of corporation and agency law. Due authorization and due execution are sometimes dealt with by an express assumption or reliance on an opinion of local counsel—for example, when the opinion does not cover the corporation law of the state in which the Company was incorporated.

Due execution is also a matter of contract law. The contract law requirements governing due execution—such as those imposed by the Statute of Frauds or Sunday “blue laws”—normally will be those of the state whose law governs the agreement. *See generally* RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 198–202 (1971) [hereinafter RESTATEMENT OF CONFLICTS].

23. This Report generally assumes that the opinion covers the law of the jurisdiction whose law governs the agreement.

24. RESTATEMENT OF LAW GOVERNING LAWYERS, *supra* note 2, § 95 cmt. c, states:

[A] legal opinion . . . is based on legal research and analysis customary and reasonably appropriate in the circumstances and . . . states the lawyer's professional opinion as to how any legal question addressed in the opinion would be decided by the courts in the applicable jurisdiction on the date of the evaluation. The lawyer is not required to state reservations or doubts about legal issues unless they are of a nature that prevents the lawyer from reasonably concluding that the opinion reflects the result that would be reached by the highest court of the applicable jurisdiction.

The American Law Institute's former director, Herbert Wechsler, set forth the following “working formula” for the Institute's restatements of the law: “We should feel obliged in our deliberations to give due weight to all of the considerations that the courts, under a proper view of the judicial function, deem it right to weigh in theirs.” President's Letter, 20 ALI Rep., Summer 1998, at 1, 3. In forming the professional judgments called for by an opinion, opinion preparers normally take similar considerations into account.

25. Closing opinions customarily state that their coverage is limited to the law of specific jurisdictions (the “coverage limitation”). *See* 1998 TriBar Report, *supra* note 1, § 4.1, at 631–32 (referring to the “laws covered limitation”). For example, if the agreement chooses New York law as the governing law and the Company is a Delaware corporation, many New York lawyers will limit the opinion's coverage to New York law, federal law, and the Delaware General Corporation Law. *See id.* § 4.1, at 631 n.85. The coverage limitation excludes from the opinion the law of other jurisdictions even though that law could affect the enforceability of the agreement. Depending on how it is drafted, the coverage limitation also may exclude areas of law within a specified jurisdiction. For example, opinions on Delaware corporations often are limited to the Delaware General Corporation Law, which is understood to include only the Delaware corporation statute, applicable provisions of the Delaware constitution, and reported judicial decisions interpreting that statute and those constitutional provisions.

Sometimes the opinion will cover the enforceability of several agreements, each of which is governed by the law of a different jurisdiction. Ideally, the coverage limitation should expressly limit the opinion on each agreement to the law governing that agreement. If, however, the coverage limitation simply

An express exception or assumption is not necessary if the legal issue arises under the law of a jurisdiction that is excluded from the opinion by the opinion's coverage limitation²⁶ or if the legal issue arises under certain laws, such as tax, antitrust, and securities laws, that, as a matter of customary practice, are understood to be excluded from the opinion.²⁷

Is the legal issue covered by the opinion?

A legal issue that otherwise would require an express exception or assumption may already be addressed in some other way. For example, the bankruptcy exception excludes from the opinion the possibility that a covenant might not be enforced or a remedial provision might be stayed in bankruptcy. Similarly, the equitable principles limitation excludes the possibility that a court might decline to order specific performance of a particular contractual provision or to grant enforcement of contractual rights to a party with unclean hands.

A legal issue that otherwise would require an express exception or assumption also may be covered by an assumption of general application (which assumptions apply whether or not stated). Thus, the assumption regarding the genuineness of signatures (whether or not stated) excuses the opinion preparers from establishing that the agreement, in fact, was signed by the person who purported to sign it.

Finally, as discussed above, the issue might relate to a matter that is understood to be excluded from the opinion even if not expressly excluded.²⁸

Can the legal issue be resolved by factual inquiry?

The enforceability of a contractual provision may depend on the facts. For example, whether a loan violates the applicable usury statute may depend on whether the charges imposed on the borrower by the lender in connection with the loan when added to the contractual interest rate cause that rate to exceed the usury limit. The opinion preparers may be able to avoid an express exception or assumption by additional inquiry into the relevant facts. Thus, in the foregoing example, they may be able to obtain a schedule quantifying all the charges the borrower is paying to the lender in connection with a loan.

recites that the law of each of the jurisdictions is covered, the remedies opinion as it applies to a particular agreement is, as a matter of customary practice, understood to cover only the law of the jurisdiction chosen in that agreement as its governing law.

26. The fact that an opinion giver has multiple offices does not change the effect of the coverage limitation. The opinion preparers are responsible only for the law designated in the opinion for coverage and are not required to check on the law of other jurisdictions with their firm's offices in those jurisdictions.

27. See, e.g., 1998 TriBar Report, *supra* note 1, § 3.5.2(c), at 629–30. As indicated in that section, however, the Investment Company Act of 1940 may sometimes be covered. *Id.*

28. See *supra* notes 15 and 16 and accompanying text. See also *infra* note 62 (comity) and sentence in the text following note 69 in last paragraph of § III.E., "Chosen-Law Provision" (describing view of some lawyers).

Can the legal issue be avoided by restructuring the transaction or revising the agreement?

Sometimes, the transaction can be restructured or a contractual provision revised to avoid a legal issue. For example, if the agreement calls for a floating rate of interest (creating a risk that the interest rate could float above the applicable usury ceiling), that rate could be capped at the usury limit.

In deciding whether they need to include an express exception or assumption, opinion preparers need not ask all the questions outlined above or ask them in any particular order. Sometimes they will recognize immediately that an undertaking raises no legal issues or that a legal issue that otherwise would be of concern arises under laws that are not covered by the opinion. At other times, they will determine that a legal issue that initially concerned them is addressed by a standard exception or an unstated assumption or they will resolve it by further factual inquiry. In some cases, a potential legal issue will have been identified early on and avoided as an opinion issue in structuring the transaction.

When the opinion preparers conclude that an express exception or assumption should be included, they should promptly alert counsel for the opinion recipient.²⁹ Several alternatives might then be considered:

- Depending on the issues involved, the opinion recipient may decide to accept the opinion as qualified.³⁰ Exceptions to remedies opinions are often acceptable, especially when they relate to provisions that are generally recognized to raise concerns.
- The opinion preparers may be asked to look into the matter further. For example, additional legal research may reveal helpful authority or further factual inquiry may confirm that what initially appeared to be a problem in fact is not.
- The parties may agree to revise the agreement or the terms of the transaction to eliminate the problem. The agreement could be modified, for example, to make a provision waiving the Company's right to a jury trial sufficiently conspicuous to meet the applicable state's standard for enforceability.³¹

Which alternative the parties pursue will depend on various factors, including the nature of the legal issues involved and the expected cost of addressing them.

29. See 1998 TriBar Report, *supra* note 1, § 1.7, at 604–05 and ABA Guidelines, *supra* note 2, § 2.4, at 877–78, both discussing obligations under rules of professional conduct.

30. Another way used on occasion (e.g., in opinions on underwriting agreements in registered public offerings) to limit the opinion is to draft it to cover only matters of contract formation, such as due authorization, execution and delivery, and not enforceability.

31. See *infra* § III.C., “Waiver of the Right to a Jury Trial.”

III. APPLYING THE PROCESS DESCRIBED IN PART II TO COMMON CONTRACTUAL PROVISIONS

A. INTEREST ON OVERDUE INTEREST

Loan agreements sometimes provide for the payment of interest on overdue interest.³² Although the enforceability of an obligation to pay interest on overdue interest varies from state to state,³³ a provision requiring payment of interest on overdue interest is unenforceable in only a few states.³⁴ Some states have statutes validating provisions calling for the payment of interest on overdue interest.³⁵ Other states give effect to such provisions if specified requirements are met, such as a requirement that the intention to charge interest on overdue interest be clearly and prominently expressed in the agreement.³⁶

In most states, therefore, interest on overdue interest does not present an enforceability issue or the issue can be avoided by satisfying specified requirements. When, however, a legal problem exists and it has not been cured, for example, by proper drafting, an express exception or assumption ordinarily will be necessary.

32. An example is a clause providing:

Upon the occurrence and during the continuance of a default, the Company shall pay interest on the unpaid principal amount of the Note and on the unpaid amount of all interest payable hereunder that is not paid when due at a rate per annum equal to 2 percent above the rate otherwise required to then be paid on the Note.

Unlike other remedial provisions such as late charges and default rate interest on overdue principal, provisions for interest on overdue interest may, depending on the state, be unenforceable without regard to reasonableness. See *infra*, § III.B., "Economic Remedies Provisions."

33. See generally 45 AM. JUR. 2D *Interest and Usury* §§ 57–63 (1999); Annotation, *Validity of Agreement to Pay Interest on Interest*, 37 A.L.R. 325 (1925), supplemented in 76 A.L.R. 1484 (1932). Some states that generally enforce interest on overdue interest may have statutes prohibiting it in specified transactions, such as consumer loans. A requirement for interest on overdue interest may also violate a state's usury law. See 45 AM. JUR. 2D *Interest and Usury* § 176 (1999).

34. Interest on overdue interest should be distinguished from compound interest. In a number of states, compound interest may not be enforceable in some circumstances. See 15 SAMUEL WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 1417 (3d ed. 1968); Annotation, *What is "Compound Interest" Within Meaning of Statutes Prohibiting Charging of Such Interest*, 10 A.L.R. 3d 421 (1966).

35. See, e.g., N.Y. GEN. OBLIG. LAW § 5-527 (McKinney 2004) (applicable when original principal amount exceeds \$250,000). Prior to enactment of the New York statute in 1989, contractual undertakings to pay interest on overdue interest were not enforceable in New York under a line of cases dating back to *Young v. Hill*, 67 N.Y. 162 (1871). Those cases necessitated exceptions to opinions on the enforceability under New York law of agreements containing interest on overdue interest provisions and may account for the continuing perception of some lawyers that such provisions are problematic. See *Debentureholders Protective Comm. of Cont'l Inv. Corp. v. Cont'l Inv. Corp.*, 679 F.2d 264, 268, 271 (1st Cir. 1982), cert. denied, 459 U.S. 894 (1982) (upholding provision for interest on overdue interest in class of debentures governed by Massachusetts law but refusing to uphold provision in class governed by New York law as then in effect).

36. See, e.g., *Coupounas v. Madden*, 514 N.E.2d 1316, 1322 (Mass. 1987); *McConnell v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 662 P.2d 916, 921 (Cal. 1983); *Mountain States Broad. Co. v. Neale*, 783 P.2d 511, 555 (Utah Ct. App. 1989).

B. ECONOMIC REMEDIES PROVISIONS

Loan agreements often contain provisions that impose on the borrower a charge for late payments and a higher interest rate while the loan is in default.³⁷ As a matter of contract law, late charges and default interest rates typically are enforceable unless they are not reasonable in the circumstances and thus constitute a penalty.³⁸ The test for determining reasonableness varies from state to state, but generally a provision will be held to be reasonable if it bears a reasonable relationship to anticipated collection costs,³⁹ or, in some states in the case of a default interest rate, if it reflects the increased risk associated with the defaulted obligation.⁴⁰ Depending on the state, the courts also may consider whether an agreement relates to a commercial transaction and whether its terms were negotiated at arm's length by the parties or are consistent with industry practice.⁴¹

37. The agreements governing so-called A/B exchange transactions also usually include a provision increasing the interest rate if the securities are not registered under the Securities Act of 1933 by a specified date. In an A/B exchange, the registration covers the issuance of securities in exchange for like securities that were initially sold in an exempt offering. The higher interest rate is intended to reflect the increased risk to the holder associated with its inability to resell the securities publicly.

38. For cases applying a liquidated damages test to the determination of late charges as a penalty, see, e.g., *Collins v. Union Fed. Sav. and Loan Assoc.*, 662 P.2d 610, 618 (Nev. 1983); *Krupp Realty Co. et al. v. Joel*, 309 S.E.2d 641, 642 (Ga. Ct. App. 1983); and *S.E. Land Fund v. Real Estate World*, 227 S.E.2d 340, 342 (Ga. 1976). See also *DeCordova v. Weeks*, 140 N.E. 269 (Mass. 1923); *A-Z Servicer, Inc. v. Segall*, 138 N.E.2d 266, 269 (Mass. 1956) (voiding the doubling of the interest rate and an acceleration of the interest to maturity as penalties). Some states also subject late charges and default interest rates to state usury laws. See, e.g., *Begelfer v. Najarian*, 409 N.E.2d 167, 175 (Mass. 1980).

39. See, e.g., *Mack Fin. Corp. v. Ireson*, 789 F.2d 1083, 1084 (4th Cir. 1986) (upholding late charges as reasonable); *In re Egea*, 167 B.R. 226, 231 (Bankr. D. Kan. 1994); *In re Consolidated Prop. Ltd. P'ship*, 152 B.R. 452 (Bankr. D. Md. 1993); *In re Melbell Assoc. Inc.*, 99 B.R. 31, 34 (Bankr. E.D. Cal. 1989) (upholding a four percent late charge); *In the Matter of Terry Ltd. P'ship*, 27 F.3d 241, 244 (7th Cir. 1994) (three percent increase not unreasonable); *Travelers Ins. Co. v. Corporex Properties, Inc.*, 798 F. Supp. 423, 427-28 (W.D. Ky. 1991) (four percent late charge not unreasonable); *In re Gas Reclamation, Inc. Sec. Litig.*, 741 F. Supp. 1094, 1098 (S.D.N.Y. 1990) (three percent increase not unreasonable); *Fleet Bank of Massachusetts, N.A. v. One-O-Six Realty, Inc.*, No. Civ. A. 94-3392-G, 1995 WL 389862, at *3 (Mass. Super. Jan. 17, 1995) (default interest rate of four percent over the contract rate reasonable, citing several federal courts that upheld an increased interest rate of three to four percent in the event of default).

The test for reasonableness cannot be applied mechanically because an economic remedy, such as a late fee or default interest rate, that has been found to be reasonable in one factual context may be found not to be reasonable in another. For example, the reasonableness of a particular percentage may depend on the amount involved and other factors. See *Howard Johnson Int'l. Inc. v. HBS Family Inc.*, No. 96 CIV. 7687(SS), 1998 WL 411334, at *7 (S.D.N.Y. July 22, 1998) ("one size fits all" economic remedy not enforced on grounds that the same damage amount is not reasonable for all defaults).

40. See, e.g., *Dikeou v. Dikeou*, 928 P.2d 1286, 1290 (Colo. 1997); *Bloom v. Trepanal*, 289 N.Y.S.2d 447 (N.Y. App. Div. 1968) and *Union Estates Co. v. Adlon Constr. Co.*, 221 N.Y. 183, 184 (1917).

41. 24 SAMUEL WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 65:13 (4th ed. 1997). See *Metlife Capital Fin. Corp. v. Wash. Ave. Assocs., L.P.*, 732 A.2d 493 (N.J. 1999) (referring to industry practice in dealing with the reasonableness of a late fee of five percent and default interest rate of three percent above the stated rate). In upholding both a late fee and default interest rate, the court stated that "[t]he overall single test of validity is whether the [stipulated damage] clause is reasonable under the totality of the circumstances" and that "liquidated damages provisions in a commercial contract between sophisticated parties are presumptively reasonable and the party challenging the clause bears the burden of proving its unreasonableness." *Id.* at 499 (alterations in original) (internal citation omitted).

Some loan agreements require borrowers under specified circumstances to pay so-called "make-whole premiums" when repaying loans prior to maturity.⁴² The enforceability of make-whole premiums also typically depends on their reasonableness.⁴³ Courts view favorably make-whole premiums expressed as a formula that discounts to present value the interest lost by a lender when a loan is discharged prior to its stated due date. Agreements often contain a formula that follows an approach approved by the courts.⁴⁴

Liquidated damages, whether or not denominated as such, are also a type of economic remedy. Courts have adopted various tests for determining when a liquidated damages provision is enforceable.⁴⁵ In applying these tests to any particular provision, courts often rely on economic analysis and expert testimony.

In routine commercial transactions, lawyers may have little difficulty satisfying themselves that the economic remedies in the agreement—e.g., the late charge and default interest rate in a loan agreement—are reasonable under the law of the jurisdiction whose law is covered by the opinion. In other transactions, however, the opinion preparers may not be able to determine the reasonableness of an economic remedy. To do so may require knowledge of facts that are not ascertainable by the opinion preparers.⁴⁶ In addition, for many provisions, the case law, to the extent it exists, may be too particularized to provide meaningful guidance. When they conclude that the reasonableness of an economic remedy cannot be determined as a practical matter, some opinion preparers routinely include an express exception or assumption in their opinion.⁴⁷ Practice, however, is not universal. Other opinion preparers, in like circumstances, regard their inability to make a determination of reasonableness to be so well understood that they follow

42. Make-whole premiums often apply not only to voluntary repayments but also to early repayments necessitated by a default, change of control or failure to maintain a specified rating.

43. What is reasonable is usually a question of state law. In the case of secured claims, section 506(b) of the Bankruptcy Code could also apply. See *In re Anchor Resolution Corp.*, 221 B.R. 330, 340 (Bankr. D. Del. 1998). However, the effect of section 506(b) is excluded from the opinion by the bankruptcy exception.

44. Courts have approved various formulas as reasonable. See *id.* See generally Chester L. Fisher III, *Make-Whole Prepayment Premiums Under Attack*, 45 BUS. LAW. 15 (1989) and cases cited therein.

45. Most states look to whether the amount specified is a reasonable estimate of the damages that would be caused by a breach, determined at the time of contract. Some states apply a "second-look" test, which requires that the amount specified also be reasonably proportionate to the damages actually caused. See *Kelly v. Marx*, 705 N.E.2d 1114, 1115 (Mass. 1999) (upholding a liquidated damages provision and cataloging the various state law tests). See also *BDO Seidman v. Hirshberg*, 93 N.Y.2d 382, 396 (1999). In *Brazen v. Bell Atlantic Corp.*, 695 A.2d 43, 48 (Del. 1997), the Delaware Supreme Court, in upholding a merger break-up fee denominated in the agreement as liquidated damages, stated that to be unenforceable "the amount at issue must be unconscionable or not rationally related to any measure of damages a party might conceivably sustain." See also *Truck Rent-A-Center, Inc. v. Puritan Farms 2nd, Inc.*, 361 N.E.2d 1015 (N.Y. Ct. App. 1977).

For a provision to be enforceable many states also require that actual damages be uncertain or difficult to ascertain at the time of contract. See RESTATEMENT OF CONTRACTS, *supra* note 10, § 356 cmt. b. In many transactions, such as long-term leases and other complex financings, opinion preparers have no difficulty concluding that this requirement is satisfied.

46. For example, the relevant facts (such as the loss the opinion recipient expects to incur in the event of a default) may be known only to the opinion recipient.

47. These opinion preparers follow the practice of omitting an express exception or assumption only when they have satisfied themselves that the economic remedy is reasonable.

the practice—unless they have serious doubts about the reasonableness of a particular remedy⁴⁸—of not taking an exception.⁴⁹ Although both practices are widely followed, the Committee believes that in most instances the preferred course is for the opinion preparers to deal with the issue of reasonableness explicitly in the opinion.⁵⁰

C. WAIVER OF THE RIGHT TO A JURY TRIAL

Agreements sometimes contain waivers by the parties of their right to trial by jury in the event of a dispute. Most jurisdictions permit such waivers.⁵¹ In those

48. Serious doubt may exist, for example, because the amount involved greatly exceeds amounts that are customary or sanctioned by controlling precedent, or the methodology for calculation differs from the methodology used in cases in which a similar remedy was upheld by the courts.

49. Lawyers who follow this practice believe that, when an economic remedy is neither clearly reasonable nor clearly unreasonable, an opinion giver cannot be expected to consider and weigh all the factors a court would need to consider when deciding whether the remedy is enforceable. The analysis required to evaluate reasonableness in these circumstances is different, in kind, from the analysis an opinion giver would conduct when the possible future event under which the provision would be unenforceable is readily identifiable and a determination of the legal consequence of the event is straightforward. In the case of a floating interest rate, for example, opinion givers may, depending on the state, be required to take an exception if the rate could increase above the applicable usury rate ceiling because that future event is easy to identify and its legal consequences are clear. See 1998 TriBar Report, *supra* note 1, § 3.5.2(c), at 629–30. In contrast, opinion preparers, in evaluating the reasonableness of an economic remedy, may have to consider a variety of factors that are not readily identifiable and susceptible to straightforward analysis, such as the nature of likely future defaults, their possible timing, and the harm that the opinion recipient may foreseeably be expected to suffer.

50. Agreements in complex leasing and secured financing transactions often provide for economic remedies (such as liquidated damages), remedies against property (such as means of repossession or foreclosure), and remedial procedures (such as confessions of judgment) that may raise legal concerns. See, e.g., *In re Trans World Airlines, Inc.*, 145 F.3d 124, 134 (3d Cir. 1998). *But see* *Wilmington Trust Co. v. Aerovias de Mexico*, 893 F. Supp. 215 (S.D.N.Y. 1995). Opinions in these transactions sometimes contain a “practical realization” exception. See 1998 TriBar Report, *supra* note 1, § 3.4, at 626–27. When they do, the enforceability opinion is understood not to cover the reasonableness of any particular remedial provision.

51. See Jay M. Zitter, Annotation, *Contractual Jury Waiver in State Civil Cases*, 42 A.L.R. 5th 53 §§ 2[a] & 3 (1996). See also *Barclays Bank of New York v. Heady Elec. Co.*, 571 N.Y.S. 2d 650, 652 (N.Y. App. Div. 1991); *Gunn v. Palmieri*, 589 N.Y.S.2d 577, 577 (N.Y. App. Div. 1992); *Palmer v. Lavers*, 105 N.E. 1000, 1002 (Mass. 1914); *Chase Commercial Corp. v. Owen*, 588 N.E.2d 705, 708 (Mass. App. Ct. 1992). Georgia and North Carolina are exceptions to the general rule. See *Bank S., N.A. v. Howard*, 444 S.E.2d 799, 800 (Ga. 1994) (waiver of jury trial entered into independently of specific litigation not enforceable); N.C. GEN. STAT. § 22B-10 (2003) (waiver of jury trial void as contrary to public policy). California may also be an exception. Compare *Grafton Partners L.P. v. Superior Court*, 2004 Cal. App. LEXIS 153 (Cal. Ct. App. Feb. 6, 2004), *rev. granted*, with *Trizec Properties, Inc. v. Superior Court*, 229 Cal. App. 3d 1616 (1991). Even in jurisdictions where jury trial waivers are enforceable generally, such waivers may not be enforceable for certain types of claims. For example, in New York waivers of jury trial in leases of real property are ineffective as to claims for personal injury or property damages. N.Y. REAL PROP. § 259-c (McKinney 2003). Many New York leases specifically exclude those claims from the waiver, thus eliminating the need for an opinion exception.

Although the effectiveness of a waiver of jury trial ultimately will be determined under the law of the forum in which the dispute is adjudicated, see *infra* note 62, unless an opinion otherwise states, it addresses enforcement of the waiver under the law of the jurisdiction whose law is covered by the opinion (and not under the law of other jurisdictions in which a dispute might, in fact, be adjudicated).

jurisdictions, no legal issue is presented, and an express exception or assumption is unnecessary.⁵²

Some jurisdictions prohibit the parties to an agreement from waiving in advance their right to a jury trial or impose conditions on such a waiver. In those jurisdictions, an express exception or assumption would be necessary unless the conditions for enforceability of the waiver are satisfied or the legal bases for not enforcing the waiver are covered by a standard exception or unstated assumption.⁵³

Often, when states impose conditions on enforcing a jury waiver, those conditions will not necessitate an exception. Some jurisdictions, for example, require that a waiver be sufficiently "conspicuous."⁵⁴ In those jurisdictions, if the waiver is not conspicuous initially, it ordinarily will be made conspicuous. Other jurisdictions require the waiver to be "knowing or intentional."⁵⁵ In those jurisdictions, the opinion preparers ordinarily will satisfy themselves that their client is aware of the waiver.

D. NO ORAL MODIFICATION CLAUSE

Many agreements state that they may not be modified or their provisions waived except by a writing signed by the party against whom enforcement is sought. Some states have statutes validating no oral modification clauses.⁵⁶ In most other states, the parties to an agreement, as a matter of freedom of contract, may legally bind themselves to such a clause.⁵⁷

In practice, however, courts often decline to enforce no oral modification clauses, even in states with statutes that expressly validate them.⁵⁸ The reason is that under the facts presented the party against whom enforcement is sought typically has relied on an oral modification to its detriment or has given additional

52. The Seventh Amendment to the U.S. Constitution does not preclude a party from agreeing to a waiver. See *Melancon v. McKeithan* 345 F. Supp. 1025, 1045 (E.D. La. 1972), *aff'd*, 409 U.S. 1098 (1973) (under Due Process Clause of Fourteenth Amendment, Seventh Amendment does not require states to provide jury trial in civil cases).

53. One basis some courts use to decline to enforce a jury trial waiver is the inequitable conduct of the party seeking enforcement in obtaining the waiver. See *Rosenberg v. Merrill Lynch*, 995 F. Supp. 190, 192 (D. Mass. 1998). An opinion is based on an unstated assumption regarding the absence of such conduct. See 1998 TriBar Report, *supra* note 1, § 3.3.4, at 625 n.77.

54. See, e.g., *Balram v. Etheridge*, 449 N.Y.S.2d 389, 391 (1982) (holding clause in lease unenforceable because of failure to conform to minimum print size required by statute); *Fairfield Leasing Corp. v. Technographics, Inc.*, 607 A.2d 703, 706 (N.J. Super. Ct. Law Div. 1997) (finding no waiver because clause was "utterly inconspicuous"); *Colgate Constr. Corp. v. Hill*, 334 N.Y.S.2d 1002, 1004 (1972) (finding waiver invalid because clause located inconspicuously on back of home improvement contract).

55. See, e.g., *Malan Realty Investors Inc. v. Harris*, 953 S.W.2d 624, 627 (Mo. 1997) (requiring that waiver be knowing and voluntary); and *Gaylord Dep't Stores, Inc. v. Stephens*, 404 So. 2d 586, 588 (Ala. 1981) (finding waiver ineffective where not knowingly or intelligently made).

56. See, e.g., N.Y. GEN. OBLIG. LAW § 15-301 (McKinney 2003). See also U.C.C. § 2-209(2) (2003).

57. For a contrary rule, see *Son-Shine Grading, Inc. v. APC Constr. Co.*, 315 S.E.2d 346, 349 (N.C. Ct. App. 1984), *disc. rev. denied*, 321 S.E.2d 900 (N.C. 1984).

58. See 15 SAMUEL WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 1828 (3d ed. 1968).

consideration for the modification.⁵⁹ These bases for refusing to enforce a no oral modification clause do not require an express exception or assumption. The first basis, detrimental reliance, is excluded from the opinion by the equitable principles limitation, which covers principles, such as equitable estoppel, that prevent a party making an oral modification from challenging the other party's reliance on it.⁶⁰ The second basis, additional consideration, is not covered by the opinion because the payment of additional consideration creates a new contract,⁶¹ and only the existing contract and not the new contract is the subject of the opinion.

E. CHOSEN-LAW PROVISION

The remedies opinion addresses the enforceability of the provision included in most agreements that chooses the law of a particular jurisdiction as the governing law.⁶² Most states take one of two approaches to the enforceability of chosen-law provisions: the statutory approach or the Restatement approach.⁶³

59. Thus, if a bank were to invoke a no oral modification clause and revoke an oral waiver by a bank officer, a court will decline to enforce the clause and will give effect to the waiver if the borrower has relied on the waiver to its detriment or given consideration for the waiver.

60. See, e.g., *Nassau Trust Co. v. Montrose Concrete Products Corp.*, 56 N.Y.2d 175, 183 (1982); *Walter v. Hoffman*, 267 N.Y. 365, 370 (1935) (“Even then, the question remains in each case whether a plaintiff has shown that a court should exercise its equitable power to prevent injustice.”). See also *Whittier v. Dana*, 92 Mass. (10 Allen) 326 (1865); *Stearns v. Hall*, 63 Mass. (9 Cush.) 31 (1851); 1998 TriBar Report, *supra* note 1, § 3.3.4, at 625.

61. Referring to oral modifications to a written contract that expressly required any modifications to be in writing, Judge (later Justice) Holmes wrote in 1889 that “[a]ttempts of parties to tie up by contract their freedom of dealing with each other are futile.” *Bartlett v. Stanchfield*, 148 Mass. 394, 395 (1889). Williston explains that an oral modification supported by sufficient consideration rescinds the no oral modification clause in the original contract. 15 SAMUEL WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 1828, at 496 (3d ed. 1972). See, e.g., *First Pa. Mortgage Trust v. Dorchester Savs. Bank*, 481 N.E.2d 1132, 1138–39 (Mass. 1985) (stating that, “[i]t is a settled principle that the mode of performance required by a written contract may be varied by a subsequent oral agreement based upon a valid consideration,” and finding the oral exchange of promises by two banks in a loan participation arrangement to be valid consideration) (internal citations omitted).

62. Even if the law chosen in the agreement to govern is determined by a court to be the law generally governing the agreement, that law will not necessarily govern every aspect of the agreement. See 1998 TriBar Report, *supra* note 1, § 4.5, at 634. Some aspects of the agreement may be governed by mandatory choice of law rules. *Id.* For example, the effectiveness of a provision relating to conduct of a judicial proceeding, such as a waiver of jury trial, is governed by the law of the forum in which the dispute is adjudicated, whether or not that is the law chosen in the agreement. A remedies opinion does not require an exception for the possibility that the substantive law of a state whose law is excluded from the opinion by the coverage limitation might be applied to some aspects of the agreement as a result of a mandatory choice of law rule. If, however, the opinion preparers recognize that the law of another state would apply—such as they might in the case of a voting trust for a corporation's shares under the “internal affairs” doctrine—and believe that it would invalidate a provision of the agreement, the opinion preparers should consider whether giving the opinion, without bringing the issue to the attention of the opinion recipient, would be misleading. See *id.* § 1.4(d), at 602–03.

Under the principle of “comity,” a court may give deference to an act of a foreign sovereign state whose law is not chosen to govern the agreement. Because application of the principle of comity is so well understood, it ordinarily does not require a further exception. *Id.* at § 3.1 n.71. Nevertheless, when the Company is a non-United States entity, some lawyers point out in their opinion that the enforceability of the agreement may be limited by the principle of comity. See *Allied Bank International v. Banco Credito Agricolade Cartago*, 757 F.2d 516, 522 (2d Cir. 1985).

63. Even if a state has a statute, it may follow the Restatement approach when the statute does not apply. This Report does not address opinions on chosen-law provisions whose enforceability is not governed by a statute or the Restatement approach.

Under the statutory approach, for commercial transactions involving more than a specified dollar amount, some states, including New York, Delaware, Illinois, and California, validate by statute contractual provisions selecting their law as the governing law regardless of whether the parties or transaction have a reasonable relation with their state.⁶⁴ Under the Restatement approach, states enforce chosen-law provisions unless (i) the jurisdiction whose law is the chosen law has no substantial or other reasonable relationship to the parties to the transaction or the transaction itself or (ii) application of the chosen law would be contrary to a fundamental policy of another jurisdiction that has a materially greater interest in the determination of the issue and that would be the jurisdiction whose law would apply in the absence of an effective chosen-law provision.⁶⁵

In states that have adopted the statutory approach, opinion preparers typically have no difficulty concluding that an exception is not required. Thus, a New York opinion giver rendering an opinion on an agreement covered by the New York statute that chooses New York law as its governing law can render the opinion based solely on its determination that the requirements of the statute have been satisfied without concerning itself about contacts with New York.⁶⁶

64. N.Y. GEN. OBLIG. LAW § 5-1401 (McKinney 2004); DEL. CODE ANN. tit. 6, § 2708 (2002); 735 ILL., COMP. STAT. § 105/5-5 (West 2004); CAL. CIV. CODE § 1646.5 (West 2004).

65. RESTATEMENT OF CONFLICTS, *supra* note 22, § 187(2) validates a chosen-law provision

unless either (a) the chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties' choice, or (b) application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of the particular issue and which, under the rule of Section 188 [the state with the most significant relationship to the transaction and the parties], would be the state of the applicable law in the absence of an effective choice of law by the parties.

States may have fundamental policies, for example, with regard to non-competition provisions and distributorship arrangements.

If the Uniform Commercial Code applies, U.C.C. § 1-301 (2003) provides that, except as specified in other provisions of the Uniform Commercial Code, in commercial transactions the parties' choice of governing law is effective whether or not the transaction bears a relation to the state or country whose law is designated, except to the extent application of the chosen law would be contrary to a fundamental policy of the state or country whose law would govern in the absence of a choice of law by the parties.

66. Many opinion preparers in New York give the opinion in negotiated commercial transactions to which the New York statute applies even when the transaction and the parties have few, if any, contacts with New York beyond the contractual choice of New York law. Some opinion preparers, however, in that situation prefer to address the contacts issue explicitly in the opinion. Although not finding constitutionality to be an issue in the case before it, one federal court has observed that the courts have not considered whether the reach of the New York statute is subject to constitutional limitations. See *Lehman Bros. Comm. Corp. v. Minmetals Int'l Non-Ferrous Metals Trading Co.*, 179 F. Supp. 2d 118, 137 (S.D.N.Y. 2000) (stating in dictum, "It remains to be seen, however, whether a state with no connection to either the parties or the transaction could apply its own law, consonant with the Full Faith and Credit Clause, when doing so would violate an important public policy of a more-interested state."). See also *Int'l Indosuez Finance B.V. v. National Reserve Bank*, No. 601467/99, 1999 N.Y. Misc. LEXIS 476 (N.Y. Sup. Ct. Oct. 22, 1999) (refusing to entertain constitutional challenge to the New York statute on the facts of that case, noting that "[t]he [t]ransactions bear a sufficient relationship to New York to support the application of New York law consistent with Due Process—wholly apart from GOL §5-1401. . . ."), *aff'd* on other grounds in *Indosuez Int'l Finance B.V. v. National Reserve Bank*, 720 N.Y.S. 2d 102 (App. Div. 2001), *aff'd* 98 N.Y.S. 2d 238 (2002); *Allstate Ins. Co. v. Hague*, 449 U.S. 302, 308 (1981).

In states that follow the Restatement approach, the analysis is more complex. In those states, the parties' choice of law will be given effect unless one of the two Restatement exceptions applies. The first exception applies when the chosen-law state has no substantial relationship with the transaction or the parties and no other reasonable basis exists for the parties' choice.⁶⁷ Whether a sufficient relationship exists depends on such factors as the jurisdictions in which the parties are organized, the parties' business locations, the place of negotiation and closing, the place where significant aspects of the agreement are to be performed (such as funding of loans, making of payments, delivery of goods, or performance of services), and the location of the subject matter of the contract or relevant bank accounts. The existence of one or more of these factors often permits the opinion preparers to make a professional judgment that the first of the Restatement's exceptions does not apply. When they cannot, the opinion preparers sometimes can arrange for a modification in the structure of the transaction to create the necessary contacts.

The second Restatement exception calls for application of the substantive law of a state other than the chosen-law state if (i) that other state has a materially greater interest in the determination of the particular issue and its law would be applied in the absence of an effective governing law clause, and (ii) application of the chosen-law state's law would be contrary to a fundamental policy of that other state.⁶⁸ This exception is not read to require opinion preparers to consider the possible application of the substantive law of a state whose law is not identified for coverage in the opinion's coverage limitation.⁶⁹ Some lawyers view this simply as an aspect of customary practice. Many others view the coverage limitation as excluding both the substantive law of states whose law is not expressly identified for coverage and the possible application of that law under choice-of-law principles. Thus, for example, when the state whose law is covered by the opinion and the chosen-law state are the same (e.g., they are both Massachusetts),⁷⁰ the

67. RESTATEMENT OF CONFLICTS, *supra* note 22, § 187, cmt. f. See *Auten v. Auten*, 308 N.Y. 155, 159–60 (1954) (applying choice-of-law principles to a contract in the absence of a chosen-law provision), which predates the New York statute. See also *Allstate Ins. Co. v. Stolarz*, 613 N.E.2d 936 (N.Y. 1993).

68. RESTATEMENT OF CONFLICTS, *supra* note 22, § 187(2)(b).

69. An opinion giver may not, however, knowingly mislead an opinion recipient with regard to matters covered by the opinion. See 1998 TriBar Report, *supra* note 1, § 1.4(d), at 602–03. Thus, if the opinion preparers recognize that a provision of the agreement is contrary to a fundamental policy of another state whose law would be applied by the chosen-law state in the absence of an effective governing law clause, they should consider whether giving an opinion that the chosen-law provision is enforceable, without bringing the issue to the attention of the opinion recipient, would be misleading.

70. When the law covered by the opinion is not the same as the law chosen in the agreement (e.g., a Massachusetts lawyer is asked to render an opinion on an agreement that chooses New York law), an opinion on the agreement might be limited to the enforceability of the chosen-law provision (i.e., whether a Massachusetts court, applying Massachusetts law, will give effect to the choice of New York law). See *id.* § 4.6, at 635–36. When it is so limited, this opinion often is accompanied by an opinion on the enforceability of the agreement if the substantive law of the state whose law is covered by the opinion (Massachusetts) were to apply. When both opinions are given, they are often combined by adding to the opinion on the enforceability of the chosen-law provision an opinion to the following effect: "but if the internal law of Massachusetts were nevertheless held to be applicable, the Agreement

opinion preparers are not required to point out in the opinion that they have only considered the chosen-law state's (Massachusetts') relationship to the parties or the transaction, and not the possibility that the substantive law of some other state might be relevant under the choice-of-law principles of the chosen-law state. Nevertheless, when another state has a significant relationship with the parties or the transaction, some lawyers choose to address the issue explicitly by including in their opinions an express assumption that the agreement does not violate the fundamental policies of other states or an express exception to like effect.

F. FORUM SELECTION CLAUSE

Commercial agreements often specify the forum where disputes between the parties are to be resolved.⁷¹ Usually that forum is a court in the state whose law is chosen in the agreement as the governing law.⁷²

Forum selection clauses may be either permissive or mandatory. A permissive clause authorizes the parties to a contract to bring suit in the specified jurisdiction but does not preclude a party from bringing suit elsewhere.⁷³ A mandatory clause

would constitute the Company's valid and binding obligation enforceable against it in accordance with its terms under Massachusetts law." This latter opinion has the same meaning as any other remedies opinion except that it does not address the enforceability of the chosen-law provision.

In a Restatement state (like Massachusetts), the opinion that the chosen-law provision selecting the law of another state (New York) will be given effect (under Massachusetts law) requires the opinion preparers to consider whether the "no substantial/reasonable relationship" exception to the Restatement's general approach to validating governing law provisions applies. If that exception does not apply (e.g., New York has a sufficient relationship to the parties or the transaction), the opinion requires the opinion preparers to determine whether the state whose law has been identified for coverage in the opinion (Massachusetts) has a fundamental policy that would be violated by the agreement. If they could render an unqualified opinion that the agreement would be enforceable if the law covered by the opinion (Massachusetts law) were to apply, they would not have to take an exception for violation of a fundamental policy of that state. If the agreement is enforceable under that state's law (Massachusetts law), that state (Massachusetts), by definition, would not have a fundamental policy against enforcement even if it were to have a materially greater interest in an issue. See *Chase Manhattan Bank, N.A. v. Greenbrier North Section II*, 835 S.W.2d 720, 725 (Tex. App. 1992). See also *Guardian Sav. & Loan Assn. v. MD Assocs.*, 64 Cal. App. 4th 309, 322-23 (1998) (choice of Texas law given effect notwithstanding violation of California's fundamental policy against deficiencies in certain transactions because California did not have a materially greater interest in the issue than Texas).

71. A forum selection clause may designate the courts within a specific jurisdiction, for example, "the courts of the State of New York or a federal court located in New York." Sometimes it may designate a specific venue within the jurisdiction, such as "the courts of the State of New York located within New York County or the United States District Court for the Southern District of New York."

72. Because forum selection clauses normally designate the courts of the jurisdiction whose law is chosen as the governing law, this Report does not address opinions on clauses that designate the courts of other jurisdictions. See *supra* note 25. See also *Cambridge Biotech Corp. v. Pasteur Sanofi Diagnostics*, 740 N.E.2d 195, 201 (Mass. 2000), for an example of a clause selecting courts not located in the chosen-law jurisdiction. This Report generally assumes that the forum selection clause designates the courts located in a jurisdiction whose law is covered by the opinion.

73. An example of a permissive clause is: "The parties agree that any action involving a dispute under this agreement may be brought in the courts of the State of New York or a federal court located in New York, and they hereby submit to the jurisdiction of those courts."

requires the parties to bring suit only in the specified jurisdiction.⁷⁴ A forum selection clause is often accompanied by a consent by the parties to jurisdiction in the selected forum and may specify acceptable methods for service of process. Sometimes a permissive clause is accompanied by a waiver by the parties of their right to assert the doctrine of *forum non conveniens*.⁷⁵

In determining whether they can render an opinion on a forum selection clause, the opinion preparers should consider the following:

Jurisdiction

Whether a clause is permissive or mandatory, a court will not give it effect unless the court has personal jurisdiction over the parties and subject matter jurisdiction over the issue in dispute.⁷⁶ Normally, inclusion of a forum selection clause in an agreement is itself sufficient to confer personal jurisdiction.⁷⁷ Similarly, selection of a court of general jurisdiction as the designated forum normally is sufficient to satisfy the requirement of subject matter jurisdiction.⁷⁸

Applicable Legal Standard

Historically, most states took the position that, whatever an agreement might specify, courts should be free to determine for themselves whether to accept cases brought before them based on such factors as the sufficiency of contacts, the burden on the court, convenience, and the availability of other forums. When a forum selection clause is governed by the law of a state that

74. An example of a mandatory clause is: "The parties agree that any dispute involving this agreement shall be brought exclusively in the courts of the State of New York or a federal court located in New York, and they hereby submit to the jurisdiction of those courts."

75. *Forum non conveniens* is the doctrine under which a court may dismiss an action if, for the convenience of the parties, the witnesses, or the court, it decides that the action should proceed in another available forum in which the action might originally have been brought. See RESTATEMENT OF CONFLICTS, *supra* note 22, § 84.

In New York, by statute, parties to a qualifying contract are deemed to have waived their right to assert the doctrine of *forum non conveniens* even when they do not do so expressly. See *infra* note 91.

76. Opinion preparers address these jurisdictional requirements based on the facts as of the date of the opinion and need not point out that circumstances may change in the future.

77. Courts generally interpret a forum selection clause as a consent to personal jurisdiction in the designated forum. See, e.g., *Nat'l Union Fire Ins. Co., v. Williams*, 637 N.Y.S.2d 36, 37, 39 (N.Y. App. Div. 1996) (addressing agreement not covered by the New York statute validating forum selection clauses). To be covered by the New York statute, N.Y. GEN. OBLIG. LAW § 5-1402 (McKinney 2004), an agreement must include an express consent to the jurisdiction of the New York courts.

78. Forum selection clauses normally do not specify a particular type of court. An exception is the selection of the Delaware Chancery Court as the venue to adjudicate disputes (as permitted by section 111 of the Delaware General Corporation Law). If a clause specifies a particular type of court, the opinion preparers must determine whether disputes under the agreement are within that court's subject matter jurisdiction. The parties cannot by contract confer subject matter jurisdiction on a court.

When a forum selection clause permits but does not require an action to be brought in federal court, many lawyers do not take an exception for the possible lack of federal subject matter jurisdiction. Some, however, do. Both practices are customary. If a clause designates the federal courts as the exclusive forum, the opinion preparers should consider whether a failure to refer in the opinion to limitations on federal jurisdiction would be misleading to the opinion recipient. See 1998 TriBar Report, *supra* note 1, § 1.4(d), at 602-03.

still takes that position, the opinion may require an express exception or assumption.

More recently, in recognition of the right of parties to order their affairs by contract, the courts of many states have abandoned old precedent and adopted the so-called "modern view," which gives forum selection clauses effect subject to some well-recognized exceptions.⁷⁹ Some states have enacted statutes that validate the enforceability of forum selection clauses in qualifying contracts.⁸⁰

An opinion on a permissive clause without a waiver of *forum non conveniens* means that under the law chosen by the parties as the governing law the parties may bring an action in the designated forum.⁸¹ Because a permissive clause, as interpreted by the courts, does not purport to foreclose a party from bringing an action in another state or, in the absence of a waiver, to prevent application of the doctrine of *forum non conveniens*,⁸² the opinion does not mean that a party

79. See RESTATEMENT OF CONFLICTS, *supra* note 22, § 80; 7 SAMUEL WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 15:15 (4th ed. 1997) (citing cases that follow the modern trend of enforcing forum selection clauses); *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972); *Carnival Cruise Lines v. Shute*, 499 U.S. 585, 595 (1991); *Jacobson v. Mailboxes Etc. U.S.A. Inc.*, 646 N.E.2d 741, 743 (Mass. 1995) ("We accept the modern view that forum selection clauses are to be enforced if it is fair and reasonable to do so."); *Nat'l Union Fire Ins. Co. v. Worley*, 690 N.Y.S.2d 57, 59 (N.Y. App. Div. 1999) (forum selection clause enforced even though New York statute did not apply).

Most states that follow the modern view will give effect to the selection by the parties of a particular venue within the state. See 7 WILLISTON ON CONTRACTS, § 15:15. In New York, by statute, a written agreement fixing the place of trial within the state, made before an action is commenced, will ordinarily be given effect. N.Y.C.P.L.R. § 501 (McKinney 2004). In some states, even though a forum selection clause will be given effect, the selection of a specific venue may not be. See, e.g., *Alexander v. Super. Ct. (Brix Group)*, 114 Cal. App. 4th 723 (2003); *Harry S. Peterson Co. v. Nat'l Union Fire Ins. Co.*, 434 S.E.2d 778 (Ga. Ct. App. 1993); *Leonard v. Paxson*, 654 S.W.2d 440 (Tex. 1983).

80. See, e.g., N.Y. GEN. OBLIG. LAW § 5-1402 (McKinney 2004); 735 ILL. COMP. STAT. ANN. 105/5-5 (West 2004); CAL. CIV. PRO. CODE § 410.40 (West Supp. 2004); DEL. CODE ANN. tit. 6, § 2708 (2002).

Several states have statutes that render void as against public policy contractual provisions that require actions against parties within the state to be brought in a forum outside the state. See, e.g., N.C. GEN. STAT. § 22B-3 (2003); IDAHO CODE § 29-110 (Michie 2004); MONT. CODE ANN. § 28-2-708 (2003); N.D. CENT. CODE § 9-08-05 (2003); OKLA. STAT. ANN. tit 15, § 216 (West 2004). Because the opinion typically covers the enforceability of a forum selection clause under the law of the jurisdiction whose law is chosen as the governing law and whose courts are selected as the forum, the opinion normally does not address the possible effect of a statute adopted by some other jurisdiction.

81. See *supra* note 73. As discussed above, the opinion also addresses the requirements for personal and subject matter jurisdiction.

82. In deciding whether to enforce a permissive clause, even in states that have adopted the modern view, courts normally regard themselves as free to apply the doctrine of *forum non conveniens* and dismiss an action when they perceive that litigating in another available forum will be more convenient for the parties, the witnesses, or the court itself. RESTATEMENT OF CONFLICTS, *supra* note 22, § 84. See also *Argonaut P'ship, L.P. v. Bankers Trustee Co.*, No. 96 CIV.1970 (MBM), 1997 WL 45521, at *12 (S.D.N.Y. Feb. 4, 1997); *Magellan Real Estate Inv. Trust v. Losch*, 109 F. Supp. 2d 1144, 1162 (D. Ariz. 2000); *Neo Sack, Ltd. v. Vinmar Impex, Inc.*, 810 F. Supp. 829 (S.D. Tex. 1993).

Sometimes courts appear to have stretched to interpret forum selection clauses as permissive so as to make it easier for them to approve maintenance of an action in another forum. See 7 WILLISTON ON CONTRACTS, § 15:15; *Orix Credit Alliance, Inc. v. Mid-South Material Corp.*, 816 F. Supp. 230, 233 (S.D.N.Y. 1993); *McDonnell Douglas Corp. v. Islamic Republic of Iran*, 591 F. Supp. 293, 302-03 (E.D. Miss. 1984), *aff'd*, 758 F.2d 341 (8th Cir. 1985), *cert. denied*, 474 U.S. 948 (1985); *Citro Florida, Inc. v. Citrovale, S.A.*, 760 F.2d 1231, 1232 (11th Cir. 1985).

may not bring an action outside the designated forum or that a court might not decline to entertain an action on the basis of the doctrine of *forum non conveniens*.⁸³ Although the doctrine of *forum non conveniens* is not covered, some lawyers nonetheless choose to point out its possible application in their opinions.

In deciding whether to enforce a mandatory clause (or a permissive clause with a waiver of *forum non conveniens*),⁸⁴ courts in a modern view state will not dismiss an action based on convenience but rather will give effect to the parties' choice of forum unless to do so would be "unfair or unreasonable." As interpreted by the courts, for enforcement to be unfair or unreasonable, a judicial determination is required that "enforcement of the clause would be so unreasonable and unjust as to make a trial in the selected forum 'so gravely difficult and inconvenient that the challenging party would, for all practical purposes, be deprived of his or her day in court.'" ⁸⁵ The grounds for not enforcing a forum selection clause under this exception are much narrower than those required to invoke the doctrine of *forum non conveniens*. This exception is commonly referred to as the "Bremen" exception.⁸⁶

In a modern view state, opinion givers rendering an opinion on a mandatory forum selection clause (or a permissive clause with a waiver of *forum non conveniens*) generally do not regard the possibility that a court might decline to enforce the clause by reason of the Bremen exception to require an opinion qualification.⁸⁷ This approach reflects the narrowness of the Bremen exception, the judicial discretion inherent in its application, and the inability of knowing in advance whether grounds for applying the Bremen exception will exist when an action is actually brought.⁸⁸ Nevertheless, the practice of not qualifying the opinion for this

83. The opinion also does not address whether a court in a jurisdiction that is not the selected forum and whose law is not covered by the opinion will dismiss a suit brought in that jurisdiction.

84. For purposes of determining whether to entertain an action in the designated forum and to decline to apply the doctrine of *forum non conveniens*, the courts treat a permissive clause with a waiver of *forum non conveniens* the same as a mandatory clause. See *Blanco v. Banco Indus. de Venezuela, S.A.*, 997 F.2d 974, 979–80 (2d Cir. 1992); *AAR Intern., Inc. v. Nimelias Enters. S.A.*, 250 F.3d 510, 525–26 (7th Cir. 2001). A permissive clause with a waiver, unlike a mandatory clause, however, does not seek to prevent a party from commencing an action elsewhere and does not constrain a court in the designated forum from dismissing an action for reasons other than *forum non conveniens* in favor of an action brought in another forum. See *Fleet Capital Corp. v. Mullins*, No. 03 CIV.6660(RJH)(KNF), 2004 WL 548240, at *5 (S.D.N.Y. Mar. 18, 2004) (action in designated forum dismissed in favor of prior pending action in another forum).

85. See *Shah v. Shah*, 626 N.Y.S. 2d 786, 788 (N.Y. App. Div. 1995) (citing, among others, *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972)); see also *Roby v. Corp. of Lloyd's*, 996 F.2d 1353, 1363 (2d Cir. 1993); *Stamm v. Barclays Bank of N.Y.*, 960 F. Supp. 724, 729 (S.D.N.Y. 1997). Courts also decline to enforce the clause if it was obtained by fraud, duress or overreaching. A remedies opinion is based on an unstated assumption regarding the absence of such conduct. See 1998 TriBar Report, *supra* note 1, § 3.3.4, at 625 n.77.

86. *M/S Bremen*, 407 U.S. 1.

87. If the opinion preparers believe that, based on the circumstances existing on the date of the opinion, the Bremen exception would be applied, they should not render the opinion without taking an exception or otherwise bringing the issue to the attention of the opinion recipient. See 1998 TriBar Report, *supra* note 1, § 3.3.4, at 625 n.77.

88. Some lawyers believe that the equitable principles limitation encompasses the possibility that a court might apply the Bremen exception and decline to enforce a forum selection clause based on facts that exist when the action is brought. See *id.* § 3.3.4, at 625 (recognizing that the limits of the

issue is not universal, and some lawyers routinely point out the possible application of the Bremen exception in the opinion.⁸⁹

In states that have enacted statutes, courts will generally enforce forum selection clauses when the criteria in the statute are met.⁹⁰ In New York, a statute enacted in 1984 expressly validates forum selection clauses in agreements relating to transactions involving not less than \$1 million that select New York law as the governing law.⁹¹ Accordingly, opinion preparers in New York typically give opinions without an exception on the enforceability of forum selection clauses (permissive or mandatory) selecting New York courts as the forum in agreements that qualify under the statute.⁹²

IV. CONCLUSION

In the 1998 TriBar Report, the Committee observed that “at its best, the opinion preparation process can serve to clarify and improve transactions.”⁹³ In this Re-

equitable principles limitation cannot be defined with precision but must remain flexible in view of the broad interest courts have to do justice).

89. A United States District Court also has discretion, under 28 U.S.C. § 1404(a), to transfer venue of a proceeding from one federal court to another. See *Stewart Org., Inc. v. Ricoh Corp.*, 487 U.S. 22, 28–30 (1988). Federal courts have generally found §1404(a) to be applicable even to mandatory forum selection clauses but have not been uniform in the standards they have adopted for deciding whether to exercise the discretion granted by § 1404(a). See 17 JAMES WM. MOORE ET AL., *MOORE'S FEDERAL PRACTICE* 111.04[2] (3d ed. 2004). Many federal courts have followed the admonition of the concurring opinion in *Stewart* that the statutory authority “should be exercised so that a valid forum-selection clause is given controlling weight in all but the most exceptional cases.” *Stewart*, 489 U.S. at 33. See, e.g., *Falconwood Fin. Corp. v. Griffin*, 838 F. Supp. 836, 840 (S.D.N.Y.1993); *Jones v. Weibrecht*, 901 F.2d 17, 19 (2d Cir. 1990); *FUL Inc. v. Unified School Dist. No. 204*, 839 F. Supp. 1307 (N.D. Ill. 1993); *Medoil Corp. v. Citicorp*, 729 F. Supp. 1456, 1459 (S.D.N.Y. 1990).

Other federal courts, however, have taken the position that the parties to a contract only have the power to limit a court's consideration of their convenience in determining whether to enforce a forum selection clause and not the convenience of witnesses or the interest of justice. See, e.g., *Capital Ventures International v. Network Commerce Inc.*, No. 01-CIV.4390(JSM), 2002 WL 417246, at *2 (S.D.N.Y. Mar. 15, 2002). As with the *Bremen* exception (and for similar reasons), many opinion preparers do not take an exception for § 1404(a) when rendering an opinion on a mandatory forum selection clause (or a permissive clause with a waiver of *forum non conveniens*) that includes the federal courts as a possible forum. Although unnecessary, some lawyers, however, to avoid uncertainty, do choose to point out the possible application of §1404(a) in the opinion.

90. See *supra* note 80.

91. N.Y. GEN. OBLIG. LAW § 5-1402 (McKinney 2004). N.Y.C.P.L.R. § 327(b) (McKinney 2004), a companion amendment to section 5-1402, provides that New York courts shall not stay or dismiss any action on the ground of inconvenient forum where section 5-1402 applies. The purpose of the statute was to assure the parties to an agreement that the courts would give effect to their choice of New York law as the governing law and their selection of the New York courts to resolve disputes. The trend for New York courts to recognize the parties' choice of forum was well under way in New York before enactment of the statute, see, e.g., *Arthur Young & Co. v. Leong*, 383 N.Y.S.2d 618, 619 (N.Y. App. Div. 1976), and since the statute was enacted New York courts have followed the modern view even when the statute does not apply. See, e.g., *Roby v. Corp. of Lloyd's*, 996 F.2d 1353, 1363 (2d Cir. 1993); *Brooke Group Ltd. v. JCH Syndicate* 488, 87 N.Y.2d 530, 534 (1996).

92. A New York court might still apply Bremen-like exceptions, but in view of the purpose of the statute to provide certainty to contracting parties, the grounds for departing from the statute, if a court were to do so, would presumably be limited to exceptional circumstances. Lawyers in New York do not routinely take an exception for such circumstances.

93. 1998 TriBar Report, *supra* note 1, at 665–66.

port, the Committee has described an approach for preparing the remedies opinion and determining when an express exception or assumption should be included, and has applied that approach to several common contractual provisions. The Committee believes that this approach, if broadly followed, will improve the opinion process and enhance the usefulness of the remedies opinion.⁹⁴

August 2, 2004
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94. As in the past we invite your comments on this Report. Address any comments to:

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APPENDIX A

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