

# HARRIET B. ALEXSON

A Professional Law Corporation



## BUSINESS ALERT

*CURRENT LEGAL ISSUES FOR THE BUSINESS COMMUNITY*

November, 2008

Vol.8, No. 1

### **IS THE ORAL AGREEMENT ENFORCEABLE?**

By: Harriet B. Alexson (949.250-9664)  
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With the volatility of today's markets, sophisticated borrowers already in financing arrangements as documented by a loan agreement, are seeking to lock in an interest rate over the permanent term of the loan. Often a borrower has entered into a construction loan agreement, and the lender has already made a commitment to fund the permanent portion of the loan.

For example, this permanent lock-in may be done to convert a LIBOR rate to a fixed by the election of an interest rate swap. An interest rate swap is the agreement of two (2) parties to buy and sell a series of cash flows which are viewed as equal at the time of such election.

The swap transaction is documented by the ISDA Master Agreement and Schedule. Upon the election of a swap, the financial terms are usually documented in a confirmation letter and the Schedule documents deal with the specifics or credit issues between a lender and borrower. The ISDA form requires the choice of law be New York as it is most favorable to the lender in this type of transaction.

What if the election is oral? Does the date of the election lock in the interest rate?

Marketplace custom and practice have been codified by statute in New York and California. Each of the New York General Obligations Law Section 5-701 Sec. b1 and b2(f) and the California Civil Code Section 1624(b)1 and (b)(2)(F) provides that a "qualified financial contract," which comprises, for these purposes, "a rate swap, basis swap [and] forward rate transaction," is an exception to the statute of frauds. Under both referenced New York and California statutes, there is "sufficient evidence that a contract has been made if" either (i) there is "evidence of electronic communication ... to indicate that a contract was made between the parties" or (ii) a "confirmation in writing ... is received by the party against whom enforcement is sought no later than the fifth business day after the contract has been made ... and the sender does not receive, on or before the third business day after receipt ..., written objection to a material term of the confirmation." New York General Obligations Law Section 5-701 Sec. b3(a) and (b) and California Civil Code Section 1624((b)(3)(A) and (B).

As a borrower or a lender, under certain circumstances, oral statements that you make may be enforceable against you. Please seek legal counsel before entering into an interest rate swap or other “qualified” financial transaction under California or New York law.

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